

Financial Statements with Report of Independent Certified  
Public Accountants

**Terrafirma Risk Retention Group LLC**

December 31, 2013 and 2012

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## **REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS**

To the Members Committee  
Terrafirma Risk Retention Group LLC

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We have audited the accompanying financial statements of Terrafirma Risk Retention Group LLC (a Vermont Company), which comprise the balance sheets as of December 31, 2013 and 2012, and the related statements of operations and comprehensive income (loss), changes in total equity, and cash flows for the years then ended, and the related notes to the financial statements.

### **Management's responsibility for the financial statements**

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

### **Auditor's responsibility**

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Company's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our qualified audit opinion.

#### Basis for Qualified Opinion

As described more fully in Note 2, the Company prepared these financial statements using accounting practices prescribed or permitted by the Vermont Department of Financial Regulation. Such accounting practices are equivalent to accounting principles generally accepted in the United States of America. However, the Vermont Department of Financial Regulation permits the Company to account for contributions from non-members as capital contributions and not as contributions revenue, as would be required by accounting principles generally accepted in the United States of America.

#### Qualified Opinion

In our opinion, except for the effects of the matter described in the Basis for Qualified Opinion paragraph, the financial statements referred to above present fairly, in all material respects, the financial position of Terrafirma Risk Retention Group LLC as of December 31, 2013 and 2012, and the results of its operations, changes in its total equity and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

*Grant Thornton LLP*

Glastonbury, Connecticut  
March 3, 2014

**TERRAFIRMA RISK RETENTION GROUP LLC**  
**Balance Sheets**  
**December 31, 2013 and 2012**

	<u>2013</u>	<u>2012</u>
<b>ASSETS</b>		
Cash and cash equivalents	\$ 1,298,536	\$ 1,003,978
Investments, available for sale, at fair value	3,551,130	3,209,703
Accrued interest receivable	24,469	22,411
Deferred acquisition costs	5,532	-
Prepaid expenses	778	768
Property, plant and equipment, net	58,384	75,066
Total assets	<u>\$ 4,938,829</u>	<u>\$ 4,311,926</u>
<b>LIABILITIES AND TOTAL EQUITY</b>		
<b>Liabilities</b>		
Unpaid losses and loss adjustment expenses	\$ 332,726	\$ -
Unearned premium	166,652	-
Accounts payable and accrued expenses	51,725	16,885
Premiums received in advance	7,832	9,146
Total liabilities	<u>558,935</u>	<u>26,031</u>
<b>Total Equity</b>		
Capital contributions	4,197,500	4,197,500
Member contributions	50,400	48,000
Accumulated other comprehensive income	(10,460)	320
Accumulated earnings	142,454	40,075
Total equity	<u>4,379,894</u>	<u>4,285,895</u>
Total liabilities and total equity	<u>\$ 4,938,829</u>	<u>\$ 4,311,926</u>

The accompanying notes are an integral part of these financial statements.

**TERRAFIRMA RISK RETENTION GROUP LLC**  
**Statements of Operations and Comprehensive Income (Loss)**  
**Years Ended December 31, 2013 and 2012**

	<u>2013</u>	<u>2012</u>
<b>REVENUES</b>		
Premiums earned	\$ 864,047	\$ -
Investment income (loss), net	3,905	(1,844)
Registration fees	12,425	10,325
Total revenues	<u>880,377</u>	<u>8,481</u>
<b>EXPENSES</b>		
Loss and loss adjustment expenses	336,978	-
Premium tax expense	28,691	-
General and administrative expenses	412,329	118,099
Total expenses	<u>777,998</u>	<u>118,099</u>
Net income (loss)	102,379	(109,618)
<b>OTHER COMPREHENSIVE INCOME</b>		
Unrealized holding (loss) gain on available for sale securities	<u>(10,780)</u>	<u>320</u>
Comprehensive income (loss)	<u>\$ 91,599</u>	<u>\$ (109,298)</u>

The accompanying notes are an integral part of these financial statements.

**TERRAFIRMA RISK RETENTION GROUP LLC**  
**Statements of Changes in Total Equity**  
**Years Ended December 31, 2013 and 2012**

	Capital Contributions	Member Contributions	Accumulated Earnings	Accumulated Other Comprehensive Income	Total
Balance as of January 1, 2012	\$ -	\$ 46,300	\$ 149,693	\$ -	\$ 195,993
Capital contributions	4,197,500	-	-	-	4,197,500
Member contributions	-	1,700	-	-	1,700
Net loss	-	-	(109,618)	-	(109,618)
Unrealized gain on available for sale securities	-	-	-	320	320
Balance as of December 31, 2012	4,197,500	48,000	40,075	320	4,285,895
Member contributions	-	2,400	-	-	2,400
Net income	-	-	102,379	-	102,379
Unrealized loss on available for sale securities	-	-	-	(10,780)	(10,780)
Balance as of December 31, 2013	\$ 4,197,500	\$ 50,400	\$ 142,454	\$ (10,460)	\$ 4,379,894

The accompanying notes are an integral part of these financial statements.

**TERRAFIRMA RISK RETENTION GROUP LLC**  
**Statements of Cash Flows**  
**Years Ended December 31, 2013 and 2012**

	<u>2013</u>	<u>2012</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net income (loss)	\$ 102,379	\$ (109,618)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation of property, plant and equipment	16,682	8,340
Investment losses, net	60,758	24,438
Changes in assets and liabilities:		
Deferred acquisition costs	(5,532)	-
Accrued interest receivable	(2,058)	(22,411)
Prepaid expenses	(10)	(768)
Unpaid losses and loss adjustment expenses	332,726	-
Unearned premium	166,652	-
Accounts payable and accrued expenses	34,840	15,769
Premiums received in advance	(1,314)	9,146
Net cash provided by (used in) operations	<u>705,123</u>	<u>(75,104)</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Purchases of available for sale securities	(1,360,773)	(4,247,329)
Proceeds from sales of available for sale securities	947,808	1,013,508
Purchase of property, plant and equipment	-	(83,406)
Net cash used in investing activities	<u>(412,965)</u>	<u>(3,317,227)</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Proceeds from capital contributions	-	4,197,500
Proceeds from member contributions	2,400	1,700
Net cash provided by financing activities	<u>2,400</u>	<u>4,199,200</u>
Net increase in cash and cash equivalents	294,558	806,869
<b>CASH AND CASH EQUIVALENTS, beginning of year</b>	<u>1,003,978</u>	<u>197,109</u>
<b>CASH AND CASH EQUIVALENTS, end of year</b>	<u>\$ 1,298,536</u>	<u>\$ 1,003,978</u>

The accompanying notes are an integral part of these financial statements.



**TERRAFIRMA RISK RETENTION GROUP LLC**  
**Notes to Financial Statements**  
**December 31, 2013 and 2012**

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**NOTE 1 - NATURE OF OPERATIONS**

Terrafirma Risk Retention Group LLC (“the Company”) is a manager-managed, tax-exempt risk retention group organized as a limited liability company under the laws of the State of Vermont. The Company was organized in 2011 and licensed in 2012 and is qualified by the Internal Revenue Service as a charitable risk pool pursuant to the Internal Revenue Code Section 501(n). The Company was formed by The Land Trust Alliance, Inc. (“the Alliance”) to pool and insure the risks of its members to help land trusts defend their conserved lands from legal challenge and to provide information to its members with respect to loss control and risk management. The Alliance is a not-for-profit corporation organized under the laws of the Commonwealth of Massachusetts. The Alliance was formed in 1982 to advance the mission of land trusts.

The Company was formed to provide conservation defense liability insurance for land trusts’ obligations to defend and enforce conservation easements and fee-owned land. The policy covers litigation expense arising out of violations, challenges, encroachments or other efforts to affect conservation rights held by insured member land trusts, and for other liabilities incurred by land trusts in connection with their duties to monitor and protect conservation easements and fee-owned land. The Company’s liability insurance policies commenced as of March 1, 2013.

The Company is managed by Alliance Risk Management Services LLC (“ARMS”), a wholly-owned subsidiary of the Land Trust Alliance, Inc. The Company is solely responsible for meeting its obligations to its insured members and others and the Land Trust Alliance, Inc., ARMS or any member of the Company is not liable for the claims, debts or other liabilities of the Company.

**NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

The significant accounting policies followed by the Company that materially affect financial reporting are summarized below.

**BASIS OF PRESENTATION**

The accompanying financial statements have been prepared on the accrual basis of accounting in accordance with practices prescribed or permitted by Vermont Captive regulations of the Vermont Department of Financial Regulation (“the Department”). Such accounting practices are equivalent to accounting principles generally accepted in the United States of America (“GAAP”). However, the Department permits the Company to account for contributions from non-members as described further in Note 2 as capital contributions and not as contributions revenue, as would be required by GAAP.

**USE OF ESTIMATES**

The preparation of financial statements in accordance with GAAP requires management to make estimates and assumptions that affect the reported amounts and disclosures in the financial statements. Actual results could differ from those estimates.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

**CASH AND CASH EQUIVALENTS**

The Company considers all highly liquid financial instruments purchased with an original maturity of three months or less to be cash equivalents. As of December 31, 2013 and 2012, the Company had cash equivalents of \$1,168,388 and \$918,747, respectively, comprised of money market funds.

**INVESTMENTS**

The Company's investments in fixed income securities are measured and reported at fair value. The Company's investment securities are exposed to various risks such as interest rate, market and credit risks. Due to the level of risk associated with investment securities, it is at least reasonably possible that changes in the values of investment securities will occur in the near term and such changes could materially affect the amounts reported in the financial statements.

**FAIR VALUE MEASUREMENTS**

The Company measures its investments at fair value in accordance with FASB ASC 820, "Fair Value Measurements and Disclosures". Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. FASB ASC 820 establishes a hierarchy of valuation techniques used to determine the fair value of assets and liabilities based upon whether the inputs to those valuation techniques reflect assumptions other market participants would use based upon market data obtained from independent sources (also referred to as observable inputs). Authoritative accounting guidance requires that the valuation techniques used to measure fair value maximize the use of observable inputs and minimize the use of unobservable inputs. The following summarizes the fair value hierarchy:

Level 1 – Quoted prices (unadjusted) in active markets for identical assets or liabilities that the Company has the ability to access at the measurement date.

Level 2 – Inputs, other than quoted prices included in Level 1, that are observable for the asset or liability, either directly or indirectly. Level 2 inputs include:

- Quoted prices for similar assets or liabilities in active markets;
- Quoted prices of identical or similar assets or liabilities in markets that are not active;
- Inputs other than quoted prices that are observable for the asset or liability and;
- Inputs that are derived principally from or corroborated by observable market data by correlation or other means.

Level 3 – Inputs that are unobservable for the asset or liability.

The level in the fair value hierarchy within which the fair value measurement in its entirety falls is determined based on the lowest level input that is significant to the fair value measurement.

The Company has classified its investments in accordance with ASC 820, as disclosed in Note 4.

**NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**PROPERTY, PLANT AND EQUIPMENT**

Property, plant and equipment represents costs incurred to create and launch the Company's website. The asset is being depreciated on a straight-line basis over its estimated useful life of five years. Website maintenance is charged to expense as incurred.

**PREMIUMS AND PREMIUMS RECEIVED IN ADVANCE**

Premiums are earned over the terms of the related insurance policies. Unearned premium reserves are established to cover the unexpired portion of premiums written. Such reserves are computed by pro-rata methods. Premiums received in advance represent amounts received prior to the Company issuing a written policy. The Company's member policies will commence effective March 1, 2013; therefore, no revenues from premiums have been recognized through December 31, 2012.

**PREMIUMS RECEIVABLE**

Premium receivable represents amounts due from insureds and are recorded net of any allowance for uncollectible accounts. The Company records an allowance against its outstanding premium receivable based on management's estimation of uncollectible accounts in the near term. As of December 31, 2013 and 2012, the Company did not have any outstanding premium balances due.

**DEFERRED POLICY ACQUISITION COSTS**

Policy acquisition costs represent premium taxes and are directly related to the successful placement of insurance contracts. These costs are deferred and expensed over the term of the related policies.

**CONTRIBUTIONS**

Contributions from non-members include contributions, grants, gifts and awards pledged or received by the Company. Under GAAP, the Company would report contributions as revenue when received or pledged by the donor. The Department has approved a permitted practice for the Company to account for contributions from non-members as capital contributions and not as contributions revenue, as would be required by GAAP.

All members of the Company are required to make an initial capital contribution of \$100. No member has a right to have its membership interest redeemed or its capital contribution returned in accordance with terms of the operating agreements. Each member of the Company has equal voting rights.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

**REGISTRATION FEES**

Registration fees represent non-refundable fees charged to land trusts applying to become members of the Company. Amounts are recognized as revenues when earned.

**INVESTMENT INCOME**

Investment income and gains and losses are recognized when earned.

**ASSUMED LOSS AND LOSS ADJUSTMENT EXPENSES**

Unpaid losses and loss adjustment expenses include an amount determined from individual case estimates and loss reports and an amount, based on past experience, for losses incurred but not reported. Such liabilities are necessarily based on assumptions and estimates and while management believes the amount is adequate, the ultimate liability may be in excess of or less than the amount provided. The methods for making such estimates and for establishing the resulting liabilities are continually reviewed and any adjustments are reflected in the period determined.

The Company's member policies are effective beginning March 1, 2013; therefore, there is no reserve for losses as of December 31, 2012.

**INCOME AND PREMIUM TAX STATUS**

The Company is a qualified charitable risk pool under section 501(n) of the Internal Revenue Code. As such, it is exempt from federal income tax under section 501(a) of the Internal Revenue Code as an organization described in section 501(c)(3) of the Internal Revenue Code. Accordingly, no provision for federal income taxes has been made in the accompanying financial statements. The Company is subject to premium taxes imposed by all states where the Company is registered. Premium taxes of \$28,691 were recognized for the year ended December 31, 2013. No premium taxes were recognized for the year ended December 31, 2012 as the Company utilized the tax credit available to first time filers in the State of Vermont.

The Company accounts for uncertain tax positions in accordance with the provisions of FASB ASC 740, "Income Taxes", which provide a framework for how companies should recognize, measure, present and disclose uncertain tax positions in their financial statements. Under FASB ASC 740, the Company may recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by the tax authorities. The tax benefits recognized in the financial statements from such position are measured based in the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement. The Company has no uncertain tax positions that qualify for recognition or disclosure in the financial statements.

It is the Company's policy to include interest and penalties related to unrecognized tax benefits as a component of general and administrative expenses. As of December 31, 2013 and 2012, the Company did not record any penalties or interest related to unrecognized tax benefits. Tax years from 2011 and forward are open and subject to examination.

**TERRAFIRMA RISK RETENTION GROUP LLC**  
**Notes to Financial Statements**  
**December 31, 2013 and 2012**

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**NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**ADVERTISING**

The Company expenses production costs for advertising the first time the advertising takes place. Advertising expense for the years ended December 31, 2013 and 2012 was \$6,946 and \$6,400, respectively.

**RECLASSIFICATIONS**

For purposes of financial statement presentation purposes the 2012 net investment loss was reclassified from the expense section of the statement of operations and comprehensive income (loss) to the revenue section in 2013.

**NOTE 3 - CUSTODIAL CREDIT RISK**

Custodial credit risk is the risk that in the event of a bank failure, the Company will not be able to recover its cash deposits or investments held. The Company maintains its cash, cash equivalents and investments in highly rated financial institutions, which are periodically reviewed by management for financial stability. Accounts are insured by the Federal Deposit Insurance Corporation (FDIC) up to certain limits. The Company's accounts may exceed FDIC depository insurance limits from time to time. However, the Company has not experienced any losses in such accounts and management believes that its cash and cash equivalents and investments are not exposed to significant credit risk.

**NOTE 4 - INVESTMENTS**

Details on carrying value, fair value and amortized cost of investments in fixed income securities as of December 31, 2013 are as follows:

	<u>Carrying Value</u>	<u>Fair Value</u>	<u>Amortized Cost</u>
U.S. government and government agency securities	\$ 1,994,766	\$ 1,994,766	\$ 2,004,999
Corporate bonds	<u>1,556,364</u>	<u>1,556,364</u>	<u>1,556,591</u>
	<u>\$ 3,551,130</u>	<u>\$ 3,551,130</u>	<u>\$ 3,561,590</u>

TERRAFIRMA RISK RETENTION GROUP LLC  
Notes to Financial Statements  
December 31, 2013 and 2012

NOTE 4 - INVESTMENTS (Continued)

Details on carrying value, fair value and amortized cost of investments in fixed income securities as of December 31, 2012 are as follows:

	<u>Carrying Value</u>	<u>Fair Value</u>	<u>Amortized Cost</u>
U.S. government and government agency securities	\$ 1,830,885	\$ 1,830,885	\$ 1,829,178
Corporate bonds	<u>1,378,818</u>	<u>1,378,818</u>	<u>1,380,205</u>
	<u>\$ 3,209,703</u>	<u>\$ 3,209,703</u>	<u>\$ 3,209,383</u>

Details on unrealized gains and losses of the Company's fixed income securities as of December 31, 2013 and 2012 are follows:

	<u>2013</u>		<u>2012</u>	
	<u>Unrealized Gains</u>	<u>Unrealized Losses</u>	<u>Unrealized Gains</u>	<u>Unrealized Losses</u>
U.S. government and government agency securities	\$ 1,786	\$ (12,019)	\$ 1,730	\$ (24)
Corporate bonds	<u>10,281</u>	<u>(10,508)</u>	<u>557</u>	<u>(1,943)</u>
	<u>\$ 12,067</u>	<u>\$ (22,527)</u>	<u>\$ 2,287</u>	<u>\$ (1,967)</u>

TERRAFIRMA RISK RETENTION GROUP LLC  
Notes to Financial Statements  
December 31, 2013 and 2012

NOTE 4 - INVESTMENTS (Continued)

The following table sets forth, as of December 31, 2013, fixed income securities that have been in a continuous loss position for less than twelve months and those that have been in a continuous unrealized loss position for twelve months or longer for which other-than-temporary impairments have not been recognized.

	Less Than 12 Months		Greater Than 12 Months	
	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value
U.S. government and government agency securities	\$ (7,264)	\$ 522,516	\$ (4,755)	\$ 900,120
Corporate bonds	(9,638)	178,890	(870)	327,673
	<u>\$ (16,902)</u>	<u>\$ 701,406</u>	<u>\$ (5,625)</u>	<u>\$ 1,227,793</u>

The following table sets forth, as of December 31, 2012, fixed income securities that have been in a continuous loss position for less than twelve months and those that have been in a continuous unrealized loss position for twelve months or longer for which other-than-temporary impairments have not been recognized.

	Less Than 12 Months		Greater Than 12 Months	
	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value
U.S. government and government agency securities	\$ (24)	\$ 112,806	\$ -	\$ -
Corporate bonds	(1,943)	1,089,263	-	-
	<u>\$ (1,967)</u>	<u>\$ 1,202,069</u>	<u>\$ -</u>	<u>\$ -</u>

TERRAFIRMA RISK RETENTION GROUP LLC  
Notes to Financial Statements  
December 31, 2013 and 2012

NOTE 4 - INVESTMENTS (Continued)

The following table sets forth the carrying value, fair value and amortized cost of fixed income securities as of December 31, 2013 by contractual or expected maturity. Actual maturities will differ from contractual or estimated maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	<u>Carrying Value</u>	<u>Fair Value</u>	<u>Amortized Cost</u>
One year to less	\$ 149,621	\$ 149,621	\$ 149,613
One to five years	<u>3,401,509</u>	<u>3,401,509</u>	<u>3,411,977</u>
	<u>\$ 3,551,130</u>	<u>\$ 3,551,130</u>	<u>\$ 3,561,590</u>

The components of net realized investment gains (losses) are as follows for the years ended December 31, 2013 and 2012:

	<u>2013</u>		<u>2012</u>	
	<u>Realized Gains</u>	<u>Realized Losses</u>	<u>Realized Gains</u>	<u>Realized Losses</u>
U.S. government and government agency securities	\$ 624	\$ (479)	\$ 267	\$ (985)
Corporate bonds	<u>-</u>	<u>-</u>	<u>254</u>	<u>(1,266)</u>
	<u>\$ 624</u>	<u>\$ (479)</u>	<u>\$ 521</u>	<u>\$ (2,251)</u>