

CONSOLIDATED FINANCIAL STATEMENTS AND
SUPPLEMENTARY INFORMATION

GC Palomar Holdings and Subsidiaries
Year Ended December 31, 2016
With Report of Independent Auditors

Ernst & Young LLP



Building a better
working world



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Report of Independent Auditors

The Board of Directors
GC Palomar Holdings and Subsidiaries

We have audited the accompanying consolidated financial statements of GC Palomar Holdings and Subsidiaries (the Company), which comprise the consolidated balance sheet as of December 31, 2016, and the related consolidated statements of income and comprehensive income, shareholder's equity, and cash flows for the year ended December 31, 2016, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in conformity with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free of 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 audit. We conducted our audit in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of 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 entity'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 entity'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 audit opinion.



Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of GC Palomar Holdings and Subsidiaries at December 31, 2016, and the consolidated results of their operations and their cash flows for the year ended December 31, 2016, in conformity with U.S. generally accepted accounting principles.

Ernst + Young LLP

June 2, 2017

GC Palomar Holdings and Subsidiaries

Consolidated Balance Sheet

December 31, 2016

Assets

Cash and cash equivalents	\$ 9,812,030
Investments available-for-sale:	
Fixed income securities	85,671,354
Equity securities	19,149,923
Accrued investment income	651,084
Premium receivable	11,242,421
Deferred policy acquisition costs	10,654,630
Reinsurance recoverable	1,543,425
Prepaid expenses and other assets	1,785,985
Property and equipment, net	919,722
Intangible assets	743,700
Net deferred tax assets	1,837,910
Total assets	<u>\$ 144,012,184</u>

Liabilities and shareholder's equity

Liabilities:

Accounts payable and other accrued liabilities	\$ 4,259,382
Reserve for losses and loss adjustment expenses	4,778,184
Unearned premiums	41,062,236
Ceded premium payable	1,582,521
Funds held under reinsurance treaty	1,720,760
Notes payable	17,500,000
Total liabilities	<u>70,903,083</u>

Shareholder's equity:

Common stock, \$1 par value, 1 share authorized and issued	1
Additional paid-in capital	68,499,999
Accumulated other comprehensive income	1,016,501
Retained earnings	3,592,600
Total shareholder's equity	<u>73,109,101</u>
Total liabilities and shareholder's equity	<u>\$ 144,012,184</u>

See accompanying notes.

GC Palomar Holdings and Subsidiaries

Consolidated Statement of Income and Comprehensive Income

Year ended December 31, 2016

Revenues:	
Net premiums earned	\$ 40,321,980
Net investment income	1,615,076
Net realized gains on investments	499,101
Commission and other income	<u>260,220</u>
Total revenues	<u>42,696,377</u>
Expenses:	
Acquisition expense and premium taxes	17,340,447
Other underwriting expenses	10,153,417
Losses and loss adjustment expenses	7,291,584
Interest expense	<u>1,633,765</u>
Total expenses	<u>36,419,213</u>
Income before income tax benefit	6,277,164
Income tax benefit	<u>337,260</u>
Net income	<u>6,614,424</u>
Other comprehensive income, net:	
Net unrealized gains on securities available for sale, net of taxes of \$733,478	<u>1,475,135</u>
Net comprehensive income	<u><u>\$ 8,089,559</u></u>

See accompanying notes.

GC Palomar Holdings and Subsidiaries

Consolidated Statement of Shareholder's Equity

	Number of Common Shares Outstanding		Common Stock	Additional Paid-In Capital	Accumulated Other Comprehensive Income	Retained Earnings	Total Shareholder's Equity
Balance at January 1, 2016	1	\$	1	\$ 68,499,999	\$ (458,634)	\$ (3,021,824)	\$ 65,019,542
Change in net unrealized gain on investments	-		-	-	1,475,135	-	1,475,135
Net income	-		-	-	-	6,614,424	6,614,424
Balance at December 31, 2016	1	\$	1	\$ 68,499,999	\$ 1,016,501	\$ 3,592,600	\$ 73,109,101

See accompanying notes.

GC Palomar Holdings and Subsidiaries

Consolidated Statement of Cash Flows

Year ended December 31, 2016

Operating activities

Net income	\$ 6,614,424
Adjustments to reconcile net income to net cash provided by operating activities:	
Depreciation expense	87,913
Amortization of debt issuance costs	88,591
Loss on asset disposal	17,504
Net realized gains on sales of investments	(499,101)
Amortization of premium on fixed income securities	972,702
Income tax benefit	(337,260)
Changes in operating assets and liabilities:	
Accrued investment income	(61,170)
Premium receivable	(2,756,538)
Deferred policy acquisition costs	(3,850,208)
Reinsurance recoverable	(1,303,713)
Prepaid expenses and other assets	(371,251)
Accounts payable and other accrued liabilities	1,772,062
Reserve for losses and loss adjustment expenses	3,009,899
Unearned premiums	12,329,597
Ceded premiums payable	(374,946)
Funds held under reinsurance treaty	486,494
Net cash provided by operating activities	15,824,999

Investing activities

Purchases of property and equipment	(898,311)
Proceeds from sale of property and equipment	3,700
Purchases of fixed income securities	(27,379,569)
Purchases of equity securities	(12,717,955)
Sales and maturities of fixed income securities	18,983,403
Sales of equity securities	10,477,432
Net cash used in investing activities	(11,531,300)

Financing activities

Restricted cash	225,000
Net cash provided by financing activities	225,000

Net increase in cash and cash equivalents	4,518,699
Cash and cash equivalents at beginning of period	5,293,331
Cash and cash equivalents at end of period	\$ 9,812,030

See accompanying notes.