

FINANCIAL STATEMENTS - STATUTORY BASIS
AND
INDEPENDENT AUDITORS' REPORT



UNIVERSAL FIDELTY LIFE INSURANCE COMPANY

December 31, 2016 and 2015

CONTENTS

	Page
INDEPENDENT AUDITORS' REPORT	3
FINANCIAL STATEMENTS (STATUTORY BASIS)	
STATEMENTS OF ADMITTED ASSETS, LIABILITIES AND CAPITAL AND SURPLUS	5
STATEMENTS OF OPERATIONS	6
STATEMENTS OF CHANGES IN CAPITAL AND SURPLUS	7
STATEMENTS OF CASH FLOWS	8
NOTES TO FINANCIAL STATEMENTS	9
OTHER FINANCIAL INFORMATION	
INDEPENDENT AUDITORS' REPORT ON OTHER FINANCIAL INFORMATION	37
SCHEDULE OF SELECTED STATUTORY BASIS FINANCIAL DATA	38
SCHEDULE OF INVESTMENT RISKS INTERROGATORIES	41
SUMMARY INVESTMENT SCHEDULE	45
NOTE TO OTHER FINANCIAL INFORMATION	47



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Independent Auditors' Report

The Board of Directors
Universal Fidelity Life Insurance Company

We have audited the accompanying statutory financial statements of Universal Fidelity Life Insurance Company (the Company), which comprise the statutory statements of admitted assets, liabilities and capital and surplus as of December 31, 2016 and 2015, and the related statutory statements of operations, changes in capital and surplus 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 the financial reporting provisions prescribed or permitted by the Oklahoma Insurance Department. Management is also responsible for 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 error or fraud.

Auditors' 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 auditors' judgment, including the assessment of the risk 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.

Other Locations

Belleville, IL • Carbondale, IL • Columbia, IL • Harrisburg, IL • Litchfield, IL • Cape Girardeau, MO • St. Louis, MO • Milwaukee, WI

Basis for Adverse Opinion on Accounting Principles Generally Accepted in the United States of America

As described in Note A2, the financial statements are prepared by Universal Fidelity Life Insurance Company on the basis of the financial reporting provisions prescribed or permitted by the Oklahoma Insurance Department, which is a basis of accounting other than accounting principles generally accepted in the United States of America, to comply with the requirements of the Oklahoma Insurance Department. The effects on the financial statements of the variances between the regulatory basis of accounting described in Note A2 and accounting principles generally accepted in the United States of America, although not reasonably determinable, are presumed to be material.

Adverse Opinion on Accounting Principles Generally Accepted in the United States of America

In our opinion, because of the significance of the matter discussed in the Basis for Adverse Opinion on Accounting Principles Generally Accepted in the United States of America paragraph, the financial statements referred to in the first paragraph do not present fairly, in accordance with accounting principles generally accepted in the United States of America, the financial position of Universal Fidelity Life Insurance Company as of December 31, 2016 and 2015, or the results of its operations or its cash flows for the years then ended.

Opinion on Regulatory Basis of Accounting

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the admitted assets, liabilities, and capital and surplus of Universal Fidelity Life Insurance Company as of December 31, 2016 and 2015, and the results of its operations and its cash flows for the years then ended, on the basis of the financial reporting provisions prescribed or permitted by the Oklahoma Insurance Department as described in Note A2.

Curby, Eck & Brueckel LLP

Springfield, Illinois
May 19, 2017

Universal Fidelity Life Insurance Company

STATEMENTS OF ADMITTED ASSETS, LIABILITIES AND CAPITAL AND SURPLUS - STATUTORY BASIS

December 31

	<u>2016</u>	<u>2015</u>
ADMITTED ASSETS		
Cash and invested assets		
Bonds	\$ 2,651,831	\$ 4,628,753
Preferred stocks - cost	1,049,308	693,812
Common stocks - principally at market	64,500	82,100
Partnership interests	10,963	19,734
Real estate - at cost, less allowances for depreciation		
Property occupied by the Company	749,485	770,274
Properties held for the production of income	316,667	333,333
Policy loans	96,280	100,455
Cash and short-term investments	<u>3,734,877</u>	<u>1,390,930</u>
Total cash and invested assets	8,673,911	8,019,391
Accrued investment income	17,302	32,428
Receivable on reinsurance	27,231	104,283
Premiums due and deferred	297,680	210,763
Funds held by reinsurer	3,060,741	3,396,633
Amounts due from third-party administration	610,102	730,209
Federal income taxes receivable	34,998	97,272
Related party receivable	599	47,673
EDP equipment	65,061	47,635
Deferred tax asset	439,335	454,504
Other assets	<u>2,432</u>	<u>2,896</u>
Total admitted assets	<u>\$ 13,229,392</u>	<u>\$ 13,143,687</u>
LIABILITIES AND CAPITAL AND SURPLUS		
Insurance reserves and claims		
Life reserves	\$ 3,978,499	\$ 3,826,372
Accident and health claim and unearned premium reserves	1,248,021	1,253,378
Liability for deposit-type contracts	6,459	6,244
Life contract claims	103,452	100,475
Accident and health contract claims	1,569,685	1,418,514
Premiums received in advance	<u>18,781</u>	<u>149,210</u>
Total insurance reserves and claims	6,924,897	6,754,193
Pension benefit liability	19,200	27,600
Accrued expenses	974,785	1,095,000
Related party payable	13,247	36,279
Amounts payable on reinsurance	201,420	205,371
Interest maintenance reserve	96,874	121,050
Asset valuation reserve	91,785	83,989
Borrowed funds	<u>-</u>	<u>365,183</u>
Total liabilities	8,322,208	8,688,665
Capital and surplus		
Common stock, \$1 par value, 2,000,000 shares authorized; 1,017,756 shares issued and outstanding	1,017,756	1,017,756
Unassigned surplus	<u>3,889,428</u>	<u>3,437,266</u>
Total capital and surplus	<u>4,907,184</u>	<u>4,455,022</u>
Total liabilities and capital and surplus	<u>\$ 13,229,392</u>	<u>\$ 13,143,687</u>

The accompanying notes are an integral part of these statements.

Universal Fidelity Life Insurance Company

STATEMENTS OF OPERATIONS - STATUTORY BASIS

Years ended December 31

	<u>2016</u>	<u>2015</u>
Premiums and other insurance income		
Life	\$ 678,935	\$ 561,722
Accident and health	9,005,993	9,197,233
	<hr/>	<hr/>
Total premiums and other insurance income	9,684,928	9,758,955
Investment income, net	180,921	185,674
Allowance on reinsurance ceded	498,475	569,490
Amortization of interest maintenance reserve	24,176	18,063
Administration fees	6,570,996	6,312,149
Miscellaneous income	2,589	5,611
	<hr/>	<hr/>
Total income	16,962,085	16,849,942
Benefits paid or provided		
Life benefits	246,790	253,426
Accident and health benefits	6,285,765	5,531,634
Surrender benefits	62,156	375,628
Refunds to members	1,772	1,616
Increase (decrease) in aggregate reserves for life, accident and health policies and contracts	146,770	(172,835)
	<hr/>	<hr/>
Total benefits paid or provided	6,743,253	5,989,469
Selling, general and administrative expenses		
Commissions	3,161,024	3,586,831
General expenses	6,112,070	6,640,917
Taxes, licenses and fees	534,031	521,701
Increase in loading on due and deferred premiums	20,315	39,479
	<hr/>	<hr/>
Total selling, general and administrative expenses	9,827,440	10,788,928
Income before federal income taxes and net realized capital losses	391,392	71,545
Federal income tax expense (benefit)	62,275	(47,470)
	<hr/>	<hr/>
Income before net realized capital losses	329,117	119,015
Net realized capital losses	(7,793)	(61,081)
	<hr/>	<hr/>
Net income	\$ 321,324	\$ 57,934
	<hr/>	<hr/>

The accompanying notes are an integral part of these statements.

Universal Fidelity Life Insurance Company

STATEMENTS OF CHANGES IN CAPITAL AND SURPLUS - STATUTORY BASIS

Years ended December 31

	<u>Common Stock</u>	<u>Unassigned Surplus</u>	<u>Total</u>
Balance as of January 1, 2015	\$ 1,017,756	\$ 3,437,737	\$ 4,455,493
Net income	-	57,934	57,934
Change in net unrealized capital losses	-	108,543	108,543
Change in net deferred income tax	-	160,082	160,082
Change in non-admitted assets	-	(289,453)	(289,453)
Change in asset valuation reserve	-	(16,575)	(16,575)
Correction of prior year error	-	(21,002)	(21,002)
	1,017,756	3,437,266	4,455,022
Balance as of December 31, 2015			
Net income	-	321,324	321,324
Change in net unrealized capital losses	-	(25,269)	(25,269)
Change in net deferred income tax	-	(313,695)	(313,695)
Change in non-admitted assets	-	477,598	477,598
Change in asset valuation reserve	-	(7,796)	(7,796)
	1,017,756	3,889,428	4,907,184
Balance as of December 31, 2016	\$ 1,017,756	\$ 3,889,428	\$ 4,907,184

The accompanying notes are an integral part of these statements.

Universal Fidelity Life Insurance Company

STATEMENTS OF CASH FLOWS - STATUTORY BASIS

Years ended December 31

	<u>2016</u>	<u>2015</u>
Cash from operating activities		
Premiums and other insurance income received	\$ 9,474,979	\$ 9,862,173
Investment income received, less investment expenses paid	231,363	233,058
Miscellaneous income received	6,909,476	6,470,688
Life, annuity, and accident and health benefits paid	(6,444,473)	(6,504,408)
Commissions and other expenses and taxes paid	(9,911,291)	(10,513,735)
Federal income taxes paid	-	26,508
Commissions and expense allowances on reinsurance ceded	<u>575,526</u>	<u>508,132</u>
Net cash provided by operating activities	835,580	82,416
Cash from investments		
Proceeds from investments matured and sold		
Bonds	2,029,241	1,835,405
Common stock	20,400	203,375
Preferred stock	-	512,294
Other invested assets	<u>9,561</u>	<u>43,029</u>
	2,059,202	2,594,103
Cost of investments acquired		
Bonds	(50,146)	(946,151)
Common stock	-	(34,267)
Preferred stock	(355,496)	(288,905)
Miscellaneous applications	<u>-</u>	<u>(52,229)</u>
	(405,642)	(1,321,552)
Policy loans - net	<u>4,175</u>	<u>15,786</u>
Net cash provided by investing activities	1,657,735	1,288,337
Cash from financing and miscellaneous sources		
Cash provided (applied)		
Repayment on note payable to Federal Home Loan Bank	(365,183)	(1,095,000)
Other cash provided (applied)	<u>215,815</u>	<u>(398)</u>
Net cash used in financing and miscellaneous sources	<u>(149,368)</u>	<u>(1,095,398)</u>
Net increase in cash and short-term investments	2,343,947	275,355
Cash and short-term investments at beginning of year	<u>1,390,930</u>	<u>1,115,575</u>
Cash and short-term investments at end of year	<u>\$ 3,734,877</u>	<u>\$ 1,390,930</u>

The accompanying notes are an integral part of these statements.

Universal Fidelity Life Insurance Company

NOTES TO FINANCIAL STATEMENTS - STATUTORY BASIS

December 31, 2016 and 2015

NOTE A - ORGANIZATION AND ACCOUNTING POLICIES

A summary of the significant accounting policies consistently applied in the preparation of the accompanying financial statements follows:

1. *Organization*

Universal Fidelity Life Insurance Company (the Company) is domiciled in Oklahoma. The Company is authorized to conduct business in Arizona, Arkansas, Mississippi, Nebraska, New Mexico, Oklahoma, and Texas. Its business consists of selling life, annuity, and accident and health insurance, along with providing administrative services to various insurers.

2. *Basis of Presentation*

The Company presents its financial statements in accordance with Statutory Accounting Principles (SAP) prescribed or permitted by the Oklahoma Insurance Department (the Department). The Department has adopted as a component of prescribed or permitted practices the National Association of Insurance Commissioners' (NAIC) *Accounting Practices and Procedures* manual, without modification. These principles and practices differ from accounting principles generally accepted in the United States of America (GAAP).

The more significant differences between statutory accounting practices and GAAP are as follows:

For statutory purposes, investments in bonds are reported at amortized cost or, in certain instances, market value based on their NAIC rating. For GAAP, such fixed maturity investments are designated at purchase as held-to-maturity, trading, or available-for-sale. Fixed maturity investments designated as held-to-maturity are reported at amortized cost, and the remaining fixed maturity investments are reported at fair value with unrealized holding gains and losses reported in operations for those designated as trading and as a separate component of capital and surplus for those designated as available-for-sale.

For statutory purposes, all single class and multi-class mortgage-backed/asset-backed securities (e.g., CMOs) are adjusted for the effects of changes in prepayment assumptions on the related accretion of discount or amortization of premium of such securities using either the retrospective or prospective methods. For GAAP purposes, all securities, purchased or retained, that represent beneficial interests in securitized assets (e.g., CMO, CBO, CDO, CLO, MBS, and ABS securities), other than high credit quality securities, are adjusted using the prospective method when there is a change in estimated future cash flows. If high credit quality securities are adjusted, the retrospective method is used.

Universal Fidelity Life Insurance Company

NOTES TO FINANCIAL STATEMENTS - STATUTORY BASIS - CONTINUED

December 31, 2016 and 2015

NOTE A - ORGANIZATION AND ACCOUNTING POLICIES - Continued

2. *Basis of Presentation - Continued*

Investments in wholly owned noninsurance subsidiaries are reported using the equity method, adjusted to a statutory reporting basis. Further, subsidiaries that are not audited are non-admitted under SAP. Under GAAP, such subsidiaries would be consolidated.

Preferred stock is reported at cost or amortized cost, and in certain instances, market value based on its NAIC rating. For GAAP purposes, preferred stock would be stated at fair value.

Deferred tax assets are limited to an amount determined utilizing a three-component admissibility calculation. The remaining deferred tax assets are non-admitted. In addition, the changes in deferred taxes are reported as a direct charge or credit to capital and surplus. In accordance with GAAP, a deferred tax asset is recorded for the amount of gross deferred tax assets expected to be realized in future years, and a valuation allowance is established for deferred tax assets not realizable. Further, changes in deferred taxes are reported as income tax expense or benefit, or as a component of other comprehensive income, depending on the nature of the tax characteristics of temporary differences.

Under a formula prescribed by the NAIC, the Company defers in the Interest Maintenance Reserve (IMR) the portion of realized capital gains and losses on sales of fixed income investments, principally bonds, attributable to changes in the general level of interest rates and amortizes those deferrals over the remaining period to maturity. For statutory purposes, realized capital gains and losses are reported in income net of transfers to the IMR. Under GAAP, realized capital gains and losses would be reported in the statement of operations in the period that the asset giving rise to the gain or loss is sold.

For statutory purposes, declines in the estimated realizable value of investments are provided for through the establishment of a NAIC prescribed, formula-determined statutory Asset Valuation Reserve (AVR), with changes charged directly to surplus. For GAAP, declines in value are recognized in the statement of operations solely when such declines are judged to be other than temporary.

Certain assets designated as "non-admitted" have been charged directly to surplus for statutory purposes rather than being reported as assets for GAAP. Included as non-admitted assets are investments in affiliated common stock, prepaid expenses, certain receivables, certain deferred tax assets and other items that do not meet statutory criteria for admitted assets.

Universal Fidelity Life Insurance Company

NOTES TO FINANCIAL STATEMENTS - STATUTORY BASIS - CONTINUED

December 31, 2016 and 2015

NOTE A - ORGANIZATION AND ACCOUNTING POLICIES - Continued

2. *Basis of Presentation - Continued*

Reserves on traditional life and accident and health insurance products for statutory purposes are based on statutory mortality and morbidity rates and interest which may differ from GAAP reserves based on reasonable assumptions of expected mortality, morbidity, interest and withdrawals which include a provision for possible adverse deviation from such assumptions.

Reinsurance amounts are netted against the corresponding receivable or payable balances for statutory purposes rather than shown as gross amounts on the GAAP balance sheets.

The costs of acquiring and renewing business are charged to current operations as incurred for statutory purposes, rather than being deferred and amortized over the premium-paying period or in proportion to the present value of expected gross profit margins for GAAP.

Policyholder dividends are recognized in full when declared for statutory purposes rather than over the term of the related policies under GAAP.

The statements of cash flows do not include a reconciliation of net income to net cash from operations as would be included under GAAP.

The effects of the foregoing variances from GAAP on the accompanying statutory-basis financial statements have not been determined, but are presumed to be material.

3. *Use of Estimates*

The preparation of financial statements in conformity with SAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities. It also requires disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

4. *Cash and Short-Term Investments*

In connection with the preparation of the statutory statements of cash flow, the Company considers all highly liquid investments with a maturity of one year or less when purchased and certain money market mutual funds to be short-term investments. These investments have been valued in the same manner as similar long-term investments.

Universal Fidelity Life Insurance Company

NOTES TO FINANCIAL STATEMENTS - STATUTORY BASIS - CONTINUED

December 31, 2016 and 2015

NOTE A - ORGANIZATION AND ACCOUNTING POLICIES - Continued

5. *Investments*

Securities are valued in accordance with methods prescribed by the NAIC. Investments in bonds and mortgage and other asset-backed securities are reported principally at cost (unpaid principal balance), adjusted for amortization of premiums and accrual of discounts. Bonds are generally carried at amortized cost using the scientific method. Bonds assigned with an NAIC designation of 6 are carried at the lower of amortized cost or fair value. The Company reviews its prepayment assumptions on mortgage and other asset-backed securities periodically and adjusts amortization rates retrospectively when such assumptions are materially changed due to experience and/or expected future patterns. The Company's prepayment assumptions are determined from available market data and the Company's investment manager.

Unaffiliated common stocks are reported at fair value, as determined by the Securities Valuation Office (SVO) of the NAIC. Investments in common stock of affiliated subsidiaries are reported using the equity method. Subsidiaries that are not audited are non-admitted for SAP. The Company has non-admitted its wholly owned subsidiaries with a value of \$ 19,811 and \$ 56,462 at December 31, 2016 and 2015, respectively.

Preferred stocks are generally carried at cost with the exception of securities assigned with an NAIC designation of 4 - 6, which are carried at the lower of cost or fair value.

Policy loans are recorded at unpaid principal balance. These loans are secured by the death benefits provided under the life insurance contracts.

Investments in real estate, including properties occupied by the Company, are reported at cost less allowances for depreciation.

Investments in limited partnerships are recorded at a value based on the underlying audited GAAP equity of the partnership. The original initial investment recorded at cost is adjusted for subsequent capital contributions, distributions received and the Company's share of the audited GAAP basis earnings or losses of the partnership after the date of acquisition. The undistributed earnings or losses of the partnership are recorded as unrealized gains and losses directly to capital and surplus.

Universal Fidelity Life Insurance Company

NOTES TO FINANCIAL STATEMENTS - STATUTORY BASIS - CONTINUED

December 31, 2016 and 2015

NOTE A - ORGANIZATION AND ACCOUNTING POLICIES - Continued

5. *Investments - Continued*

The Asset Valuation Reserve (AVR) provides a reserve for losses from investments in bonds, preferred and common stocks, real estate, and other invested assets, with related increases or decreases being recorded directly to surplus. The Interest Maintenance Reserve (IMR) provides a reserve for realized capital gains and losses that result from changes in interest rates for certain fixed income securities and amortizes these capital gains and losses into income over the remaining life of the investments sold.

Realized capital gains and losses on investments are determined on the basis of specific identification of investments. Unrealized capital gains and losses on investments carried at fair value are recorded directly in unassigned surplus, with a comparable adjustment made to the AVR. The carrying amounts of all investments are reviewed on an ongoing basis for credit deterioration. If this review indicates a decline in market value that is other-than-temporary, the carrying amount of the investment is reduced to its estimated fair value, and a specific write down is taken. Such reductions in the carrying amounts are recognized as realized capital losses on investments.

Interest income is recognized on an accrual basis. The Company does not accrue interest on bonds in default. Further, income is not accrued when collection is uncertain. At December 31, 2016 and 2015, no amounts were excluded from investment income due or accrued with respect to this policy.

6. *Depreciation and Amortization*

Owned real estate is depreciated on a straight-line basis over the estimated useful lives of the property. Data processing equipment owned by the Company is carried at cost, less accumulated depreciation computed on a straight-line basis, over the estimated useful life of the equipment. The cost of furniture and fixtures, less accumulated depreciation is computed on a straight-line method (3 to 7 years).

7. *Non-Admitted Assets*

Non-admitted assets (principally affiliated common stock, agent balances, deferred taxes, prepaid expenses and certain affiliate receivables) are excluded from the statements of admitted assets, liabilities and surplus. Changes in non-admitted assets are reported as charges or credits directly to surplus.

Universal Fidelity Life Insurance Company

NOTES TO FINANCIAL STATEMENTS - STATUTORY BASIS - CONTINUED

December 31, 2016 and 2015

NOTE A - ORGANIZATION AND ACCOUNTING POLICIES - Continued

8. *Reserves*

The reserves for life contracts, all developed by actuarial methods, are established and maintained on the basis of published mortality and morbidity tables using assumed interest rates and valuation methods that will provide, in the aggregate, reserves that are greater than the minimum valuation required by law or guaranteed policy cash values. Tabular interest, tabular less actual reserves released, and tabular cost have been determined by NAIC formula. Tabular interest on funds not involving life contingencies is the weighted average interest rate using the reserves at the beginning and ending of the year.

The Company waives deduction of deferred fractional premiums upon death of the insured and the Company returns the unearned portion of the final premium for periods beyond the date of death. Surrender values are not promised in excess of the legally computed reserves.

Additional premiums are charged for policies issued on substandard lives according to underwriting classification. If the extra premium is a permanent addition to the standard premium, the corresponding reserves held on such policies are calculated using the same interest rate as standard policies but employing mortality rates, which are multiples of standard mortality. If the extra premium is only a temporary addition to the standard premium, an additional reserve equal to one-half the extra premium charge for the year is added to the reserve calculated using standard mortality and interest assumptions. At December 31, 2016 and 2015, the Company had no insurance in force for which the gross premiums are less than the net premiums according to the standards of valuation set by the State of Oklahoma.

Policy reserves for accident and health insurance include claim reserves and unearned premium reserves. Claim reserves, including incurred but not reported claims, represent management's estimate of the ultimate liability associated with unpaid policy claims, based upon analysis of past experience. To the extent that the ultimate liability differs from the amounts recorded, such differences are reflected in operations when additional information becomes known.

Unearned premium reserves of Medicare supplement policies are determined using the daily pro rata method. Student accident policies consist of risks associated with football activities and non-football activities. Unearned premium reserves associated with football activities are determined on a monthly basis from August through December. Unearned premium reserves on non-football activities are determined on a monthly basis from August to July.

Universal Fidelity Life Insurance Company

NOTES TO FINANCIAL STATEMENTS - STATUTORY BASIS - CONTINUED

December 31, 2016 and 2015

NOTE A - ORGANIZATION AND ACCOUNTING POLICIES - Continued

9. *Revenue Recognition and Acquisition Costs*

Premium income for contracts with mortality and morbidity risks is recorded when received, adjusted for advance premiums and premiums deferred and uncollected. Accident and health premiums are earned when received. Acquisition costs, such as commissions and other costs related to acquiring new business are charged to current operations as incurred.

10. *Policyholder Dividends*

The amount of dividends paid to policyholders is determined annually by the Company's Board of Directors. The aggregate amount of policyholders' dividends is related to actual interest, mortality, morbidity, and expense experience for the year and judgment as to the appropriate level of statutory surplus to be retained by the Company.

11. *Income Taxes*

Deferred income taxes are recorded based on temporary differences using a balance sheet approach whereby statutory and tax basis balance sheets are compared.

Deferred tax assets are limited based on a three-component admissibility calculation. Under the first part of the admissibility calculation, deferred tax assets are admitted up to the amount of federal income tax paid in prior years that can be recovered through loss carry backs for existing temporary differences that reverse in a time frame not to exceed three years. Under the second part of the admissibility calculation, deferred tax admissibility is based on the pattern and timing of reversals of temporary differences subject to a ratio of current period adjusted capital and surplus and Authorized Control Level risk-based capital. Under the third part of the admissibility calculation, deferred tax admissibility is based on any remaining deferred tax assets set equal to any deferred tax liabilities. The remaining deferred tax assets are non-admitted.

Universal Fidelity Life Insurance Company

NOTES TO FINANCIAL STATEMENTS - STATUTORY BASIS - CONTINUED

December 31, 2016 and 2015

NOTE A - ORGANIZATION AND ACCOUNTING POLICIES - Continued

12. Subsequent Events

Management has evaluated subsequent events for recognition and disclosure in the financial statements through May 19, 2017, which is the date the financial statements were available to be issued. On April 14, 2017, as approved by the Oklahoma Insurance Department, the Company and Mr. Brent Haggard closed on a transaction to purchase all of Mr. Steve Hague's ownership in the Company. The Company purchased 212,032 of Mr. Hague's 339,252 shares at a cost of \$ 1,250,000. The remainder of the shares were acquired by Mr. Haggard. Concurrently with closing, Mr. Hague resigned from his position as a member of the Board of Directors of the Company.

13. Accounting Changes

The NAIC revised Statement of Statutory Accounting Principles ("SSAP") No. 1, *Disclosure of Accounting Policies, Risks, & Uncertainties, and Other Disclosures*. This pronouncement is effective December 31, 2016 and thereafter. The revision requires management to evaluate and disclose whether substantial doubt exists about an entity's ability to continue as a going concern. This guidance is not expected to affect the Company's results of operations, financial position or liquidity.

Universal Fidelity Life Insurance Company

NOTES TO FINANCIAL STATEMENTS - STATUTORY BASIS - CONTINUED

December 31, 2016 and 2015

NOTE B - INVESTMENTS

At December 31, the carrying value and estimated market values of the Company's portfolio of bonds are as follows:

<u>2016</u>	Cost/ Amortized Cost	Gross Unrealized		Fair Value
		Gains	Losses	
Bonds				
U.S. government	\$ 653,245	\$ 727	\$ (3,794)	\$ 650,178
U.S. government agencies	597,606	-	(6,984)	590,622
Mortgage-backed securities	106,582	24,790	-	131,372
Industrial and miscellaneous	<u>1,294,398</u>	<u>80,258</u>	<u>(15,979)</u>	<u>1,358,677</u>
Total bonds	<u>\$ 2,651,831</u>	<u>\$ 105,775</u>	<u>\$ (26,757)</u>	<u>\$ 2,730,849</u>
Preferred stocks	<u>\$ 1,049,308</u>	<u>\$ 5,303</u>	<u>\$ (45,868)</u>	<u>\$ 1,008,743</u>
Common stocks	<u>\$ 64,500</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 64,500</u>
Other invested assets				
Partnership interest	<u>\$ 15,315</u>	<u>\$ -</u>	<u>\$ (4,352)</u>	<u>\$ 10,963</u>
<u>2015</u>				
Bonds				
U.S. government	\$ 652,698	\$ 504	\$ (6,125)	\$ 647,077
U.S. government agencies	2,597,434	-	(54,450)	2,542,984
Mortgage-backed securities	130,673	32,923	-	163,596
Industrial and miscellaneous	<u>1,247,948</u>	<u>82,111</u>	<u>(31,851)</u>	<u>1,298,208</u>
Total bonds	<u>\$ 4,628,753</u>	<u>\$ 115,538</u>	<u>\$ (92,426)</u>	<u>\$ 4,651,865</u>
Preferred stocks	<u>\$ 693,812</u>	<u>\$ 199</u>	<u>\$ (20,711)</u>	<u>\$ 673,300</u>
Common stocks	<u>\$ 73,529</u>	<u>\$ 8,571</u>	<u>\$ -</u>	<u>\$ 82,100</u>
Other invested assets				
Partnership interest	<u>\$ 50,808</u>	<u>\$ -</u>	<u>\$ (31,074)</u>	<u>\$ 19,734</u>

Universal Fidelity Life Insurance Company

NOTES TO FINANCIAL STATEMENTS - STATUTORY BASIS - CONTINUED

December 31, 2016 and 2015

NOTE B - INVESTMENTS - Continued

The following investments have been in a continuous loss position for less than twelve months at December 31:

	2016		2015	
	<u>Fair Value</u>	<u>Unrealized Loss</u>	<u>Fair Value</u>	<u>Unrealized Loss</u>
U.S. government	\$ -	\$ -	\$ 541,421	\$ (6,125)
U.S. government agencies	-	-	596,304	(1,130)
Industrial and miscellaneous	<u>108,204</u>	<u>(2,074)</u>	<u>263,045</u>	<u>(31,851)</u>
Total bonds	<u>\$ 108,204</u>	<u>\$ (2,074)</u>	<u>\$ 1,400,770</u>	<u>\$ (39,106)</u>
Preferred stocks	\$ 484,675	\$ (23,353)	\$ 48,080	\$ (1,339)

The following investments have been in a continuous loss position for more than twelve months at December 31:

	2016		2015	
	<u>Fair Value</u>	<u>Unrealized Loss</u>	<u>Fair Value</u>	<u>Unrealized Loss</u>
U.S. government	\$ 544,345	\$ (3,794)	\$ -	\$ -
U.S. government agencies	590,622	(6,984)	1,946,680	(53,320)
Industrial and miscellaneous	<u>161,095</u>	<u>(13,905)</u>	<u>-</u>	<u>-</u>
Total bonds	<u>\$ 1,296,062</u>	<u>\$ (24,683)</u>	<u>\$ 1,946,680</u>	<u>\$ (53,320)</u>
Preferred stocks	\$ 264,800	\$ (22,515)	\$ 470,198	\$ (19,372)
Partnership interests	10,963	(4,352)	19,734	(31,074)

Universal Fidelity Life Insurance Company

NOTES TO FINANCIAL STATEMENTS - STATUTORY BASIS - CONTINUED

December 31, 2016 and 2015

NOTE B - INVESTMENTS - Continued

The Company recorded one impairment for \$ 52,229 during 2015. The Company did not experience any other-than-temporary declines in the value on any investments during 2016. The Company's decision to record an impairment loss is primarily based on whether the Company will recover the entire amortized cost basis of the security. Factors that are considered include the length of time the security's fair value has been below carrying value, the credit worthiness of the issuer, and the coupon and/or dividend payment history of the issuer. The Company also assesses whether it intends to sell or it is more likely than not that it will be required to sell a security before recovery of its amortized cost basis less any current-period credit losses. For securities that are other-than-temporarily impaired, the security is adjusted to fair value and the resulting losses are recognized in realized gains (losses) in the statements of operations.

The carrying amount and fair value of bonds by contractual maturity at December 31, 2016, are shown below. Expected maturities may differ from contractual maturities because certain borrowers have the right to call or prepay obligations with or without call or prepayment penalties.

	<u>Carrying Value</u>	<u>Fair Value</u>
Due in one year or less	\$ 60,034	\$ 60,063
Due after one year through five years	1,123,783	1,159,793
Due after ten years	1,361,432	1,379,621
Mortgage-backed and other asset-backed securities	<u>106,582</u>	<u>131,372</u>
	<u>\$ 2,651,831</u>	<u>\$ 2,730,849</u>

The Company, as a member of the reconstituted Federal Home Loan Bank System administered by the Federal Housing Finance Board, is required to maintain an investment in capital stock of the Federal Home Loan Bank of Topeka (FHLB). The stock is recorded at a cost of \$ 64,500 and \$ 82,100 at December 31, 2016 and 2015, respectively, which approximates its fair value. The FHLB places restrictions on the transferability of the stock, and as a result, transactions occur with the FHLB at the stock's par value.

Universal Fidelity Life Insurance Company

NOTES TO FINANCIAL STATEMENTS - STATUTORY BASIS - CONTINUED

December 31, 2016 and 2015

NOTE B - INVESTMENTS - Continued

The Company's investment in FHLB capital stock is summarized below at December 31:

	<u>2016</u>	<u>2015</u>
Class A (membership stock)	\$ 13,800	\$ 29,400
Class B (activity)	<u>50,700</u>	<u>52,700</u>
Total FHLB capital stock	<u>\$ 64,500</u>	<u>\$ 82,100</u>

Major categories of net investment income for the years ended December 31 are summarized as follows:

	<u>2016</u>	<u>2015</u>
Bonds	\$ 39,059	\$ 93,732
Other bonds	74,308	72,019
Preferred and common stocks (unaffiliated)	48,825	59,307
Preferred and common stocks (affiliated)	55,000	-
Real estate	95,505	95,505
Other	<u>5,431</u>	<u>5,782</u>
	318,128	326,345
Investment expenses	<u>(137,207)</u>	<u>(140,671)</u>
Net investment income	<u>\$ 180,921</u>	<u>\$ 185,674</u>

Universal Fidelity Life Insurance Company

NOTES TO FINANCIAL STATEMENTS - STATUTORY BASIS - CONTINUED

December 31, 2016 and 2015

NOTE B - INVESTMENTS - Continued

The major components of realized capital gains (losses) on investments reflected in operations and unrealized capital gains on investments reflected directly in surplus are summarized as follows as of December 31:

	Realized		Change in Unrealized	
	2016	2015	2016	2015
Bonds	\$ -	\$ 2,071	\$ -	\$ -
Preferred stocks	-	15,000	-	-
Common stocks	-	(59,827)	(33,852)	71,397
Other assets	(7,793)	(6,108)	8,583	37,146
	(7,793)	(48,864)	(25,269)	108,543
Transferred to interest maintenance reserve	-	(18,510)	-	-
Tax on realized gains	-	6,293	-	-
Net realized and unrealized capital gains (losses)	\$ (7,793)	\$ (61,081)	\$ (25,269)	\$ 108,543

Proceeds from the sale and maturity of bonds were \$ 2,029,241 and \$ 1,835,405 in 2016 and 2015, respectively. The Company recognized realized gains from the sale of bonds of \$ 8,397 in 2015. The Company recognized realized losses from the sale of bonds \$ 6,326 in 2015. No gains or losses were recognized on bonds sold or matured in 2016.

Bonds having a carrying value of \$ 1,325,060 and \$ 1,349,233 and a fair value of \$ 1,341,931 and \$ 1,377,951 were on deposit with regulatory authorities in Oklahoma, New Mexico, and Louisiana in accordance with statutory requirements, as of December 31, 2016 and 2015, respectively. As of December 31, 2015, the Company has pledged a security with a carrying value of \$ 1,000,000 to secure a line of credit.

Universal Fidelity Life Insurance Company

NOTES TO FINANCIAL STATEMENTS - STATUTORY BASIS - CONTINUED

December 31, 2016 and 2015

NOTE C - FAIR VALUE MEASUREMENTS

Fair value is defined to be 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. A three-level hierarchy has been established for fair value measurements based upon the inputs to the valuation of an asset or liability as follows:

Level 1 – Valuation is based on quoted prices for identical assets and liabilities in active markets.

Level 2 – Valuation is derived from inputs, other than quoted prices included in Level 1, which are observable for the asset or liability either directly or indirectly. Investments classified as Level 2 are generally valued by benchmarking model-derived prices to quoted market prices and trade data for identical or comparable securities. The significant inputs used in this approach include interest rates, prepayment timing, yield spreads, maturities, credit losses and credit ratings of the securities.

Level 3 – Valuation is derived from unobservable inputs that are not corroborated by market data.

Fair values of common stocks actively traded on an exchange, are based on values published by the SVO, where available. The Company obtains fair values from pricing service companies where values are not provided by the SVO.

The following table presents the Company's fair value hierarchy for those assets measured at fair value on a recurring basis as of December 31:

	<u>Fair Value</u>	<u>Admitted Assets</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
<u>2016</u>					
Common stocks	\$ 64,500	\$ 64,500	\$ -	\$ 64,500	\$ -
<u>2015</u>					
Common stocks	\$ 82,100	\$ 82,100	\$ -	\$ 82,100	\$ -

Universal Fidelity Life Insurance Company

NOTES TO FINANCIAL STATEMENTS - STATUTORY BASIS - CONTINUED

December 31, 2016 and 2015

NOTE D - FAIR VALUES OF FINANCIAL INSTRUMENTS

SSAP Statement No. 100, *Fair Value Measurements*, requires disclosure of fair value information about financial instruments, whether or not recognized in the statement of admitted assets, liabilities and capital and surplus, for which it is practicable to estimate that value. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. In that regard, the derived fair value estimates cannot be substantiated by comparison to independent markets and, in many cases, could not be realized in immediate settlement of the instrument. SSAP Statement No. 100 excludes certain financial instruments and all non-financial instruments from its disclosure requirements. These fair value disclosures are not intended to represent the fair value of the Company.

The following methods and assumptions were used by the Company in estimating its fair value disclosures for financial instruments:

1. *Bonds, Stocks and Other Invested Assets*

Fair values of bonds, preferred stocks, common stocks and other invested assets as presented herein, are based on values published by the SVO, where available. The Company obtains fair values from pricing service companies where values are not provided by the SVO. In instances in which the Company believes fair values provided by pricing services are indicative of distressed prices, the Company applies a market yield to expected future cash flows to determine fair values.

2. *Policy Loans, Cash, Short-Term Investments, and Accrued Investment Income*

Due to the short-term nature of these assets, the carrying amounts approximate their fair values.

3. *Liability For Deposit-Type Contracts*

The fair values for the Company's reserves and liabilities under investment-type insurance contracts (deferred annuity and other contracts that do not involve significant mortality risk) are estimated using surrender values.

Universal Fidelity Life Insurance Company

NOTES TO FINANCIAL STATEMENTS - STATUTORY BASIS - CONTINUED

December 31, 2016 and 2015

NOTE D - FAIR VALUES OF FINANCIAL INSTRUMENTS - Continued

The fair values for the Company's insurance contracts (insurance, annuity, and other policy contracts that involve significant mortality risk), other than investment-type contracts, are not required to be disclosed. However, the fair value of liabilities under all insurance contracts are taken into consideration in the Company's overall management of interest rate risk, such that the Company's exposure to changing interest rates is minimized through the matching of investment maturities with amounts due under insurance contracts. The following sets forth a comparison of the estimated fair values and carrying amounts of the Company's financial instruments at December 31:

	<u>Fair Value</u>	<u>Admitted Assets</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
<u>2016</u>					
Financial assets					
Investments					
Bonds	\$ 2,730,849	\$ 2,651,831	\$ 1,346,676	\$ 1,384,173	\$ -
Preferred stocks	1,008,743	1,049,308	-	1,008,743	-
Common stocks	64,500	64,500	-	64,500	-
Other invested assets	10,963	10,963	-	10,963	-
Policy loans	96,280	96,280	-	96,280	-
Cash and short-term investments	3,734,877	3,734,877	3,734,877	-	-
Accrued investment income	17,302	17,302	-	17,302	-
Financial liabilities					
Deposit-type contracts	6,459	6,459	-	6,459	-

Universal Fidelity Life Insurance Company

NOTES TO FINANCIAL STATEMENTS - STATUTORY BASIS - CONTINUED

December 31, 2016 and 2015

NOTE D - FAIR VALUES OF FINANCIAL INSTRUMENTS - Continued

	<u>Fair Value</u>	<u>Admitted Assets</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
<u>2015</u>					
Financial assets					
Investments					
Bonds	\$ 4,651,865	\$ 4,628,753	\$ 3,321,669	\$ 1,330,196	\$ -
Preferred stocks	673,300	693,812	-	673,300	-
Common stocks	82,100	82,100	-	82,100	-
Other invested assets	19,734	19,734	-	19,734	-
Policy loans	100,455	100,455	-	100,455	-
Cash and short-term investments	1,390,930	1,390,930	1,390,930	-	-
Accrued investment income	32,428	32,428	-	32,428	-
Financial liabilities					
Deposit-type contracts	6,244	6,244	-	6,244	-

NOTE E - REAL ESTATE

Real estate occupied by the Company consists of the following at December 31:

	<u>2016</u>	<u>2015</u>
Buildings	\$ 900,784	\$ 900,784
Less accumulated depreciation	<u>(151,299)</u>	<u>(130,510)</u>
Real estate occupied by Company, net	<u>\$ 749,485</u>	<u>\$ 770,274</u>

The Company recorded depreciation expense of \$ 20,789 during 2016 and 2015.

Universal Fidelity Life Insurance Company

NOTES TO FINANCIAL STATEMENTS - STATUTORY BASIS - CONTINUED

December 31, 2016 and 2015

NOTE E - REAL ESTATE - Continued

Real estate held for the production of income consists of the following at December 31:

	<u>2016</u>	<u>2015</u>
Buildings	\$ 500,000	\$ 500,000
Less accumulated depreciation	<u>(183,333)</u>	<u>(166,667)</u>
Real estate held for the production of income, net	<u>\$ 316,667</u>	<u>\$ 333,333</u>

The Company recorded depreciation expense of \$ 16,666 and \$ 16,667 during 2016 and 2015, respectively.

NOTE F - PREMIUMS DUE AND DEFERRED

A reconciliation of gross premiums, loading, and net premium at December 31 is as follows:

<u>2016</u>	<u>Gross</u>	<u>Loading</u>	<u>Net</u>
Ordinary new business	\$ 115,064	\$ 77,219	\$ 37,845
Ordinary renewal	<u>298,786</u>	<u>38,951</u>	<u>259,835</u>
Totals	<u>\$ 413,850</u>	<u>\$ 116,170</u>	<u>\$ 297,680</u>
<u>2015</u>	<u>Gross</u>	<u>Loading</u>	<u>Net</u>
Ordinary new business	\$ 102,009	\$ 69,664	\$ 32,345
Ordinary renewal	<u>204,609</u>	<u>26,191</u>	<u>178,418</u>
Totals	<u>\$ 306,618</u>	<u>\$ 95,855</u>	<u>\$ 210,763</u>

Universal Fidelity Life Insurance Company

NOTES TO FINANCIAL STATEMENTS - STATUTORY BASIS - CONTINUED

December 31, 2016 and 2015

NOTE G - INCOME TAXES

The Company is taxed for federal income taxes as a life insurance company. The main components of deferred tax amounts at December 31 are as follows:

	<u>Ordinary</u>	<u>Capital</u>	<u>Total</u>
<u>2016</u>			
Total gross deferred tax assets	\$ 666,777	\$ -	\$ 666,777
Total gross deferred tax liabilities	<u>(227,442)</u>	<u>-</u>	<u>(227,442)</u>
Net admitted deferred tax assets	<u>\$ 439,335</u>	<u>\$ -</u>	<u>\$ 439,335</u>
Change in non-admitted deferred tax assets			<u>\$ 298,526</u>
<u>2015</u>			
Total gross deferred tax assets	\$ 842,377	\$ 10,876	\$ 853,253
Total gross deferred tax liabilities	<u>(100,223)</u>	<u>-</u>	<u>(100,223)</u>
Net gross deferred tax assets	742,154	10,876	753,030
Non-admitted deferred tax assets	<u>(287,650)</u>	<u>(10,876)</u>	<u>(298,526)</u>
Net admitted deferred tax assets	<u>\$ 454,504</u>	<u>\$ -</u>	<u>\$ 454,504</u>
Change in non-admitted deferred tax assets			<u>\$ (173,307)</u>

Universal Fidelity Life Insurance Company

NOTES TO FINANCIAL STATEMENTS - STATUTORY BASIS - CONTINUED

December 31, 2016 and 2015

NOTE G - INCOME TAXES - Continued

The net admitted deferred tax asset was determined using the guidance related to admissibility provided in the following paragraphs in SSAP 101 as of December 31:

	<u>Ordinary</u>	<u>Capital</u>	<u>Total</u>
<u>2016</u>			
<u>Admissible under paragraph</u>			
11a. ability to recoup previous taxes paid	\$ 72,276	\$ -	\$ 72,276
11b. lesser of adjusted gross deferred tax assets			
i. Expected to be recognized within three years	453,415	-	453,415
ii. Allowed per limitation threshold of 15% of surplus less deferred tax asset			672,443
11c. adjusted gross deferred tax assets offset against existing deferred tax liabilities	<u>141,086</u>	<u>-</u>	<u>141,086</u>
Total admitted deferred tax asset	<u>\$ 666,777</u>	<u>\$ -</u>	<u>\$ 666,777</u>

<u>2015</u>			
<u>Admissible under paragraph</u>			
11a. ability to recoup previous taxes paid	\$ 454,504	\$ -	\$ 454,504
11b. lesser of adjusted gross deferred tax assets			
i. Expected to be recognized within three years	-	-	-
ii. Allowed per limitation threshold of 15% of surplus less deferred tax asset			593,138
11c. adjusted gross deferred tax assets offset against existing deferred tax liabilities	<u>100,223</u>	<u>-</u>	<u>100,223</u>
Total admitted deferred tax asset	<u>\$ 554,727</u>	<u>\$ -</u>	<u>\$ 554,727</u>

The Company is a risk based capital reporting entity. As a risk based capital reporting entity, the Company utilized the realization threshold limitation table for risk based capital reporting entities to determine its limitation under paragraph 11.b. of SSAP 101.

Universal Fidelity Life Insurance Company

NOTES TO FINANCIAL STATEMENTS - STATUTORY BASIS - CONTINUED

December 31, 2016 and 2015

NOTE G - INCOME TAXES - Continued

At December 31, 2016 and 2015, the Company's adjusted capital, less deferred tax assets, was \$ 4,427,015 and \$ 3,954,252, respectively. The resulting authorized control level risk based capital ratio, excluding deferred tax assets, was 1199% and 1023%, respectively.

The main components of deferred tax amounts as of December 31, are as follows:

	<u>2016</u>	<u>2015</u>	<u>Change</u>
Deferred tax assets (liabilities)			
Deferred acquisition costs	\$ 513,469	\$ 506,063	\$ 7,406
Discount of reserves	109,162	170,883	(61,721)
Deferred and uncollected premium	(124,732)	(97,223)	(27,509)
Other	<u>(58,564)</u>	<u>173,307</u>	<u>(231,871)</u>
Total gross deferred tax assets	439,335	753,030	(313,695)
Non-admitted deferred tax assets	<u>-</u>	<u>(298,526)</u>	<u>298,526</u>
Admitted deferred tax assets	<u>\$ 439,335</u>	<u>\$ 454,504</u>	<u>\$ (15,169)</u>

The Company has no unused operating loss carryforwards available to offset against future taxable income. The Company incurred income tax expense of \$ 8,285, \$ 10,357, and \$ 53,634 in 2016, 2015, and 2014, respectively, which is available for recoupment in the event of future losses.

All of the Company's deferred tax assets are expected to be utilized based on the Company's projected net earnings and historical experience as it relates to the utilization of the above timing differences. Tax planning strategies did not further impact adjusted gross deferred tax assets or net admitted deferred tax assets.

Universal Fidelity Life Insurance Company

NOTES TO FINANCIAL STATEMENTS - STATUTORY BASIS - CONTINUED

December 31, 2016 and 2015

NOTE G - INCOME TAXES - Continued

Current income taxes incurred consist of the following major components:

	<u>2016</u>	<u>2015</u>
Federal income tax expense on operations	\$ 8,285	\$ 28,587
Taxes attributable to capital gains	-	6,293
Prior years adjustment	<u>53,990</u>	<u>(76,057)</u>
Current federal income tax expense (benefit)	<u>\$ 62,275</u>	<u>\$ (41,177)</u>

The Company's income taxes incurred and the change in its deferred tax assets and deferred tax liabilities is different from the result obtained by applying the federal statutory rate to its pretax net income due to the following significant reconciling items:

- the small life insurance company deduction
- the dividends received deduction
- nondeductible expenses
- adjustments made to prior year's tax calculation
- amendments of prior year returns

Effective January 1, 1984, life insurance companies are taxed under the Deficit Reduction Act of 1984 (the 1984 act). Prior to 1984, life insurance companies were taxed under the 1959 Act on the lesser of taxable investment income or gain from operations plus one-half any excess of gain from operations over taxable income. The one-half of the excess of the gain from operations was accumulated in a special memorandum tax account known as the "policyholders' surplus account" (PSA). Accumulations at December 31, 1983, were approximately \$ 1,477,000 for the Company.

Pursuant to the 1984 Act, the PSA was "frozen" at the December 31, 1983 amount, and accordingly, no further additions to the PSA will be made. Should the balance in the PSA exceed a prescribed maximum amount or should distributions to stockholders exceed certain stated maximum amounts, such excess would become subject to income taxes at rates then effective. The Company has paid the appropriate taxes related to the reduction in the PSA.

Universal Fidelity Life Insurance Company

NOTES TO FINANCIAL STATEMENTS - STATUTORY BASIS - CONTINUED

December 31, 2016 and 2015

NOTE H - ELECTRONIC DATA PROCESSING EQUIPMENT AND OTHER EQUIPMENT

The balance of EDP equipment and other equipment as of December 31 is summarized as follows:

	<u>2016</u>	<u>2015</u>
EDP equipment	\$ 435,142	\$ 403,762
Furniture and fixtures	70,489	40,513
Less accumulated depreciation	<u>(440,570)</u>	<u>(396,640)</u>
Admitted EDP equipment and software, net	<u>\$ 65,061</u>	<u>\$ 47,635</u>

Depreciation expense was \$ 43,930 and \$ 54,213 during 2016 and 2015, respectively.

NOTE I - LIABILITY FOR UNPAID ACCIDENT AND HEALTH CLAIMS

Changes in the balances of the total liability for unpaid accident and health claims at December 31 were as follows:

	<u>2016</u>	<u>2015</u>
Liability for claims, beginning of year	\$ 1,418,514	\$ 1,738,014
Incurred claims related to		
Current year claims	6,376,765	5,301,634
Prior years' claims	<u>(91,000)</u>	<u>230,000</u>
Total incurred claims	6,285,765	5,531,634
Paid claims related to		
Current year claims	4,809,956	4,280,458
Prior years' claims	<u>1,324,638</u>	<u>1,570,676</u>
Total paid claims	<u>6,134,594</u>	<u>5,851,134</u>
Liability for claims, end of year	<u>\$ 1,569,685</u>	<u>\$ 1,418,514</u>

Universal Fidelity Life Insurance Company

NOTES TO FINANCIAL STATEMENTS - STATUTORY BASIS - CONTINUED

December 31, 2016 and 2015

NOTE I - LIABILITY FOR UNPAID ACCIDENT AND HEALTH CLAIMS - Continued

As a result of changes in estimates of insured events in prior years, the provision for policy and accident claims liability decreased by \$ 91,000 in 2016, due to favorable development on case-basis reserves and less than anticipated incurred but not reported claims and increased by \$ 230,000 in 2015 due to unfavorable development on case-basis reserves.

NOTE J - BORROWED FUNDS

The Company entered into a line of credit with the FHLB during 2009. At December 31, 2015, the outstanding balance was \$ 365,183, which was secured by securities with a carrying value of \$ 1,000,000 and fair value of \$ 964,660 as of December 31, 2015. The line of credit bears variable interest, which is repriced daily based on FHLB's cost of funds (0.48 percent at December 31, 2015). The line of credit matured in 2016.

NOTE K - CAPITAL AND SURPLUS

The Company has 500,000 shares of preferred stock authorized with no preferred shares issued. The preferred stock has a par value of \$ 1.00 per share.

The Company is required to maintain minimum surplus levels established by the Department. The Company is also subject to risk-based capital (RBC) requirements promulgated by the NAIC and adopted by the Department. The RBC standards establish uniform minimum capital requirements for insurance companies. The RBC formula applies various weighting factors to financial balances or various levels of activities based on the perceived degree of risk. As of December 31, 2016, the Company's surplus significantly exceeded the minimum levels required by the Department and RBC standards.

Dividends on Company stock are paid as declared by the Board of Directors. The Company may not pay dividends except from available surplus funds derived from realized net profits. In addition, the payment of an extra ordinary dividend whose fair market value, together with that of other dividends or distributions made within the preceding 12 months, exceeds the greater of 10 percent of the Company's surplus as of the preceding December 31 or the net income, excluding capital gains, for the 12-month period ended the preceding December 31, requires approval of the Oklahoma Insurance Commissioner.

Universal Fidelity Life Insurance Company

NOTES TO FINANCIAL STATEMENTS - STATUTORY BASIS - CONTINUED

December 31, 2016 and 2015

NOTE L - POST RETIREMENT BENEFIT PLANS

On December 31, 2001, the Company implemented a trustee profit sharing plan covering substantially all of its full-time employees. Employees become eligible to participate after one year of continuous service and attaining the age of 21. In 2005, the Company revised the plan to make all contributions by the Company discretionary. The Company did not make contributions in 2016. The Company contributed \$ 12,477 to the plan in 2015. The plan contains a 401(k) feature, which provides for voluntary employee contributions of up to 15 percent of qualifying wages.

NOTE M - REINSURANCE

The Company utilizes various reinsurance agreements to reduce its exposure to large losses in all aspects of its insurance business. Such reinsurance permits recovery of a portion of losses from reinsurers, although it does not discharge the primary liability of the Company as direct insurer of the risks reinsured. The Company evaluates the financial strength of potential reinsurers and continually monitors the financial condition of reinsurers.

The effect of reinsurance on premiums written and earned for December 31 are as follows:

	<u>2016</u>		<u>2015</u>	
	<u>Written</u>	<u>Earned</u>	<u>Written</u>	<u>Earned</u>
Direct	\$ 8,720,404	\$ 8,859,106	\$ 10,152,825	\$ 9,974,777
Assumed	4,708,362	4,786,391	4,513,741	4,596,817
Ceded	<u>(3,952,864)</u>	<u>(3,960,569)</u>	<u>(4,840,002)</u>	<u>(4,812,639)</u>
Net premium	<u>\$ 9,475,902</u>	<u>\$ 9,684,928</u>	<u>\$ 9,826,564</u>	<u>\$ 9,758,955</u>

The effect of reinsurance on benefits to policyholders for December 31 are as follows:

	<u>2016</u>	<u>2015</u>
Direct	\$ 8,554,472	\$ 9,524,607
Assumed	2,776,570	2,069,737
Ceded	<u>(4,736,331)</u>	<u>(5,433,656)</u>
Net	<u>\$ 6,594,711</u>	<u>\$ 6,160,688</u>

Universal Fidelity Life Insurance Company

NOTES TO FINANCIAL STATEMENTS - STATUTORY BASIS - CONTINUED

December 31, 2016 and 2015

NOTE N - CONCENTRATIONS

The Company maintains its cash and bank deposit accounts in various financial institutions which, at times, may exceed federally insured limits. The Company has not experienced any losses in such accounts and believes it is not exposed to any significant credit risk on such accounts.

Revenues are concentrated in the life and accident and health insurance industry, which is highly competitive. Significant changes in the industry, regulatory requirements, customer requirements, or the emergence of competitive products could adversely affect operating results. During the years ended December 31, 2016 and 2015, revenue and receivables by customers with more than 10 percent of income or accounts receivable balances were as follows:

	<u>2016</u>		<u>2015</u>	
	<u>Revenue</u>	<u>Receivable</u>	<u>Revenue</u>	<u>Receivable</u>
LifeShield National Insurance	\$ 2,665,209	\$ 370,323	\$ 2,093,410	\$ 451,159
Unified Life Insurance Co.	<u>4,918,278</u>	<u>3,162,177</u>	<u>5,312,449</u>	<u>3,550,091</u>
Total	<u>\$ 7,583,487</u>	<u>\$ 3,532,500</u>	<u>\$ 7,405,859</u>	<u>\$ 4,001,250</u>

The Company performs third party administration work for several companies. Revenue from two customers was 21% and 20% of total income as of December 31, 2016 and 2015, respectively.

NOTE O - LEASES

The Company has operating leases for equipment. Lease expense was \$ 17,973 and \$ 17,726 for the years ended December 31, 2016 and 2015, respectively. As of December 31, 2016, the minimum aggregate rental commitments are as follows for the three succeeding years:

2017	\$ 7,620
2018	7,620
2019	2,443

Universal Fidelity Life Insurance Company

NOTES TO FINANCIAL STATEMENTS - STATUTORY BASIS - CONTINUED

December 31, 2016 and 2015

NOTE P - RELATED PARTY TRANSACTIONS

The Company is the parent company of Universal Fidelity Administrators Corp. (UFAC), a wholly owned subsidiary. During the years ended December 31, 2016 and 2015, the Company received \$ 359,965 and \$ 397,752 for the processing of ERISA benefit plan administration in accordance with an administrative services agreement with UFAC. The Company received a \$ 55,000 dividend from UFAC during the year ended December 31, 2016.

As of December 31, 2016, the Company had a receivable of \$ 599 from affiliated entities and a payable of \$ 13,247 to affiliated entities. As of December 31, 2015, the Company had a receivable of \$ 47,673 from affiliated entities and owed \$ 36,279 to affiliated entities.

On April 16, 2015, an entity owned by two stockholders executed a promissory note with a credit limit of \$ 200,000 from the Company. The note matured on May 15, 2016, with interest at 5 percent. At December 31, 2015, the balance was \$ 76,887 and this balance was not admitted in accordance with SAP and has been excluded from these statements. During the year ended December 31, 2016, this entity also reimbursed the Company \$ 306,770 for the salaries of two employees who perform work for the Company and the entity owned by two stockholders.

NOTE Q - PARTICIPATING POLICIES

At December 31, 2016 and 2015, the Company had 3 percent of its policies participating. The Company pays dividends to eligible participating policies under a dividend formula approved by the Company. Dividends vary by age and duration. The total annual policy dividend is the unit dividend for the issue age and duration times the number of units in force. The amount of policyholder dividends was \$ 1,772 and \$ 1,616 for 2016 and 2015, respectively.

OTHER FINANCIAL INFORMATION



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Independent Auditors' Report on Other Financial Information

The Board of Directors
Universal Fidelity Life Insurance Company

We have audited the statutory basis financial statements of Universal Fidelity Life Insurance Company as of and for the year ended December 31, 2016, and our report thereon dated May 19, 2017, which expressed an unmodified opinion on those statutory basis financial statements, appears on pages 3 and 4. Our audit was performed for the purpose of forming an opinion on the statutory basis financial statements as a whole. As explained in the sixth paragraph of our auditors' report on the statutory basis financial statements, these statutory basis financial statements do not purport to be presented in conformity with accounting principles generally accepted in the United States of America. The accompanying supplemental schedules of selected statutory basis financial data, investment risks interrogatories and summary investment schedule are presented to comply with the National Association of Insurance Commissioners' *Annual Statement Instructions and Accounting Practices and Procedures Manual* and are not a required part of the statutory basis financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the statutory basis financial statements. The information has been subjected to the auditing procedures applied in the audit of the statutory basis financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the statutory basis financial statements or to the statutory basis financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the statutory basis financial statements as a whole.

A handwritten signature in black ink, reading "Kerber, Eck & Braeckel LLP". The signature is written in a cursive, flowing style.

Springfield, Illinois
May 19, 2017

Other Locations

Belleville, IL • Carbondale, IL • Columbia, IL • Harrisburg, IL • Litchfield, IL • Cape Girardeau, MO • St. Louis, MO • Milwaukee, WI

Universal Fidelity Life Insurance Company

SCHEDULE OF SELECTED STATUTORY
BASIS FINANCIAL DATA

December 31, 2016

Investment income earned	
U. S. Government bonds	\$ 39,059
Other bonds (unaffiliated)	74,308
Bonds of affiliates	-
Preferred stocks (unaffiliated)	48,448
Preferred stocks of affiliates	-
Common stocks (unaffiliated)	377
Common stocks of affiliates	55,000
Mortgage loans on real estate	-
Real estate	95,505
Contract loans	3,175
Cash and short-term investments	685
Other invested assets	-
Derivative instruments	-
Aggregate write-ins for investment income	<u>1,571</u>
Total gross investment income	<u>\$ 318,128</u>
Real estate owned, at book value less encumbrances	\$ 1,066,152
Mortgage loans on real estate by collateral classification, at book value	
Farm mortgages	\$ -
Residential mortgages	-
Commercial mortgages	-
Total mortgage loans on real estate	<u>\$ -</u>
Mortgage loans on real estate by standing, at book value	
Good standing	\$ -
Good standing with restructured terms	-
Interest overdue more than ninety days, not in foreclosure	-
Foreclosure in process	-
Total mortgage loans on real estate	<u>\$ -</u>
Other long-term assets, at statement value	\$ 10,963
Collateral loans	\$ -

Universal Fidelity Life Insurance Company

SCHEDULE OF SELECTED STATUTORY
BASIS FINANCIAL DATA - CONTINUED

December 31, 2016

Bonds and stocks of parents, subsidiaries and affiliates, at book value	
Bonds	\$ -
Preferred stocks	-
Common stocks	-
	<hr/>
Total bonds and stocks of parents, subsidiaries and affiliates	<u>\$ -</u>
Bonds and short-term investments by maturity, at statement value	
Due within one year or less	\$ 246,964
Over 1 year through 5 years	1,123,783
Over 5 years through 10 years	-
Over 10 years through 20 years	736,560
Over 20 years	731,454
	<hr/>
Total bonds and short-term investments	<u>\$ 2,838,761</u>
Bonds and short-term investments by class, at statement value	
Class 1	\$ 2,065,490
Class 2	638,613
Class 3	134,658
Class 4	-
Class 5	-
Class 6	-
	<hr/>
Total bonds and short-term investments	<u>\$ 2,838,761</u>
Bonds and short-term investments by trading category, at statement value	
Total bonds publicly traded	\$ 2,838,761
Total bonds privately placed	-
	<hr/>
Total bonds and short-term investments	<u>\$ 2,838,761</u>
Preferred stocks, at statement value	\$ 1,049,308
Common stocks, at market value	64,500
Short-term investments, at book value	186,930
Options, caps and floors owned, at statement value	-
Options, caps and floors written and in force, at statement value	-
Collars, swap and forward agreements open, at statement value	-
Futures contracts open, at current value	-
Cash on deposit	3,547,947

Universal Fidelity Life Insurance Company

SCHEDULE OF SELECTED STATUTORY
BASIS FINANCIAL DATA - CONTINUED

December 31, 2016

Life insurance in force	
Ordinary (\$ 33,645,000 less reinsurance ceded of \$ 16,108,000)	\$ 17,537,000
Amount of accidental death insurance in force under ordinary policies	1,903,000
Supplementary contracts in force	
Ordinary, not involving life contingencies	
Amount on deposit	-
Income payable	-
Ordinary, involving life contingencies - income payable	-
Annuities	
Ordinary	
Immediate - income payable	-
Deferred - fully paid (account balance)	-
Deferred - not fully paid (account balance)	-
Accident and health insurance (premiums in force)	
Ordinary	4,323,413
Group	1,164,307
Deposit funds and dividend accumulations (account balance)	
Deposit funds	-
Dividend accumulations	-
Claim payments for the year ended December 31, 2016	
by year in which losses were incurred	
Group accident and health	
2016	1,898,651
Prior	872,293
Other accident and health	
2016	2,911,305
Prior	452,345

Universal Fidelity Life Insurance Company

SCHEDULE OF INVESTMENT RISKS INTERROGATORIES

December 31, 2016

INVESTMENT RISK INTERROGATIVES

1. The Company's total admitted assets as reported on page two of its Annual Statement is \$ 13,229,392.
2. Following are the ten largest exposures to a single issuer/borrower/investment, by investment category, excluding: (i) U.S. government, U.S. government agency securities and those U.S. government money market funds listed in the Appendix to the *SVO Practices and Procedures Manual* as exempt, (ii) property occupied by the Company, and (iii) policy loans:

<u>Investment Category/Issuer</u>	<u>Amount</u>	<u>Percentage of Total Admitted Assets</u>
a. Investment Real Estate	\$ 316,667	2.39%
b. Dominion Resources	149,419	1.13
c. Indexplus	126,207	.95
d. MetLife Inc.	110,278	.83
e. Stanley Black & Decker	107,686	.81
f. Charles Schwab	107,160	.81
g. Wells Fargo & Company	103,634	.78
h. Assured Guaranty	103,255	.78
i. Prudential Financial Inc.	103,228	.78
j. Morgan Stanley	101,067	.76

3. The Company's total admitted assets held in bonds and preferred stock by NAIC rating:

<u>Bonds</u>	<u>Amount</u>	<u>Percentage of Total Admitted Assets</u>
1	\$ 2,065,490	15.61%
2	638,613	4.83
3	134,658	1.02
4	-	.00
5	-	.00
6	-	.00

Universal Fidelity Life Insurance Company

SCHEDULE OF INVESTMENT RISKS INTERROGATORIES - CONTINUED

December 31, 2016

INVESTMENT RISK INTERROGATIVES - Continued

3. The Company's total admitted assets held in bonds and preferred stock by NAIC rating: -
Continued

<u>Preferred Stocks</u>	<u>Amount</u>	<u>Percentage of Total Admitted Assets</u>
1	\$ -	.00%
2	896,886	6.78
3	152,422	1.15
4	-	.00
5	-	.00
6	-	.00

4. At December 31, 2016, assets held in foreign investments are less than 2.5% of the Company's total admitted assets.

Interrogatories 5 through 10 are not applicable.

11. Assets held in Canadian investments are less than 2.5% of the Company's total admitted assets.
12. Assets held in investments with contractual sales restrictions are less than 2.5% of the Company's total admitted assets.

Universal Fidelity Life Insurance Company

SCHEDULE OF INVESTMENT RISKS INTERROGATORIES - CONTINUED

December 31, 2016

INVESTMENT RISK INTERROGATIVES - Continued

13. Assets held in equity interests are greater than 2.5% of the Company's total admitted assets. Following are the Company's ten largest equity interests:

<u>Issuer</u>	<u>Amount</u>	<u>Percentage of Total Admitted Assets</u>
a. Indexplus	\$ 126,207	.95%
b. Stanley Black & Decker	107,686	.81
c. Wells Fargo & Company	103,634	.78
d. Assured Guaranty	103,255	.78
e. Prudential Financial Inc.	103,228	.78
f. Navient Corporation	99,000	.75
g. United States Cellular STRATS	53,422	.40
h. Affiliated Managers Group	52,329	.40
i. Nextera Energy	51,909	.39
j. AFLAC Inc.	51,607	.39

14. Assets held in nonaffiliated, privately placed equities are less than 2.5% of the Company's total admitted assets.

15. Assets held in general partnership interests are less than 2.5% of the Company's total admitted assets.

Interrogatories 16 through 17 are not applicable.

Universal Fidelity Life Insurance Company

SCHEDULE OF INVESTMENT RISKS INTERROGATORIES - CONTINUED

December 31, 2016

INVESTMENT RISK INTERROGATIVES - Continued

18. Assets held in one parcel or group of contiguous parcels of real estate are less than 2.5% of the Company's total admitted assets.

Interrogatories 19-23 are not applicable.

Universal Fidelity Life Insurance Company

SUMMARY INVESTMENT SCHEDULE

December 31, 2016

<u>Investment Categories</u>	<u>Gross Investment Holdings*</u>		<u>Admitted Assets as Reported in the Annual Statement</u>	
	<u>Amount</u>	<u>Percentage of Total Invested Assets</u>	<u>Amount</u>	<u>Percentage of Total Invested Assets</u>
Bonds				
U.S. Treasury securities	\$ 653,245	7.5 %	\$ 653,245	7.5 %
U.S. government agency obligations (excluding mortgage-backed securities)				
Issued by U.S. government agencies	-	-	-	-
Issued by U.S. government-sponsored agencies	597,606	6.9	597,606	6.9
Foreign government (including Canada, excluding mortgage-backed securities)	-	-	-	-
Securities issued by states, territories, and possessions and their political subdivisions in the U.S.				
State, territories and possessions - general obligations	-	-	-	-
Political subdivisions of states, territories and possessions - general obligations	-	-	-	-
Revenue and assessment obligations	-	-	-	-
Industrial development and similar obligations	-	-	-	-
Mortgage-backed securities (includes residential and commercial MBS)				
Pass-through securities				
Issued or guaranteed by GNMA	-	-	-	-
Issued or guaranteed by FNMA and FHLMC	106,582	1.2	106,582	1.2
All other	-	-	-	-
CMOs and REMICs				
Issued by GNMA, FNMA, FHLMC, or VA	-	-	-	-
Issued by non-US Government issuers and collateralized by mortgage-backed securities	-	-	-	-
All other	-	-	-	-
Other debt and other fixed income securities (excluding short term)				
Unaffiliated domestic securities (includes credit tenant loans rated by the SVO)	1,294,398	14.9	1,294,398	14.9
Unaffiliated foreign securities	-	-	-	-
Affiliated securities	-	-	-	-

Universal Fidelity Life Insurance Company

SUMMARY INVESTMENT SCHEDULE - CONTINUED

December 31, 2016

<u>Investment Categories</u>	<u>Gross Investment Holdings*</u>		<u>Admitted Assets as Reported in the Annual Statement</u>	
	<u>Amount</u>	<u>Percentage of Total Invested Assets</u>	<u>Amount</u>	<u>Percentage of Total Invested Assets</u>
Equity interests				
Investments in mutual funds	\$ -	- %	\$ -	- %
Preferred stocks				
Affiliated	-	-	-	-
Unaffiliated	1,049,308	12.1	1,049,308	12.1
Publicly traded equity securities (excluding preferred stocks)				
Affiliated	-	-	-	-
Unaffiliated	-	-	-	-
Other equity securities				
Affiliated	-	-	-	-
Unaffiliated	64,500	0.7	64,500	0.7
Other equity interests including tangible personal property under lease				
Affiliated	-	-	-	-
Unaffiliated	-	-	-	-
Mortgage loans				
Construction and land development	-	-	-	-
Agricultural	-	-	-	-
Single family residential properties	-	-	-	-
Multifamily residential properties	-	-	-	-
Commercial loans	-	-	-	-
Real estate investments				
Property occupied by company	749,485	8.7	749,485	8.7
Property held for production of income	316,667	3.7	316,667	3.7
Property held for sale	-	-	-	-
Contract loans	96,280	1.1	96,280	1.1
Receivables for securities	-	-	-	-
Cash and short-term investments	3,734,877	43.1	3,734,877	43.1
Other invested assets	10,963	.1	10,963	.1
Total invested assets	<u>\$ 8,673,911</u>	<u>100.0 %</u>	<u>\$ 8,673,911</u>	<u>100.0 %</u>

* Gross investment holding as valued in compliance with *NAIC Accounting Practices and Procedures Manual*.

Universal Fidelity Life Insurance Company

NOTE TO OTHER FINANCIAL INFORMATION

December 31, 2016

NOTE A - BASIS OF PRESENTATION

The accompanying schedules and interrogatories present selected statutory basis financial data as of December 31, 2016, and for the year then ended, for purposes of complying with the Annual Audited Financial Reports in the Annual Audited Report section of the National Association of Insurance Commissioners' *Annual Statement Instructions* and the National Association of Insurance Commissioners' *Accounting Practices and Procedures Manual* and agrees to or is included in the amounts reported in the Company's 2016 Statutory Annual Statement as filed with the Oklahoma Insurance Department.

Certain items required of the Annual Audited Financial Reports in the Annual Audited Report section of the National Association of Insurance Commissioners' *Annual Statement Instructions* and the National Association of Insurance Commissioners' *Accounting Practices and Procedures Manual* have been omitted from the schedule presented herein as amounts are zero or items are not applicable.