Risk Factors Comparison 2023-03-28 to 2022-03-16 Form: 10-K

Legend: **New Text** ~~Removed Text~~ Unchanged Text Moved Text Section

Insurance Operational Risks Our success depends on our ability to price accurately the risks we underwrite. Our results of operations and financial condition depend on our ability to underwrite and set premium rates accurately for a wide variety of risks. Establishing adequate premium rates is necessary to generate sufficient revenues, together with investment income, to pay losses, loss settlement expenses and underwriting expenses and to earn a profit. To price our products accurately, we must collect and properly analyze a substantial amount of data; develop, test and apply appropriate pricing techniques; closely monitor and timely recognize changes in trends; and project both severity and frequency of losses with reasonable accuracy. Our ability to undertake these efforts successfully, and as a result price our products accurately, is subject to a number of risks and uncertainties, some of which are outside our control, including: ● the availability of sufficient reliable data; ● our ability to properly analyze available data; ● the uncertainties that inherently characterize estimates and assumptions; ● our selection and application of appropriate pricing techniques; and ● changes in applicable legal liability standards and in the civil litigation system generally. If we do not accurately assess the risks we underwrite, we may not charge adequate premiums to cover our losses and expenses, which would adversely affect our results of operations. Alternatively, if we set our premiums too high, it could reduce our sales volume and competitiveness. In either case, our profitability could be materially and adversely affected. Estimating reserves is inherently uncertain. If our loss reserves are not adequate, it will have an unfavorable impact on our financial condition and results of operations. We maintain loss reserves to cover our estimated ultimate liability for unpaid losses and LAE for reported and unreported claims incurred as of the end of each accounting period. Reserves represent management' s estimates of what the ultimate settlement and administration of claims will cost. These estimates, which generally involve actuarial projections, are based on management' s assessment of facts and circumstances then known, as well as estimates of future trends in claim severity and frequency, judicial theories of liability, and other factors. These variables are affected by both internal and external events, such as changes in claims handling procedures, inflation, judicial trends and legislative changes. Many of these factors are not quantifiable. Additionally, there may be a significant lag between the occurrence of an event and the time it is reported to us. The inherent uncertainties of estimating reserves are greater for certain types of liabilities, particularly those in which the various considerations affecting the type of claim are subject to change and in which long periods of time may elapse before a definitive determination of liability is made. Reserve estimates are continually refined in a regular and ongoing process as experience develops and further claims are reported and settled. Adjustments to reserves are reflected in the results of the periods in which such estimates are changed. For example, a 1 % change in December 31, ~~2021~~ **2022** unpaid losses and LAE would have produced a $ 8. ~~2~~ **8** million change to pretax earnings. Our gross loss and LAE reserves totaled $ ~~816~~ **880** . ~~7~~ **9** million at December 31, ~~2021~~ **2022** . Our loss and LAE reserves, net of reinsurance recoverable on unpaid loss and LAE, were $ ~~428~~ **460** . ~~8~~ **2** million at that date. Because setting reserves is inherently uncertain, there can be no assurance that the current reserves will prove adequate. Catastrophic losses are unpredictable and may adversely affect our results of operations, liquidity and financial condition. Property / casualty insurance companies are subject to claims arising out of catastrophes that may have a significant effect on their results of operations, liquidity and financial condition. Catastrophes can be caused by various events, including hurricanes, windstorms, earthquakes, hail storms, explosions, severe winter weather and fires, and may include man- made events, such as terrorist attacks. The incidence, frequency, and severity of catastrophes are inherently unpredictable. The extent of losses from a catastrophe is a function of both the total amount of insured exposure in the area affected by the event and the severity of the event. Claims from catastrophic events could reduce our net income, cause substantial volatility in our financial results for any fiscal quarter or year or otherwise adversely affect our financial condition, liquidity or results of operations. Catastrophes may also negatively affect our ability to write new business. Increases in the value and geographic concentration of insured property and the effects of inflation could increase the severity of claims from catastrophic events in the future. ~~Our~~ **19Our** geographic concentration ties our performance to the business, economic and regulatory conditions of certain states. The following states accounted for approximately ~~49~~ **56** % of our gross written premiums for ~~2021~~ **2022** : Texas (~~19~~ **20** %), ~~California~~ **Arizona** (~~14~~ **16** %), ~~Florida~~ **Oregon** (~~7~~ **9** %) ~~Arizona~~ **New Mexico (6 %) and Idaho** (5 ~~%) and Oregon (4~~ %). Our revenues and profitability are subject to the prevailing regulatory, legal, economic, political, demographic, competitive, weather and other conditions in the principal states in which we do business. Changes in any of these conditions could make it less attractive for us to do business in such states and would have a more pronounced effect on us compared to companies that are more geographically diversified. In addition, our exposure to severe losses from localized natural perils, such as windstorms or hailstorms, is increased in those areas where we have written significant numbers of property / casualty insurance policies. Our failure to maintain favorable financial strength ratings could negatively impact our ability to compete successfully. Third- party rating agencies assess and rate the claims- paying ability of insurers based upon criteria established by the agencies. AHIC, HIC, HSIC and HNIC have entered into a pooling arrangement, pursuant to which AHIC retains ~~32~~ **28** % of the net premiums written by any of them, HIC retains ~~32~~ **38** % of the net premiums written by any of them, HSIC retains ~~26~~ **21** % of the net premiums written by any of them and HNIC retains ~~10~~ **13** % of the net premiums written by any of them. A. M. Best has pooled its ratings of these four insurance company subsidiaries and assigned a financial strength rating of " A- " (Excellent) and an issuer credit rating of " a- " to the individual insurance company subsidiaries comprising the pool. Also, A. M. Best has assigned HCM a financial strength rating of " A- " (Excellent) and an issuer credit rating of " a- ". A. M. Best has indicated a negative outlook for each of the ratings assigned to our insurance company subsidiaries. A. M. Best does not assign a financial strength rating or an issuer credit rating to TBIC. These financial

strength ratings are used by policyholders, insurers, reinsurers and insurance and reinsurance intermediaries as an important means of assessing the financial strength and quality of insurers. These ratings are not ~~23~~ evaluations directed to potential purchasers of our common stock and are not recommendations to buy, sell or hold our common stock. Our ratings are subject to change at any time and could be revised downward or revoked at the sole discretion of the rating agencies. We believe that the ratings assigned by A. M. Best are an important factor in marketing our products. Our ability to retain our existing business and to attract new business in our insurance operations depends largely on these ratings. Our failure to maintain our ratings, or any other adverse development with respect to our ratings, could cause our current and future independent agents and insureds to choose to transact their business with more highly rated competitors. If A. M. Best downgrades our ratings or publicly indicates that our ratings are under review, it is likely that we would not be able to compete as effectively with our competitors, and our ability to sell insurance policies could decline. If that happened, our sales and earnings would decrease. For example, many of our agencies and insureds have guidelines that require us to have an A. M. Best financial strength rating of " A- " (Excellent) or higher. A reduction of our A. M. Best rating below " A- " would prevent us from issuing policies to insureds or potential insureds with such ratings requirements. **Following the announcement of the transaction with Core Specialty, A. M. Best placed under review with negative implications the financial strength ratings of A- (Excellent) and the issuer credit ratings of a- (Excellent) of each of AHIC, HIC, HSIC, HNIC and HCM, as well as the pool comprised of AHIC, HIC, HSIC and HNIC. While acknowledging the mitigating impact of the transaction with Core Specialty, A. M. Best expressed concern over the uncertainty of the arbitration proceedings with the Reinsurers under the LPT Contract, potential additional unfavorable prior year loss development in excess of the aggregate limit under the LPT Contract, and the Company' s ability to restore profitability to its continuing operations. (See Note 7, " Reinsurance – Loss Portfolio Transfer " in the Notes to Consolidated Financial Statements and Item 3. " Legal Proceedings ".) A. M. Best indicated that these ratings will remain under review until they can fully assess the impacts of the Core Specialty transaction, in addition to the effects of initiatives to improve operating performance and stem further material adverse reserve development. In the event of a ratings downgrade by A. M. Best, we would explore options including placing our business on companies with an A. M. Best rating of " A- " or better.** Lenders and reinsurers also use our A. M. Best ratings as a factor in deciding whether to transact business with us. The failure of our insurance company subsidiaries to maintain their current ratings could dissuade a lender or reinsurance company from conducting business with us or might increase our interest or reinsurance costs. In addition, a ratings ~~downgrade~~ **20downgrade** by A. M. Best below " A- " would require us to post collateral in support of our obligations under certain of our reinsurance agreements pursuant to which we assume business. We rely on independent agents ~~and specialty brokers~~ to market our products and their failure to do so would have a material adverse effect on our results of operations. We market and distribute our insurance products exclusively through independent insurance agents ~~and specialty insurance brokers~~ . As a result, our business depends in large part on the marketing efforts of these agents and ~~brokers and~~ on our ability to offer insurance products and services that meet the requirements of the agents, ~~the brokers~~ and their customers. However, these agents ~~and brokers~~ are not obligated to sell or promote our products and many sell or promote competitors' insurance products in addition to our products. Some of our competitors have higher financial strength ratings, offer a larger variety of products, set lower prices for insurance coverage and / or offer higher commissions than we do. Therefore, we may not be able to continue to attract and retain independent agents ~~and brokers~~ to sell our insurance products. The failure or inability of independent agents ~~and brokers~~ to market our insurance products successfully could have a material adverse impact on our business, financial condition and results of operations. Our reliance on independent agents ~~and specialty brokers~~ exposes us to credit risk that could adversely affect our results of operations and financial position. Certain premiums produced by independent agents ~~and specialty brokers~~ are collected from policyholders by the agents and ~~brokers and~~ forwarded to our insurance company subsidiaries. When the insured pays its policy premium to its agent ~~or broker~~ , the premium may be considered to have been paid to us under applicable insurance laws and regulations. Accordingly, the insured would no longer be liable to us for those amounts, whether or not we actually received the premium from the agent or broker. Consequently, we assume a degree of credit risk associated with the agents ~~or brokers~~ with whom we work. Where necessary, we review the financial condition of potential new agents ~~and brokers~~ before we agree to transact business with them. Although the failure by any of our agents ~~or brokers~~ to remit premiums to us has not been material to date, there may be instances where our agents ~~or brokers~~ collect premiums but do not remit them to us and we may be required under applicable law to provide the coverage set forth in the policy despite the absence of related premiums being paid to us. Because the possibility of these events occurring depends in large part upon the financial condition and internal operations of our agents ~~and brokers~~ , we monitor ~~broker~~ **agent** behavior and review financial information on an as- needed basis. If we are unable to collect premiums from our agents ~~and brokers~~ in the future, our underwriting profits may decline and our financial condition and results of operations could be materially and adversely affected. ~~24~~ Our results may be unfavorably impacted if we are unable to obtain adequate reinsurance. As part of our overall risk and capacity management strategy, we purchase reinsurance for significant amounts of risk, especially catastrophe risks that we and our insurance company subsidiaries underwrite. Our catastrophe and non- catastrophe reinsurance facilities are generally subject to annual renewal. We may be unable to maintain our current reinsurance facilities or to obtain other reinsurance facilities in adequate amounts and at favorable rates. The amount, availability and cost of reinsurance are subject to prevailing market conditions beyond our control, and may affect our ability to write additional premiums as well as our profitability. If we are unable to obtain adequate reinsurance protection for the risks we have underwritten, we will either be exposed to greater losses from these risks or be required to reduce the level of business that we underwrite, which will reduce our revenue. If the companies that provide our reinsurance do not pay our claims in a timely manner, we could incur severe losses. We purchase reinsurance by transferring, or ceding, part of the risk we have assumed to a reinsurance company in exchange for part of the premium we receive in connection with the risk. Although reinsurance makes the reinsurer liable to us to the extent the risk is transferred or ceded to the reinsurer, it does not relieve us of our liability to our policyholders.

Accordingly, we bear credit risk with respect to our reinsurers. It is not guaranteed that our reinsurers will pay all of our reinsurance claims, or that they will pay our claims on a timely basis. At December 31, ~~2021~~ **2022** , we had a total of $ ~~696~~ **815** . ~~4~~ **8** million due us from reinsurers, including $ ~~550~~ **578** . ~~0~~ **4** million of recoverables from losses and $ ~~146~~ **237** . ~~4~~ **1** million in ceded unearned premiums. The largest amount due us from a single reinsurer as of December 31, ~~2021~~ **2022** was $ ~~175~~ **202** . ~~4~~ **0** million reinsurance ~~and~~ **21and** premium recoverable from Swiss Reinsurance America Corporation. If any of our reinsurers are unable or unwilling to pay amounts they owe us in a timely fashion, we could suffer a significant loss or a shortage of liquidity, which would have a material adverse effect on our business and results of operations. Our failure to accurately and timely pay claims could materially and adversely affect our business, financial condition and results of operations. We must accurately and timely evaluate and pay claims that are made under our policies. Many factors affect our ability to pay claims accurately and timely, including the training and experience of our claims representatives, our claims organization' s culture, our ability to develop or select and implement appropriate procedures and systems to support our claims functions and other factors. Our failure to pay claims accurately and timely could lead to regulatory and administrative actions or material litigation, undermine our reputation in the marketplace and materially and adversely affect our business, financial condition and results of operations. Adverse securities market conditions can have a significant and negative impact on our investment portfolio. Our results of operations depend in part on the performance of our invested assets. As of December 31, ~~2021~~ **2022** , ~~86~~ **94** % of our investment portfolio was invested in fixed- income securities. Certain risks are inherent in connection with fixed- income securities, including loss upon default and price volatility in reaction to changes in interest rates and general market factors. In general, the fair value of a portfolio of fixed- income securities increases or decreases inversely with changes in the market interest rates, while net investment income realized from future investments in fixed- income securities increases or decreases along with interest rates. In addition, ~~24~~ **55** % of our fixed- income securities have call or prepayment options. This subjects us to reinvestment risk should interest rates fall and issuers call their securities. Furthermore, actual net investment income and / or cash flows from investments that carry prepayment risk, such as mortgage- backed and other asset- backed securities, may differ from those anticipated at the time of investment as a result of interest rate fluctuations. An investment has prepayment risk when there is a risk that cash flows from the repayment of principal might occur earlier than anticipated because of declining interest rates or later than anticipated because of rising interest rates. The fair value of our fixed- income securities as of December 31, ~~2021~~ **2022** was $ ~~290~~ **426** . ~~1~~ **6** million. If market interest rates were to increase 1 %, the fair value of our fixed- income securities would decrease by approximately $ ~~1~~ **3** . ~~7~~ **4** million as of December 31, ~~2021~~ **2022** . The calculated change in fair value was determined using duration modeling assuming no prepayments. In addition to the general risks described above, although ~~73~~ **83** % of our fixed- income portfolio is investment- grade, our fixed- income securities are nonetheless subject to credit risk. If any of the issuers of our fixed- income securities suffer ~~25~~ financial setbacks, the ratings on the fixed- income securities could fall (with a concurrent fall in market value) and, in a worst case scenario, the issuer could default on its obligations. As of December 31, ~~2021~~ **2022** , Hallmark had $ 1. ~~9~~ **4** million total exposure in mortgage- backed securities. Future changes in the fair value of our available- for- sale fixed income securities will be reflected in other comprehensive income. Similar treatment is not available for liabilities. Therefore, interest rate fluctuations could adversely affect our stockholders' equity, total comprehensive income and / or cash flows. State statutes limit the aggregate amount of dividends **and management fees** that our subsidiaries may pay Hallmark, thereby limiting its funds to pay expenses and dividends. Hallmark is a holding company and a legal entity separate and distinct from its subsidiaries. As a holding company without significant operations of its own, Hallmark' s principal sources of funds are dividends **, management fees** and other sources of funds from its subsidiaries. State insurance laws limit the ability of Hallmark' s insurance company subsidiaries to pay dividends and require our insurance company subsidiaries to maintain specified minimum levels of statutory capital and surplus. The aggregate maximum amount of dividends permitted by law to be paid by an insurance company does not necessarily define an insurance company' s actual ability to pay dividends. The actual ability to pay dividends may be further constrained by business and regulatory considerations, such as the impact of dividends on surplus, by our competitive position and by the amount of premiums that we can write. ~~Without regulatory~~ **Any dividends paid to Hallmark during 2023 will require prior** approval **from state regulators** ~~, the aggregate maximum amount of dividends that could be paid to Hallmark in 2022 by our insurance company subsidiaries is $ 22. 7 million~~ . State insurance regulators have broad discretion to limit the payment of dividends by insurance companies and Hallmark' s right to participate in any distribution of assets of any one of our ~~insurance~~ **22insurance** company subsidiaries is subject to prior claims of policyholders and creditors except to the extent that its rights, if any, as a creditor are recognized. Consequently, Hallmark' s ability to pay debts, expenses and cash dividends to our stockholders may be limited **. Any dividends paid to Hallmark during 2023 will require prior approval from state regulators** . Our insurance company subsidiaries are subject to minimum capital and surplus requirements. Failure to meet these requirements could subject us to regulatory action. Our insurance company subsidiaries are subject to minimum capital and surplus requirements imposed under the laws of their respective states of domicile and each state in which they issue policies. Any failure by one of our insurance company subsidiaries to meet minimum capital and surplus requirements imposed by applicable state law will subject it to corrective action, which may include requiring adoption of a comprehensive financial plan, revocation of its license to sell insurance products or placing the subsidiary under state regulatory control. Any new minimum capital and surplus requirements adopted in the future may require us to increase the capital and surplus of our insurance company subsidiaries, which we may not be able to do. ~~26 Insurance~~ **23Insurance** Industry RisksOur industry is very competitive, which may unfavorably impact our results of operations. Our competitors include entities that have access to greater financial and other resources than us. Our competitors may attempt to increase market share by lowering rates. In that case, we could experience reductions in our underwriting margins, or sales of our insurance policies could decline as customers purchase lower- priced products from our competitors. Losing business to competitors offering similar products at lower prices, or having other competitive advantages, could adversely affect our results of operations. In recent years, the insurance industry has undergone increasing consolidation,

which may further increase competition. In addition, an increase in capital- raising by companies in our lines of business could result in new entrants to our markets and an excess of capital in the industry. Federal, rather than state, regulatory oversight of the insurance industry has been proposed from time to time which, if adopted, could ease the entry of new competitors into our markets. If we have difficulty competing as industry conditions change, our results of operations may be adversely affected. Our results may fluctuate as a result of cyclical changes in the property / casualty insurance industry. Our revenue is primarily attributable to property / casualty insurance, which as an industry is cyclical in nature and has historically been characterized by soft markets followed by hard markets. A soft market is a period of relatively high levels of price competition, less restrictive underwriting standards and generally low premium rates. A hard market is a period of capital shortages resulting in lack of insurance availability, relatively low levels of competition, more selective underwriting of risks and relatively high premium rates. If we find it necessary to reduce premiums or limit premium increases due to competitive pressures on pricing in a softening market, we may experience a reduction in our premiums written and in our profit margins and revenues, which could adversely affect our financial results. We are subject to comprehensive regulation, and our results may be unfavorably impacted by these regulations. We are subject to comprehensive governmental regulation and supervision. Most insurance regulations are designed to protect the interests of policyholders rather than of the stockholders and other investors of the insurance companies. These regulations, generally administered by the department of insurance in each state in which we do business, relate to, among other things: ● approval of policy forms and rates; ● standards of solvency, including risk- based capital measurements, which are a measure developed by the National Association of Insurance Commissioners and used by the state insurance regulators to identify insurance companies that potentially are inadequately capitalized; ● licensing of insurers and their agents; ● restrictions on the nature, quality and concentration of investments; ● restrictions on the ability of insurance company subsidiaries to pay dividends; ● restrictions on transactions between insurance company subsidiaries and their affiliates; ● requiring certain methods of accounting; ● periodic examinations of operations and finances; ● the use of non- public consumer information and related privacy issues; ~~27~~ **24** ● the use of credit history in underwriting and rating; ● limitations on the ability to charge policy fees; ● the acquisition or disposition of an insurance company or of any company controlling an insurance company; ● involuntary assignments of high- risk policies, participation in reinsurance facilities and underwriting associations, assessments and other governmental charges; ● restrictions on the cancellation or non- renewal of policies and, in certain jurisdictions, withdrawal from writing certain lines of business; ● prescribing the form and content of records of financial condition to be filed; ● requiring reserves for unearned premium, losses and other purposes; and ● with respect to premium finance business, the federal Truth- in- Lending Act and similar state statutes. In states where specific statutes have not been enacted, premium finance is generally subject to state usury laws that are applicable to consumer loans. State insurance departments also conduct periodic examinations of the affairs of insurance companies and require filing of annual and other reports relating to the financial condition of insurance companies, holding company issues and other matters. Our business depends on compliance with applicable laws and regulations and our ability to maintain valid licenses and approvals for our operations. Regulatory authorities may deny or revoke licenses for various reasons, including violations of regulations. Changes in the level of regulation of the insurance industry or changes in laws or regulations themselves or interpretations by regulatory authorities could have a material adverse effect on our operations. In addition, we could face individual, group and class- action lawsuits by our policyholders and others for alleged violations of certain state laws and regulations. Each of these regulatory risks could have an adverse effect on our profitability. The exclusions and limitations in our policies may not be enforceable. Many of the policies we issue include exclusions or other conditions that define and limit coverage, which exclusions and conditions are designed to manage our exposure to certain types of risks and expanding theories of legal liability. In addition, many of our policies limit the period during which a policyholder may bring a claim under the policy, which period in many cases is shorter than the statutory period under which these claims can be brought by our policyholders. While these exclusions and limitations help us assess and control our loss exposure, it is possible that a court or regulatory authority could nullify or void an exclusion or limitation, or legislation could be enacted modifying or barring the use of these exclusions and limitations. This could result in higher than anticipated losses and LAE by extending coverage beyond our underwriting intent or increasing the number or size of claims, which could have a material adverse effect on our operating results. In some instances, these changes may not become apparent until sometime after we have issued the insurance policies that are affected by the changes. As a result, the full extent of liability under our insurance contracts may not be known for many years after a policy is issued. Catastrophe models may not accurately predict future losses. Along with other insurers in the industry, we use models developed by third- party vendors in assessing our exposure to catastrophe losses that assume various conditions and probability scenarios. However, these models do not necessarily accurately predict future losses or accurately measure losses currently incurred. Catastrophe models, which have been evolving since the early 1990s, use historical information about various catastrophes and detailed information about our in- force business. While we use this information in connection with our pricing and risk management activities, there are limitations with respect to their usefulness in predicting losses in any reporting period. Examples of these limitations are significant variations in estimates between models and modelers and material increases and decreases in model results due to changes and refinements of the underlying data elements and assumptions. Such limitations lead to questionable ~~28 predictive~~ **25predictive** capability and post- event measurements that have not been well understood or proven to be sufficiently reliable. In addition, the models are not necessarily reflective of company or state- specific policy language, demand surge for labor and materials or loss settlement expenses, all of which are subject to wide variation by catastrophe. Because the occurrence and severity of catastrophes are inherently unpredictable and may vary significantly from year to year, historical results of operations may not be indicative of future results of operations. If actual claims exceed our claims and claim adjustment expense reserves, or if changes in the estimated level of claims and claim adjustment expense reserves are necessary, including as a result of, among other things, changes in the legal, regulatory and economic environments in which the Company operates, our financial results could be materially and adversely affected. Unpaid loss and LAE reserves represent management

estimates of what the ultimate settlement and administration of claims will cost, generally utilizing actuarial expertise and projection techniques, at a given accounting date. The process of estimating loss reserves involves a high degree of judgment and is subject to a number of variables. These variables can be affected by both internal and external events, such as: changes in claims handling procedures, including automation; adverse changes in loss cost trends, including inflationary pressures, technology or other changes that may impact medical, auto and home repair costs (e. g., more costly technology in vehicles resulting in increased severity of claims); economic conditions, including general and wage inflation; legal trends, including adverse changes in the tort environment that have continued to persist for a number of years (e. g., increased and more aggressive attorney involvement in insurance claims, increased litigation, expanded theories of liability, higher jury awards, lawsuit abuse and third- party litigation finance, among others); and legislative changes, among others. The impact of many of these items on ultimate costs for loss reserves could be material and is difficult to estimate, particularly in light of **ongoing** ~~the recent~~ disruptions to the ~~judicial system,~~ supply chain and labor market. Loss reserve estimation difficulties also differ significantly by product line due to differences in claim complexity, the volume of claims, the potential severity of individual claims, the determination of occurrence date for a claim and lags in reporting of events to insurers, among other factors. The increase in inflation in recent periods has increased our loss costs in our auto and property businesses. It is possible that, among other things, past or future steps taken by the federal government and the Federal Reserve to stimulate or support the U. S. economy, including actions taken in response to COVID- 19, supply chain issues and labor shortages, could lead to higher and / or prolonged inflation, which could in turn lead to further increases in our loss costs. The impact of inflation on loss costs could be more pronounced for those lines of business that are considered " long tail, " such as general liability, as they require a relatively long period of time to finalize and settle claims for a given accident year or require payouts over a long period of time. The estimation of loss reserves may also be more difficult during extreme events, such as a pandemic, or during volatile or uncertain economic conditions, due to unexpected changes in behavior of claimants and policyholders, including an increase in fraudulent reporting of exposures and / or losses, reduced maintenance of insured properties, increased frequency of small claims or delays in the reporting or adjudication of claims. We refine our loss reserve estimates as part of a regular, ongoing process as historical loss experience develops, additional claims are reported and settled, and the legal, regulatory and economic environment evolves. Business judgment is applied throughout the process, including the application of various individual experiences and expertise to multiple sets of data and analyses. Different experts may apply different assumptions when faced with material uncertainty, based on their individual backgrounds, professional experiences and areas of focus. As a result, these experts may at times produce estimates materially different from each other. This risk may be exacerbated in the context of an extreme event or an acquisition. Experts providing input to the various estimates and underlying assumptions include actuaries, underwriters, claim personnel and lawyers, as well as other members of management. Therefore, management often considers varying individual viewpoints as part of its estimation of loss reserves. Due to the inherent uncertainty underlying loss reserve estimates, the final resolution of the estimated liability for claims and claim adjustment expenses will likely be higher or lower than the related loss reserves at the reporting date. In addition, our estimate of claims and claim adjustment expenses may change. These additional liabilities or increases in estimates, could vary significantly from period to period and could materially and adversely affect our results of operations and / or our financial position. (See ~~"~~ **"** Item 7 — Management ~~'~~ **'** s Discussion and Analysis of Financial Condition and Results of Operations — Critical Accounting Estimates — Reserves for unpaid losses and LAE. ") ~~29 The~~ **26The** effects of litigation on our business are uncertain and could have an adverse effect on our business. As is typical in our industry, we continually face risks associated with litigation of various types, including disputes relating to insurance claims under our policies as well as other general commercial and corporate litigation. Although we are not currently involved in any material litigation with our customers, other members of the insurance industry are the target of class action lawsuits and other types of litigation, some of which involve claims for substantial or indeterminate amounts, and the outcomes of which are unpredictable. This litigation is based on a variety of issues, including insurance coverage and claim settlement practices. We cannot predict with any certainty whether we will be involved in similar litigation in the future or what impact such litigation would have on our business. We are subject to assessments and other surcharges from state guaranty funds, mandatory reinsurance arrangements and state insurance facilities, which may reduce our profitability. Virtually all states require insurers licensed to do business therein to bear a portion of the unfunded obligations of impaired or insolvent insurance companies. These obligations are funded by assessments, which are levied by guaranty associations within the state, up to prescribed limits, on all member insurers in the state on the basis of the proportionate share of the premiums written by member insurers in the lines of business in which the impaired, insolvent or failed insurer was engaged. Accordingly, the assessments levied on us by the states in which we are licensed to write insurance may increase as we increase our premiums written. In addition, as a condition to the ability to conduct business in certain states, insurance companies are required to participate in mandatory reinsurance funds. The effect of these assessments and mandatory reinsurance arrangements, or changes in them, could reduce our profitability in any given period or limit our ability to grow our business. We monitor developments with respect to various state facilities, such as the Texas FAIR Plan and the Texas Windstorm Insurance Association. The impact of any catastrophe experience on these facilities could result in the facilities recognizing a financial deficit or a financial deficit greater than the level currently estimated. They may, in turn, have the ability to assess participating insurers when financial deficits occur, adversely affecting our results of operations. While these facilities are generally designed so that the ultimate cost is borne by policyholders, the exposure to assessments and the availability of recoupments or premium rate increases from these facilities may not offset each other in our financial statements. Moreover, even if they do offset each other, they may not offset each other in financial statements for the same fiscal period due to the ultimate timing of the assessments and recoupments or premium rate increases, as well as the possibility of policies not being renewed in subsequent years. ~~30 General~~ **27General** Business RisksThe loss of key executives or the inability to attract and retain qualified personnel could disrupt our business. Our success will depend in part upon the continued service of certain key executives. Our success will also depend on our ability to

attract and retain additional executives and personnel. The pool of talent from which we actively recruit is limited and may fluctuate based on market dynamics specific to our industry and independent of overall economic conditions. As such, higher demand for employees having the desired skills and expertise could lead to increased compensation expectations for existing and prospective personnel, making it difficult for us to retain and recruit key personnel and maintain labor costs at desired levels. The loss of key personnel, or our inability to recruit and retain additional qualified personnel, could cause disruption in our business and could prevent us from fully implementing our business strategies, which could materially and adversely affect our business, growth and profitability. Our variable rate indebtedness subjects us to interest rate risk, which could cause our debt service obligations to increase significantly. As of December 31, ~~2021~~ **2022** , we had outstanding $ 56. 7 million of trust preferred securities bearing interest at a weighted average rate of ~~3~~ **7** . ~~29~~ **86** % per annum. (See, " Item 7. Management' s Discussion and Analysis of Financial Condition and Results of Operations – Liquidity and Capital Resources – Subordinated Debt Securities. ") Our trust preferred securities bear interest at a variable rate which is adjusted quarterly. A 1 % increase in the applicable interest rates would result in a $ 0. 6 million increase in interest expense attributable to the currently outstanding balance of the trust preferred securities, which could adversely affect our operating results, cash flow and financial position. In addition, the interest rates under our trust preferred securities are adjusted quarterly using LIBOR. On July 27, 2017, the Financial Conduct Authority (the authority that regulates LIBOR) announced that it intends to stop compelling banks to submit rates for the calculation of LIBOR after 2021, and it will formally cease publication in June 2023. If LIBOR is unavailable on an interest calculation date, the trustee is authorized to calculate the interest rate on the basis of quotations from certain major banks in London or New York. If the trustee is unable to determine an interest rate in this manner, the immediately preceding interest rate remains in effect. It is not possible to predict the effect of these changes. Uncertainty in the determination of the interest rate applicable to our trust preferred securities could adversely affect our financial planning. U. S. and global economic and financial industry events and their consequences could harm our business, our liquidity and financial condition, and our stock price. The consequences of adverse global or regional market and economic conditions may affect (among other aspects of our business) the demand for and claims made under our products, the ability of customers, counterparties, and others to establish or maintain their relationships with us, our ability to access and efficiently use internal and external capital resources, the availability of reinsurance protection, the risks we assume under reinsurance programs covering variable annuity guarantees, and our investment performance. Volatility in the U. S. and other securities markets may adversely affect our stock price. An increased inflation rate or a period of sustained inflation may adversely impact our results of operations. Inflation may negatively impact both interest rates and the amount we pay to settle claims. We take into account the effects of inflation when we set our prices; however, if we do not change our pricing to adequately account for inflation, our results of operations may be negatively impacted. We also consider inflation when we estimate reserves for unpaid losses and LAE, because of the increase on our claims costs that is caused by inflation. While we plan for the inflation we expect, the actual effects of inflation on results of operations are not known until claims are ultimately settled. In addition to general price inflation, we are exposed to the upward trend in the judicial awards for damages. We attempt to mitigate the effects of inflation in the pricing of policies and establishing reserves for losses and LAE. **28We** ~~31 We~~ may experience difficulty in integrating acquisitions into our operations. The successful integration of any newly acquired business into our operations will require, among other things, the retention and assimilation of their key management, sales and other personnel; the coordination of their lines of insurance products and services; the adaptation of their technology, information systems and other processes; and the retention and transition of their customers. Unexpected difficulties in integrating any acquisition could result in increased expenses and the diversion of management time and resources. If we do not successfully integrate any acquired business into our operations, we may not realize the anticipated benefits of the acquisition, which could have a material adverse impact on our financial condition and results of operations. Further, any potential acquisition may require significant capital outlay and, if we issue equity or convertible debt securities to pay for an acquisition, the issuance may be dilutive to our existing stockholders. Our internal controls over financial reporting are not fail- safe. We continually enhance our operating procedures and internal controls over financial reporting (" ICFR ") to effectively support our business and comply with our regulatory and financial reporting requirements. As a result of the inherent limitations in all control systems, no system of controls can provide absolute assurance that all control objectives have been or will be met, and that every instance of error or fraud has been or will be detected. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. These inherent limitations include the realities that judgments in decision- making can be faulty and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by individual acts or by collusion of two or more persons. The design of any system of controls is based in part upon assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. ICFR may also become inadequate because of changes in conditions, or the degree of compliance with policies or procedures may deteriorate. Further, the design of a control system must reflect resource constraints, and the benefits of controls must be considered relative to their costs. As a result of the inherent limitations in a cost- effective control system, misstatement due to error or fraud may occur and not be detected. Accordingly, our ICFR and procedures are designed to provide reasonable, not absolute, assurance that the control objectives are met. We rely on our information technology and telecommunications systems and the failure or disruption of these systems could disrupt our operations and adversely affect our results of operations. Our business is highly dependent upon the successful and uninterrupted functioning of our information technology and telecommunications systems. We rely on these systems to perform accounting, policy administration, actuarial and other modeling functions necessary for underwriting business, as well as to process and make claims and other payments. Our systems could fail of their own accord or might be disrupted by factors such as natural disasters, power disruptions or surges, cybersecurity intrusions or terrorist attacks. Failure or disruption of these systems for any reason could interrupt our business and adversely affect our results of operations. Cybersecurity risks in particular are evolving and

include malicious software, unauthorized access to data and other electronic security breaches. We have not experienced successful cybersecurity attacks in the past and believe that we have adopted appropriate measures to mitigate potential risks to our information technology systems. However, the timing, nature and scope of cybersecurity attacks are difficult to predict and prevent. Therefore, we could be subject to operational delays, compromised confidential or proprietary information, destruction or corruption of data, manipulation or improper use of our systems and networks, financial losses from remedial actions and / or damage to our reputation from cybersecurity attacks. A cybersecurity attack on our information technology systems could disrupt our business and adversely affect our results of operations and financial position.