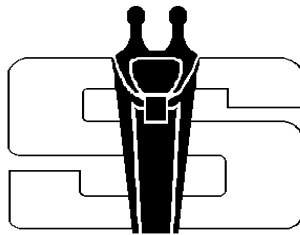


# **STEWART INFORMATION SERVICES CORPORATION**



## **NATIONAL ACCOUNTING GUIDE**

## **INTRODUCTION**

If you are responsible for the accounting records and financial statements for a Stewart office or subsidiary, this Accounting Guide was written for you. We have referred to you as “controller” throughout this Guide, meaning anyone who has the above accounting responsibilities, even though your title may be something different.

This is an accounting manual for Stewart Information Services Corporation (SISCO) and its subsidiaries and includes the accounting policies we follow. But it is much more. Every major aspect of the duties of a Stewart controller are addressed by the Guide. This is done in the form of a series of releases of individual topics. Releases will be periodically added to the Guide. Please file them in this notebook.

Your comments and suggestions for topics are welcome. Please write to Alison Evers, Senior Vice President and Controller, Stewart Information Services Corporation, P.O. Box, 2029, Houston, TX 77252

Date: August 2001 (previously November 1998)

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Date: August 2001 (Previously November 1998)

## **GETTING STARTED AT STEWART**

The first days in a new position are important. Accounting personnel and new controllers should make use of common sense measures and certain opportunities made available by Stewart in getting off to a good start. Here are some suggestions:

- 1 Become familiar with your responsibilities and duties. Determine specifically what is expected of you.
- 2 Have your manager conduct a tour of the office for you. Understand the nature of the business. Your full talents cannot be used otherwise. Acquaint yourself with the special language and terms that are used. Read the Stewart publication "Sold! What Happens Next?"
- 3 Learn the names and responsibilities of the other associates. Make a point of meeting and getting to know them.
- 4 Stewart office controllers report to local management but many of their duties require them to interface effectively and frequently with associates at National Accounting (Houston Corporate Headquarters). Find out who those associates are (see Item 11 for a list of the National Accounting associates along with a brief summary of their responsibilities), call and introduce yourself and lay the groundwork for a productive relationship.
- 5 The Stewart Information Review is a self-study program for learning about the title business and Stewart. See your manager about enrolling in the program.
- 6 Study the recent annual and quarterly reports to the shareholders of Stewart for more information about the business and the company. If you have internet access, look at Stewart.com for current news about the Company.
- 7 Study this Accounting Guide.
- 8 Study the Financial Executive Information System (FEIS) Users Guide, as this will be your primary source for financial reporting and analysis both locally and with National Accounting.
- 9 Consider enrolling in an accounting course or a related subject at an area college.

Release No. 1

Date: August 2001 (previously November 1998)

## **REPORT DEADLINES**

Stewart Information Services Corporation (SISCO), like most public companies, has numerous internal and external financial reporting requirements. It is of utmost importance that the company meet established deadlines and report accurate, timely information. Much of the accounting and financial information necessary to produce the reports outlined in this section is provided by Stewart's affiliated and partially owned offices. In other words, your office plays an integral role in the company's reporting requirements.

National Accounting's reporting requirements consist of the collection of (1) sales / order data four times a month and (2) financial results at each month and quarter end.

Sales / Order Data. By 11:00 AM (Houston time) of the second working day after the 5th, 10th, 15th and last working day of each month, the following data is due to National Accounting:

1. Gross sales recorded in the week covered by the report (Note: "Gross sales" represent the amounts which are reported on Line one, Schedule A).
2. Gross sales recorded in the month-to-date. This is the sum of the amounts reported in (1) above for this period plus amounts in previous reports for the month.
3. The number of orders received during the week covered by the report, and
4. The number of orders received during the month-to-date. This is the sum of the amounts reported in (3) above plus amounts in previous reports for this month.

The required data should be entered into the FEI system before the deadline.

In late December of each year, National Accounting will furnish each office with a "sales report calendar" for the upcoming year. It includes due dates, reporting dates and a list of home office holidays that are recognized for this report.

Month End Financial Reports. These reports, the preparation and handling of which are discussed in detail in other Releases, consist of an income statement and balance sheet on Schedules A and B, respectively, financial and non-financial "other data" on Schedule A-1, Report Card and certain other supplemental schedules when applicable. Data for Schedules A and B may be electronically transmitted to Houston using the FEI General Ledger Extract Utility or the data may be manually keyed into the FEI system. Schedule A-1, Schedule B other data and local manager information must be keyed manually into the FEI system. All monthly data must be keyed/transmitted on or before the 10<sup>th</sup> calendar day following the close of the reporting month.

The Flash Report is a consolidated income statement prepared each month by National Accounting and distributed to upper management. The Flash Report figures are due no later than 12:00 Noon (Houston time) on the fourth working day following the end of the reporting month. The following income statement and balance sheet information must be keyed into the FEI system:

1. Total title insurance fees year-to-date from Line 1 of Schedule A
2. Total net revenues year-to-date from Line 20 of Schedule A

**REPORT DEADLINES**

(continued)

3. Pretax income (loss) year-to-date from Line 71 of Schedule A
4. State and Federal Income taxes year-to-date from Lines 72 and 73 of Schedule A
5. This year-to-date totals for guaranty premium expense (Line 5) and other income (Line 11) of Schedule A
6. This year-to-date totals for policy escrow losses from Line 29 of Schedule A, and
7. The total amounts payable to Stewart Title Guaranty Company (STG) or any other STG underwriter from Line 125 of Schedule B.

Release No. 2

Date: August 2001 (previously November 1998)

## **INCOME STATEMENT (SCHEDULE A)**

Use the Schedule A format (see Appendix, Item 1) for your monthly income statement. Timely completion of Schedule A is important. As stated in the previous release, Schedule A should be submitted by the 10<sup>th</sup> calendar day following each month-end. Budget data shown on Schedule A is submitted and loaded during January of each year. This is done immediately following the annual Goals and Budgets meetings. See the detailed discussion on this submission process in the FEIS Users Guide.

### **Items to note:**

1. National Accounting combines the Schedules of all Stewart companies line-by-line to prepare consolidated reports on a quarterly basis. For this reason, **line numbers and names must be used uniformly**. Specifically, you should summarize and report totals for each line on Schedule A in accordance with the line description provided for each line.
2. After preparing and submitting Schedule A data, it is imperative that you review the Schedule for any obvious errors or unreasonable results. Net income (loss) YTD (Line 74) must agree to Line 140 from the balance sheet, Schedule B.
3. Certain lines in the body of Schedule A are the subject matter of other Releases.

Release No. 3

Date: August 2001 (previously November 1998)

### **(SCHEDULE A-1) "OTHER DATA"**

The instructions for completing the "Other Data" section on Schedule A-1 for title offices follow. **Please note** that all lines preceded by an asterisk (\*) will be automatically calculated for title offices in the FEIS system. The lines without an asterisk (\*) will require manual entry into the FEI system.

Schedule A-1 includes five columns for the prior year periods, the Last YTD, and the Last Month. This historical data should already be in the FEIS database. The amounts for the previous five years are usually 12-month totals ended December 31. After the columns are updated in January of each year, the amounts entered each month will be the same until the following January. **All "non-title" companies should complete only Lines 1, 2 and 3 and disregard all other requirements of the "Other Data" section as discussed below. Other data collected from non-title entities is specific to each individual entity. If you are a non-title company, please contact your Region Controller for specific details on what reporting is required for your company.**

The three columns shown as "Current Month", "Last Month" and "This YTD" should be completed as follows:

- \* Line 1 - Enter Schedule A Line 71, year-to-date income (loss) before taxes, rounded to the nearest thousand dollars.
- \* Line 2 - Calculate the year-to-date pretax profit margin by dividing Schedule A Line 71 (pretax profit) by Schedule A Line 20 (total net revenues). Calculated amounts are rounded to the nearest tenth of a percent.

Line 3 - Enter the number of full-time equivalent associates on the payroll at the current month-end. The total you enter should be rounded to the nearest tenth (i.e. you may enter "0.5" for a part-time, non-contract associate). For the "This YTD" column on the Schedule A-1 report, the system will automatically calculate a YTD average number of associates by adding the current month's total to the total for the previous month's and dividing by the number of months to date this year.

Line 4 - Enter the total number of title insurance orders received this year-to-date. For this purpose an order represents any request for the issuance of a title policy and for which premium revenues are reasonably expected to be reported eventually on Line 1 of Schedule A. Orders that do not generate premiums that will be booked to Line 1 should not be counted. Report gross totals and do not reduce numbers for cancellations.

The following items should be reported as one order:

1. Title only order
2. Title and escrow order (not two orders)
3. STEP policy (and other title policies with less exposure)
4. STIC policy
5. Simultaneous issues
6. Resale/refi
7. Trustee Sales Guarantee (TSG)

The following are not to be counted:

1. "Escrow only" order

2. Mobile home escrows
3. Orders processed/serviced/examined for Stewart Title Guaranty agents
4. "Report only" order

Line 5 – Enter the total number of orders received year-to-date for non-title insurance orders. Revenues from non-title insurance orders are recorded in lines 2 through 4 of Schedule A.

The following items should be reported as a non-title insurance order:

1. "Escrow only" order
2. Title Reports
3. Orders processed/serviced/examined for Stewart Title Guaranty agents
4. Mobile home escrows

Line 6 – Enter the estimated total gross revenues (Line 1 – 4 of Schedule A) expected to be earned from the orders received during the current month. Round amounts to the nearest thousand dollars. To estimate the total gross revenue from orders received, perform the following:

Take the number of title insurance orders received for the current month and multiply by the YTD average revenue per closing (Schedule A-1, Line 12). Then multiply your result by the office's recent ratio of orders that close. Make sure the ratio is one that is reasonable and normally experienced by your office. This amount should then be reviewed by the office manager and adjusted for any unusual circumstances which may be present. The manager should not allow the calculation of Line 6 to become just that, a calculation. This should not be a "formula" used without exercising good judgment.

EXAMPLE: Office XYZ has 200 title orders in the current month and a YTD average revenue per closing of \$450. The office also has approximately a 30% cancellation rate on orders. The estimated total gross revenues from orders would be:

Number of orders .....	200
YTD average revenue per closing .....	<u>x 450</u>
	\$ 90,000
Ratio of orders that close .....	<u>70%</u>
	\$ 63,000

The office manager of XYZ reviews the orders received and notes no unusual orders. Therefore, Line 6 = \$63,000.

\* Line 7 – "Cost Per Order" is calculated by dividing Line 70 of Schedule A (total expenses) by other data Line 4 (orders). Amounts are rounded to the nearest dollar.

**'OTHER DATA' SECTION OF THE INCOME STATEMENT**

(continued)

Line 8 - Enter the number of files closed this year-to-date. A file is closed, for this purpose, when the revenue relating to the file has been included in Line 1 of Schedule A. See the definition of an order above in Line 4.

\* Line 9 – “Cost Per File Closed” is calculated by dividing Schedule A Line 70 (total expenses) by other data Line 8 (files closed). Amounts are rounded to the nearest dollar.

\* Line 10 – To calculate “Orders Per Associate” (OPA) divide other data Line 4 (orders) by Line 3 (associates). For the YTD column, Line 4 is divided by the average number of associates YTD. Amounts are rounded to the nearest tenth of a percent.

\* Line 11 - To calculate “Files Closed Per Associate” (FCPA) for the current month, other data Line 8 (files closed) is divided by Line 3 (associates). For the this YTD column, Line 8 is divided by the average number of associates year-to-date. Amounts are rounded to the nearest tenth of a percent.

\* Line 12 - To calculate “Average Revenue Per Closing,” divide Lines 1-4 of Schedule A (operating revenues) by other data Line 8 (files closed). Amounts are rounded to the nearest dollar.

\* Line 13 – To calculate “Revenues Per Associate” for the current month, divide Lines 1-4 of Schedule A (operating revenues) by other data Line 3 (associates). For the this YTD column, divide Line 1-4 TYTD by the average number of associates year-to-date. Round all amounts to the nearest thousand dollars.

\* Line 14 – To calculate “Rent Per Associate” for the current month, divide Schedule A Line 33 (rent) by other data Line 3 (associates). For the this YTD column divide Schedule A Line 33 by the average number of associates year-to-date. Round all amounts to the nearest thousand dollars.

\* Line 15 - To calculate “Delivery, Telephone, Copy and Postage Per Closing” divide the sum of Schedule A Lines 44, 50, 51 and 53 by other data Line 8 (files closed). Round to the nearest dollar.

Line 16 - Enter percent of business using a consistent and reasonable method of determination. Round to the nearest tenth of a percent.

Line 17 - Enter the numeric value representing your offices’ market share rank during the current month in the area it services.

Line 18 - Enter the total revenue amounts included in Lines 1-4 of Schedule A from refinancing transactions. Round to the nearest thousand dollars.

Line 19 - Enter the total amounts included in Lines 1 and 2 of Schedule A from issuance of policies of \$750,000 or more. Round to the nearest thousand dollars.

Line 20 - Enter the total number of policies generating the amount entered on Line 19. Count simultaneously issued policies as one.

**“OTHER DATA” SECTION OF THE INCOME STATEMENT**

(continued)

Lines 21 & 22 - These YTD amounts will be furnished to you each month by National Accounting. Because of time constraints, these amounts will represent the YTD amounts prior to the reporting month.

Line 23 – To calculate turntime on commitments, divide the number of workdays (excluding weekends and holidays for your office) spent in processing orders to “delivery” by the total number of orders processed. Enter turntime for the current month. Round to the nearest tenth of a percent.

Turntime is the time, expressed in number of 24 hour work-days, that expires from the time an order is in our hands until the first time we deliver the preliminary title report of commitment into the hands of the customer (“Delivery”). In measuring orders, you should exclude all acreage files, refinancings and out-of-county files. The intent is to measure “normal” subdivision files.

In making calculations of an “hour”, you should round to the nearest hour. In making calculations for a “day”, count a full day for the day of receipt if the order is received before noon. Do not count a “day” if the order is received after noon.

Example:

Assume an order is received on October 18 (Friday) at 8:35 AM and your office delivers the commitment on October 23 (Wednesday) at 4:47 PM. Count the number of calendar days. The answer is five days. Then, subtract two weekend days. The answer is three days. Then count the number of hours for October 23, and that is 8 hours (from the rounded 9AM to the rounded 5PM). Then, to convert to a decimal point, divide 8 by 24 and that equals 0.3. In this example, the turntime would be 3.3 days.

Line 24 – Follow the guidance for Line 23 to calculate turntime on policy issuance. Policy issuance turntime is the measurement of time from the recording data to the date the policy is mailed to the policyholder. Enter turntime for the current month.

Line 25 – Enter the contract rate (%) to STG per the underwriting agreement. Enter the percent in effect as of the current month-end.

**Other Data for Underwriters**

If your company is an underwriter, your other data items to be reported will be as follows:

Lines 1 – 3 - Follow the guidance above.

Line 4 - Enter the number of policies received this year to date. Round to the nearest one thousand policies.

Line 5 – Enter the number of issuing offices as of the current monthend. The “This YTD” column will be calculated by the system as an average number of issuing offices for the year-to-date.

\* Line 6 – Losses recorded this year-to-date (Schedule A, Line 29) by total operating income (Schedule A, Line 10).

Line 7 – Enter the number of new claims opened during the current month.

**‘OTHER DATA’ SECTION OF THE INCOME STATEMENT**  
(continued)

Line 8 – Enter the number of claims that were closed during the current month.

Line 9 – Enter the total number of claims that remained open at the end of the current month.

Line 10 – Enter the total amount of cash paid on policy losses this year-to-date. Round to the nearest thousand dollars.

\* Line 11 – Policies per associate is calculated by dividing other data Line 4 (policies) by Line 3 (associates).

\* Line 12 – Calculated by dividing operating revenues (Schedule A, Lines 1-4) by policies received other data (Line 4).

\* Line 13 – Revenue per Associate is calculated by dividing Schedule A, Lines 1-4 (gross operating revenues) by other data Line 3 (associates).

Release No. 4

Date: August 2001 (previously November 1998)

## **BALANCE SHEET (SCHEDULE B)**

Use the Schedule B format (see Appendix, Item 2) for your monthly balance sheet. As is the case on Schedule A, the schedule should be completed and submitted by the 10<sup>th</sup> calendar day following each month-end. Additionally, you should key Schedule B other data information into the FEI system so that it will be displayed at the bottom of Schedule B.

### **After the end of the period:**

1. Enter the amounts in the current YTD column from a final ledger or trial balance.
2. Collect and enter data in the "Other Data" section.
3. After you have prepared and submitted the schedule, it is imperative that you review the schedule for any obvious errors or unreasonable results.

### **Other matters:**

National Accounting combines the Schedules of all Stewart companies line-by-line to prepare consolidated reports on a quarterly basis. For this reason, **line numbers and names must not be changed.**

Beginning of year Retained Earning amounts are automatically pulled forward from the prior year end. If you make any prior period adjustments to retained earnings, please contact National Accounting to provide details so that an appropriate adjustment may be made in FEIS.

When entries appear on Lines 105, 123 and/or 124 of Schedule B, one or both of Schedules B-1 and B-2 will be required for quarter-end months. See separate Releases on these schedules.

When entries appear on Lines 108, 126 and/or 129 of the Schedule, Schedule C will be required. See separate Release on this schedule.

Certain lines in the body of the Schedule and in the "Other Data" are the subject matter of other Releases.

Release No. 5

Data: August 2001 (previously November 1998)

## **NOTES PAYABLE (SCHEDULE B-1)**

The Summary of Notes Payable (Schedule B-1, see Appendix, Item 3), must be prepared at the end of each quarter if an entry appears in the current month column of Schedule B, Line 123 and/or 124. The information provided by Schedule B-1 is used by National Accounting to support amounts shown on the consolidated balance sheet, to calculate cash flow information used in SEC filings, to summarize obligations of the company for the annual report to shareholders and to eliminate any intercompany balances, among other uses. Therefore, complete and accurate information is of great importance.

1. Follow the detailed instructions in the FEIS User Guide on how to enter data into the FEI system.
2. Flag the names of other Stewart companies to whom notes are payable on Lines 1-10 on the top half of the schedule and the names of non-Stewart companies on Lines 11-20 at the bottom of the schedule.
3. Enter information concerning the original note amount, the date originated, payment terms, collateral, if any, and the interest rates in the columns provided.
4. Enter the note balances as of the beginning of the current year. These balances in total must agree to the Balance Sheet "Last Fiscal Year", Lines 123 and/or 124.
5. Enter the Additions (increases, new notes, etc.) and Reductions (principal payments made) in the columns provided.

**[Do not include renewals and extensions or notes rewritten for minor changes, such as changes in interest rates.]**

6. Ending balances will be calculated for you in the last column. The total Intercompany notes payable (Lines 1-10) must agree to Schedule B, Line 123. The total notes payable to Outsiders (Lines 11-20) must agree to Schedule B, Line 124.
7. The Schedule B "check" totals are displayed in the report for your convenience.

Release No. 6

Date: August 2001 (previously November 1998)

## **NOTES RECEIVABLE (SCHEDULE B-2)**

**NOTE: This Release does not apply to branch offices.**

The Summary of Notes Receivable (Schedule B-2, see Appendix, Item 4), must be prepared at the end of each quarter if an entry appears in the current month column of Schedule B, Line 105. The information provided by Schedule B-2 is used by National Accounting to provide support for consolidated notes receivable balances, to calculate certain cash flow information used in SEC filings and to eliminate any intercompany balances, among other uses.

1. Follow the detailed instructions in the FEIS User Guide on how to enter data into the FEI system.
2. Flag the names of other Stewart companies on Lines 1-10 on the top half of the schedule and enter the names of non-Stewart companies on Lines 11-20 at the bottom of the schedule.
3. Enter the original amount of the note in the space provided.
4. Enter information concerning payment terms, collateral, if any, and the interest rates in the columns provided.
5. Enter the note balances as of the beginning of the current year. The total must agree to the balance sheet "Last Fiscal Year", Line 105.
6. Enter the Additions (increases, new notes, etc.) and Reductions (principal payments received) in the columns provided.

**[Do not include renewals and extension or notes rewritten for minor changes, such as changes in interest rates.]**

7. Ending balances will be calculated for you in the last column. The total Notes Receivable must agree to Schedule B, Line 105.
8. The Schedule B "check" totals are displayed in the report for your convenience.

Release No. 7

Date: August 2001 (previously November 1998)

## **CHART OF ACCOUNTS**

The Company does not require each subsidiary (other than the branch offices of Stewart Title Company) to use a specific chart of accounts. The balance sheet and income statement format is required, however. You will find it much easier to prepare the required statements if you use a chart of accounts that puts the accounts in the same order as they will appear in the statements.

The Stewart chart of accounts has the additional feature of sub-accounts which will permit you to collect more detail than the financial statements require.

Please see the Appendix, Item 6, for the Stewart chart of accounts with a brief explanation of each major account.

## **HOW TO ANALYZE FINANCIAL STATEMENTS**

Your training and experience in accounting should qualify you to analyze and interpret financial statements of local management. The controller has a responsibility to management to perform these functions.

We encourage you to arrange a meeting with management each month as soon as possible after the preparation of the statements. Discuss the positive or negative trends that may be developing, areas for possible cost savings and/or opportunities for additional income.

Analysis and interpretive styles will ultimately be shaped in response to the needs and styles of the individual managers. The following represents a useful array of information with which to begin:

1. Explain why this month's net income is more or less than last month's net income. Also, explain why this YTD's net income is more or less than last YTD's net income.
2. In (1) above, include the reasons for any changes in revenues. Simply stating that changes in revenue occurred is not sufficient.

You will need to develop answers to questions like these:

- a. Were there more or less closings?
  - b. Were average premiums more or less?
  - c. Were there exceptionally large transactions?
  - d. Is any part of the change attributable to a rate increase? If so, how much?
  - e. Is any part of the change attributable to the addition of new customers or the loss of old customers?
  - f. Does any part of a decline result from a failure to collect reimbursable items or a failure to charge enough for these items?
3. Also explain significant changes in expenses. (Again, to explain means more than to simply point out.) The determination of what changes are considered significant is a matter of judgment.

Place your emphasis on employee costs because they are relatively large and somewhat controllable. Period-to-period changes should be explained in terms of changes in specific associates and/or departments. Period-to-period changes in the bonus element of associates costs should be explained in terms of changes in revenues and/or profits.

Significant changes in other non-employee expenses should also be analyzed. The cost percentages and the budget information included on the income statement may be useful in such analysis.

## **HOW TO ANALYZE FINANCIAL STATEMENTS**

(continued)

4. It is sometimes helpful to separate costs during your analysis into categories for review purposes:
  - a. Fixed (rent, depreciation, etc.) costs were based upon commitments and are easiest to review.
  - b. Variable (commissions, bonuses, etc.) costs are most volatile and vary proportionately with revenues.
  - c. Semi-variable (utilities, office supplies, etc.) costs have components of both a and b.

Release No. 9

Date: January 1991 (Previously January 1984)

## **INTERNAL ACCOUNTING CONTROLS**

Local management is responsible for developing and maintaining effective controls that provide (1) a basis for management decisions (i.e. reliance on accounting records), (2) a basis for accurate and timely external reporting and (3) the safeguarding of company assets. The controller must assist the manager in meeting these responsibilities.

Common elements of a good internal control structure include detailed policies and procedures to (1) control the environment (i.e. organizational structure, personnel policies, management's philosophy, etc.), (2) enable the organization to identify, assemble, analyze, record and report transactions, and to (3) ascertain that transactions are properly authorized, that there is a proper segregation of duties, adequate documentation and independent checks of accounts and records.

The Company has determined that the following four controls are required of all Stewart Title offices, no matter how **small** in size:

1. Incoming checks are to be restrictively endorsed "for deposit only" immediately upon receipt.
2. Two signatures are required on all checks in excess of a reasonable amount, the limit to be set by local management.
3. The controller is not to be a check signer.
4. All bank reconciliations must be reviewed and formally approved by the manager or their designee (who must not perform accounting functions).

Stewart Title offices should not, without the prior approval of Larry Davis, Director of Audit Services, utilize signature stamps or check signing machines for any purposes.

Once a year each Stewart office is required to answer a detailed questionnaire on internal controls sent by Houston-Audit Services. The controller should play a leading role in preparing the office's response.

Release No. 10

Date: November 1998 (previously December 1990)

### **STEWART BOOKKEEPING TEST**

National Accounting has developed a brief test, which it will send to you on request, that is useful in evaluating the technical skills of persons being considered for bookkeeping and accounting duties. Taking the test requires about thirty minutes of your applicant's time. An answer sheet accompanies the test and permits you to score the test immediately in your office. For a copy of the test, contact Kim Peterson, Manager of Financial Reporting.

Release No. 11  
Date: November 1998 (Previously January 1984)

## **CORPORATE MINUTES**

**Note: This Release does not apply to branch offices.**

Houston Audit Services collects minutes of the corporate meetings of all Stewart companies as part of its oversight and review function. The controller has the responsibility of forwarding these minutes to Houston. In many instances the controller is also the corporate secretary and can simply add Houston- Audit Services to the distribution list for the minutes. In other cases the controller will need to develop a system with the secretary to handle this.

Release No. 12  
Date: January 1984

## **CASH MANAGEMENT**

One of local management's responsibilities is to manage cash resources to meet cash needs. The controller must provide information to make management more effective and efficient in this effort. Three reports are commonly used.

**Daily Cash Report.** A Daily Cash Report is published early each business day and presents the balance in the operating cash accounts through transactions of the prior business day. To help maintain the accuracy of this report it is important to remember to (1) balance it to the general ledger account at the end of each month and (2) correct it for any items discovered in reconciling the bank account in a timely manner. An example of the form is included in the Appendix, Item 7.

**Cash Forecast.** A Cash Forecast is published monthly and presents a projection of what the cash balance will be at one or more future month ends. This helps in the planning of major expenditures, necessary borrowings, etc. Theoretically, it would be nice to include many months in the report, but as a practical matter, it is difficult to accurately project more than a few months and the information becomes less useful as it extends out. Four-month projections are considered optimum by many. This period encompasses a sufficiently lengthy period to be of value and is short enough to allow for reasonable accuracy.

Typically, cash forecasts begin with the actual cash balances at the last completed month-end. To this is added, as one line item, cash receipts expected to be generated from normal operations. This amount is closely related to expected revenues and guidance from management is critical to making this estimate. To this can be added, in detail, major and/or irregularly occurring receipts so that they can be reviewed, rescheduled, or otherwise dealt with. Cash disbursement items are generally forecast in a similar manner, the amounts from normal operations followed by major recurring and irregular occurring disbursements. An example of the form is included in the Appendix, Item 8.

**Report Card.** The Report Card consists of three parts: Cash to Houston, Delinquent Report, And Excess Cash. There are two purposes for the Report Card:

- (1) To focus an affiliate's attention on its obligations to STC General and STG, regarding the payment of debts and dividends. For example, there should be no dividends declared if any delinquent debts to STG or STC are outstanding.
- (2) To help the Executive Offices and Treasury to monitor the ability of affiliates to send cash to Houston.

Regarding part 3, Excess Cash, this form is designed to measure when an affiliate's cash position is excessive. The form permits a cash position consisting of an average of two weeks of expenses plus reserves for major capital and other anticipated cash outflows.

**CASH MANAGEMENT**  
(continued)

Any excess cash position should be applied according to the following priority:

1. Delinquent payroll (to STC payroll account)
2. STG premiums
3. Inter-company Federal income tax
4. Inter-company insurance billing
5. Inter-company bills which are not current (i.e. Landata, etc.)
6. STC loans not current
7. Dividends: No dividends should be declared unless STC loans are current; or, if the terms of the loan are "on demand" then the loan should be paid down first before any dividend is declared.

An example of this form is included in the Appendix, Item 9.

The Report Card information should be keyed into the FEI system on or before the 10<sup>th</sup> calendar day following each month end. For specific details on how to enter this data, please refer to the FEIS User Guide.

## INSURANCE

**NOTE: The ONLY companies included in Stewart's Insurance program are those of which Stewart's total ownership exceeds 50.00%, regardless of where the ownership lies. For example, Stewart Title Company may own 35.00% of Stewart Title of DEF and Stewart Title of ABC owns 20.00% of Stewart Title of DEF. [Assuming that Stewart Title Company owns 75.00% of Stewart Title of ABC, then for insurance purposes, the total Stewart ownership is 55.00%; 35.00% + 20.00%. This is unlike ownership percentages used for consolidation purposes in which the ownership would be calculated as:  $(100.00\% * 35.00)$  for a total of 35.00% +  $(75.00\% * 20.00\%)$  for a total of 15.00%, which would result in a grand total of 50.00%.]**

**In the example above, Stewart Title of DEF would be included in Stewart's insurance program since the ownership percentage by Stewart for insurance purposes is 55.00%, which exceeds 50.00%.**

National Accounting maintains property and casualty insurance policies for the Company with coverages, deductibles and other relevant information specified by top management. The primary policies are for the risks of general liability, auto liability, director and officer liability, workers' compensation, and fire and extended coverage on buildings, contents and valuable papers. Other policies dealing with various miscellaneous risks are also maintained. National Accounting maintains a booklet describing all of the coverages and claim procedures, and furnishes copies to Stewart companies once a year after renewal. You may request additional copies if needed.

The controller's role is to be aware of the coverages maintained and be alert for situations where additional or special coverage may be appropriate. Such situations should be referred to National Accounting. Examples might include the purchase of a building or moving into new leased premises or something required or inquired about by a lender, lessor or other outside party. On the other hand, routine buying or exchanging of automobiles or new office furnishings are not examples. The policies are structured to include such new or different liability risks automatically and are updated each year at renewal.

No property and casualty insurance coverages should be acquired locally without specific approval from Stewart Morris, Jr.

In many offices the controller or someone in their office has the responsibility for filing claims against the various policies. To report an insurance claim, contact the Risk Manager, Vickie Brown, at (800) 729-1900 ext. 8030, for the current procedure.

Stewart Title Company-General bills each covered Stewart company for their share of the costs of master insurance policies. The insurance billings are calculated on an annual basis and each covered year has a minimum of three different billings sent out over a period of several years. During the covered year, each company will be sent an estimated bill, which is the basis of which premiums are paid to Stewart Title Company-General. After the close of the covered year, an actual bill will be sent to the covered offices, usually within the first six months of the year following the covered year. Once the insurance company has completed the audit for the insurance policies of the covered year, the audit information is reviewed, and an audited billing is provided for the covered year. **Please note: The insurance company will continue to audit the covered year annually until all claims have closed, which may result in several audited bills being sent to the covered offices until all claims have closed.**

**INSURANCE**  
(continued)

The estimated insurance billing is calculated using the current year's insurance premiums with the previous years' risk information. The actual insurance billing is calculated using the covered years' policy premium with the covered years' risk information. The audited insurance billing is calculated using the audited information received from the insurance company.

Because Stewart Title Company-General frequently encounters delays in receiving billings for insurance from its agents, billings to the other Stewart companies may not be made until some time after the policies become effective. Where this is the case, costs for these policies must be estimated.

Example: Assume that the Stewart policy for comprehensive general liability coverage expires on August 31 each year. No billing has been received by the end of September for the current policy. You know, however, that last year the coverage cost your company \$1,200 and that the premium is a function of the square footage of premises occupied.

Your square footage occupied has not changed substantially from the prior year and you have no other reason for believing that this year's premium will differ from the prior year's. Your entries in September, then, would be:

D - Prepaid insurance (L. 120, 121 or 122, Schedule B)	1,200	
C - Other amounts payable to Stewart companies (L. 126, Schedule B)		1,200

(To record estimated cost of general liability coverage for period August 31 / August 31.)

D - Insurance expense (L. 45, Schedule A)	100	
C - Prepaid insurance		100

(To charge to expense the September portion of the cost of general liability coverage.)

**INSURANCE**  
(continued)

Now, in October, the billing for the policy is received, and because of rate changes, the amount is \$1,500 which you promptly pay. Your entries in October, then, would be:

D - Prepaid insurance	300	
D - Other amounts payable to Stewart companies	1,200	
C - Cash		1,500

(To record payment for general liability coverage.)

D - Insurance expense	127	
C - Prepaid insurance		127

(To charge to expense the October portion of the cost of general liability coverage ( $\$1,200 + \$300 - \$100 \div 11$  months))

Release No. 14

Date: August 2001 (Previously November 1998)

## **ENGAGING OUTSIDE AUDITORS**

Certain subsidiaries are required by state laws to have all or a part of their accounts audited each year by independent certified public accountants. Certain other subsidiaries choose to have such audits because of sizable minority ownership interests or for other reasons.

Because Stewart is a publicly-owned company, it is required to have an annual audit of its consolidated accounts. To improve efficiency and minimize costs, National Accounting coordinates the work of its independent accountants with that of those employed by subsidiaries to perform the audits described above. You should consult with and obtain the approval of National Accounting (Alison Evers) before engaging an independent accountant.

A comprehensive engagement letter should be used each time an independent accountant is employed. An example of the standard engagement letter is included in the Appendix, Item 16.

Release No. 15

Date: November 1998 (Previously January 1987)

## **SALES REPORT**

Please see Release No. 2 for details on what and when information must be supplied to National Accounting by your office for inclusion in the Sales Report.

The Sales Report helps Stewart management (executive, regional, district, local) assess the difficult problems faced in a cyclical, seasonal business and also shows the local manager how local fluctuations are part of broader economic movements.

The Sales Report presents comparative data for premium income and orders received. The amounts reported are arranged by region, by district, by office and for Stewart in total. The key to its usefulness to management is its timeliness. It is published two working days subsequent to the 5th, 10th, 15th and last working days of every month. Another important element is that all Stewart offices are represented.

The three statistics presented in the middle section of the Sales Report, immediately after the name of each office, represent the best estimates of (1) the number of associates at the location, (2) the amount of premium income to break even and (3) the number of orders required for the location to break even.

To calculate part (2), you simply divide the monthly expense incurred by 1000 to arrive at the amount of premium income needed to break even (Note: this is stated in thousands). To calculate part (3), divide the total in Line 47 of Schedule A (total expenses) by the number of months represented in the total. This number is your monthly expense incurred. Next, divide the total from Line 10 of Schedule A (net revenues YTD) by Line 54 of Schedule A (orders received YTD). This number represents the net revenue per order. Finally, divide the first number (monthly expense) by the second number (revenue per order), the result is the number of orders required to break even.

Reference to these amounts help the local, district, region and Houston management make better use of the data presented. Although these amounts are calculated by the FEI system, it is your responsibility to review these three statistics and report any discrepancies to National Accounting. Please contact National Accounting if you need help in calculating break-even premium income and orders.

An example of the Sales Report is included in the Appendix, Item 10.

Release No. 16

Date: August 2001 (Previously January 1987)

## **STATE / LOCAL TAXES**

Each office is responsible for knowing and complying with state and local laws. Generally, National Accounting does not file state tax returns for Stewart subsidiary companies. However, if you receive notice of a penalty or other assessment you may contact National Accounting for assistance in working with your local taxing authority.

### **State Income Tax**

#### **More than 50% Owned Corporate Affiliates in Arizona, California, Illinois, Minnesota**

Currently, SISCO files a consolidated state income tax return for Arizona, California, Illinois and Minnesota. If you are a more than 50% owned corporate affiliate doing business in these states, you will be included in SISCO's consolidated state filings. The consolidated filings are prepared by David Nicholson of National Accounting in Houston. Copies of the consolidated filings will be kept in Houston and will not be sent to you unless you specifically request for a copy.

To avoid underpayment penalties, quarterly estimated payments are being made by SISCO throughout the year for the consolidated state filings. The quarterly estimates are determined by making necessary state tax adjustments to the estimated federal taxable income for the quarter. This calculation can only be made following the closing of each quarter. Therefore, instead of monthly remittance of tax payments, you will be billed each quarter for your share of the state tax liability. Following the actual filing of the state tax returns, your quarterly billings will be adjusted to reflect the actual amount being reported on the tax returns. Any under or over remittance will be reflected in future tax billings or refunded.

#### **All Other Corporate Affiliates**

You are responsible for the filing of your state income or franchise tax returns. Note that if you do business in more than your state of incorporation, you may be required to file a state income or franchise tax return in those states as well. As mentioned under federal income tax, if you are a more than 80% owned affiliate, a copy of your federal income tax return prepared on a stand alone basis will be send to you to facilitate your preparation of your state income or franchise tax return. Note that this return will not be ready until mid September which is usually past the due date for the filing of your state tax return. You should therefore be prepared to request for an extension of time for filing. In the event that you have failed to file for an extension request, please contact David Nicholson of National Accounting in Houston. Most states accept the federal extension request which will be on file in Houston.

Note that if your state tax liability is above a certain dollar amount, you will be required to remit quarterly payments to the state to avoid underpayment penalty.

#### **All Non Corporate Affiliates**

You are responsible for the filing of your state tax returns. Caution should be taken if you are an LLC. Different states have different provisions for LLC. Some states provide a special tax form for LLC while others use either the partnership or corporate tax forms. Note that if you do business in more than your state of formation, you may be required to file a state tax return in those states as well.

### **Sales Tax**

#### **Purchases**

Sales tax relates to the purchase and/or consumption of tangible personal property and services performed. The fundamental relationship between seller and buyer is that the seller is

## **STATE/LOCAL TAXES**

(continued)

responsible for the collection and remittance of sales tax to the state where the product is consumed. The buyer, considered the 'end-user', in turn owes the tax to the seller. Therefore when you are invoiced, it will usually include an amount for sales tax. However, if the seller is an out-of-state vendor, they are not required to collect the tax from your company. However, your state is still due the appropriate sales tax, and it must be paid by your company.

For use tax purposes, you should examine your purchase policy. When you purchase tangible personal property or certain taxable services, you should be charged a sales tax unless you are purchasing the property for resale in which case you should supply the vendor with a valid resale exempt certificate. In all other situations, if no sales tax is being charged on the purchase, you are potentially liable for use tax. You should set up policies and procedures in your office that require the review of all invoices prior to approval for payment to make sure that a proper sales tax has been charged and separately stated on your invoice. If not, you should contact the vendor for correction prior to payments.

Many of you receive taxable materials from the SISCO Forms and Information Department. In effect, you are 'buying' the product from an out-of-state vendor. Also, SISCO is not a seller but simply is inventorying the materials. As a result, you will not be billed the tax from SISCO, and you must accrue. This is why the invoices from the Forms and Information Department will include a statement explaining this relationship and indicating your responsibility. When you see this, it is telling you that you must remit the tax to the proper authority in your state.

### **Sales**

For sales tax purposes, you should examine your operations to determine if your business activities are sales taxable. If yes, you should be charging your customer the appropriate sales tax unless your customer can supply you with a valid resale exempt certificate. You should also register with the appropriate state department and starting filing your sales tax reports and making the necessary remittance of sales tax collected from the customers.

Compliance typically involves the preparation and filing of forms provided by the taxing authorities and remittances of amounts due. In most cases the forms can be prepared from records readily available in your office. Certain income and franchise tax returns, however, may require copies of your federal income tax return. National Accounting files a consolidated federal income tax return which includes returns for all 80%-or-more owned Stewart companies (see separate Release). If your company is in this category you can obtain a copy of the part of the consolidated return you need from National Accounting.

### **Property Tax**

All affiliates are responsible for the filing and remittance of any state, city or local property taxes. In general, you will receive assessments of such property taxes for property you owned in the state, city or local municipalities. You should be given a chance to review the assessment and file for any protest of the assessed value of the property on which the property taxes would be levied.

Release No. 17

Date: August 2001 (previously November 1998)

## FEDERAL TAXES

### Federal Income Taxes

**Note: This section does not apply to branch offices.**

IF YOUR COMPANY IS OWNED 80% OR MORE BY STEWART:

If you are an 80% or more owned corporate affiliate, you will be included in Stewart Information Services Corporation's (SISCO) consolidated filing. This filing will be prepared by David Nicholson of National Accounting in Houston. You will be responsible for the timely completion of Schedule T's to facilitate National Accounting's preparation of the consolidated return.

Due to the complexity of the consolidated return, it is usually filed by the extended due date which is September 15 of the following year. Upon the filing of the consolidated return, a copy of your tax return prepared on a separate company basis will be send to you for your files.

In order to avoid underpayment penalties, quarterly estimated payments are being made by SISCO throughout the year. Your monthly remittance will help ensure that SISCO has the cash flow to make the necessary quarterly payments. You will receive a quarterly federal tax bill if your monthly remittance is delinquent.

The monthly payments are calculated as shown below:

Pretax income This YTD (Line 71, Sch A) .....	\$	
Less state taxes (Line 73, Sch A) .....	(	)
Sub-total .....		
Tax rate (currently) .....	X	.35
Tax liability .....	\$	
Less payments made to Stewart Title Company .....	(	)
Amount due Stewart Title Company .....	\$	

Example: Assume your March Schedule A showed pretax income to date of \$30,000 and state taxes of \$1,500.

Pretax income This YTD (Line 71, Sch A) .....	\$	30,000
Less state taxes (Line 73, Sch A) .....		(1,500)
Sub-total .....		28,500
Tax rate .....	X	.35
Tax liability .....	\$	9,975
Less payments made to date (for January and February to STC) .....		(8,738)
Amount due Stewart Title Company .....	\$	<u>1,237</u>

The amount due should be paid to Stewart Title Company (ATTENTION: National Accounting) by no later than 15 days after month-end.

Your entry at the end of March would be:

Debit - Income taxes - federal (Line 72, Sch A).....	\$1,237
Credit - Federal income tax (Line 133, Sch B) .....	\$1,237

(To record federal income tax expense for the month of March.)

## **FEDERAL TAXES**

(continued)

In making the above monthly calculation, a subsidiary should also take advantage of any loss carryforwards from prior years. Current tax law allows a company to carryback a current unused net operating loss for a period of two (2) years before the loss year in hopes of offsetting it against taxable income in those periods. For losses incurred prior to 1997, a company is allowed a carryback period of three (3) years. There are special rules for losses incurred in 1997. For tax years beginning from January 1, 1997 to August 5, 1997, use the three-year carryback rule. For tax years beginning from August 6, 1997 to December 31, 1997, use the two-year carryback rule.

If your losses exceed the income from these prior periods, you are allowed to carry the unused amounts forward (into future years) for twenty (20) years following the loss year and offset these against taxable income. For losses incurred prior to 1997, you are allowed a carryforward period of fifteen (15) years. There are special rules for net operating losses incurred in 1997. For tax years beginning from January 1, 1997 to August 5, 1997, use the 15-year carryforward rule. For tax years beginning from August 6, 1997 to December 31, 1997, use the 20-year carryforward rule.

What this means for your office is that if you have had income recently (last three years), and now are suffering losses, you may be entitled to a refund of taxes paid during those profitable years. National Accounting keeps track of this and will inform you if your office qualifies for a refund.

Otherwise, the net unused operating losses are carried forward and will be available for offset against future income. Again, National Accounting monitors this. If your office does not receive a quarterly invoice, it may be for this reason.

For the calculation of tax refunds or loss carryforwards, subsidiary corporations are generally treated as if they were separate corporations filing separate returns. Refer to the federal income tax allocation agreement for details.

Upon the filing of the actual tax return, your total remittance will be compared to your share of the actual tax liability based on the actual taxable income being reported on the tax return. Any under or over remittance will be reflected in your future tax billings or refunded. Note that in general, your taxable income will be higher than your book income due to the nature of tax laws that require current recognition of income and delayed recognition of deductions. Schedule M-1 of your tax return shows a reconciliation of your book income to taxable income.

You must meet your federal income tax obligation by providing information requested by National Accounting each year-end and by making monthly payments to Houston.

### **LESS THAN 80% OWNED CORPORATE AFFILIATE:**

Local management of companies owned less than 80% by Stewart is responsible for filing their own federal income tax return with the federal income tax authority. Tax specialists at National Accounting will research tax questions and provide advice upon request. Companies owned greater than 50% but less than 80% by Stewart are included in the combined California, Minnesota and Illinois state tax filings. Therefore, a copy of these companies' federal return should be forwarded to National Accounting for these state filing purposes no later than September 16th of each year.

Note that in order to avoid underpayment penalty, you are usually required to estimate your income tax liability on a quarterly basis and remit any tax liability due on a quarterly basis.

## **FEDERAL TAXES**

(continued)

### **NON-CORPORATE AFFILIATE:**

If you are a limited liability company (LLC) or a partnership, regardless of your percentage ownership by Stewart, you are responsible for the filing of the appropriate federal income tax return. Since a partnership return is merely an informational return, you will not be required to make any federal tax payments. Note that you are responsible for making sure that any partners or members of your partnership or LLC timely receive a copy of their respective K-1's. The K-1 shows each partner's or member's share of taxable items of the partnerships or LLC which is necessary for the partner or member for their respective income tax filings.

### **Payroll Tax**

Although Employee Services in Houston may provide services to facilitate the processing of your payroll information through ADP, you are ultimately responsible for timely remittance of federal and state payroll (employment and unemployment) taxes and any quarterly and yearly filings.

In general, each quarter you are required to file Form 941, Employer's Quarterly Federal tax Return. However, depending on your tax liability, you may be required to deposit your tax payments monthly or semi-weekly to avoid failure to deposit penalties. If your tax liability for the quarter is less than \$500, you may remit payment when you file your Form 941.

Each year, you may also be required to File Form 940, Employer's Annual Federal Unemployment (FUTA) Tax Return. The federal unemployment tax is computed on the first \$7,000 you pay each employee as wages during the year. The wage base for your state unemployment tax may be different. Usually, you can take a credit against your FUTA tax for amounts you paid into the state unemployment funds. Any FUTA tax liability should be determined on a quarterly basis and be deposited on a quarterly basis unless your liability for the quarter is \$100 or less.

You are also responsible for your state employment and unemployment tax filings and deposits if applicable. Since different states set out different rules and regulations, it is outside the scope of this checklist to go into details. You should however, familiarize yourself with your state's policies.

Finally, by January 31 of the following year, you are responsible for furnishing a completed Form W-2, Wage and Tax Statement, to each employee. Copy A of all Form W-2's are to be filed with Form W-3, Transmittal of Wage and Tax Statements, with the Social Security Administration.

For more information, you should refer to IRS Publication 15, Circular E, Employer's Tax Guide.

### **Information Returns**

Please refer to the Guide to Information Returns published by the IRS (Appendix, Item 17). This schedule provides a listing of different information returns that a taxpayer may be required to file. Note that no tax payments are associated with information returns. However, failure to file the necessary information returns or filing information returns with incorrect data do carry a penalty ranging from \$15 to \$50 per information return.

(NOTE: See Release 17 on state income taxes).

Release No. 18

Date: August 2001 (previously November 1998)

## **INTERNAL AUDITS**

The Company maintains a staff of internal auditors in Houston which report directly to the president. This group is charged with the responsibility of routinely conducting audits of Stewart operations. The auditors must receive complete cooperation and be given access to all information while performing their audits.

The typical internal audit covers both accounting and operational matters. The accounting matters usually dealt with most often include the adequacy of internal controls and the accuracy and completeness of amounts reported on the entity's income statement and balance sheet. Operational matters reviewed by the audit team include conformity with Company policies and procedures, as outlined in the Stewart Ten Standards and Manager's Manual, as well as guaranty file documentation, personnel practices and policy issuance/reporting procedures.

Exit interviews are conducted with management at the close of the audit to discuss audit issues and action items. Audit reports are typically issued during these exit interviews and management has the opportunity to respond to all issues and develop plans of action for resolution. Management's responses are included in the final audit report which is distributed to the local office manager and upper management.

Release No. 19

Date: June 1995 (previously January 1984)

## **PROFIT CENTER STATEMENTS**

Stewart operations are commonly divided into small profit center units for management purposes. A unit may be a branch office, an escrow officer and escrow assistants or some other logical structure. Where operations are set up in this manner, it is necessary that financial information be developed that measures the results of these smaller units. This information is used to evaluate the unit manager and frequently becomes the basis for part of his or her compensation.

The financial information presented is called the profit center statement. The format used for these statements is at the discretion of local management unless the profit center level data is being supplied to the FEI system. In FEIS, the format is Schedule A, the standard Stewart income statement. Where this format is used, a group of income statements is generated each month which equal, in total, the income statement for the subsidiary itself. The procedure involved in preparing these statements is, in general, to credit each unit with income generated by it and to charge each unit with its identifiable direct costs and its allocable share of all other costs in some rational, systematic and consistent manner.

The SISCO FEI system can accommodate profit center reporting. Reporting at this level is not a requirement, however, a decision on whether to report profit center level data must be made at the time that a new office is added to the FEI system.

Release No. 20

Date: August 2001 (previously January 1984)

## **ACCOUNTING FOR TITLE PLANTS & PRIOR FILES INDEXES**

The rules for accounting for title plants are formalized in Statement of Financial Accounting Standards No. 61 issued by the Financial Accounting Standards Board.

The direct costs of constructing a title plant, up to the point in time it can be used to do title searches, are capitalized. A purchased title plant, or an undivided interest in a title plant, is recorded at cost as of the acquisition date. The cost of back plant subsequently acquired or constructed is also capitalized. The capitalized costs of title plant are not depreciated or otherwise charged to income unless circumstances indicate that the value of the plant has been impaired (see Release No. 51 on impairment of long-lived assets).

The cost of updating or maintaining the plant on a daily or other frequent basis is expensed as incurred along with the cost of making title searches. Costs incurred to modernize or modify a title plant which is seen as infrequent and beneficial to future periods may be expensed or separately deferred (i.e., recorded as an "other asset"), but not added to the carrying value of the title plant. If you elect to defer such costs, you should amortize the cost over an appropriate period of time, generally five (5) years or less.

Sales of title plants are accounted for as follows:

1. If an undivided interest in the plant is sold, the sale is reported in the income statement, less a pro-rata portion of the cost of the plant;
2. If a copy or a right to use the plant is sold, the sale is reported in the income statement at the amount received, i.e., no cost is ordinarily allocated to the sale; and
3. If the plant is sold outright and completely, the sale is reported in the income statement net of the cost of the plant.

### **Prior Files Indexes**

The Company is automating prior files indexes in various states throughout the country. The necessity for these indexes arises because these policies are not kept in a form that will allow easy access to the records and the company is incurring additional costs to "re-examine" the related property. The indexes serve as starter files that can be used when the related property is involved in a subsequent sale, etc.

A title plant (according to FAS 61) must be a historical record of all matters affecting title to parcels of land in a particular geographic area. Since prior title insurance contracts and reports do not constitute a historical record of all matters affecting title, the prior files index does not meet the definition of a title plant. However, the prior files indexes will be operating assets with future economic benefits (reduced examination costs on policies with a prior file) and would qualify for capitalization as an "other asset". Capitalizable costs primarily include labor costs, hardware, and software costs. These "other assets" should be amortized on a straight-line basis over a period not to exceed five (5) years.

The cost of maintaining the prior files index on an on-going basis, once it has been placed in service, is expensed as incurred, similar to the accounting treatment with regard to maintaining a title plant.

Release No. 21

Date: November 1998 (previously December 1990)

## **RECOGNITION OF TITLE PREMIUM REVENUES**

Title companies in certain regions of the country credit revenue at the time they issue a commitment. Stewart's accounting policy is to delay the credit to revenues until the closing. Stewart believes that recognizing revenues at the time of the commitment is an inferior method of accounting for the following reasons:

1. Stewart believes that a title company is a part of a revenue process that is not complete until the real estate transaction itself is closed. Typically, the parties to a real estate transaction are not paid unless there is a closing. This includes not only real estate agents, for example, but also title agents.
2. Stewart also believes that the "conditional" liability assumed with the issuance of the commitment and the additional work required of a title company after the commitment is issued are factors in favor of delaying revenue recognition until the closing.
  - A. The commitment does obligate the title company to issue its policy, but it is subject to conditions such as a closing will take place and that appropriate deeds and other "evidence satisfactory to" the title company will be prepared. Also, exceptions listed in the commitment may require curative work preparatory to a closing. Finally, the commitment expires in six months.
  - B. The title company performs additional work and incurs costs after issuing its commitment, such as the check down of title, work in clearing the title and exceptions, typing policies and, in many areas, closing the title. Additional revenues received for such post-commitment work may be relatively small. Thus, those expenses may not be properly matched with revenues if revenues are recognized when the commitment is issued.
3. Experience indicates that a material number of transactions with commitments outstanding are never closed, or if so, they are closed after the six-month period of the commitment. The rate of cancellation may be 10%, 15%, 20% or more. Local and national economic conditions often change the rate of cancellation, and do so frequently. Companies which attempt to guess at the number of future cancellations included in the commitments they are recording as this month's revenues may base their guess on prior experience, but it remains a guess.
4. Finally, experience leads us to believe that recognizing revenue at the time of the commitment does not reflect the economic reality of a real estate transaction. Companies using the method frequently report extremely large revenues and profits, but the corresponding cash realized from such revenues is not received until significantly later. Companies may not have sufficient cash flow to finance their operations, may over pay profit bonuses and experience similar problems created by this method.

Release No. 22

Date: November 1998 (previously December 1990)

## **RETAINED EARNINGS - BEGINNING AND ENDING BALANCES**

The amount shown on Schedule B as beginning retained earnings for this year is automatically populated in the FEIS database using the amount reported to National Accounting on Schedule B as ending retained earnings from last year (December 31 for calendar year-end offices).

Because the amount you reported as ending retained earnings was used as part of the consolidated ending retained earnings, you cannot change your beginning balance without creating an imbalance in consolidated retained earnings.

Ask your auditors (if applicable) to make all of their proposed adjustments, including income tax provisions, so that the adjustments can be included in the final statement you authorize National Accounting to use in the consolidation at year end.

**If an adjustment is absolutely required after you have cleared National Accounting (and such adjustments should be rare), then you should call either Alison Evers (ext. 8036) or Kim Peterson (ext. 8041) in National Accounting.**

Release No. 23

Date: August 2001 (previously November 1998)

## **ORGANIZATIONAL CHART**

The controller should assist local management in meeting its responsibility to keep the organizational chart updated and stored in the FEIS system. See the FEIS User's Guide for specific instructions. Each organizational chart should show lines of authority, the number of people reporting to each supervisor and the name and job title of each person employed by the company.

## **QUARTER AND YEAR-END CLOSING INSTRUCTIONS**

As a publicly-owned company, Stewart issues quarterly and annual reports and proxy statements to its shareholders and the Securities and Exchange Commission. The end of each quarter triggers a chain of events that requires cooperation and planning by many people. Management, lawyers, accountants, writers and others from within and outside the Company participate. You are an important part of the process because the Stewart subsidiary controllers supply much of the basic financial data.

Quarterly closing packages are not distributed by National Accounting. See the Appendix, Item 5, for copies of these schedules. Schedules B-1, B-2 and C should be entered directly into the FEI system. All other schedules are available in spreadsheet form. Contact Kim Peterson for the spreadsheets.

Before each year-end, usually in November, National Accounting sends year-end closing instructions to all Stewart subsidiaries. In general, these instructions indicate the deadlines, details and the format for data required. These will consist primarily of the information necessary to prepare consolidated financial statements, footnotes to consolidated financial statements and to comply with requirements of the Securities and Exchange Commission. Information necessary to prepare the consolidated federal income tax return is also requested.

Upon receipt of the instructions, the subsidiary controller should read the requirements and contact National Accounting if they are not clear. They should then begin arranging their scheduling to meet the deadlines. This may involve special coordination of the work of subordinates, outside accountants and perhaps others. Controllers often find that a great deal of the work of organizing and setting up can be done in advance and usually results in a less harried closing.

Release No. 25

Date: August 2001 (previously November 1998)

## **CAPITALIZATION OF FIXED ASSETS**

Generally accepted accounting principles require that amounts expended for tangible items used in operations be recorded as assets if they can be expected to provide economic benefits to the Company for more than a year. Such items commonly encountered in the title insurance business include desks, chairs, typewriters, copy machines, automobiles and leasehold improvements.

Items meeting this description but which cost less than \$500 should be charged to appropriate expense accounts. Their minor values do not justify the maintenance of asset records. General Supplies is an account frequently used for these items.

In applying the above rule, you should not expense items which are an integral part of a unit if the unit exceeds \$500. For example, if you bought a "unit" of eight chairs and a table for your board room costing over \$500 in total, but below \$500 individually, you should not expense such items. Please use judgment in these areas.

An exception to the \$500 rule is permitted for subsidiaries with net revenues of less than \$500,000 for the previous calendar year (per Line 20, Schedule A). Such subsidiaries may lower their capitalization limit to \$200 each. Offices with net revenues exceeding \$5 million may increase the capitalization limit to \$1,000.

Finally, some items that meet the criteria above for capitalization must be capitalized when they are being used under leases. In general, this is the case when the lease includes one or more of the following features:

1. Ownership of the item transfers to the lessee at the end of the lease term;
2. The lessee has the option of buying the item for a "bargain" price;
3. The lease term is as much as 75% of the economic life of the item;
4. The present value of the lease payments is as much as 90% of the fair value of the item.

If you have questions concerning whether a particular lease qualifies for capitalization or how to prepare entries to account for such leases, please contact Kim Peterson (ext. 8041) in National Accounting.

Items that are capitalized appear on Lines 114, 115 and 117, as appropriate on Schedule B, the balance sheet.

Fixed assets should be reviewed periodically for impairment (i.e., missing, damaged, obsolete) as required by Statement of Financial Accounting Standards No. 121. See Release No. 51 which discusses this requirement.

Release No. 26

Date: August 2001 (previously November 1998)

## **DEPRECIATION**

The depreciable base of property and equipment items must be charged to expense over the estimated economic life of the items. The depreciable base is equal to the original cost of the item less an estimate of what the Company can expect to receive as salvage value for the item upon disposition at the end of its economic life. The estimated economic life is the period of time management estimates that the item will be used in the Company's operations. This is not the physical life of the asset and such factors as expected wear and tear, obsolescence and inadequacy must be considered (see Release No. 51 on impairment of long-lived assets).

Depreciation expense should be calculated using the straight-line method. That is, the depreciable base should be divided by the economic life expressed in months and the resulting amount should be charged to expense each month until the depreciable base is exhausted or the asset is disposed of, whichever comes first. When depreciation expense is recorded the credit side of the entry is to accumulated depreciation. Useful lives of assets should follow these general guidelines:

Furniture & fixtures:

Personal computer	- 3 years
Computer (CPU, drives & mainframe attachments)	- 3 years
Computer (CRT, printers & modems)	- 3 years
Software (purchased from LDI, LDI subsidiaries or non-Stewart companies)	- 3 years
Office equipment	- 5 years
Furniture & fixtures	- 5 years
Automobiles owned	- 3 years
Leasehold improvements	- Life of lease
Buildings	- 30 - 40 years

Land and title plants are not depreciated.

Depreciation expense appears on Line 36 of Schedule A, the income statement, and accumulated depreciation appears on Lines 116 and 118, as appropriate, of Schedule B, the balance sheet.

Release No. 27

Date: August 2001 (previously November 1998)

## INTERCOMPANY TRANSACTIONS

Stewart companies must record transactions and maintain balances at each month-end accounting period which agree with the corresponding amounts recorded by other Stewart companies with which they do business. If they do not, errors will occur in the consolidated financial statements. For example, assume one Stewart company records revenue of \$30,000 from another Stewart company, but the latter company erroneously does not record an expense for the transaction. Unless the error was subsequently caught, consolidated pretax income would be overstated by that amount.

The following line items on Schedule A (income statement) and Schedule B (balance sheet) are likely accounts to be affected by intercompany transactions. These items are discussed in separate releases.

<u>Schedule</u>	<u>Line</u>	<u>Line Description</u>	<u>Release</u>
A	1	Title insurance fees	29
	11	Interest income	30
	5	Guaranty premiums	31
	6	Reinsurance	32
	29	Losses-escrow, etc.	33
	45	Insurance	14
	55	Interest expense	30
	72	Income taxes-federal	18
B	105	Notes receivable	30
	123	Notes payable	30
	125	Premiums payable to STG	31
	128	Policy losses payable	33
	133	Federal income taxes payable	18

The following line items are also often affected by intercompany transactions. Since the intercompany problems encountered with such items are not dealt with in other releases, comments are included below:

1. Other (gains, etc.) – revenue. Schedule A, Line 12. A Stewart company may sell a fixed asset to another Stewart Company. The accounting for the transaction must be the same (yet in reverse) by both seller and buyer (i.e. the seller eliminates the asset cost and accumulated depreciation while the buyer records the same cost and depreciation value on their books). **Note two important points:**
  - (a) Cash should equal the net book value of the fixed asset resulting in no intercompany gains or losses; and
  - (b) The consolidated asset and accumulated depreciation values are unaffected by the transaction.

Finally, the asset should be depreciated over the remaining useful life, as previously established by the seller.

## **INTERCOMPANY TRANSACTIONS**

(continued)

2. Salaries, etc. Schedule A, Lines 21-27. Salaries, bonuses, payroll taxes, group insurance and other costs flow to most Stewart companies through the Houston central payroll system. This is simply an administrative device. These do not represent intercompany transactions.

Accruals of these items, where necessary, should be credited to regular accrual or payable accounts and not to the intercompany payable accounts, unless some formal arrangement has been made for another Stewart company to lend the money. Where this latter situation is the case, the accounting discussed under Interest Income (Release No. 30) will apply.

3. Computer - LDI. Schedule A, Line 32  
Rent - title plant - Line 38  
Business promotion, advertising - Line 41  
General supplies - Line 52

Many Stewart companies acquire computer services from Landata, Inc., some rent their title plants from another Stewart company and others acquire advertising materials or various supplies from a related company. In accounting for these and similar dispositions and acquisitions of goods and services in the normal course of business, the standard rules of accrual basis accounting should be followed.

For example, if your company obtains \$1,000 of services in the month of April from Landata, Inc. and you have not paid for it, the expense should be recorded in April by a charge to Computer-LDI, Line 32 on the Schedule A income statement, and a credit to Accounts Payable to Landata, Line 129 on Schedule B balance sheet. As is the case with all payables, an estimate (agreed to by LDI) of the expense may be necessary if a billing is not received by the deadline for closing the books.

If your company sells materials or supplies that have previously been charged to expense to another Stewart company, you should credit the same expense account at the time of the sale and charge Receivable from other Stewart companies, Line 108 on the Schedule B balance sheet.

4. Receivables-other Stewart companies, Schedule B, Line 108. This account is charged with all amounts due from other Stewart companies that have not been reduced to a promissory note. Examples are noted in some of the captions above. In order for proper eliminations to be made in the SISCO consolidation, it is imperative that all intercompany receivables be itemized on Schedule C.
5. Investments-affiliates, Schedule B, Line 111. This account is charged with the amounts of capital investments made in other Stewart companies. When more than half the outstanding stock of another company is owned, consolidated statements should be prepared. Interests of 20% to 50% in affiliated companies should be accounted for by the equity method. Please contact National Accounting if you have questions about accounting for the investment in and income from affiliated companies.

## **INTERCOMPANY TRANSACTIONS**

(continued)

6. Other amounts payable to Stewart companies, Schedule B, Line 126. This account is credited with all amounts due to other Stewart companies that (1) have not been reduced to a promissory note or (2) do not have a line dedicated for their use, such as the lines, Premiums Payable to Stewart Title Guaranty, Line 125 on the Schedule B balance sheet and Payables to Landata, Line 129 on the Schedule B balance sheet. As with intercompany receivables, amounts payable to other Stewart companies must be itemized on Schedule C.
7. Dividends. Schedule B, Line 141. Dividends are recorded when declared by the board of directors by a debit to the Dividends Account, Line 141 on the Schedule B balance sheet. The portion of the dividend that is payable to another Stewart company should be credited to Other Amounts Payable to Stewart companies, Line 126 on the Schedule B balance sheet. The balance of the dividend should be put on one of the miscellaneous liability lines, Lines 130-132 on the Schedule B balance sheet and labeled "Portion of Dividend Payable to Outside Interests".

Release No. 28

Date: August 2001 (previously November 1998)

### **"SPLIT" TITLE INSURANCE PREMIUM REVENUES**

Title insurance premium revenues may be "split" between title companies when a buyer and seller reside in one county and the property lies in another, and in other cases, one Stewart company may handle some parts of the transaction and another the rest. Assume, for example, that your company conducts the closing and issues the policy but another Stewart company performs the title search and examination. Pursuant to the arrangement, the other Stewart company is to receive 60% of the premium. Your company should record the receipt of the premium from the customer in the usual manner. The payment of the 60% to the other Stewart company should be charged to Title insurance fees, Line 1 on the Schedule A income statement. Some companies choose to put these payments in a separate sub-account, and the Stewart standard chart of accounts provides for this (see Release No. 8). If your company is the recipient of a title insurance premium split, you should credit Title insurance fees, Line 1 on the Schedule A income statement.

It is important when your company records a receivable or payable involving another Stewart company that you ascertain that the other company has booked a corresponding entry in the same accounting period.

## **INTEREST INCOME AND EXPENSE**

Interest income and interest expense should be accrued monthly. Recording interest on a cash basis is not acceptable unless the amounts are minor. Interest on intercompany loans should be accrued monthly in the same amount by the lender and the borrower.

Please call National Accounting each quarter-end and agree any intercompany loan balances you may have with Stewart Information Services or Stewart Title Company-General, whichever applies.

When payments of less than the full principal and interest due are made on a note, the payment should be applied first to all interest due and then to principal. Where more than one note relationship exists between the parties, these same sequencing rules are followed but the payment is first applied to the oldest note if the payment more than liquidates all unpaid interest.

Where intercompany notes have no stated interest rates or are stated to be non-interest bearing, no imputation of interest should be made in the accounts even though generally accepted accounting principles might call for doing so.

### **DETAILED EXAMPLE: HOW TO ACCRUE INTEREST**

An example of how to calculate accrued interest, particularly as it applies to intercompany loans, follows. Assume that your company borrows \$10,000 from another Stewart company on April 10. The borrowing is evidenced by a note that bears interest at 12% and is payable upon demand. On April 10 you should record a debit to Cash, Line 101 on the Schedule B balance sheet and a credit to Notes payable, Stewart companies, Line 123 on the Schedule B balance sheet, both for \$10,000. Add details of the note to Schedule B-1, Summary of Notes Payable. (If your company were the lender, your debit would be to Notes receivable, Line 105 on the Schedule B balance sheet with appropriate details supplied on Schedule B-2, the Summary of Notes Receivable.)

Assuming that no payments of either principal or interest are made in April, interest expense should be recorded at April 30. Interest is equal to the principal balance times the interest rate times the period of time ( $i = prt$ ). In our example the principal is \$10,000, the rate of interest is 12% and the period of days of out 360 is 20/360 (April 11 - April 30) so that interest expense for April would amount to \$66.67. This amount is recorded by a debit to Interest expense, Line 55 on the Schedule A income statement and a credit to Other amounts payable to Stewart companies, Line 126 on the Schedule B balance sheet. Note that the credit is not made to a note payable account. (Again, if your company were the lender, your debit would be to Receivables from other Stewart companies, Line 108 on the Schedule B balance sheet, and your credit would be to Interest income, Line 11 on the Schedule A income statement.)

Release No. 30

Date: August 2001 (previously December 1985)

## **UNDERWRITING (GUARANTY) FEES**

This Release discusses the appropriate accounting for the underwriting fees paid to Stewart Title Guaranty Company.

The key accounting issue is matching the guaranty fee with the related revenues from the issuance of policies in the same month. The starting point is the recording of revenue for policies issued. Release No. 22 discusses the appropriate time to do this. The recognition and recording of the premium revenue triggers two events:

1. The policy issued must be reported to Stewart Title Guaranty Company, and
2. The related underwriting fee must be recorded in the books of account.

Reporting to the underwriter is typically done in one of two ways. The first, a manual method, involves listing each policy on a register as the policy is issued. At the end of each month, the register is totaled and mailed to Stewart Title Guaranty Company with a check for the underwriter's fee. This amount then becomes available for you to use in the accounting records.

The second system now in use involves the title agent simply accumulating copies of the policies as they are issued and monthly or more frequently sending them to Stewart Title Guaranty Company. The policy copy must reflect all premium charges and the net portion that belongs to STG (in some states property type, county codes and risk rates are also required). Agency Accounting will then process the policy copies and bill the agent. The billing will consist of a statement copy and a register that details all policies and premiums processed. Stewart companies should not wait to receive the bill but should instead pay the amount owed (estimated if necessary) to Stewart Title Guaranty Company, recording the amount as the expense on its income statement.

The third method is the use of electronic policy reporting. This method involves entering the policy information described above into a program which can then be downloaded to electronic media and then forwarded to Stewart Title Guaranty Company (on tape or diskette via U.S. mail or by e-mail). There are several electronic options, including the AIM products, PCR+ and other programs generated in a title agents' office that are compatible with STG systems. The policy copies are forwarded to Agency Accounting along with a hard copy of the transmittal register of the electronic report for verification and auditing purposes. For more information on electronic reporting, contact Sandra Zoppe (x. 8281) in Agency Accounting.

The entry to record underwriting fees is a debit to Guaranty premiums, Line 5 on the Schedule A income statement, and a credit to Premiums payable to Stewart Title Guaranty, Line 125 on the Schedule B balance sheet.

Note that if you issue policies for any underwriter other than STG, an additional breakout of premiums to underwriters is required reporting at each month end. The schedule is included in the FEIS web site in the monthly input schedules directory.

Release No. 31

Date: May 2001 (previously November 1998)

## **REINSURANCE**

Title insurance companies sometimes issue policies for amounts in excess of a limit either self-imposed or set by state insurance authorities based on the amount of statutory net worth of the underwriter. Stewart maintains a maximum self-imposed single risk retention limit of \$100 million; \$100 million on multi-property transactions issued on one policy with appropriate approvals. When this occurs, it becomes necessary for the underwriter to reinsure this excess risk with one or more other title insurance issuers.

EXAMPLE: XYZ Underwriter, Inc. is domiciled in Texas and has a net worth of \$50,000,000. Under Texas law this net worth entitles it to accept the risk for policies of up to \$25,000,000. XYZ and its agents may issue policies for amounts in excess of \$25,000,000, but when they do, other title insurance underwriters must be paid to assume the portion of the risk that exceeds \$25,000,000.

If reinsurance is obtained, Stewart Title Guaranty Company may retain an extra \$20 million on a tertiary level, subject to state laws and appropriate approvals.

The controller may or may not be involved in the steps leading toward the obtaining of reinsurance. Stewart agents are instructed to notify Lynne Demarest in the reinsurance section of National Title Services (NTS) in Houston as soon as it appears that a policy in excess of the reinsurance limit will be issued. The lead time is necessary to contact other underwriters, solicit their interest, inform them of the details of the risk and so on. Considerable coordination between the agent and NTS ensues as the transaction comes into focus.

Underwriting agreements between Stewart Title Guaranty Company and its agents typically provide that the cost of obtaining reinsurance shall be shared between them. You should record the cost of reinsurance in the same month you record the revenue from the related policy. An estimate of this cost may be required to close the books if no billing has been received from NTS. The cost should appear on Line 6 of the income statement on Schedule A and the credit, if the reinsurance has not been paid for, should appear on Line 126 of the balance sheet on Schedule B. It represents an intercompany payable and should be itemized on Schedule C.

Release No. 32

Date: August 2001 (previously November 1998)

### **LOSSES - ESCROW, ETC.**

The line item, Losses-escrow, etc., on the income statement on Schedule A, is used to account for losses arising from escrow and policy-issuing matters. These losses in a title agency come about in one of two ways. The first is the result of errors made in the closing process where it is decided that it would be inappropriate to go to the parties to the transaction for additional funds. These losses will usually be minor in amount. The second way in which losses arise is through the operation of the contract between the title agency and the title insurance underwriter. Underwriting agreements between Stewart Title Guaranty Company and its agents typically provide that the cost of defending and settling certain claims against the policies shall be shared on some basis. The procedures used in the National Legal Department when a claim arises, whereby the office is sharing the responsibility, is to bill the office for 100% of the loss adjustment expenses (attorneys' fees, etc.) as they are incurred. When the claim is actually settled, all costs, including the adjustments, are reviewed. The office is responsible for 50% of the total loss if it is determined that the office was negligent. The National Legal Department prepares the final invoicing to close out the claim and equitably spread the cost involved.

Accounting for the first category of losses is generally simple. Because they are usually minor in amount they can be accounted for on the cash basis. Typically, an escrow officer will request a check to be made payable to the escrow account to cover the shortage. The check should be charged to Losses-escrow, etc., Line 29 on the Schedule A income statement. In addition, someone in the accounting department should scan a trial balance/open file listing of the customer escrow accounts each month to ascertain that some appropriate resolution is being made of any debit balances. A large debit balance may indicate a serious problem.

Accounting for the second category of loss is more complicated. These should be recorded when it (1) becomes probable that a loss has been incurred and (2) the amount can be estimated with reasonable accuracy. The amount recorded should be your best estimate of the loss, net of recoveries. If only a range can be estimated, at least the minimum amount of the range should be recorded. A file of claims against policies issued by your company should be maintained and a status report should be obtained at least quarterly from the NCC in the National Legal Department who is responsible for the claims. When the conditions for recording the claims are met, a debit should be made to Loss-escrow, etc., Line 29 on the Schedule A income statement for the estimated total amount for which you expect your office to be liable. The credit should be to Policy losses, Line 128 on the Schedule B balance sheet. Any amounts accrued on Line 128, for which your office has received an invoice from the STG National Legal Department, should also be shown on Schedule C.

Finally, some Stewart-owned title agencies follow a practice of recording the losses related to escrow and policy-issuing activities by regular monthly charges based on a percentage of revenues. This practice should only be carried out by companies which clear this procedure with National Accounting (see separate Release 45).

Release No. 33

Date: August 2001 (previously November 1998)

## BONUSES

Many Stewart companies provide part of an associate's compensation in the form of bonuses. Stewart bonuses are typically based on the pretax income of the segment of the business for which the person receiving the bonus is responsible.

The primary problems in accounting for bonuses are to (1) fully understand the terms of the bonus arrangements and (2) accruing the costs in the appropriate accounting periods.

Bonus plans for company officers should be fully described in the minutes of the board of directors. Bonus plans for other associates should also exist in written form and be controlled by the manager.

Rules for recording bonus costs in the appropriate accounting periods might be summarized as follows:

- 1 YTD expense should always represent the amount earned to date by the bonus recipient and the expense for the month should be the difference between the current month YTD expense and the prior month YTD expense.
- 2 YTD expense not be a negative (credit) amount, neither in total nor as to any individual.

Example: Assume that a manager is to receive a bonus of 5% of pretax income of the company and the payment is to be made in February of the subsequent year. Assume further that pretax income amounts are a loss of \$12,000 in January, income of \$8,000 in February, and income of \$16,000 in March. Entries to account for bonus expense would be:

January:		
	(None)	
February:		
	(None)	
March:		
	D-Bonus expense (line 22, Sch A)	600
	C-Bonus payable (lines 130-132, Sch B)	600

To record bonus expense for the month (YTD earnings x 5%)

**BONUSES**  
(continued)

Some bonuses that are a function of income present the circular problem of not knowing what bonus expense is until income is known and not knowing what income is until bonus expense is known. This problem can be solved algebraically using the following formula:

$$\frac{\text{Pre-tax income before bonus} \times \text{Bonus \%}}{1 + \text{Bonus \%}}$$

Example: An individual is to receive a bonus of 5% of income before taxes. Income before tax and before calculation of the bonus is \$100,000. Calculate as follows:

$$\frac{\$100,000 \times .05}{1.05} \\ = \$4,762$$

Bonus expense, regardless of the basis used for its calculation, should not be presented on line 25 of the Schedule A income statement. Use of that line is limited to the cost of qualified profit sharing associate benefit plans.

## GOODWILL

Most Stewart companies do not have goodwill balances. If goodwill arises in your company, please contact Kim Peterson in National Accounting.

Like all intangible assets, goodwill is only recorded as part of the purchase of an affiliate. It is the amount by which the purchase price of an acquired company exceeds the fair market value of its net assets. Purchased goodwill is presented on Line 119 of the balance sheet on Schedule B.

**NOTE: In July 2001, the FASB issued Statements 141 and 142 which include substantial changes to the accounting treatment of goodwill. We will update this release in the near future to provide for these changes. In the meantime, please contact National Accounting with any questions you might have.**

Release No. 35

Date: August 2001 (previously November 1998)

## ESCROW FUNDS

Many title agencies maintain escrow or trust bank accounts in which they hold buyer and/or lender funds until they are disbursed at closing. Although the accounts involved do not appear in the financial statements of the title agency, detailed and timely records must be maintained.

The escrow accounting system involves only two control accounts so that, when the double-entry method is employed, every transaction will affect both accounts. An escrow account is commonly opened by the parties to a proposed real estate transfer delivering an earnest money or escrow agreement to the title agency. The agreement will normally provide that the prospective buyer put up an earnest money deposit and, where the title agency is to be the escrow agent, this deposit accompanies the agreement and is turned over to the title agency. On receipt of these materials, a file is established and the earnest money, usually a restrictively endorsed check, is routed to the accounting department with a note as to the file number assigned.

The accounting department deposits the earnest money received into an escrow bank account and makes this entry in the escrow accounting system:

D - Cash	x,xxx	
C - Customer account		x,xxx

As the real estate transaction progresses, additional funds will be provided by the buyer and, in many cases, a lender. These, too, are deposited into the escrow account with entries like the one shown above. Finally, amounts will be disbursed from the account at closing (or later, if there are complications) and the entries will be the reverse of that shown above. The customer account will be debited and the cash account will be credited.

While nothing could be simpler in theory than an accounting system with only two control accounts, complications can and do arise. On the asset side of the ledger, the aggregate cash is commonly put in numerous bank accounts and/or investments. Most title agencies with a substantial amount of escrow business prefer to maintain the funds in more than one bank. Furthermore, customers who are being required under the terms of their earnest money contracts to put up substantial sums of money for lengthy periods may ask that their money be invested for them. Separate subsidiary accounts must be maintained for each bank account used and each investment established. On the credit, or accountability side of the ledger, each file becomes a subsidiary account.

The overriding complexity of the escrow accounting system is that there are often numerous relatively small transactions going through the system, and exact, rather than reasonably accurate records, must be kept.

A proper system will, by at least the end of each day, show the amounts in each bank account, each investment and each customer account. Furthermore, the sum of the first two must always equal the sum of the customer files. Bank statements should be reconciled to the book general control records promptly upon receipt each month. Any errors should be corrected and unusual items investigated. Someone should be assigned to periodically review the open file listing of customer files for debit balances and items that have been inactive for long periods of time. All such items noted should be investigated.

**ESCROW FUNDS**  
(continued)

Individual reconciling items should be noted on the bank reconciliation by file number. No accumulation of these items should be made. All reconciliations must be reviewed and initialed by the manager each month. Additional accounting controls to be followed:

1. Escrow cash must not be co-mingled with operating cash.
2. All disbursements out of escrow accounts with balances outstanding more than six months must be properly approved.
3. Any imbalances between escrow detailed records and general ledger control accounts, and any debit balances in escrow accounts, should be corrected promptly.
4. Escrow funds must not be disbursed before the "good funds" required to cover such disbursements have been received.

**Please also refer to the current ALTA guidelines on the handling and safeguarding of escrow funds which are included in the Appendix, Item 15.**

## **BORROWING FROM HOUSTON**

In certain instances Stewart companies use the Houston-based Stewart companies as a source of debt financing. This may be accomplished by direct loans, some form of debt guarantee, or both. The Stewart office controller is often involved in this activity.

The controller should assist management in avoiding the need for borrowing on an emergency basis. Carefully prepared cash projections are essential. See Release No. 16. Direct or indirect borrowings from Houston are like borrowings from any other source, in that time must be allowed for appropriate approvals to be obtained and financial reporting must be current. Generally, a signed note must be on hand in Houston before a loan will be funded. Accounting procedures for intercompany borrowings are discussed in Release No. 28.

No Stewart company shall lend money, commit to lend money, borrow money, commit to borrow money, purchase a note or commit to purchase a note without the prior approval of the executive committee of Stewart Title Company - General.

Release No. 37

Date: November 1998 (previously September 1984)

## **BAD DEBT EXPENSE**

In some geographical areas in which Stewart companies operate, the title company collects its premiums and fees subsequent to the appropriate time for recognizing the revenue (see Release No. 22 regarding the recognition of revenue). This situation creates trade receivables and the accounting problem of evaluating their net realizable value.

Proper accounting seeks to record bad debt expense as accurately as possible in the same accounting period as the related revenue. The difficulty, of course, is it may take several months before it is known which receivables are ultimately uncollectible. Because of this, estimates must be made. The best way of making these necessary estimates, in the case of trade receivables, is to base them on historical results, judgmentally adjusted for such factors as current economic conditions, any changes in credit granting policy and so on.

Please keep in mind that current tax law states that we are allowed a tax deduction for a debt or receivable that you determine to be wholly or partially worthless, thus presumably a candidate for being written off, not for the monthly accrual of expense. As a result, try to avoid overstating your reserve due to an arbitrary system of accruing for bad debt, yet continue to obtain good coverage. Our goal is to keep these reserves for bad debt as low as possible, while at the same time, fairly stated.

Sub-accounts should be set up for bad debt expense as follows:

### 3700. Bad debt Expense (Schedule A, Line 49)

- a) 3700.xx Monthly bad debt accrual - not tax deductible
- b) 3700.xx Amounts completely written off or specific accounts reserved - tax deductible

Recoveries - Amounts later collected on expensed amounts should be credited to the same bad debt expense account that it was originally expensed through.

Example: At the end of a year a Stewart company reviewed its records for the past few years and determined that it had written off as uncollectible 1% of its credit sales each year and that the percentage seemed to be growing a little each year. With this as a basis, the company might decide to charge to expense 1.25% of its credit sales each month in the next year. The appropriate monthly entry would be:

D - Bad debt expense [(a) above]	xxx
(Schedule A, line 49)	
C - Doubtful receivables	xxx
(Schedule B, line 109)	

**BAD DEBT EXPENSE**  
(continued)

As accounts receivables are determined to be definitely uncollectible, they should be written off against the allowance so established. The appropriate entry is:

D - Doubtful receivables	xxx	
C - Trade accounts (Schedule B, line 106)		xxx

and

D - Bad debt expense [(b) above]	xxx	
C - Bad debt expense [(a) above]		xxx

Periodically, or at least once a year, the historical results should be updated to see if an adjustment in the bad debt percentage is necessary. For accounts receivable which have not been set up in doubtful receivables, which are determined to be definitely uncollectible, a direct write-off entry can be made:

D - Bad debt expense [(b) above]	xxx	
C - Trade accounts		xxx

\* \* \* \* \*

Stewart companies may also have bad debt considerations of a different sort. Some subsidiaries make loans which are evidenced by notes or notes may be taken in connection with a loss. These note receivables do not lend themselves to the statistical approach discussed above and require some good accounting judgment. Again, the objective is to state the note at its expected net realizable value.

The portfolio of notes receivable should be reviewed with management before the preparation of each quarterly financial statement. Some accountants have a tendency to defer these considerations to the end of the year but, because of the importance of the published interim statements, this should not be done. Notes receivable balances should be reviewed at each month-end and if evidence exists that a note will not ultimately be collected in full, a bad debt reserve (or write down) must be recorded. Good judgment cannot be prescribed and the facts of each case differ, but the following points should be considered:

- History of payment on the note
- Solvency of debtor
- Collateral adequacy

**BAD DEBT EXPENSE**  
(continued)

The journal entries involved are the same as those described above to account for bad debts associated with trade receivables. Bad debt expense is charged with the estimated loss and the doubtful receivables account is credited. When the account or note becomes definitely uncollectible, it is charged off against this allowance.

Finally, bad debt provisions may be necessary on guarantees of indebtedness. These guarantees are sometimes made on behalf of third parties. If a loss is likely as a result of such an arrangement, it must be recorded as soon as this determination is made. Evaluation of these situations is often overlooked because they do not appear anywhere in the accounts.

## **BANK RECONCILIATIONS**

Title companies have large numbers of transactions involving cash and, of course, cash is attractive to someone with a view toward theft. For this reason and others, proper procedures for reconciling both operating and bank accounts must be followed.

The bank reconciliation is an excellent control because it gives the company an opportunity to compare its records with an independently-kept record of the same transactions. The reconciliation should be prepared as soon as possible after the bank statement and supporting items are received. On the other hand, the preparation and publication of financial statements should not be delayed in order to prepare the bank reconciliation, unless there is some reason to believe a material adjustment of the accounts will result therefrom.

To best take advantage of the control opportunities provided by bank reconciliations, the reconciler should be someone not involved in either the handling of cash or the accounting for cash. This is difficult in a small company, however, and frequently the reconciliation is prepared by someone in the accounting department. It is a Stewart policy that all companies, no matter how small, must have all bank reconciliations reviewed and formally approved by the manager or his designee. If a designee is used, that person must not perform accounting functions (see Release No. 10 for more details).

The bank statement and supporting items should be delivered unopened to the person who is to prepare the reconciliation. The steps in the process are these:

1. The items are sorted. Paid checks are put in numerical order; deposit slips and other items are put in order by date.
2. The endorsements on paid checks are examined on a test basis.
3. Paid checks are matched, first, with items on the prior month outstanding checklist and, then, with the current month disbursement records. The matching should extend to check number, payee and amount.
  - a. Where a mismatch occurs, full details should be noted for use in reconciliation.
  - b. Where there is no match - a disbursement has not yet cleared the bank - the item should be added to an outstanding check list for the current month.
  - c. Where a disbursement does not clear the bank within a reasonable period of time, an investigation should be made. Sometimes these checks have been voided, for example. (Note: All states have some sort of Unclaimed Property regulations regarding the maintenance and disposition of unclaimed/abandoned funds. Violations of these laws, can result in heavy penalties. You should investigate the laws specific to the state(s) in which you conduct business).

## **BANK RECONCILIATIONS**

(continued)

4. Deposit slips are matched, first with items on the prior month list of deposits-in-transit and, then, with the current month receipt records.
  - a. Where a mismatch occurs, full details should be noted for use in the reconciliation.
  - b. Where there is no match - a receipt has not yet cleared the bank - the item should be added to a deposits-in-transit list for the current month.
  - c. Where a receipt does not clear the bank by the subsequent month, some problem exists. Either an accounting error has been made, the deposit has been lost, or something else has happened requiring prompt attention.
  
5. Other items, if any, returned with the bank statement, are compared with the accounting records and differences are noted.

This part of the process should isolate all differences between the bank's record of the cash account and the company's record. The next step is this:

6. Enter the differences noted into an appropriate framework for determining that all differences have been located.

Example:		Prior		
Current				
		<u>Month</u>	<u>Receipts</u>	<u>Disbursements</u>
<u>Month</u>				
	Balance, per bank statement	xx,xxx	xx,xxx	xx,xxx
xx,xxx	Add:			
	Deposits in transit - prior	xx,xxx	(xx,xxx)	-
	Deposits in transit - current (list attached)			xx,xxx
xx,xxx				
	Less:			
	Outstanding checks - prior	(xx,xxx)	(xx,xxx)	-
	Outstanding checks- current (list attached)			xx,xxx
(xx,xxx)				
	Error in recording of Check #123	_____	_____	(xx,xxx)
xx,xxx				
	Balance, per general ledger	<u>xx,xxx</u>	<u>xx,xxx</u>	<u>xx,xxx</u>
xx,xxx				

## **BANK RECONCILIATIONS**

(continued)

If the items entered into the framework do not reconcile the balances, the preparer will need to recheck the work. It is perhaps most efficient to work backwards, first rechecking arithmetic in the reconciliation, then the footings of the deposits-in-transit and outstanding checklists, then rematching the clearings with the accounting records. Proving the bank statement -- determining that the items enclosed with the bank statement are identical to the items posted -- is recommended as a last resort.

Locating all of the reconciling items does not quite complete the process. The next step is:

7. Analyze the reconciling items to determine which, if any, require the recording of adjustments to the cash account. Ideally, there should be none. The deposits-in-transit and outstanding checks represent mere timing differences. In the example in Step 6 above, the bank charges and the recording error would require an adjustment.

When making the adjustments to the books, adjusting the Daily Cash Report (see Release No. 13) should not be overlooked.

8. Obtain the written approval of the manager or his designee on the face of the reconciliation (signature and date).
9. File the reconciliation where it will be available for use in the following month and for audit purposes.

Release No. 39

Date: November 1998 (previously September 1984)

## **ACCRUAL OF TRADE PAYABLES**

Proper accounting requires that expenses be recorded in the period in which they are incurred and assets be recorded in the period in which they are acquired. When these expenses and assets are in the form of services or goods received near the end of an accounting period, an accurate cut-off between periods must be made. See Release No. 53 which discusses earnings management.

In the case of services received, their cost should be recorded in the period the services were performed. Goods must be recorded at the time that title to them passes from the vendor to the company. This will usually be at the time of delivery but may be earlier in instances where the terms are F.O.B. the vendor's location.

The entry or entries to record trade payables should be made toward the end of the closing process each month to allow as much time as possible for details concerning these items to surface. The process of locating items to record should proceed generally as follows:

1. Review the support for checks issued subsequent to month end.
2. Review the file of unpaid invoices.
3. Discuss with management and any other appropriate party whether amounts may be owing for which documentation has not yet been received through the normal channels. Invoices in dispute, billings from professional firms, and similar items may fall into this category.

The entry to record items located in this process is to debit the appropriate asset and/or expense account and to credit accounts payable-trade (line 127) on the Schedule B balance sheet.

Release No. 40

Date: August 2001 (previously December 1985)

## **REIMBURSEMENT OF EXPENSES**

When an office incurs expenses directly associated with a file (other than outside searches) and is reimbursed for these expenses at closing, both the collection of the reimbursement and the payment of the associated expense should be recorded as follows:

- 1 "Other Operating Income" (Account #1300, Line 4, Schedule A)
  - a. Recording fees (reimbursement and expense)
  - b. Tax certificate fees (reimbursement and expense)
  - c. Copy income (income only; collections for photocopies)
- 2 "Delivery" (Account #3600, Line 44, Schedule A)
  - a. Messenger/courier service (reimbursement and expense)
  - b. Overnight deliveries (reimbursement and expense)
- 3 "Telephone" (Account #3720, Line 50, Schedule A)
  - a. Long distance charges (reimbursement and expense)
- 4 "Miscellaneous" (Account #3950, Line 56, Schedule A)
  - a. Wire transfer fees (reimbursement and expense)

Release No. 41

Date: August 2001 (previously November 1998)

## **ANALYSIS OF COMPUTER COSTS**

Note: This schedule (a required quarterly schedule, see Appendix, Item 13) applies to offices owning their own mainframe computer (MICROVAX II, etc.) and/or have a local area network (LAN) or wide area network (WAN).

Use the attached schedule for reporting your automation expenses. You may find it helpful to set up sub-accounts within related general ledger expense accounts in your general ledger. The comments at the bottom of this schedule refer to the appropriate line item on Schedule A and are as follows:

- 21. **Salaries** - report only the direct salaries relating to operation, network administration and programming associates. Do not allocate salaries from non-computer areas.
- 22. **Bonuses** - report bonuses related to associates included in Line 21, above.
- 23. **Payroll taxes** - report payroll taxes related to associates included in Line 21, above.
- 52. **Computer LDI** - report amounts paid to Landata for maintenance on software, hardware, etc. Also report programming charges, management fees, software license fees and frame relay charges if you are on the Stewart network. You should include all fees paid to other vendors (other than Landata); however, you should separate such expense under separate sub-accounts.
- 33. **Rent** - report rent related to additional floor space needed for computer hardware. Most likely this will only be applicable if you own a VAX 750 or 780 or a network configuration.
- 34. **Other occupancy** – report additional utilities, janitorial services and parking related to computer operations. You may need to allocate these expenses (floor space, associate, etc.).
- 36. **Depreciation** - report depreciation related to capitalized computer software, hardware, and office equipment needed to support associates in Line 11 as well as computer users. See Release No. 27 for discussion on depreciable lives of computer equipment.
- 42. **Rent-equipment** - report expenses for all rented automation equipment. Leases that are in the form of a purchase should be capitalized and properly amortized.
- 45. **Travel** - report travel expenses of associates included in line 21 (i.e., training, seminars, etc.).
- 50. **Insurance** – report additional insurance expenses related to computer equipment or operations.
- 52. **Telephone** – report additional telephone expenses related to computer operations (long lines, dial-in-lines, etc.). This would include any dedicated lines for computer communications (modem lines) and the associated monthly/long distance charges.
- 55. **General supplies** - report expenses directly related to automation (i.e. printer ribbons, paper, toner, etc.).

## **ANALYSIS OF COMPUTER COSTS**

(continued)

- 56. **Interest expense** - report any interest on notes related to the purchase of computer equipment, loans, etc. as it is incurred. Accrue the appropriate amounts for which no payment has been made.
- 46. **Miscellaneous** - other expenses related to computer or automation not included in one of the above lines.

Release No. 42

Date: August 2001 (previously June 1996)

## MEALS AND ENTERTAINMENT EXPENSE

### Expenses allowed as deductions

Traveling expenses in the pursuit of business, including amounts spent for meals and lodging while away from home, are deductible. This includes air travel costs (the *associate only*), hotel bills and auto rentals (which *may* include a spousal portion - see comments under separate section). However, for entertainment costs to be deductible, they must be **directly related** to the conducting of business or directly preceding or following a business discussion.

*Business* meals are also subject to the same requirements noted above. There is one additional requirement regarding meals - they cannot be lavish or extravagant. The IRS considers this to be purely a judgment call.

There are a few *exceptions* allowed (whereby entertainment expenses are still deductible even though they fail the directly related test) representing common costs most offices incur:

- food and beverages for associates at the business site
- recreational expenses, like picnics, social events, etc.
- expenses treated as compensation to the associate

Finally, the use of an outside entertainment facility is not deductible unless the taxpayer can show that more than 50% of the use was business related. Then the deduction is limited to the amount that is *directly related* to the active conduct of business, usually calculated as a percentage. These facility costs include: rent, utility charges, repairs, insurance, etc. An entertainment facility is defined as any property used by a taxpayer in connection with entertainment, such as a yacht, hunting lodge, etc. One thing to keep in mind: the costs to hold a business meeting in a local hotel, or some similar place, are not considered *entertainment* because the facility is not generally used for entertainment. These costs would not fall under the restrictions discussed above.

### How much of the expense is deductible?

Thus far, we have been talking about 'allowable' expenses and what qualifies for a tax deduction. Now the question becomes "Does the entire amount become deductible or is there some IRS limitation on what is claimed as a deduction?" As of 1/1/94, **the amount allowable as a deduction for business meal and entertainment expense is limited to 50% of such expense.** Food and beverage costs incurred in the course of travel away from home fall within the scope of this rule as do the costs associated with an entertainment facility. But as with all rules, there are several exceptions (meaning that these expenses falling under 'meals and entertainment' are **100%** deductible):

- recreational expenses (see above)
- food and beverage expenses associated with benefits to the associate that are excludable from the recipient's gross income as a *de minimis* fringe benefit

Remember, air travel costs, hotel bills and auto rentals are fully deductible. Only meals, business or in the course of travel away from home, and entertainment costs have deductible limits.

## **MEALS AND ENTERTAINMENT EXPENSE**

(continued)

### **Spousal Travel**

Another area that has received much attention is the handling of spousal travel. Up until 1/1/94, the travel costs of an associates' spouse were deductible. However, these costs are *no longer* deductible unless the spouse is an associate. We have elected to treat 'approved' spouse's air travel in Stewart Title Guaranty as a **non-deductible** expense. (Thus this is not a tax benefit. It will in effect increase your effective tax rate).

Other forms of travel-related costs, such as hotel, meals, etc. are so closely tied to the associate that an attempt to separate them (between associate and spouse) would at best be inaccurate. It also could be argued that these costs would be incurred anyway regardless of whether the spouse accompanied the associate or not. As a result, we are not treating these costs as part of spousal travel, and thus they are deductible under the restrictions noted above.

What are we doing to account for these costs? We are keeping 'approved' spousal air travel under a separate sub-code under the travel expense line of the income statement. Also, under the same travel line, we keep associate meals under a separate sub-code. Any other expenses where the associate breaks out specific spousal costs will also go under this sub-code, designating it as non-deductible.

### **Club Dues**

In the area of club dues, the general rule is that they are not deductible for tax purposes as of 1/1/94 if the club is considered a social, athletic, or sporting one. However, the regulations do permit deductions for professional organizations, such as bar associations or medical associations, and civic or public service associations, such as Kiwanis, Lions, Rotary or similar organizations. The rules also permit deductions for dues of certain organizations similar to professional organizations, such as business leagues, trade associations, chambers of commerce, and real estate boards. We account for these costs in a way similar to spousal costs. We have a separate sub-code under the dues and subscriptions line of the income statement to record all non-deductible club dues.

### **Conclusion**

To conclude, you should be familiar with the restrictions placed upon business and travel meals and entertainment by the IRS. Essentially, meals are limited to a 50% deductibility, provided they are 'directly related' to the conduct of business. The only exceptions to this are the 'de minimis' fringe benefit rule - meals provided associates on the business premises, and recreational expenses, such as meals provided at company picnics, etc. These meals are 100% deductible.

Entertainment costs have similar restrictions as meals, noted above. Remember, the limitations discussed above essentially mean that we lose 50% of the tax benefit on the expenditures for meals and entertainment. Finally, dues which you are paying to any social, athletic, or sporting club are not deductible. The idea is to separate these non-deductible costs, by sub-codes, from the deductible ones in order to properly arrive at your company's tax deduction.

Release No. 43

Date: May 1995

## **COMPUTER SOFTWARE DEVELOPMENT COSTS**

Deciding whether to capitalize or expense computer software development costs is difficult. The following guidelines should be followed in accounting for these costs.

Generally, the Company expenses most costs in developing computer software. The kind of software development costs that may be capitalized (as deferred charges) fall into one of the following two categories:

1. "External" - This is a separate phase of or is the total product itself to be sold or marketed to third parties who are not affiliated with Stewart. Example: a new "AIM-for-Windows" operating system sold to independent agents.
2. "Internal" - This is a separate phase of or is the total "major" (defined below) product itself that is to be used internally by Stewart companies and for which there exists no plan to market the product externally. Example: a major claims-management system developed for Stewart Title Guaranty Company's legal department. The replaced claims system will be abandoned after installing the new one.

An enhancement to an existing product is considered a "separate phase" (see above) if the enhancement is "major" and significantly improves the marketability or use of the original product. Minor enhancements are expensed.

### **1. EXTERNAL PRODUCTS**

Before capitalizing any costs on a particular project involving an external product, the following questions must be answered "yes":

1. Has the project reached the "technological feasibility" stage?
2. Is the estimated future "net realizable value" of the project, generally to be received from a third party, at least equal to the capitalized cost on the balance sheet?

Management should have a high confidence level, say 95% or more, in answering the above questions. The project should have reached a "no-fail" stage, both as to completion of the project and in the sufficiency of future income from third parties to cover costs.

Technological feasibility. The three stages of producing a software product and the accounting to be followed for each stage are:

1. Until technologically feasible (\*) ..... expense
  2. From date technologically feasible ("window") ..... capitalize
  3. From date general release is issued to customers ..... expense
- ....

(\*) In this first stage, the costs usually relate to planning, designing, coding and testing. These are expensed until stage two is reached.

## **COMPUTER SOFTWARE DEVELOPMENT COSTS**

(continued)

The second stage (above) is called a “window” because it is only during this period of time, between stage one and three, that costs are capitalized. In the other two stages, the costs are expensed.

The determination of technological feasibility must be made for an entire software product and not on a module-by-module basis. An exception is when a module is marketed separately.

The Company considers “technological feasibility” to be reached when there are no significant risk development issues yet to be resolved. Generally, the Company considers that this occurs on the date when a “working model” has been completed.

Most of the costs that will be capitalized after reaching the working model stage will relate to testing, de-bugging, final coding and documenting.

The “technological feasibility” stage can also be considered reached, for certain projects, on the date a “detail program design” is completed. The detail program design will not be considered complete until:

1. The product design and detail program have been completed, and it has been established that the necessary skills, hardware and software technology are available to finish the product.
2. The completeness of the detail program design has been confirmed by documenting and tracing the detail program to product specifications.
3. The detail program has been reviewed for high-risk development and any uncertainties about such risk have been resolved through coding and testing.

### **Cost to be capitalized**

Not all projects should be capitalized because of the uncertainty of realization and because the amounts involved may be immaterial. Therefore, the Company generally does not consider any project for capitalization unless it is “major”, which by definition is a project with an estimated total cost in excess of \$500,000.

The costs to be capitalized during the “window” stage two (see above) are those that relate to the specific project: direct labor hours spent on the project multiplied by the compensation rate of the employee, including salaries, bonuses, payroll taxes and other personnel costs. Other costs will include contracted services, materials and an allocation of indirect personnel costs, rent and other costs.

The allocations should include the costs of managing the Stewart computer operations. Example: Landata’s president and staff. However, amounts expended in the personnel, corporate executive and other departments of the Company are to be excluded.

As stated above, capitalization of development costs of a software product should stop at the end of the “window”, when the product is available for general market release. The Company’s records must clearly support the costs capitalized during the “window” period.

## **COMPUTER SOFTWARE DEVELOPMENT COSTS**

(continued)

Amortization. Amortization of the amounts capitalized should begin the month following the date the product is available for general release. The Company will amortize the costs on a straight-line basis over the useful life of the software product. However, the amortization can not exceed 36 months from the date the amortization begins.

Net realizable value. The Company will evaluate the net realizable value of capitalized costs of computer software on a product-by-product basis at each month-end balance sheet date. Net realizable value is defined as:

“the estimated future gross revenues from that product reduced by the estimated future costs of completing and disposing of that product, including the costs of performing maintenance and customer support to satisfy the enterprise’s responsibility set forth at the time of sale” (FAS 86, Par 10)

In estimating the future revenue stream from a product, the Company should consider revenues from third parties only and should document the files in a manner that facilitates auditing. The Company files should address the following:

- the size of the overall market for the product
- the share of the market the Company expects to receive
- names and amounts of specific (or group of) customers
- the number of software products expected to be sold
- pricing of the product
- competitive products
- effects of technological advances, hardware developments
- revenues from new agents who sign with the Company (\*)
- additional revenues from existing agents (\*)
- any other factors that could have an impact on future revenues

(\*) Resulting from the related software product. This should be conservatively estimated. From these revenues must be deducted such costs as loss provisions, commissions to managers based on premiums, premium taxes, etc.

Commissions to be paid in the future and any other estimated costs to sell the product (distribution costs, costs of minor enhancements, etc.) must be deducted in estimating net realizable values.

Net realizable value writedown. At any time the carrying costs of a software development project exceeds its estimated net realizable value, the costs must be reduced to net realizable value. The writedown will be included in amortization expense.

Revenue recognition. Sales of software are recorded by the Company at the time the product is delivered to the third party. Fees for monthly maintenance and other services are recorded when earned.

## **COMPUTER SOFTWARE DEVELOPMENT COSTS**

(continued)

### 2. INTERNAL PRODUCTS

AICPA Statement of Position ("SOP") 98-1, *Accounting for the Costs of Computer Software Developed or Obtained for Internal Use*, was issued in March 1998. The SOP requires that certain costs related to the development, modification or purchase of internal-use software be capitalized and amortized over the estimated useful life of the software. For this statement to apply, the software must be solely to meet the company's internal needs and no substantive plan must exist for marketing the software externally.

SOP 98-1 segregates the process of computer software development into three stages as follows:

- Preliminary Project Stage - this stage includes conceptual formulation of software alternatives, evaluation of the alternatives, determination of the existence of needed technology and final selection of alternatives.
- Application Development Stage – this stage includes the design of a chosen path, including software configuration and software interfaces, coding, installation to hardware, and testing, including parallel processing. Certain internal and external costs incurred during this stage should be capitalized (see following section on Capitalizable Costs).
- Post-Implementation/Operation Stage – this stage includes training and application maintenance. Internal and external costs incurred in this stage should be expensed as incurred.

Software developed for internal use by the Stewart companies should be capitalized if the answers to the following questions are "yes":

1. Is the preliminary project stage completed?
2. Has management, with the relevant authority, authorized and committed to funding the project and is it probable that the project will be completed and the software used to perform the intended function?
3. Are the future costs "major"? (See below).

Management should have a high confidence level, say 95% or more, in answering "yes" to these questions.

"Major" internal projects. Not all projects should be capitalized because of the uncertainty of realization, the period benefited may be brief, the useful life is difficult to estimate and the amounts involved may be immaterial. Therefore, the Company generally does not consider any project for capitalization unless it is "major", which by definition is a project with an estimated total cost in excess of \$500,000.

In determining the estimated future total cost of a project, estimated amounts shown in budgets or otherwise may require revision. All projects, even those with estimated costs below \$500,000 should be included when reviewing for possible revisions of amounts. At a minimum, this review should be performed monthly.

## **COMPUTER SOFTWARE DEVELOPMENT COSTS**

(continued)

The amounts should be increased if past experience indicates that the estimated amounts used in authorizing projects have proven to be low. (Or decreased if the reverse proves true).

If a project is later determined to be "major" after costs have already been incurred on it, the amount to be capitalized should be limited to the amounts spent after that date. Amounts charged to expense up to that date should not be reversed and capitalized.

Capitalized costs, amortization, etc. Costs to be capitalized for internal software are limited to external direct costs of materials and services consumed in developing or obtaining internal-use computer software; payroll and payroll-related costs for employees who are directly associated with and who devote time to the internal-use computer software project (to the extent of the time spent directly on the project). Note that this differs from the costs for external products which includes management and other overhead. Amortization (up to 36 months) should generally be the same for internal products as external products. See above.

While the evaluation of external products centers on estimating future income streams from third parties (see above), the evaluation of internal products should be considered in accordance with FASB Statement No. 121, *Impairment of Long-Lived Assets* (see Release No. 51).

### **Internal-Use Software Sold**

If an entity decides to market internal-use software after the development of the software is completed, proceeds from the sale of the computer software (net of direct incremental cost of sales) should be applied against the carrying amount of that software. No profit should be recognized until aggregate proceeds from the sales and amortization have reduced the carrying amount of the software to zero.

The following accounting pronouncements were used in developing these policies: FAS 86, FAS 2, FIN 6 and SOP 98-1.

Release No. 44

Date: August 2001 (previously November 1998)

## **ACCRUED LOSS PROVISIONS**

From time to time it becomes necessary to accrue for potential future claims based upon an historical trend of claims' payments, both escrow and policy related, your office may have experienced. As noted in Release 33, a liability for losses is usually recorded when the loss (1) becomes probable and (2) can be estimated with reasonable accuracy.

In order to justify the recording of a loss prior to the knowledge of its occurrence, the issue of 'probable occurrence' can be somewhat proven by the historical trend of analyzing claims payments over a period of years. If there is a clear trend of payments, an accrual of a loss provision would seem to be prudent (see example of appropriate analysis in the Appendix, Item 12 – Analysis of Loss Expense).

You should analyze your payment history, over at least seven years, showing the loss accrual, (the debit to Line 29, losses-escrow, etc. of Schedule A) both in dollars and as a percentage of Line 1 revenues. You should also show the corresponding years' payments, those of escrow, negligent (related to policy losses) and any other type of loss payment. The difference between the accrual and the sum of all payments should equal the increase or decrease in the provision liability, Line 128 of Schedule B, balance sheet for the period analyzed.

The matter of reviewing policy loss activity on a consolidated basis has made it imperative that we document significant charges, payments and/or adjustments to the policy loss liability account. If your office accrues a loss provision, you must fill out an Analysis of Loss Expense and submit it with your December 31, xxxx (year-end) financial Schedules A & B to National Accounting. If your office records loss expense on a cash basis, or if your losses for the current year are immaterial (say below \$5,000), you will not be required to submit a current year analysis schedule.

If you have any questions, please contact Kim Peterson in National Accounting.

Release No. 45

Date: August 2001 (previously June 1995)

## **IMPREST ACCOUNTS**

Many STG region and district offices maintain imprest checking accounts primarily for the purpose of paying invoices which are immaterial in amount. Proper utilization of an imprest account gives field personnel the opportunity to promptly pay small expenses as they are incurred and eliminates unnecessary paperwork in STG's Accounts Payable department. The information outlined below details company policies and procedures for establishing and maintaining imprest accounts.

### **Opening an Imprest Account**

- Requires STG executive committee approval.
- Upon approval, the STG Accounts Payable department will forward a check to the STG field office to open the account.
- The account will be styled "Stewart Title Guaranty Company Imprest Account".
- Two signatures are required on all checks written on the account.

### **Proper Usage of the Account**

#### **Acceptable Disbursements (no checks > \$500 may be issued):**

- general office supplies and expenses
- postage/delivery expenses
- printing/photocopying expenses
- telephone/paging/answering services expenses
- agent licensing fees
- purchases of educational material (manuals, videotapes, etc.)
- seminar registration fees
- professional dues/subscriptions (other than land title association dues)
- associate lunches/luncheons

#### **Unacceptable Disbursements (due to tax accounting requirements):**

- business development and promotion expenses
- purchase of promotional items (tickets, note pads, mugs, pens, etc.)
- reimbursements to associates for travel and/or business promotion expenditures
- payments to hotels and other facilities for seminars and banquets
- contract labor or service oriented expenses to non-incorporated entities
- purchases of fixed assets (furniture, fixtures, equipment, autos, etc.)
- land title association dues
- associate cash advances/loans
- dues for social clubs/country clubs
- political lobbying related expenditures
- payroll/bonus expenses
- claim related attorney fees/settlements
- computer equipment purchases

## **IMPREST ACCOUNTS**

(continued)

### **Acceptable Deposits into the Imprest Account**

- STG's check for reimbursing the imprest account
- refunds of overpayments paid out of the imprest account
- reimbursements of recording fees paid out of the imprest account when the net result is zero (i.e., amount disbursed for recording fees equals amount reimbursed)

All other receipts should be forwarded to Steve Gottardy, Senior Accountant - National Accounting department. A description of the nature of the receipt (i.e., the type of services provided) should accompany each receipt forwarded to National Accounting.

### **Imprest Account Reimbursement Procedures**

Each office must maintain an Imprest Account Log (see sample in the Appendix, Item 14) detailing all account receipts/disbursements and the associated transaction date, payee/remitter, transaction description, check/receipt number and amount. A running book balance should also be included on the log.

Requests for reimbursement of the imprest account must be submitted to STG's Accounts Payable department as needed or on a quarterly basis, at a minimum. Requests for reimbursement must include the following documentation:

- ◇ Complete and current Imprest Account Log, detailing all account receipts and disbursements since the last request for reimbursement.
- ◇ Supporting invoices, receipts and any other documents for each transaction detailed on the Imprest Account Log.

Incomplete requests will result in reimbursement delays.

### **Internal Control Guidelines**

- All checks must require two signatures.
- Signature stamps/plates may not be used.
- No checks exceeding \$500 may be written out of the imprest account.
- Unused checks must be maintained in a secure, locked location.
- Unused checks must be accounted for on a regular basis.
- Incoming funds must be restrictively endorsed immediately upon receipt and must be deposited within twenty-four hours of receipt.
- All transactions (receipts and disbursements) must be recorded in the proper accounting period.

## **IMPREST ACCOUNTS**

(continued)

- Imprest account bank statements must be forwarded unopened to the individual responsible for reconciling the account.
- The imprest account bank balance must be reconciled to the imprest account book balance (detailed on the Imprest Account Log) on a regular monthly basis by an individual not responsible for the custody and/or maintenance of the account (if office size permits).
- Office management must review and approve, in writing, each bank reconciliation upon completion.
- **Copies of imprest account bank reconciliations, approved and signed by management, and the related supporting documents (bank statements, outstanding check and deposit in transit listings, Imprest Account Log) should be forwarded to Steve Gottardy, Senior Accountant - STG National Accounting Department, by the fifteenth working day of the month following the end of each quarter. (For example, bank reconciliations covering the months of January - March should be forwarded to Steve by the fifteenth working day of April).**

Release No. 46

Date: August 2001 (previously November 1998)

## **RECORDS RETENTION POLICY**

### **Operating Accounting Records**

In order to fulfill IRS requirements and other reporting requirements of the Company, all records supporting an affiliate's financial statements and tax returns should be retained for ten (10) years. The records to be retained include, but are not necessarily limited to, the following:

- a. Detailed general ledgers.
- b. Receipt and disbursement registers.
- c. Bank reconciliations and supporting schedules.
- d. Bank statements and enclosures. See Note.
- e. Payroll registers, payroll tax returns, and evidence of payroll tax payments.
- f. External audit reports.

The retained operating accounting records listed above should be stored ON SITE for a minimum of six (6) years. Retained records that are seven (7) to ten (10) years old may be stored OFF SITE.

Other more detailed supporting documents such as paid invoices, purchase orders, check copies, etc. should be maintained for a minimum of six (6) years. These records should be stored ON SITE for a minimum of three (3) years. The remaining three years' may be stored OFF SITE.

### **Escrow Accounting Records**

1. All escrow accounting records which support all escrow transactions should be retained for the specific time periods shown below. The records to be retained include, but are not necessarily limited to, the following:

- a. Transaction registers documenting receipts, disbursements, wires, file transfers, and journal entries.
- b. Trial balance/open file listings.
- c. Selective file histories.
- d. Bank reconciliations and supporting schedules.
- e. Bank statements and enclosures. See Note.
- f. Unclaimed Property (a/k/a Escheat) reports.
- g. External audit reports.

2. Retain all escrow bank records for ten (10) years after the last bank activity.

Example: An escrow bank statement dated January 31, 1997 and its related enclosures (canceled checks, deposit slips, debit/credit memos, etc.) should be retained through January 31, 2007.

3. Retain all escrow accounting records of transactions on a particular file for ten (10) years after the last file activity.

## **RECORDS RETENTION POLICY**

(continued)

Example One: The file history for a file which closed on December 31, 1997, but which carried a file balance until December 31, 1999, should be retained until December 31, 2009. This example applies even though "held" funds may have been moved to an investment account. The fact that the funds are being maintained in an investment account rather than the regular escrow account does not change the fact that the file actually has a balance. (For instance, if funds were held in a file as an indemnity, it would not be unusual for that file to have a balance for several years.)

Example Two: If a file closed on December 31, 1997, but all checks and deposits did not clear the bank until December 31, 1998, the file history should be retained until December 31, 2008.

**NOTE:** Certain offices may opt to receive check images on CD ROM in lieu of cancelled checks and paper statements. This is an allowable policy as long as (1) your state permits the use of imaged checks and (2) you are receiving images of both the front and back of the checks.

### **Guaranty Files**

1. Guaranty Files (including both title files and escrow files) should be preserved and retained (and not destroyed) for a **minimum** of ten (10) years. It is possible that a state may have, or may introduce, its own rule or regulation requiring files to be retained for a longer time period.\* In these cases, the state regulation will overrule STG policy and files should be retained for the state specified time period.

\*Missouri has its own state regulation that applies to the retention of title evidence. Reference is made to STG Bulletin No. MO000002 dated 1/31/96. The bulletin details what must be retained and that it must be retained for fifteen (15) years after the title insurance policy has been issued. The State of Texas also requires 15 year retention. Reference is made to Article 9.34 in Chapter nine of the Texas Title Insurance Act.

Files can be preserved and retained in various formats such as hard copy files, microfilm, computer optic images (i.e., "scanned" documents), etc. The IRS has specific requirements with respect to its acceptance of computer images as supporting documentation. If you have any questions regarding these requirements you should contact the IRS directly or David Nicholson (x. 8039) in National Accounting.

2. When a file has been totally completed\*\* and is ready to be vaulted (sent to permanent storage), the size of the file can be reduced to save storage space by discarding the following items:

\*\*(Totally completed is defined as follows: (1) all releases of prior liens have been received and recorded, (2) policies have been issued, (3) all funds have been received and disbursed and file has a zero balance, and (4) all transactions (checks, deposits, wires, etc.) have cleared the bank.)

## **RECORDS RETENTION POLICY**

(continued)

- a. Duplicate copies of deeds and mortgages signed at closing. One copy of each signed document is sufficient for the file.
- b. Copies of recorded documents that were used in the examination process because they can be easily reproduced if they are needed at some later date. This does not include such items as the search sheet (a/k/a run sheet) or title plant printouts or examiner's notes as these items should be retained in the file.

NOTICE: THE ABOVE NO. "b" DOES NOT APPLY TO MISSOURI. REFERENCE IS MADE TO STG BULLETIN NO. MO000002 DATED 1/31/96 WHICH STATES THAT TITLE EVIDENCE (INCLUDING COPIES OF RECORDED DOCUMENTS) MUST BE RETAINED IN THE FILES.

- 3. All non-recorded documents (such as indemnities, etc.) on which reliance was placed in order to issue title insurance should be preserved and retained in their original executed hard copy form for a minimum of ten (10) years.

Release No. 47

Date: August 2001 (previously November 1998)

## **1099 REPORTING**

Each year, corporations are required by the IRS to submit payment information concerning payments made to certain non-corporate vendors (i.e. individuals, partnerships and others) in the form of 1098's and 1099's. The rules governing this reporting requirement are usually consistent from year to year, reflecting very little change. Following is a summary of the more common types of forms:

### **Form 1099-MISC. – Miscellaneous Income**

Issued to persons receiving at least \$10 in royalties or at least \$600 in rents, services or other income payments for the reporting year. Payments made to corporations are not subject to 1099-MISC reporting.

### **Form 1099-INT – Interest Income**

Issued to persons receiving interest payments of at least \$10 during the reporting year paid in the course of our trade or business.

### **Form 1098 – Mortgage Interest Statement**

Issued to persons receiving mortgage interest payments of at least \$600 during the reporting year paid in the course of our trade or business. The \$600 threshold applies to each mortgage, therefore a separate Form 1098 must be filed for each mortgage.

In order to fulfill these requirements, you should routinely request from your vendors their Tax Identification Numbers (TIN) or their Social Security Number (SS), whichever is applicable. Also, verify complete mailing addresses. To simplify this process, you may wish to have vendors complete a Form W-9 prior to payment. The Form W-9 requests correct TIN or SS numbers as well as the vendor's or individual's reporting status, i.e. a corporation, partnership or a sole proprietor. The completed form W-9 should be kept on file in case of any dispute over 1099 information submitted. If a vendor fails to supply a completed Form W-9, or submits erroneous information, they may become subject to backup withholding. Normally, this would come as a request from the IRS to the corporation making payments to the vendor.

1099 information is submitted to the IRS either on paper forms or magnetic media, depending upon the number of records being filed. The current requirement is for magnetic media if over 250 records are being submitted, but you should obtain current IRS instructions each year to verify this requirement.

Failure to file correct information pertaining to vendor payments for the reporting year may result in penalties ranging in severity from \$50 per record to an annual maximum of \$100,000. The IRS will use the 1099 information that you file to verify amounts reported to them on corresponding tax returns filed under the same TIN or SS.

Further information can be obtained from the IRS Instructions for Forms 1099, 1098, 5498 & W-2G.

Note: Requirements pertaining to Form 1099-S (sellers proceeds) are not discussed in this release. Please see Legal Bulletin NL000016 (dated November 25, 1992) for information on filing requirements for title offices.

Release No. 48

Date: August 2001 (previously November 1998)

## **MAINTAINING CASH ACCOUNTS**

STG Bank accounts may only be opened with a Corporate Resolution approved by the Executive Committee of the Board of Directors. This policy will also apply to most Stewart companies due to the fact that most banks typically require this type of a resolution before a corporate account will be opened.

Changes made to Articles 3 & 4 of the Uniform Commercial Code have divided the liability for fraudulent checks between the banking customer and the bank. If a loss occurs due to negligence by the customer, the customer will be responsible for the fraud. The absence of “ordinary care” as defined by Section 3-103(7) of the UCC code can result in heavy penalties for any company.

### **Internal Controls**

The following controls should be implemented to reduce the risk of loss due to fraud and to demonstrate that ordinary care has been taken in the management of these accounts:

- Use Positive Pay
  - This service will identify any disbursement that was not legitimately issued. More information is provided on the Positive Pay system later in this section.
- Use Secure Check Stock
  - All checks should have at least 7 of the following security features:
    - **Controlled Paper**  
Check stock is securely distributed and monitored when printing. The stock is not available for “over-the-counter” sales.
    - **Laid Lines**  
Lines are unevenly spaced on the back of the check. This makes it more difficult for counterfeiters to copy.
    - **“VOID” Pantographs**  
When copied or scanned, “VOID” appears on the check.
    - **Fourdrinier Watermarks**  
Designs pressed into the paper while being manufactured. Fourdrinier watermarks can be seen easily from either side of the paper, but cannot be copied or scanned.
    - **Artificial Watermarks**  
Designs printed on the paper. Artificial watermarks can be seen when held at a 45-degree angle and marks cannot be copied.
    - **Thermochromic Inks**  
Inks change color when heated (body heat when touched, for example), making it very difficult to copy or scan.
    - **Dual Image Numbering**  
Creates a red halo around the check number or MICR line of the check. The red ink also bleeds through to the back of the check, making it impossible to accurately duplicate.
    - **Microprinting**  
Printing so small, to the naked eye, it appears to be a line.
    - **High Resolution Borders**  
Intricately designed borders. Borders appear smeared, making it very difficult to duplicate.
    - **Prismatic Printing**  
Multicolored background with gradations.

## **MAINTAINING CASH ACCOUNTS**

(continued)

- Warning Bands  
Printed messages that call attention to the safety features added to the check.
- Holograms  
Multi-colored three-dimensional images that appear in a reflective material when viewed at an angle.
- Safety Papers  
If erased, the paper “bleeds” making it obvious that a forgery attempt has been made. Controlled safety paper stock is recommended, as anyone can buy generic safety paper from any office supply store.
- Multichemical Reactive Papers  
“VOID” appears if chemicals are used on the check (chemicals are commonly used when trying to change payees or amounts.)

“**SAFE**Checks®” are business checks created specifically to fight check fraud. They are the nation’s first highly secure image-friendly checks available for all companies. For more information, please call **1-800-755-2265**.

- Review Bank Statements Promptly
  - If a company suffers a loss due to a forgery and the bank can prove that bank statements weren’t reviewed promptly, the bank’s liability can be limited. Also, if a forged check is not detected within 30 days, the bank’s liability for subsequent forged checks may also be limited. Be aware of such policies which should be set out in your banking agreement.
- Report Losses Promptly
  - All losses must be reported within one year of occurrence.
- Maintain Tight Security Over Your Checks
  - The unused check supply should be locked when not in use, with access limited only to those with check issuing responsibility.
  - Someone other than the check preparer should perform an inventory of the unused check supply, at least quarterly.
  - The re-order form should be under lock and key until new checks are needed.
- Maintain an Adequate Segregation of Duties
  - The person preparing checks should not be the person responsible for reconciling the account nor be a check signer.
- Conduct Periodic Audits
  - An independent third party should periodically perform surprise checks of accounting controls.

### **Positive Pay**

Positive Pay is another available technique in the fight against misappropriation of funds. Two processing systems exist:

## **MAINTAINING CASH ACCOUNTS**

(continued)

### **POSITIVE PAY-BANK MATCH**

- ◆ Check information is transmitted electronically to the bank after checks are prepared and either prior to or on the same day checks are disbursed to customers.
- ◆ When checks are presented for bank payment, they are compared to the check information previously received. A report of any discrepancies is printed and faxed to the office for review.
- ◆ The office can then make the decision whether or not to allow payment of the check.

It is very important that the discrepancy report is not returned to the person preparing or disbursing the check. To keep this process completely segregated, a person independent of the check preparation function should be in charge of the review.

### **REVERSE POSITIVE PAY-CUSTOMER MATCH**

- ◆ Each morning, the bank provides the office with a listing of all checks presented for payment the previous day.
- ◆ It is the office's responsibility to compare the checks presented for payment at the bank to information maintained at the office.
- ◆ As above, the office decides whether or not something is paid.

Also as above, it is very important to have the person reviewing this information independent of the person preparing and disbursing checks.

Most large banks throughout the United States provide these services to banking customers.

## **ACCOUNTING FOR FOREIGN OPERATIONS**

FAS-52 establishes accounting and reporting standards for (a) foreign currency transactions and (b) translation of foreign currency financial statements that are included by consolidation, combination, or the equity method in a parent company's financial statements. As Stewart expands into foreign markets, an increasing number of Stewart entities will be required to record such transactions and translations. Following is a summary of the translation provisions of FAS-52.

### **Foreign Subsidiaries**

The first type of foreign operation is the self-contained foreign operation, located in a particular country, whose daily operations are not dependent on the economic environment of the parent's functional currency. An important objective in translating foreign currency is to preserve the financial results and relationships that are expressed in the foreign currency. This is accomplished by maintaining the books of the foreign subsidiary using the *functional currency* of the foreign entity. The functional currency is the currency of the primary economic environment in which the entity generates and expends cash (its local/domestic currency). The functional currency is then translated into the *reporting currency* of the reporting entity (which for Stewart is U.S. dollars). This translation will typically be done at the end of each required reporting period.

Assets and liabilities are translated from the foreign entity's functional currency to the reporting entity's functional currency using the current exchange rate at the balance sheet date of the foreign entity. Capital accounts are translated at their historical exchange rates when the capital stock was issued, or at the historical exchange rate when the capital stock was acquired. Retained earnings are translated at the translated amount at the end of the prior period, plus the translated amount of net income for the current period, less the translated amount of any dividends declared during the current period.

Revenue, expenses, and gains and losses are translated from the foreign entity's functional currency to produce the approximate results that would have occurred if each transaction had been translated using the exchange rate in effect on the date that the transaction was recognized. Since the separate translation of every transaction is impractical, an appropriate weighted-average exchange rate for the period should be used. The current rate of exchange is used to translate changes in financial position other than those items found in the income statement.

Financial statements must be in conformity with U.S. GAAP prior to translation. The translation of foreign currency financial statements to the functional currency of the reporting entity does not produce realized gains or losses. Instead, the gains or losses are considered unrealized and are recorded and reported as a separate component of stockholders' equity.

### **Foreign Divisions**

The second type of foreign operation is a direct component or extension of the parent company's operation. Although the daily transactions of the operation may be settled in the local currency of the operation, the functional currency for this type of operation is the same as that of the parent company (U.S. dollars). As such, the books shall be maintained in U.S. dollars. This will require the recording of a gain or loss to net income from the translation of these transactions. It is possible with many accounting systems to maintain dual-currency books and this may be necessary in some instances in order to fulfill the local reporting requirements of the foreign operation.

**ACCOUNTING FOR FOREIGN OPERATIONS**  
(continued)

There are certain exceptions to the accounting policies described above such as for foreign operations in highly inflationary economies. Please contact National Accounting if you have any questions regarding a specific entity.

Release No. 50  
Date: November 1998

## **IMPAIRMENT OF LONG-LIVED ASSETS**

Statement of Financial Accounting Standards No. 121 issued by the Financial Accounting Standards Board requires us to verify that the carrying value of certain long-lived assets have not suffered any permanent impairment, or if they have, to make the necessary adjustments to reduce the carrying value to its fair value. Asset categories that are affected include: Real Estate Held for Development & Sale, Title Plants, Land, Buildings, Furniture & Fixtures and certain Intangibles. **Assets covered by Statement 121 should be reviewed for possible impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.**

### **Causes of Impairment**

The following are examples of events or changes in circumstances that require assessment of an asset:

- A significant decrease in the market value of an asset;
- A significant change in the extent or manner in which an asset is used or a significant physical change in an asset;
- A significant adverse change in legal factors or in the business climate that could affect the value of an asset;
- An accumulation of costs significantly in excess of the amount originally expected to acquire or construct an asset; and
- A current period operating or cash flow loss combined with a history of operating or cash flow losses or a forecast that demonstrates continuing losses associated with an asset used for the purpose of producing revenue.

### **Recognition of an Impairment Loss**

An impairment loss should be recognized when the aggregate of estimated future cash inflows (less estimated future cash outflow) to be generated by an asset is less than the asset's carrying value. Future cash inflows includes an estimate of the proceeds from eventual disposition. Estimated future cash flows are determined without reference to their discounted present value.

If the sum of undiscounted estimated future cash inflows is less than carrying value, a loss on impairment should be recorded. Such a loss is measured as the excess of the asset's carrying value over its fair value (the amount at which an asset could be bought or sold in a current transaction between a willing buyer and seller other than in a forced or liquidation sale).

Quoted market prices represent the best evidence of fair value, and, if available, such market prices should be used. If quoted market prices are unavailable, fair value should be determined based on the best information under the circumstances, which might include:

- Quoted market prices for similar assets

## IMPAIRMENT OF LONG-LIVED ASSETS

(continued)

- Valuation techniques such as:
  - present value of expected future cash flows;
  - matrix pricing;
  - option pricing models; and
  - fundamental analysis

Note that in measuring impairment, fair value is determined on the basis of the present value of expected future cash flows, whereas, in the test for assessing whether impairment exists, undiscounted estimated future cash flows are used.

### **Examples**

Title Plants – impairment could be indicated if the plant is no longer being updated; if the plant is not being utilized or if other economic conditions indicate a deterioration of the value.

Buildings – for economic or other reasons the building is not being leased or impairment has been caused by damage to the building.

Furniture & Fixtures – impairment caused by damage to property, unused or unlocated items.

Note that after an impairment loss is recognized, the written down carrying value becomes the asset's new cost and the basis for future depreciation or amortization charges. Once an impairment loss has been recognized, the resultant reduction in carrying value of an asset may not be restored.

### **INCOME TAX SHARING AGREEMENT**

For federal income tax purposes, if you are an 80% or more owned corporate affiliate, you will be included in Stewart Information Services Corporation's (SISCO) consolidated filing. Accordingly, it is necessary that a tax sharing agreement be executed to provide details as to how the consolidated tax liability or benefits will be shared by each affiliate. The executed tax sharing agreement is applicable beginning with the tax year stated in the agreement and all subsequent tax years so long as the affiliate is at least 80% owned and remains as part of SISCO's consolidated filing.

A sample tax sharing agreement effective beginning with the 1997 tax year is included in the Appendix (see Item 18). As stated in the tax sharing agreement, if you have lower tier affiliates, you and your affiliates will be considered as one consolidated affiliate (subgroup). Similarly, if you are a lower tier affiliate of another affiliate, you and your direct parent will be considered as one consolidated affiliate. What this means is that income and losses within your subgroup will be consolidated for the calculation of any federal income tax obligation due to Stewart Title Company (STC).

If you are part of a subgroup, the tax sharing agreement will be executed between STC and the parent company of your subgroup. There must be similar tax sharing agreement between the parent company and the subsidiary companies in your subgroup. A copy of such executed agreement should be provided to National Accounting.

In order to ensure that federal tax payments collected by the parent company of the subgroup are being disbursed according to SISCO's company policy, the payments collected from lower tier affiliates must be applied in the following order:

1. Any outstanding payables to SISCO, STC or Stewart Title Guaranty Company (STG) such as delinquent payroll, STG Premiums or intercompany insurance billing.
2. Any outstanding STC loans.

Relevant reports should be provided to National Accounting to demonstrate that the above policy is being followed. For example, a copy of deposit slip showing amount of tax payment received from lower tier affiliates together with copies of checks showing disbursements of such cash receipt will serve this purpose.

Release No. 52  
Date: November 1998

## **EARNINGS MANAGEMENT**

As a publicly traded company on the New York Stock Exchange, Stewart Information Services Corporation and its subsidiaries must accurately report its earnings to comply with all securities regulations. Therefore, Stewart will not tolerate any practice of deliberately “smoothing” or otherwise manipulating earnings. Person(s) involved in such practices are subject to reprimand, including dismissal.

Smoothing. “Smoothing” may take several forms. One example of an improper practice is for an office to record a liability reserve in the current year and release the liability reserve to income the next year. This would have the impact of misstating the company’s earnings and the earnings reported by Stewart to public investors.

To record a liability that is not actually owed by the company at the current balance sheet date is not GAAP accounting (“generally accepted accounting principles”). Nor is it GAAP to record a current reserve for repairs or for a business promotion function planned for next year. Another example of improper accounting would be not expensing an item that is incurred and belongs in the current year, even though the item is not paid for until the next year. The list of examples could be expanded.

If the “real” intent of an entry is to smooth or manipulate earnings, it would not be GAAP and such entries would be dishonest.

Improper rationale. A manager may believe that smoothing is being done for the good of the company. It may make the profit trends of the company look better. Some would say that other companies have been known to do this, and therefore we should do it also. However, smoothing is not a practice of, and is prohibited by, reputable corporations. Regardless, we want to do the right thing.

Region Controllers and Houston. Some amounts may seem relatively small to you. However, accountants should not use “materiality” in justifying any *deliberate* improper entry. The Securities & Exchange Commission (SEC) has recently made clear that such entries are unacceptable accounting.

As to gray areas, where you are unclear, accountants should always feel free to talk with your Region Controllers or National Accounting (Kim Peterson x. 8041 or Alison Evers x. 8036) about any entry. No accountant should ever feel that his/her manager can require that an improper entry be made in the company’s books. Capitulating to such demands by management places the accountant at risk of severe discipline. Any management attempt to override appropriate accounting practices will not be tolerated.

**Please refer to Appendix Item 20 for further definitions and examples of proper and improper accounting treatment of certain events.**

Release No. 53  
Date: August 2001

## **APPENDIX**

<b><u>Description</u></b>	<b><u>Item</u></b>
Income Statement - Schedule A .....	1
Balance Sheet - Schedule B .....	2
Other Data – Schedule A-1 .....	3
Summary of Notes Payable - Schedule B-1 .....	4
Summary of Notes Receivable - Schedule B-2 .....	5
Other Quarterly Schedules .....	6
Stewart Chart of Accounts, including a brief explanation of major accounts .....	7
Daily Cash Report.....	8
Cash Forecast .....	9
Report Card.....	10
Sales Report .....	11
National Accounting Personnel .....	12
Analysis of Loss Expense .....	13
Analysis of Computer Costs .....	14
Imprest Account Log .....	15
ALTA Escrow Guidelines .....	16
Outside Auditors – Model Letter of Engagement.....	17
IRS Guide to Information Returns.....	18
Sample Tax Sharing Agreement.....	19
Improper Accounting Treatment Examples.....	20
Stewart Bookkeeping Test .....	*

\* Available from National Accounting on request.

Date: August 2001 (previously November 1998)

# **APPENDIX**

## **ITEM 1**

### **SCHEDULE A - INCOME STATEMENT**

SCHEDULE A			OFFICE NAME						
			Months Ended ____ / ____ / ____						
						Expenses to Revenue			
This Month	Last Month			This YTD Budget	This YTD Actual	Las YTD Actual	This YTD Budget	This YTD	Last YTD
\$	\$	1	Title insurance fees	\$	\$	\$	%	%	%
		2	Escrow fees						
		3	Abstract income						
		4	Other operating income						
		5	Guaranty premiums						
		6	Reinsurance						
		7	Management fees						
		10	Total operating income						
		11	Interest income						
		12	Other (dividends, gains, etc)						
		19	Total investment income						
		20	Total net revenues						
			EXPENSES:						
		21	Salaries						
		22	Bonuses						
		23	Payroll taxes						
		24	Contract labor						
		25	Profit sharing (401k)						
		26	Group insurance						
		27	Other employee costs						
		28	Employee cost						
		29	Losses-escrow, etc.						
		30	Outside search fees						
		31	Attorney fee split						
		32	Computer – LDI						
		33	Rent						
		34	Other occupancy						
		35	Repairs and maintenance						
		36	Depreciation and amortization						
		37	Rent – equipment, etc.						
		38	Rent – title plant						
		39	Title plant expenses						
		40	Attorney fees						
		41	Business promo and advertising						
		42	Travel						
		43	Auto						
		44	Delivery expenses						
		45	Insurance						
		46	Taxes, not on payroll						
		47	Auditing, accounting						
		48	Professional fees						
		49	Bad debts						
		50	Telephone						
		51	Copy supplies						
		52	General supplies						

		53	Postage						
		54	Dues, subscriptions						
		55	Interest expense						
		56	Miscellaneous expense						
		57	Misc – 1						
		58	Misc – 2						
		59	Misc – 3						
		<b>70</b>	<b>Total Expenses</b>						
		<b>71</b>	<b>Income before taxes</b>						
		72	Income taxes - federal						
		73	Income taxes - state						
		<b>74</b>	<b>Net Income (Loss)</b>						

# **APPENDIX**

## **ITEM 2**

### **SCHEDULE B - BALANCE SHEET**

**SISCO Office**  
**Schedule B**

	<b>3/01</b>	<b>Last Year</b>
<b>ASSETS</b>		
Cash and cashlike items:		
101. Cash	201,852	201,898
102. Time deposits	-	-
103. Marketable investments	-	-
Subtotal	201,852	201,898
Receivables:		
105. Notes receivable	-	-
106. Trade accounts	6,296	2,930
107. Employees and other	2,816	462
108. Other stewart companies	37,514	10,811
109. Allowance for doubtful receivables	-	-
Investments, at cost:		
110. Real estate	-	-
111. Affiliates	1,011,308	983,308
112. Other	-	-
Property, plant and equipment, at cost:		
113. Title plant	697,412	697,412
114. Land	-	-
115. Buildings	-	-
116. Accum depreciation - buildings'	-	-
117. Furniture, equipment, vehicles, etc.	471,405	467,607
118. Accum depreciation - furniture, etc.	(323,714)	(296,818)
Other assets:		
119. Goodwill	-	-
120. Prepaids	6,606	4,625
121. Deposits	8,228	8,477
122. Other assets	15,528	16,138
<b>TOTAL ASSETS</b>	<b>2,135,252</b>	<b>2,096,850</b>
<b>LIABILITIES</b>		
Notes payable:		
123. Stewart Title companies	-	-
124. Other than Stewart companies	-	-
Accounts payable and accrued liabilities:		
125. Premiums payable to STG	24,592	14,032
126. Accts payable to Stewart co.'s	-	-
127. Trade	9,970	10,964
128. Policy losses	7,342	7,000
129. Landata	-	-
130. Other liabilities	12,359	8,702
131. Other liabilities	30,955	17,314
132. Other liabilities	132,433	131,540
133. Federal income tax payable	-	-
134. State income tax payable	-	-
<b>TOTAL LIABILITIES</b>	<b>217,652</b>	<b>189,552</b>
135. Common stock	1,000	1,000
136. Other stock	-	-
137. Additional paid-in capital	2,757,227	2,729,227
138. Treasury stock	-	-
139. Retained earnings - beginning of	(822,929)	(787,342)

year		
140. Net income - YTD	82,303	(587)
141. Dividends	(100,000)	(35,000)
142. Retained earnings - end of period	(840,627)	(822,929)
143. Net worth	1,917,601	1,907,298
<b>TOTAL LIABILITIES AND EQUITY</b>	<b>2,135,252</b>	<b>2,096,850</b>

144. Above excludes escrow bank account balances aggregating (\$)	<u>1,247,284</u>
145. Escrow detail records were reconciled with control account through (mm/yy)	<u>01-Feb</u>
146. All escrow bank accounts were reconciled with bank statement through (mm/yy)	<u>01-Feb</u>
147. All operating bank accounts were reconciled with bank statement through (mm/yy)	<u>01-Feb</u>
148. Last board of directors meeting was held on (mm/yy)	<u>01-Feb</u>
149. Last dividend was declared on (mm/yy)	<u>01-Mar</u>
150. Last dividend was in the amount of (\$)	<u>100,000</u>
151. Capital budget authorized for this year was (\$)	<u></u>
152. Amount of capital budget expended to date is (\$)	<u></u>
153. Last internal audit was in (mm/yy)	<u>Jul-98</u>

# **APPENDIX**

## **ITEM 3**

### **OTHER DATA – SCHEDULE A-1**

**SISCO Office**  
**Schedule A-1 Other Data**  
**For the six months ended 6/30/xx**

[illegible]

# **APPENDIX**

## **ITEM 4**

### **SUMMARY OF NOTES PAYABLE - SCHEDULE B-1**

Schedule B-1 Summary of Notes Payable 12/31/xx										
	Payee	Original Date of Note	Original Amt Of Note	Payment terms	Collateral*	Interest rate	Amount at Beginning of Year	Additions	Reductions	Ending Balance
<b>Intercompany Notes Payable:</b>							0	0	0	0
Note 1 Stewart Title Company	STC	07/01/1999	797,907	Int only for one year		7%	797,907			797,907
Note 2 Stewart Title Company	STC	02/02/2000	932,126	Int only through 12/31/06, with balloon due at end of term		7%	932,126			932,126
Total:							<b>1,730,033</b>	-	-	<b>1,730,033</b>
Total per G/L:							-	-	-	<b>1,730,033</b>
Variance:										<b>0</b>
							-	-	-	-
							-	-	-	-
<b>Outside Notes Payable:</b>							-	-	-	-
Outside Note Payable #1	Bank XYZ	04/01/1998	90,000	Int only thru 9/98 then 5389.48 per mo. principal plus int.	Unsecured	9.5	-			-
Outside Note Payable #2	Bank ABC	12/21/1998	130,000	mo. payments incl princ & int	unsecured	8.5	67,632		(8,261)	59,371
Outside Note Payable #3										
Outside Note Payable #4										
Outside Note Payable #5										
Outside Note Payable #6										
Outside Note Payable #7										
Outside Note Payable #8										
Outside Note Payable #9										
Outside Note Payable #10										
Total:							<b>67,632</b>	-	<b>(8,261)</b>	<b>59,371</b>
Total per G/L:							-	-	-	<b>59,361</b>
Variance:										<b>10</b>

# **APPENDIX**

## **ITEM 5**

### **SUMMARY OF NOTES RECEIVABLE - SCHEDULE B-2**

[illegible]

# **APPENDIX**

## **ITEM 6**

### **OTHER QUARTERLY SCHEDULES**

Intercompany Balance Sheet Accounts

Schedule C

Company Name: -

Quarter Ending: 9/30/01

1. Schedule B, line 108: Receivables from other Stewart companies:

Payor	Reason for Receivable	Amount
Total must agree with Schedule B, line 108		

2. Schedule B, line 126: Payables to other Stewart companies:

Payee	Reason for Payable	Amount
Total must agree with Schedule B, line 126		

3. Schedule B, line 129: Payables to Landata companies:

LDI Company	Month of billing / invoice	Amount
Total must agree with Schedule B, line 129		

Prepared by: -

**Analysis of Retained Earnings**

**Schedule K-1**

Company Name:

-

Quarter Ending: 12/31/00

1. Retained earnings, as reported to Houston at end of prior year

\_\_\_\_\_

2. Net income per Schedule A, line 74

\_\_\_\_\_

3. Dividends per Schedule B, line 141

\_\_\_\_\_

4. Other changes (describe in detail)

\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

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\_\_\_\_\_

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\_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

5. Ending retained earnings (must agree to Sch B, line 142)

-

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Prepared by:

-

**Details to Other Income****Schedule K-4**

Company Name: -

Quarter Ending: 12/31/00

1. Gain (loss) on sale of assets (\*)

---

2. Rent income

---

3. Royalty income

---

4. Dividend income

---

5. Real estate income

---

6. Partnership income (\*\*)

---

7. Other (describe)

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8. Total (must agree with Sch A, line 12)

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(\*) Please give details as to the type of asset sold. Information should tie to Schedule T-4 at year-end. If not, please explain.

(\*\*) List name and profit/loss percent. Attach K-1's at year-end.

Prepared by: -

**Premiums & Other STG Payables****Schedule K-7**

Company Name: -

Quarter Ending: 12/31/00

Premiums payable:

- |   |         |
|---|---------|
| 1. Accounts payable to STG @ end of prior year                        | _____   |
| 2. Add: Guaranty premium expense (Sch A, line 5                       | _____   |
| 3. Deduct: Payments made to STG in current year                       | _____   |
| 4. Accounts payable to STG @ end of current quarter (Sch B, line 125) | _____ - |

Note: If line 4 does not agree with Sch B, line 125, explain below.

- |  |                          |       |
|--|--------------------------|-------|
| 5. The last premium payment to STG       | (mailed on __/__/__)     | _____ |
| 6. Total reinsurance payable to STG      | (included in Sch B, line | _____ |
| _____)                                   |                          |       |
| 7. Total negligent losses payable to STG | (included in Sch B, line | _____ |
| _____)                                   |                          |       |
| 8. The last negligent loss payment       | (mailed on __/__/__)     | _____ |

Prepared by: -

**Other Assets & Liabilities****Schedule K-8**

Company Name: \_\_\_\_\_

Quarter Ending: 12/31/00

Schedule B, Lines 120, 121 &amp; 122:

Description	Beginning Balance	YTD Additions	YTD Reductions	Other (Explain)	Ending Balance
_____	_____	_____	_____	_____	-
_____	_____	_____	_____	_____	-
_____	_____	_____	_____	_____	-
_____	_____	_____	_____	_____	-
	-	-	-	-	-

Schedule B, Lines 130, 131 &amp; 132:

Description	Beginning Balance	YTD Reductions	YTD Additions	Other (Explain)	Ending Balance
_____	_____	_____	_____	_____	-
_____	_____	_____	_____	_____	-
_____	_____	_____	_____	_____	-
_____	_____	_____	_____	_____	-
	-	-	-	-	-

Please provide details of deferred revenue , if any, such as:

- nature of revenue
- when services will be performed

Please state amount and nature of any contingent liability.

Prepared by: \_\_\_\_\_

# **APPENDIX**

## **ITEM 7**

### **CHART OF ACCOUNTS**

## CHART OF ACCOUNTS

### LINE-BY-LINE EXPLANATION OF ACCOUNTS

#### STEWART INFORMATION SERVICES CORPORATION AND SUBSIDIARIES

Line-by-line explanations for the income statement, Schedule A, and the balance sheet, Schedule B, follow. National Accounting combines the Schedules of all Stewart companies line-by-line to prepare consolidated reports on a quarterly basis. **For this reason, line names must not be changed.** You may accumulate amounts in subsidiary detail accounts as you deem appropriate for your particular operations, but such amounts must be reported within the appropriate line item.

Also shown are suggested general ledger account codes corresponding with each line of the financial statements. The explanations are limited to the "prime" accounts, which are the first four digits of each accounting code number. You may use the suggested codes or feel free to design your own code of accounts.

<b>Schedule A - Line No.</b>	<b>Prime Account No.</b>	<b>Account Description / Explanation</b>
<b>1</b>	<b>1000</b>	<b>Title insurance fees</b>  Comprises the title insurance premiums received or billed on <u>closed</u> transactions.
<b>2</b>	<b>1100</b>	<b>Escrow fees</b>  Escrow fees collected or billed.
<b>3</b>	<b>1200</b>	<b>Abstract income</b>  Abstract fees collected or billed.
<b>4</b>	<b>1300</b>	<b>Other operating income</b>  Any other <u>title business-related</u> income.
<b>5</b>	<b>2000</b>	<b>Guaranty premiums</b>  The amount of guaranty premiums to Stewart Title Guaranty Co. which corresponds to the amount of title insurance fees recorded (see Account 1000). Accrue any amount unpaid. Do not account for guaranty premium expense on a cash basis. NOTE: a separate schedule must be completed in FEIS each month showing amounts Paid/accrued to other underwriters if applicable (for purposes of reconciliation).
<b>6</b>	<b>2100</b>	<b>Reinsurance</b>  The amount accrued on title insurance fees earned on any policies with a liability in excess of reinsurance limits set by Stewart Title Guaranty Co. This expense should be accrued when the title

Schedule A - Line No.	Prime Account No.	Account Description / Explanation
		insurance fee is earned and recorded. The resulting payable to Stewart Title Guaranty Co. should be recorded on Line 127 of Schedule B (see Account 5180).
7	2200	<b>Other</b>  Any other direct underwriting costs. Note that this account should not be used for attorney fee split. See Account 3150 for attorney fee split.
11	1400	<b>Interest income</b>  Non-title business income earned from various time deposits, including money market funds, or from notes receivable.
12	1500	<b>Other (gains, etc.)</b>  Non-title business income (loss) earned from the sale of assets, the sale of investments, from rent or real estate owned, from dividends on stock held as an investment, from royalties, etc. Includes casualty losses not reimbursed by insurance. The key word here is non-title. Income (loss) that is not title related and is not interest should be classified here.
21	3000	<b>Salaries</b>  Gross salaries expense per payroll. Excludes bonuses. Includes temporary (seasonal) and part-time help - those we provide supplies to, control their hours and under direct supervision of corporate personnel, etc.
22	3010	<b>Bonuses</b>  Gross bonuses expense accrued for all employees.
23	3020	<b>Payroll taxes</b>  Employer's share of FICA, federal and state employment taxes and other payroll related tax you are responsible for paying. Note that this does not include any amounts withheld from employees.
24	3030	<b>Contract labor</b>  Amounts paid to temporary employees.
25	3040	<b>401K Plan</b>  Contributions to a profit sharing plan. This does not include profit sharing bonus plans.

Schedule A - Line No.	Prime Account No.	Account Description / Explanation
--------------------------	----------------------	-----------------------------------

26	3050	<b>Group insurance</b>
		Employer contributions to a group employee insurance plan.
27	3090	<b>Other</b>
		Other employee related expenses or benefits including personnel agency fees, schooling and employee training costs.
29	3470	<b>Losses - escrow, etc.</b>
		Losses derived from escrow shortages, policy claims, or attorney fees paid in connection to such which the company participates in as part of their agency agreement with Stewart Title Guaranty Co. Note: extraordinary losses of fixed assets by natural causes, for example, should not be coded to this account, but instead to Account 1500.
30	3100	<b>Outside search fees</b>
		General expenses of individuals outside the Company's employ who perform title services. Amounts paid to third parties for searches should be recorded here instead of an offset against search income.
31	3150	<b>Attorney fee split</b>
		Amount of title insurance fee relating to amounts recorded as revenue from title insurance fees, which is shared with an attorney for services performed. This amount should be accrued when the title insurance premiums are booked. Please call National Accounting before using this account.
32	3200	<b>Computer LDI</b>
		Expenses incurred as a result of services provided by LDI or LDI subsidiaries. It is important all billings from LDI be accrued promptly. If an amount is in dispute call LDI immediately to resolve the matter. <b><u>Also call the LDI Systems accounting department each month to agree your payable to their receivable.</u></b> Remember, this account is to be used for all expensable transactions with LDI or LDI subsidiaries.
33	3250	<b>Rent</b>
		Expense of renting or leasing office space.
34	3280	<b>Other occupancy</b>
		Non-rental expenses associated with occupying office space such as utilities, janitorial services, parking expense associated with the occupied building and other occupancy-related expenses.

Schedule A - Line No.	Prime Account No.	Account Description / Explanation
35	3300	Repairs, maintenance

Minor repairs and maintenance on furniture, equipment, fixtures and automobiles. Do not use this account for major improvements that would be more appropriately capitalized. Minor repairs to the office building should be put in Account 3280 - Other occupancy.

**36                      3350                      Depreciation and Amortization**

Amounts which have been capitalized as depreciable assets should be depreciated or amortized over the useful lives of the assets. Depreciable assets are limited to furniture and fixtures, office equipment, automobiles and buildings owned by the Company. Leasehold improvements (Account 4600) are to be amortized over the remaining life of the lease with the expense charged to Account 3350. Software, as well as software development (see Release 44) are to be amortized up to three years with the expense charged to Account 3350. The straight-line method of depreciation is the only depreciation method to be used.

Title plants are not to be amortized or depreciated. See Accounts 3450 and 4450.

**37                      3400                      Rent - equipment**

Rent expenses for all rental equipment except rented equipment used in title plant operations and copiers. Leases that are in the form of a purchase should be capitalized and properly amortized. Payments on such capital leases would be coded partially to interest expense and to reduce the liability set up for the lease. Any questions regarding whether or not a lease is capital in nature should be directed to National Accounting or to your local CPA.

**38                      3420                      Rent - title plant**

Expenses incurred for the use of a title plant or for information normally contained in a title plant. This account is used when the Company does not own its plant. This account is distinguished from outside searching in that the latter usually involves the searching of courthouse records and is not a fixed charge for the privilege of use.

**39                      3450                      Title plant expenses**

Expenses incurred to keep a title plant up-to-date. Included in this account are rental of equipment used in title plant operations that are not considered capital leases. This account is for title plant maintenance only. It is not for the purchasing of a plant or back-dating of a plant, which should be capitalized (see discussion of Account 4450).

Schedule A - Line No.	Prime Account No.	Account Description / Explanation
40	3500	<b>Attorney fees</b>
		Fees paid for legal services not related to escrow or policy losses.
41	3520	<b>Business promotion, advertising</b>

Expenses incurred in the marketing of services. It is mandatory to keep separate sub-accounts for advertising, entertainment and dues. Furthermore, entertainment should be separated into a sub-account for business development and a separate sub-account for business meals and entertainment where a customer is present. Club dues should also have a separate sub-account for non-deductible dues. A review should be made periodically of the details supporting such expenditures to insure proper documentation for income tax purposes. (Refer to the required information on Schedule T-5 of the year-end closing package).

**42                      3550                      Travel**

Expenses incurred by employees for travel while away from home over night. Such expenses include airfare, hotels, meals, auto rent, parking and tips. Keep a separate sub-account for spousal travel, which are not tax deductible, and another sub-account for employee meals, which have deductible limits. All employee-reimbursed expenses should be properly reported on the Company's Employee Expense Report along with documentation supporting those expenditures. Auto allowances for day-to-day travel on the Company's behalf should be coded to Account 3570.

**43                      3570                      Auto**

All expenses incurred in the use of an automobile including rent (if not a capital lease), maintenance, minor repairs and fuel. Auto allowances / reimbursements paid to employees for use of their automobiles in Company matters should be coded to this account as well.

**44                      3600                      Delivery expenses**

Expenses incurred using an outside service to pick up orders, checks, deliver commitments, policies and closing packages. Examples would include the use of a local courier service, Federal Express, air freight and bus service. It would also include Federal Express of items sent to Houston. Note: any reimbursement of these expenses from clients should be credited to this account.

**45                      3620                      Insurance**

Generally this account is for casualty and other liability insurance. Houston carries certain insurance coverage for all affiliated offices. See the Manager's Manual for a description of such coverages. Houston bills its affiliated offices for these coverages. Each affiliated office should estimate its insurance expense each month based upon the previous billing and accrue accordingly. For those offices not affiliated with Stewart, insurance expense should be accrued each month (usually an amortization of prepaid insurance over the life of the policy).

<b>Schedule A</b>	<b>Prime</b>	
<b>Line No.</b>	<b>Account No.</b>	<b>Account Description / Explanation</b>
<b>46</b>	<b>3650</b>	<b>Taxes, not on payroll</b>  Expenses for real and personal property taxes, notary bonds and license fees.
<b>47</b>	<b>3670</b>	<b>Auditing, accounting</b>  Expenses relating to the use of an outside accounting firm for various accounting, auditing and tax matters.
<b>48</b>	<b>3680</b>	<b>Professional fees</b>  Expenses for third-party professional services such as consulting.
<b>49</b>	<b>3700</b>	<b>Bad debts</b>  Expenses to reserve for or write-off uncollectible receivables. There are two generally acceptable methods for charging off bad debts: the reserve method and the direct charge-off method. Whichever method is followed, it should be used consistently. The reserve method is preferred.
<b>50</b>	<b>3720</b>	<b>Telephone</b>  Expenses for use of the telephone including rent on equipment (if not a capital lease) and long distance charges.
<b>51</b>	<b>3750</b>	<b>Copy supplies, etc.</b>  Expensing of supplies for copiers and rent on copiers (if not a capital lease) not used in title plant operations.
<b>52</b>	<b>3770</b>	<b>General supplies, etc.</b>  Expensing of all other office supplies including purchases of fixed assets under the capitalization limit.
<b>53</b>	<b>3800</b>	<b>Postage</b>  Stamps or meter postage used in the mailing of correspondence. The account should also include any rent on a post office box. This account should not be used for Federal Express or similar expenses which should be charged to Delivery expense (Account 3600).
<b>54</b>	<b>3810</b>	<b>Dues, subscriptions</b>  Amounts paid to professional organizations and societies. Also include subscriptions to industry publications.

<b>Schedule A</b>	<b>Prime</b>	
<b>Line No.</b>	<b>Account No.</b>	<b>Account Description / Explanation</b>
<b>55</b>	<b>3820</b>	<b>Interest expense</b>  Any interest on outstanding notes, loans, etc., as it is incurred. Accrue if it is not paid. Interest on loans from Stewart Title Company should be agreed with National Accounting calculations. Please call National Accounting each quarter to verify outstanding balances.
<b>56</b>	<b>3950</b>	<b>Miscellaneous</b>  Expenses not described in the preceding accounts. Examples include directors fees, coffee bar expenses and contributions.
<b>57-59</b>		<b>Other Miscellaneous</b>  These lines are reserved for use by REI companies. Each individual company may choose to customize the descriptions related to these lines by providing the descriptions to National Accounting.
<b>72</b>	<b>3980</b>	<b>Income taxes – federal</b>  Accrued provision for federal income taxes.
<b>73</b>	<b>3990</b>	<b>Income taxes – state</b>  Accrued provision for state income taxes.

<b>Schedule B Line No.</b>	<b>Prime Account No.</b>	<b>Account Description / Explanation</b>
<b>101</b>	<b>4000</b>	<b>Cash</b>  Cash in checking accounts plus petty cash. Petty cash should be kept on an imprest basis only. Note: escrow cash is not a balance sheet item.
<b>102</b>	<b>4050</b>	<b>Time deposits (S&amp;L's and Cds)</b>  All such invested funds earning interest. This would include savings accounts, CD's and money market accounts.
<b>103</b>	<b>4080</b>	<b>Marketable investments</b>  Normally investments in securities traded on an exchange. This would include stocks and bonds traded over-the-counter, or on the New York or American Stock Exchanges. Investments in bank stock or non-Stewart companies which have no public market but are still readily marketable may also be included in this account. The fair market value of such securities must be provided to National Accounting at the end of each calendar quarter. Note: generally, offices should seek approval from Houston before investing in <u>any</u> securities.
<b>105</b>	<b>4100</b>	<b>Notes</b>  Any notes owed to the Company. If any notes are non-interest bearing or have an unusually low rate of interest, please contact National Accounting for advice. Be sure to fill out Schedule B-2 and send it along with Schedules A & B to Houston.

Schedule B - Line No.	Prime Account No.	Account Description / Explanation
106	4200	<b>Trade accounts</b>  Regular accounts receivable resulting from the normal operations of business. A trade receivable is the result of a title operation transaction having been closed. The Company must have a legal right to demand payment.
107	4240	<b>Employees and other</b>  Receivables due the Company from employees and others. Employee advances are discouraged. The Stewart Credit Union is available for lending money to employees.
108	4270	<b>Other Stewart companies</b>  Receivables due the Company from other Stewart Companies.
109	4290	<b>Doubtful accounts</b>  This account is for reserving receivables considered uncollectible provided the Company uses the reserve method of accounting. If receivables are written off directly to bad debt, then this account is not used.
110	4300	<b>Real estate</b>  Investments in real estate. This account should not be used for purchased land and buildings used in the business. This account is strictly for investments.
111	4350	<b>Affiliates</b>  Investments in other companies that result in ownership of 20% or more of their outstanding stock. National Accounting should be notified of these acquisitions and appropriate advice will be given as to the accounting treatment.
112	4400	<b>Other</b>  Investments that are non-real estate, which do not result in 20% or more control of a company, which are long-term in nature and not readily marketable. An example would be a small investment in the stock of a local bank or savings and loan company and for which there is no market for the stock.

<b>Schedule B - Line No.</b>	<b>Prime Account No.</b>	<b>Account Description / Explanation</b>
<b>113</b>	<b>4450</b>	<b>Title plant</b>  The cost of establishing, acquiring or substantially improving (back-dating) a title plant. No title plant maintenance should be coded to this account (see separate Release 21).
<b>114</b>	<b>4500</b>	<b>Land</b>  Land owned and used by the Company for its normal title business. This account should not be used for land purchased as an investment.
<b>115</b>	<b>4540</b>	<b>Buildings</b>  Buildings owned and used in the normal course of business.
<b>116</b>	<b>4570</b>	<b>Accumulated depreciation on buildings</b>  The accumulated depreciation on buildings (Account 4540) from the time they were put into use.
<b>117</b>	<b>4600</b>	<b>Furniture, equipment, vehicles, etc.</b>  All equipment, furniture, leasehold improvements and vehicles acquired for the use in the normal course of business. Included in this account would be capital leases. Note: Stewart's capitalization policy is that all expenditures for fixed assets under \$500 should be expensed.
<b>118</b>	<b>4630</b>	<b>Accumulated depreciation on furniture, etc.</b>  Accumulated depreciation on furniture and equipment (Account 4600). This does not include leasehold amortization since it is netted against leasehold improvements directly.
<b>119</b>	<b>4660</b>	<b>Goodwill</b>  Goodwill is the excess cost over the fair market value of the net assets purchased in an acquisition of a company. Most Stewart Companies will not use this account.
<b>120</b>	<b>4700</b>	<b>Prepaid expenses</b>  Expenses paid in advance, such as general insurance, rents, etc. These costs should be amortized in a systematic and periodic charge to expense, reflecting the utilization of the assets over time.
<b>121</b>	<b>4720</b>	<b>Deposits</b>  Payments on deposits for utilities, dues, etc.

<b>Schedule B - Line No.</b>	<b>Prime Account No.</b>	<b>Account Description / Explanation</b>
<b>122</b>	<b>4750</b>	<b>Other</b>  Open
<b>123</b>	<b>5000</b>	<b>Notes payable to Stewart Title Co. and other Stewart companies</b>  Balance of all notes payable to Stewart companies. Be sure to attach Schedule B-1 detailing all notes.
<b>124</b>	<b>5050</b>	<b>Notes payable to other than Stewart companies</b>  Balance of all notes payable to outsiders. Be sure to attach Schedule B-1 detailing all notes.
<b>125</b>	<b>5100</b>	<b>Premiums payable to Stewart Title Guaranty Company</b>  Accounts payable to Stewart Title Guaranty for title insurance premiums only. Do not put any other amounts owed to Stewart Title Guaranty Company in this account.
<b>126</b>	<b>5150</b>	<b>Other amounts payable to Stewart companies</b>  Amounts owed to any Stewart company that are not in the nature of notes payable. Examples would include casualty insurance, rent, telephone expense and interest payable on notes outstanding. Note on this line which company is owed and how much. This account does not apply to federal income taxes owed STC.
<b>127</b>	<b>5180</b>	<b>Trade</b>  Regular trade payables incurred in the normal course of business should be included in this account.
<b>128</b>	<b>5200</b>	<b>Policy losses</b>  Provisions for policy and escrow losses that the company participates in as a result of its agency agreement with Stewart Title Guaranty Co.
<b>129</b>	<b>5300</b>	<b>Landata</b>  Amounts owed as a result of services provided by Landata should be included in this account. It is important that all billings from Landata be accrued promptly.
<b>130</b>	<b>5310</b>	<b>Other</b>  Open
<b>131</b>	<b>5330</b>	<b>Other</b>  Open

<b>Schedule B - Line No.</b>	<b>Prime Account No.</b>	<b>Account Description / Explanation</b>
<b>132</b>	<b>5360</b>	<b>Other</b>  Open
<b>133</b>	<b>5400</b>	<b>Federal income tax</b>  Amounts owed the Federal Government (if you file a separate return) for corporate income taxes. If the company is a part of the Stewart Information Services consolidated return, then this account represents the amount owed to STC.
<b>134</b>	<b>5420</b>	<b>State income tax</b>  Amounts owed the state government for corporate income taxes.
<b>135</b>	<b>6000</b>	<b>Common stock</b>  Par value of the common stock issued and outstanding (including any treasury shares). State the number of shares outstanding on Schedule B.
<b>136</b>	<b>6040</b>	<b>Other stock</b>  Refers usually to a different class of common stock, or preferred stock dealing with voting rights.
<b>137</b>	<b>6060</b>	<b>Additional paid-in capital</b>  Amounts paid to the Company by stockholders for stock in excess of its par value. Other common additions include donated assets, forgiveness of debt and the sale of treasury stock.
<b>138</b>	<b>6100</b>	<b>Treasury stock</b>  The amount paid to repurchase the Company's stock. Include the number of shares repurchased.
<b>139</b>	<b>6150</b>	<b>Retained earnings - beginning of period</b>  Total accumulated earnings net of accumulated dividends paid as of the prior year-end.
<b>140</b>	<b>6200</b>	<b>Net income</b>  Net income from Schedule A, Line 51.
<b>141</b>	<b>6210</b>	<b>Dividends</b>  Dividends declared and/or paid to investors during the year. Note: dividends should not be paid if you have negative retained earnings.

<b>Schedule B - Line No.</b>	<b>Prime Account No.</b>	<b>Account Description / Explanation</b>
<b>142</b>	<b>N/A</b>	<b>Retained earnings-end of period</b>  Sum of Accounts 6150, 6200 and 6210.
<b>143</b>	<b>N/A</b>	<b>Net worth</b>  Sum of Accounts 6000, 6040, 6060, 6100, 6150, 6200 and 6210.

August 2001 (Previously November 1998)

# **APPENDIX**

## **ITEM 8**

### **DAILY CASH REPORT**

**STEWART TITLE COMPANY**  
**Location – Anywhere, USA**  
**Daily Cash Balance**  
**Monthly – July**

Beginning balance .....						10,862.34
DATE	ADD RECEIPTS	DEDUCT DISBURSEMENTS	OTHER ADD	ITEMS DEDUCT	ADDITIONAL INFORMATION (NOTE A)	BALANCE
1	5,130.63					15,992.97
2						
3						
4						
5						
6	5,320.24	3,254.70				18,058.51
7						
8						
9	3,285.30	1,283.24				20,060.57
10	2,021.21	4,326.83				17,754.95
11	1,042.00	250.33				18,546.62
12	200.00	6,000.00				12,746.62
13						
14				6,650.72	Payroll	6,095.90
15			11,000.00		Transfer from savings	17,095.90
16						
17	5,600.30	2,003.42				20,692.78
18						
19	2,321.00	3,226.54				19,787.24
20						
21	526.80					20,314.04
22						
23	5,285.21	2,223.00				23,376.25
24						
25	3,657.00					27,033.25
26						
27						
28						
29						
30				6,783.25	Payroll	20,250.00
31						
Totals	34,389.69	22,568.06	11,000.00	13,433.97	Ending balance .....	20,250.00

Note A – “Other items” should include voided receipts (an item to deduct from bank balance) and voided disbursements (an item to add to bank balance). Show check numbers and receipt numbers in support of all voided items.

# **APPENDIX**

## **ITEM 9**

### **CASH FORECAST**

**Anywhere, USA**  
**Cash Forecast for Next Four Months**

20\_\_\_\_

	Month of August	Month of Sept	Month of Oct	Month of Nov
Cash – Beginning of Month	<u>20,250</u>	<u>32,950</u>	<u>33,270</u>	<u>21,600</u>
ADD Cash Receipts:				
Operating revenues	35,000	25,000	30,000	25,000
Collections on notes	2,000	2,000	2,000	2,000
Collections on accounts receivable	5,000	3,000	2,500	2,000
Revenues from investments	200	220	230	240
Other receipts:				
a. Proceeds on sales of assets		3,000		
b. Proceeds from loans			10,000	
<b>TOTAL Cash Receipts</b>	<b>42,200</b>	<b>33,220</b>	<b>44,730</b>	<b>29,240</b>
DEDUCT Cash Disbursements:				
Operating expenses	25,000	30,000	35,000	28,000
Payments on notes	1,000	1,000	1,000	2,000
Payments on accounts payable	2,000	1,000	1,000	500
Income tax payments	500	400	400	500
Dividends			3,000	
Expenditures for capital assets	1,000	500	6,000	
Loans to:				
a.				
b.				
Expenditures for investments:				
a. Money market fund			10,000	
b.				
c.				
Other disbursements:				
a.				
b.				
<b>TOTAL Cash Disbursements</b>	<b>29,500</b>	<b>32,900</b>	<b>56,400</b>	<b>31,000</b>
Cash – End of Month	<u>32,950</u>	<u>33,270</u>	<u>21,600</u>	<u>19,840</u>

# **APPENDIX**

## **ITEM 10**

### **REPORT CARD (Three Pages)**

**REPORT CARD****PART 1****Cash to Houston****06/30/99**

Date

**Anytown, USA**

Office/City

This YTD

Prior Year

YTD Income before taxest (Line 71) (Mag. Mgr. Measure)	64,490	1	59,250
YTD Revenue (Line 20 + Line 5)	476,791	2	408,962
Excess Cash Available (from Part 3)	37,042	3	0
Notes Payable to STC (Line 123)	130,979	4	140,979
Current STG Loss Reserve Set Up for Your Co. (Reported monthly to you by Nat'l Acct. Dept.)	25,000	5	0
Dividends or Remittance to ST YTD	0	7	0
Management Fee Paid to ST YTD	0	8	0
Note Payments (Principal & interest) to ST YTD	5,000	9	5,000
Note Payments (Principal) to Non-ST YTD		10	
STG Premium Paid YTD	59,583	11	45,673
Title Plant Rent YTD	0	12	0
Interest payments on approved technology loans YTD		13	
Technology-related depreciation YTD		14	
Less Loans Advanced to you from ST YTD	0	15	35,000
Less Loans from Non-ST YTD		16	
Less Other Advances to You from ST YTD	0	17	0
Less Investments in Your Company from ST YTD	0	18	0
Less STG Claims Paid on Your Behalf YTD (Reported monthly to you by Nat'l Acct. Dept.)	2,575	19	0
Less Total Delinquencies (from Part 2)	12,509	20	14,835
Total YTD Net Cash Yield (Mag. Mgr. Measure) (Add Lines 7 thru 20)	49,499	21	838
YTD Cash Yield as % of Revenue (Mag. Mgr. Measure) (Divide Line 21 by Line 2)	10.40%	22	0.2%

Manager:

Date Became Manager:

**AUG 01**  
**Office Name**

**Report Card**

**Part 2**

**Delinquencies to Houston**

	<u>AUG 01</u>
Payroll	0
Income Tax	7,057
Benefit Trust	0
Notes Payable to Stewart Title	0
Title Plant Rent	0
Casualty Insurance	5,452
STG Premium	0
Management Fees & Other	0
Negligent Loss Payments	0
Landata System Billing	0
Total Delinquency	<u><u>12,509</u></u>

AUG 01  
Any Office

REPORT CARD

PART 3

Calculation of 2 Weeks Expense Needs

**From Schedule A:**

Total Expense (line 70) for current + last month	138,619
Add: Guaranty premiums (line 5) for current + last month	23,761
Add: Reinsurance (line 6) for current + last month	0
Add: Mgmt fees (line 7) for current + last month	0
Minus: Depreciation (line 36) for current + last month	2,486
Add (line 29 thru 33) Total	159,535
<b>Total cash balance permitted (line 34 divided by 4)</b>	<b>39,884</b>

**From Schedule B:**

Total cash on hand @ month end (line 104)	76,926
Less - Immediate capital expenditures expected (capital expenditures/immediate payables)	0

Explain: \_\_\_\_\_

\_\_\_\_\_

\_\_\_\_\_

<b>Total cash on hand less capital expenditures</b>	<b>76,926</b>
(line 36 minus line 37)	

<b>Excess cash (line 38 minus line 35)</b>	<b>37,042</b>
--	---------------

Excess cash is to be applied in the following priority:

1. Delinquent payroll.
2. STG premiums.
3. Inter-company federal income tax.
4. Inter-company insurance billing.
5. Inter-company bills that are not current, I.e. Landata, etc.
6. STC loans that are not current or could be paid down.
7. Dividends. Dividends should not be paid unless STC loans are current. If the Terms of the loan are on demand, then it should be paid down before any Dividend is declared.

Manager:

# **APPENDIX**

## **ITEM 11**

### **SALES REPORT**

31-Dec	Dec-01	Nov-01	Dec-00	12 Mo		Breakeven				31-Dec	Dec-01	Nov-01	Dec-00	12 Mo
This	This Mo	Last Mo	Last Yr	Avg Mo	*** Office ***	Emp	\$	B/E		This	This Mo	Last Mo	Last Yr	Avg Mo
Week	To Date	To Date	This Mo To Date	To Date						Week	To Date	To Date	This Mo To Date	To Date
*****PREMIUMS*****										*****ORDERS*****				
70	60	283	260	257	El	53	299	535		219	767	654	449	490
78	37	258	160	167	Corpus	6	45	82		36	117	87	69	72
6	7	31	46	41	Eagle	16	19	136		81	287	284	194	188
60	42	180	120	161	Cameron	6	34	140		27	112	132	0	42
16	7	56	0	23	Victoria	6	53	58		28	90	80	0	36
22	11	65	55	59	Rockport	37	297	370		137	396	364	821	615
51	29	178	115	115	Amarillo	7	68	92		26	49	150	126	92
51	29	193	126	133	Lubbock	7	36	0		213	735	702	434	479
23	9	81	45	55	Texarkana	6	28	0		101	408	328	277	268
166	98	595	432	385	Oklahoma	8	46	63		20	86	85	69	55
5	2	15	16	15	Lawton	3	16	46		33	61	76	49	48
17	29	70	0	41	Wichita	0	0	0		0	0	0	0	0
421	262	1274	1061	1010	Dallas	11	59	81		34	131	121	143	137
19	33	111	5	91	Priority	3	8	0		1364	3740	3186	2026	2139
23	4	40	49	36	Dominion	33	130	254		62	272	329	147	196
724	343	2328	1728	1834	Houston	15	91	274		113	348	347	0	162
26	22	102	54	77	Priority	0	20	561		0	0	0	0	10
40	23	128	132	115	Millenium	7	51	73		0	72	78	75	68
133	73	373	274	305	Fort	20	128	178		65	222	237	165	194
84	112	322	322	284	Galveston	7	35	74		26	94	94	58	59
107	69	760	609	463	Woodlands	27	216	125		72	249	296	207	235
45	15	97	91	104	Beaumont	24	105	160		45	168	152	183	157
23	11	85	36	56	Premier-Houston	6	46	32		13	200	47	69	84
62	28	110	127	118	Pacific-Ft.	7	34	25		44	91	125	62	96

43	8	43	49	71	Dominion	6	33	33	17	74	71	44	62
59	38	210	200	165	Brazoria	33	149	8	63	199	186	217	183
25	25	97	117	83	New	34	225	187	68	309	324	196	247
116	43	401	273	299	Albuquerque	42	274	313	100	514	427	361	386
17	6	43	56	47	Las	12	48	103	34	94	106	117	103
38	27	219	98	163	Santa	22	159	179	54	201	197	184	185
280	80	545	628	534	Austin	77	449	418	163	339	334	521	427
96	37	309	178	220	San	39	161	319	127	399	339	325	328
17	9	73	63	61	Medina	9	40	65	36	97	95	93	97
11	13	57	16	41	Midland	11	42	57	17	74	85	46	72
<b>2974</b>	<b>1641</b>	<b>9732</b>	<b>7541</b>	<b>7627</b>	<b>REGION B</b>				<b>3438</b>	<b>10995</b>	<b>10118</b>	<b>7727</b>	<b>8010</b>
-----													
29	70	77	44	52	Carson	31	179	364	90	316	451	288	202
45	127	168	129	114	Minden	19	92	204	67	214	221	179	356
24	72	55	51	53	Elko	86	551	912	271	955	1022	522	175
155	422	439	287	334	Reno	108	735	1329	287	1379	1458	784	782
283	633	701	317	510	Las	3	19	53	16	43	52	51	1046
5	15	17	13	11	Fallon	28	227	406	81	270	220	75	41
18	90	122	14	54	Oregon	26	165	172	125	341	263	143	187
46	248	309	198	167	Alaska	32	230	649	224	832	842	0	227
91	247	243	0	141	Snohomish	44	361	1044	332	1223	1177	556	563
79	386	399	244	224	Seattle	0	236	0	209	900	1126	0	853
0	363	389	0	68	W.	0	40	0	0	0	57	61	370
0	0	18	18	22	Kittitas	0	44	0	NR	0	0	109	44
<b>775</b>	<b>2673</b>	<b>2937</b>	<b>1315</b>	<b>1750</b>	<b>REGION C</b>				<b>1702</b>	<b>6473</b>	<b>6889</b>	<b>2768</b>	<b>4846</b>
-----													
120	353	303	245	222	Clearwater	53	299	535	219	767	654	449	490
19	38	25	18	24	Jacksonville	6	45	82	36	117	87	69	72

42	97	59	93	64	Lakeland	16	19	136	81	287	284	194	188
17	34	34	0	8	St.	6	34	140	27	112	132	0	42
30	42	29	0	13	Sarasota	6	53	58	28	90	80	0	36
139	295	277	180	216	Stuart	37	297	370	137	396	364	821	615
13	26	17	16	23	Tampa	7	68	92	26	49	150	126	92
17	57	43	34	39	Kissimmee	7	36	0	213	735	702	434	479
16	45	34	28	28	Acquire	6	28	0	101	408	328	277	268
25	79	52	46	45	Cape	8	46	63	20	86	85	69	55
14	19	11	11	12	Ocala	3	16	46	33	61	76	49	48
0	0	0	0	0	Southern	0	0	0	0	0	0	0	0
26	68	58	49	54	MGS	11	59	81	34	131	121	143	137
9	23	8	15	12	Punta	3	8	0	1364	3740	3186	2026	2139
28	70	82	51	51	Manatee	33	130	254	62	272	329	147	196
37	81	66	0	25	Guarantee	15	91	274	113	348	347	0	162
0	0	0	0	1	Tallahassee	0	20	561	0	0	0	0	10
0	39	81	36	47	Shalimar	7	51	73	0	72	78	75	68
49	131	159	111	117	Executive	20	128	178	65	222	237	165	194
17	42	41	37	26	Jackson	7	35	74	26	94	94	58	59
618	1539	1379	970	1026	REGION D				2585	7987	7334	5102	5349
-----													
146	0	42	38	38	Fresno	44	234	331	147	0	84	82	68
125	0	26	12	21	Modesto	48	221	311	231	0	99	52	67
22	0	20	9	11	Monterey	8	30	54	30	0	18	18	16
79	0	33	32	26	San	31	160	222	80	0	57	46	62
13	8	9	0	9	San	9	43	80	32	26	19	0	16
38	10	10	8	9	Bakersfield	9	48	73	31	27	41	28	25
60	10	27	31	19	Los	16	86	142	66	39	38	41	41
63	0	34	19	22	Irvine	19	109	159	82	0	77	39	45

31	7	8	5	9	Santa	10	42	64	42	26	17	21	20
316	0	79	58	53	Riverside	56	316	587	239	0	202	145	144
8	2	3	2	3	San	11	32	107	44	33	37	0	26
42	5	47	0	10	San	18	59	95	57	103	30	0	27
424	131	135	153	138	Ventura	139	1341	1270	322	377	401	297	383
49	2	17	0	8	San	11	61	93	18	33	71	80	75
9	3	2	0	2	Phoenix	1	8	5	0	3	8	8	9
1137	122	138	402	186	Tucson	250	1799	1736	736	479	575	352	482
51	0	12	0	2	Yuma	7	64	30	78	2	52	43	37
85	14	3	15	11	Cuesta	71	178	190	182	686	690	0	178
<b>2698</b>	<b>314</b>	<b>645</b>	<b>784</b>	<b>575</b>	<b>REGION E</b>				<b>2417</b>	<b>1834</b>	<b>2516</b>	<b>1252</b>	<b>1720</b>

56	0	12	0	9	Gillette	17	112	287	193	0	181	0	67
23	0	10	14	14	Hamilton	7	53	72	45	0	18	12	18
83	0	16	20	15	Helena	22	143	157	45	0	65	20	47
24	0	10	16	4	Ketchum	9	41	69	17	0	11	13	17
0	0	0	3	1	Pocatello	0	3	1	0	0	0	2	0
6	0	2	1	1	Idaho	1	15	16	9	0	6	12	5
8	0	2	0	2	Coeur	0	4	5	4	0	3	0	2
2	0	0	0	0	Nampa	0	1	2	6	0	5	0	1
2	0	0	0	1	Aspen	0	1	0	0	0	0	0	0
17	25	32	15	22	Glenwood	6	39	48	14	33	27	8	24
0	0	0	0	0	Breckenridge	0	0	0	0	3	0	0	0
14	13	16	7	7	Grand	3	40	45	15	19	9	4	11
13	0	17	0	7	Vail	5	11	9	13	0	10	0	8
23	0	21	16	21	Steamboat	4	38	45	25	0	23	12	21
37	31	15	22	22	Greely	6	37	322	261	149	148	131	132
11	20	20	0	5	Loveland	4	23	210	158	102	50	0	41

8	9	10	5	7	Sterling	5	21	110	33	54	56	32	44
122	114	114	84	84	Colorado	128	633	1098	491	391	264	188	287
255	633	618	299	512	Denver	114	1051	4263	1201	4060	4404	2846	4216
100	123	130	131	115	Pueblo	21	87	411	158	432	460	465	402
151	667	758	443	519	Canon	151	698	1471	85	1432	1656	1070	1407
131	0	0	96	60	Fort	0	0	0	NR	0	0	357	191
<b>1086</b>	<b>1635</b>	<b>1803</b>	<b>1172</b>	<b>1427</b>	<b>REGION F</b>				<b>2773</b>	<b>6675</b>	<b>7396</b>	<b>5172</b>	<b>6942</b>

1137	122	138	402	186	Chicago	250	1799	1736	736	479	575	352	482
51	0	12	0	2	Memphis	7	64	30	78	2	52	43	37
85	14	3	15	11	Kansas	11	77	60	57	43	111	29	47
155	0	84	30	69	O'Rourke	19	191	80	48	0	19	21	26
230	21	26	52	28	McPherson	31	181	225	126	90	60	64	74
231	52	83	39	50	Minneapolis	31	224	153	104	77	53	40	58
70	10	13	9	13	Detroit	24	102	154	67	43	51	40	38
36	2	7	6	5	Title	7	51	40	60	6	6	3	20
49	0	14	16	30	Choice	6	37	34	26	0	19	19	22
30	3	6	12	10	Remerica	6	32	27	29	3	3	11	10
75	0	40	37	29	Arkansas	32	147	156	94	0	55	54	41
31	5	0	11	7	McDonald	34	269	239	98	103	44	49	71
240	75	72	27	50	Garland	46	303	387	163	175	115	79	112
11	9	10	9	11	Tucker	12	54	81	34	25	19	19	26
68	0	33	56	33	Sheboygan	22	154	197	81	0	50	57	49
295	0	45	68	38	Milwaukee	73	443	411	136	0	87	110	92
191	66	22	12	37	Accurate	13	56	182	45	203	231	129	172
20	0	0	8	3	Abstract	0	3	4	7	19	19	16	18
<b>3005</b>	<b>379</b>	<b>608</b>	<b>809</b>	<b>610</b>	<b>REGION G</b>				<b>1989</b>	<b>1268</b>	<b>1569</b>	<b>1135</b>	<b>1396</b>

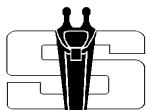
120	246	230	325	254	Indianapolis	40	229	354	116	368	346	404	328
35	106	147	179	151	Central	33	187	261	86	288	216	266	222
12	48	22	60	49	Goshen	8	28	49	22	86	67	67	73
84	190	124	157	142	Merrillville	34	157	222	87	258	249	215	215
9	26	49	0	8	Smart	9	40	68	19	82	62	0	18
32	67	40	84	58	Fairfax	8	43	74	38	116	75	108	88
74	133	106	113	108	Potomac	15	75	152	68	223	183	168	168
61	134	128	131	120	Manassas	19	97	169	95	259	198	206	169
17	44	44	52	54	Fredricksburg	10	40	75	30	90	78	98	83
201	416	307	373	347	Reston	49	273	663	206	724	610	636	534
7	14	13	17	14	Harrisonburg	10	26	85	29	110	88	140	97
17	55	48	0	17	Americlose	9	47	59	21	100	100	0	29
319	983	916	966	981	Maryland	140	1277	1337	365	1512	1235	1291	1153
33	101	72	65	93	Cambridge	11	64	82	51	219	159	114	189
4	23	37	0	42	Chesapeake	1	7	0	3	45	18	0	37
1066	1833	1392	1624	1616	SSC	245	1582	1747	746	2696	2108	2159	1752
35	72	49	65	62	Ohio	5	65	19	9	66	19	72	119
59	110	76	117	109	Columbus	10	62	40	41	112	118	196	159
113	268	275	262	284	Newark	19	186	81	40	143	130	132	119
150	287	198	316	279	STMI	35	169	261	107	338	316	341	287
204	381	263	429	433	SRTA	30	196	177	71	231	247	230	208
60	105	85	144	100	Stewart	23	93	170	62	178	168	240	163
39	69	52	49	45	Stewart	6	50	33	15	145	41	75	72
48	104	112	96	120	Stewart	7	38	35	47	137	119	112	91
48	77	63	64	72	Freehold	6	33	25	50	74	40	90	60
89	171	128	108	161	Your	31	135	155	71	224	150	153	196
72	121	64	79	76	Princeton	34	239	242	76	294	226	204	213
121	350	259	336	276	Stewart	43	255	381	141	480	432	382	357

21	48	50	78	48	Bergen	12	51	50	47	128	114	162	106
53	156	97	132	143	Asheville	22	136	218	63	208	203	137	170
273	502	439	655	553	ST	72	397	499	134	442	513	625	472
67	178	178	188	197	Rhode	39	204	405	106	375	385	374	321
27	76	48	85	62	Stonne	11	45	95	40	119	119	138	90
24	46	41	34	27	New	11	43	63	19	95	63	23	53
0	0	0	0	0	Vermont	0	0	0	NR	0	0	0	0
0	0	0	0	0	Connecticut	0	0	0	NR	0	0	0	0
0	314	298	249	248	Massachusetts	0	0	0	31	1703	1649	1072	1335
81	0	0	0	0	Maine	0	0	0	NR	0	0	0	0
<b>3675</b>	<b>7854</b>	<b>6450</b>	<b>7632</b>	<b>7348</b>	<b>REGION H</b>				<b>3152</b>	<b>12668</b>	<b>10844</b>	<b>10630</b>	<b>9742</b>
-----													
43	77	55	62	56	White	15	75	242	95	299	196	115	168
72	168	106	117	126	Albany	31	177	411	170	451	365	377	336
23	55	57	45	58	Syracuse	19	92	172	53	221	139	163	172
237	439	302	351	361	Manhattan	78	532	921	294	1022	773	580	672
399	701	496	430	513	Long	105	697	1273	431	1458	1153	865	907
<b>774</b>	<b>1440</b>	<b>1016</b>	<b>1005</b>	<b>1113</b>	<b>STIC</b>				<b>1043</b>	<b>3451</b>	<b>2626</b>	<b>2100</b>	<b>2254</b>
5	17475	24570	21360	21583	*****TOTAL*****				19099	51351	49292	36143	40449
24	2273	2572	1603	1996	LESS				1938	7581	7693	5123	6631
73					NON-PREMIUM								
<b>16</b>	<b>15202</b>	<b>21999</b>	<b>19757</b>	<b>19587</b>	<b>**GRAND TOTAL**</b>				<b>17161</b>	<b>43770</b>	<b>41599</b>	<b>31020</b>	<b>33818</b>

# **APPENDIX**

## **ITEM 12**

### **NATIONAL ACCOUNTING PERSONNEL**



## STEWART TITLE GUARANTY COMPANY

Inter-company Correspondence - National Accounting

Date: September 28, 2001

To: All Accounting Personnel,  
Region and District Managers,  
Region Controllers

cc: National Accounting

Associates

From: Alison Evers

Enc.: X

### **Subject: Re-introduction of the National Accounting Department**

Due to the many personnel and reorganization changes that have taken place in our department over the past year I thought now would be an appropriate time to “re-introduce” the National Accounting Department to you. I believe it is quite important for all of you to know who we are, what we do, and **how we can assist you** in your day-to-day, monthly, quarterly and annual accounting and financial statement preparation efforts.

Our relationship is unique--we are each others **customers**. I want to make sure that our department exceeds your expectations of customer service. I also want to emphasize that we are NEVER too busy to assist you with any of your financial questions. You should not hesitate to pick up the phone or E-mail and contact the appropriate person who can assist you with your questions, problems and concerns. The following introduction of National Accounting associates and the attached organization chart will help you identify the appropriate associate to contact:

**Max Crisp**, Executive Vice President-Finance. Extension 8026. Responsible for leading the National Accounting Department. Primary contact for investor relations.

**Sue Pizzitola**, Assistant to Senior Vice President-Finance and Corporate Secretary. Extension 8025. Responsible for corporate secretary functions, shareholder relations and coordinating the production of the annual report.

**Teresa Segraves**, Assistant to Vice President-Finance. Extension 8038. Assists with finance projects such as acquisitions and quarterly company financial analyses. Coordinates audit with KPMG Peat Marwick.

**Elizabeth Cahill**, Accounting Assistant-Acquisitions. Extension 8130. Assists with acquisitions.

**Ken Anderson, Vice President and Treasurer.** Extension 8029. Responsible for treasury functions (banking relations, investment management, accounts payable, insurance programs.)

**Alison Evers, Senior Vice President and Controller.** Extension 8036. Oversees all corporate financial reporting (monthly, quarterly and annual financial statements, Form 9 (statutory annual statement), tax returns, SEC reporting, premium taxes, statutory statistical reporting.)

**Sharon Thompson, Administrative Assistant.** Extension 8035. Responsible for coordination of agent license renewals and preparation of the year-to-date Loss Memorandum.

**Lisa Nelson, Director of Agency Accounting.** Extension 8277. Responsible for the activities of Agency Accounting, including processing of policies (data entry, filing, reporting, inventory), deposit preparation, and preparation of Schedule XL and the Delinquent Premium Report.

**Kim Peterson, Manager of Financial Reporting.** Extension 8041. Responsible for corporate reporting to stockholders, SEC (10Q and 10K), and management via the Flash, Directors' Report, quarterly and annual reports to shareholders, Option Report and Magnificent Managers. Responsible for updating and maintaining the accounting manual and answering inquiries from the field regarding such. Responsible for the coordination and preparation of the quarterly and year-end consolidation.

**Lisa McClure, Assistant Controller-STG.** Extension 8049. Responsible for STG accounting records and reports. Also responsible for loss reserves and statutory premium reserve calculations.

**Sharon Hollis, Statutory Accounting Manager.** Extension 8040. Responsible for statutory filings such as Form 9's and various state statistical reporting. Responsible for investment accounting.

**Anna John, Assistant Controller-STC.** Extension 8050 and 8044. Responsible for the accounting records of STC-General and its branches and SISCO. Responsible for loans made to STC subsidiaries.

**David Nicholson, Tax Manager.** Extension 8039. Responsible for corporate tax issues, preparation of the consolidated federal income, state and franchise tax returns. Responsible for tax billings to subsidiaries. Assists in quarterly and year-end consolidation.

**Steve Gottardy, Senior Accountant.** Extension 8037. Responsible for STG notes receivable, preparation of the National Experience Report, daily deposits, premium taxes, personal property taxes, STG district office accounting and Canada and assists Sharon Hollis with statutory duties.

**Claudia Light, Assistant Controller-STG.** Extension 2803. Assists Senior VP and Controller with various project and acquisitions. Target market and ROI analysis. Assist in performing quarterly and year-end financial statement analyses. Assist in analysis of potential acquisitions. Assist CFO in preparation of forecasts. Assist in the preparation of Federal Income Tax Returns. Prepare loss reserve calculations and related analyses. Help on special projects as assigned by CFO or Controller . Report directly to Controller.

**Lori McManis, Senior Accountant.** Extension 8051. Lori's main responsibilities are preparation of monthly STG financial statements and making estimated premium tax payments.

**Norma Starling, Accounting Assistant.** Extension 8048. Responsible for the preparation of Sales Report and Region Performance Report. Responsible for the preparation of the Magnificent Managers and President's Reports. Assists the Assistant Controller.

**Barbara Wilson, Accounting Assistant.** Extension 2203. Prepares and keys deposits, daily journal entries, fixed asset accounting, property taxes, rent and parking allocations and assists in preparation of various reports, including unclaimed property reports.

**Vickie Brown, Assistant Treasurer and Risk Manager.** Extension 8030. Assists Treasurer with short-term investing, cash management; supervises the company's casualty insurance program including gathering underwriting data and intercompany billings.

**Angela Thomas, Accounts Payable Supervisor.** Extension 8290. Supervises Accounts Payable, processes Imprest Accounts for Regions B and C, expense reports for Forms & Information, National Accounting and STC and SISCO payments, rushes for STG, STC & SISCO.

**Allison Jasky, Treasury Assistant.** Extension 2286. Assists Treasurer with short-term investing, maintains CD portfolio and maintains P-Card Program. Please send all payables calls or inquiries to Angela Thomas.

**Matthew Mott, Accounts Payable Administrator.** Extension 8032. Processes Imprest Accounts for Regions D & E, expenses for National Legal, National Title Services and Agency Accounting and Federal Express payments.

**Gertrude Graham, Accounts Payable Administrator.** Extension 8207. Processes Imprest Accounts for Regions F, G & I, expenses for Mast, Employee Services, Executive Offices, Audit Services, Communications/Publications, Quality and handles fixed assets.

**Joni Anderson, Handles Imprest Accounts for Region H (is part-time staff).**

Please let us hear from you should you have suggestions for improvement for the National Accounting Department, the Accounting Guide, financial reporting packages or any other matters for which our department is responsible.

**Remember, we are here for you. Do not hesitate to use our services to provide guidance and support to your accounting function.**

# **APPENDIX**

## **ITEM 13**

### **ANALYSIS OF LOSS EXPENSE**

### **ANALYSIS OF LOSS EXPENSE**

		<b>2000</b>	<b>1999</b>	<b>1998</b>	<b>1997</b>	<b>1996</b>	<b>1995</b>	<b>1994</b>	<b>1993</b>
(1)	Line 1 revenue	200,000	300,000	300,000	400,000	200,000	250,000	300,000	350,000
(2)	Loss accrual (%) (Line 29 ÷ Line 1)	5.0	2.0	2.0	5.0	3.0	5.0	3.0	3.0
(3)	Loss accrual (\$)	10,000	6,000	6,000	20,000	6,000	12,500	9,000	10,500
(4)	Beg. balance: policy loss liability	2,000	8,000	10,000	3,000	6,500	1,500	8,500	0
(5)	Add : loss accrual (Line 29)	10,000	6,000	6,000	20,000	6,000	12,500	9,000	10,500
(6)	Less: escrow losses-actual payments	5,000	10,000	5,000	13,000	5,000	3,000	15,000	2,000
(7)	: negligent losses-paid to Houston	1,000	0	1,000	0	4,500	3,500	1,000	0
(8)	: other loss payments	1,000	2,000	2,000	0	0	1,000	0	0
(9)	Ending balance: policy loss liability	5,000	2,000	8,000	10,000	3,000	6,500	1,500	8,500

# **APPENDIX**

## **ITEM 14**

### **ANALYSIS OF COMPUTER COSTS**

**Analysis of Computer Costs**  
**Company Name:**  
**Quarter Ending:** 12/31/XX

This Quarter	Last Quarter	Sch A Line #	Line Description	This YTD	Last YTD
		21	Salaries (direct)		
		22	Bonuses		
		23	Payroll taxes		
		32	Computer - LDI		
		33	Rent		
		34	Other occupancy		
		36	Depreciation		
		37	Rent - equipment		
		42	Travel		
		45	Insurance		
		50	Telephone		
		52	General supplies		
		55	Interest expense		
		56	Miscellaneous		
			<b>Totals</b>		

Comments:

- 21. Salaries related to operation, network administration & programming personnel.
- 32. Amounts paid to Landata & outside vendors for maintenance, programming and network fees.
- 33. Utilities, janitorial services & parking related to computer operations.
- 37. Expense related to rental of computer equipment.
- 45. Insurance expense related to computer operations.
- 50. Include any modem lines dedicated to computer communication.
- 55. Interest on notes, loans, etc. related to the purchase of computer equipment.

Note: See the Accounting Guide (Release 42) for further instructions for this form.

Prepared by:

# **APPENDIX**

## **ITEM 15**

### **IMPREST ACCOUNT LOG**

**Stewart Title Guaranty Company**

Date: \_\_\_\_\_

# **APPENDIX**

## **ITEM 16**

### **ALTA ESCROW GUIDELINES**

**1997**

**Escrow Internal Control Guidelines  
For Title Insurance Companies,  
Agencies and Approved Attorneys**

Title insurance and escrow companies provide services that reflect the unique nature of real estate transactions in our society. Services provided vary from one area of the country to another and may include acting as escrow agent, obtaining releases, and conducting the actual closing or settlement. However, the essential purpose is the same, i.e., to assist the parties in real estate transactions by ensuring that the acquisition or transfer of property interest can be effected with a maximum degree of efficiency, security, and safety.

An escrow is a transaction in which an impartial third party acts in a fiduciary capacity as an agent for the seller, buyer, borrower, and lender.

The escrow holders have fiduciary responsibility for prudent processing, safeguarding, and accounting for funds entrusted to them by escrow customers. Accordingly, this responsibility results in significant exposure to losses from inadvertent or intentional failure to execute their duties properly.

It is the purpose of these guidelines to present minimum internal control objectives for escrow operations and to establish fundamental control practices and procedures necessary to achieve these objectives.

The implementation of these guidelines should help achieve several internal control objectives, including:

- Improved customer service.
- A reduction of errors.
- Protection of depositors' funds.
- Reduced potential for losses.
- More effective and efficient control of operations.
- Providing a framework for industry-wide control standards.

Management is responsible for reviewing and evaluating its operations considering their size, complexity, and local statutes. Based on this evaluation, management must establish an effective accounting system and an effective system of internal control to achieve the stated objectives.

**Escrow Internal Control**

Custody of escrow funds is a stewardship function. To fulfill that responsibility, management must establish control procedures in the day-to-day operations which will safeguard customers' assets and ensure reliable recording of all escrow transactions.

**Internal Control Elements**

It should be recognized that the following elements of internal control are not alternatives, but are a complementary group designed to be utilized in conjunction with one another.

### *Adequate Personnel*

An adequate number of trained and supervised personnel are an important element of a system of internal control. Competent, reliable employees may compensate for weaknesses in other areas.

### *Adequate Segregation Duties*

The concept of segregation of duties provides that no one person is solely responsible for the initiation, authorization, and recording of a transaction. To the extent that staff size permits, escrow activities, bookkeeping activities, cashiering activities, and title production activities should be performed by different employees. Because small businesses often do not have sufficient staff to provide for a complete segregation of duties, the day-to-day supervision by an owner/ manager provides an important control over escrow activities. Irrespective of size, it is management's duty to segregate the responsibilities of employees and to provide adequate supervision.

### *Authorization of Transactions*

All transactions must be authorized by the proper level of management. Company policy should establish authorization limits based upon the amount and type of transaction. Specific authorization is needed for transactions not covered by company policy.

### *Adequate Documents and Records*

Documents and records, such as escrow ledgers, escrow files, trial balances, and bank account reconciliations, are the evidence for transactions. Documents should be consistent, prepared in a timely manner, and easily understood. Documents supporting each transaction must be retained for an appropriate period of time as established by management and statutes.

### *Physical Control Over Escrow Assets and Records*

Assets and records must be safeguarded from theft, misplacement, or destruction. Special attention should be given to unused checks, escrow files, and undeposited receipts.

### *Management Review*

Periodic independent reviews by operating management are necessary to insure compliance with company policies and procedures.

An independent audit is another effective mean for evaluating the control environment.

## **Records, Documents, and Procedures Fundamental To All Escrows**

The records, documents, and procedures outlined in these guidelines should not be considered as "all-inclusive", but rather as fundamental to the establishment of a basic system of internal controls for escrow operations.

### *Essential Records and Documents*

- A separately maintained file, bearing an identification number, which is used for the retention of documents pertaining to each transaction.

### *American Land Title Association*

- A formal agreement, signed by appropriate parties, which authorizes actions taken by escrow holders.

- Amendments, as required, signed by appropriate parties, as authorization for actions of escrow holder, not included in the original agreement.
- Closing or settlement statement signed by the appropriate parties.
- Correspondence and other documents that support the actions of escrow holder.
- Individual escrow ledger records listing receipts and disbursements in chronological order and showing the balance of escrow funds at each transaction date.
- Control account, i.e., a cumulative daily balance of escrow funds received and disbursed (balance per checkbook).
- Correspondence and other documents required by state and federal authorities.
- Monthly trial balances of individual escrow ledger records.
- A control listing of all escrow bank accounts including; checking, savings, and indemnities.

#### *General Escrow Procedures*

- All escrow funds should always be deposited in a federally insured institution and used for escrow or closings in connection with real estate transactions only. Escrow funds are not to be commingled with operating, non-real estate settlement, or attorney trust funds. Escrow bank accounts must be designated as such on the account signature card and bank resolution.
- Checks and drafts received for escrows should be restrictively endorsed immediately and promptly deposited.
- Whenever possible, cash transactions should be avoided. If avoidance is not possible, receipts should be provided and all federal forms completed.
- Checks and drafts should be pre-numbered, used in numerical sequence, and properly safeguarded. (Dual signatures should be considered where practical).
- Management should implement effective controls over wire transfers. Internal controls should, at a minimum, include: proper segregation of authorization, initiation and verification; review of supporting documentation (e.g., written escrow agreement, closing statements, instructions, etc.) prior to execution of wire outs; immediate verification of bank advises against escrow authorizations and instructions; use of personal identification numbers; and independent call backs.
- Overdrafts (i.e., shortages, negative balances) in individual escrows should be reviewed by management immediately and corrective action initiated.
- A trial balance of the individual escrow ledger records should be prepared monthly and retained.

- A three-way reconciliation of the bank account to the control account and to the trial balance should be prepared and a copy retained monthly. Prompt investigation should be made of unusual reconciling items, including old out-standing checks. Management should periodically review the reconciliation to ensure reconciling items are being done on a timely basis. Account reconciliation is not considered complete until all reconciling items have been identified and resolved by management.
- Management should review inactive escrows with balances and initiate action, as required. Also, outstanding checks over six months old should be investigated and any reissue of checks approved by management. State escheat laws should be adhered to. Written approval should be required for any disbursement from an inactive escrow.

#### *Procedures for Individual Escrows*

- Documents (agreement, amendments, closing statements, etc.) should be retained in a file that has been assigned to the specific escrow.
- Individual accounting escrow ledger record should be posed as transactions occur and retained by persons responsible for bookkeeping functions.
- Files should be balanced prior to closing to assure sufficient deposits have been made to equal calculated disbursements. Disbursements should be made only from collected funds related to the same escrow. Collected funds as used herein, means cash or wire transfers, certified, cashier, and teller checks from an institution insured by the FDIC, the FSLIC, or the National Credit Union Share Insurance Fund, United States Treasury Checks, and checks that, given local banking customs, should have cleared the banking system.
- Funds accepted in an individual escrow transaction must be invested in accordance with, and only upon, signed instructions by the proper parties. Authorization should include, but not be limited to, the name of the institution, the type of investment, the principal, and the rate of interest (of applicable). Registration of the investment (savings account, security, etc.) should include the customer's name and the title company's name, such as "Escrowee under Escrow No \_\_\_\_\_", "Trustee For", or "Escrow Agent for." However, the customer must not have signatory authority on the account.
- Documents evidencing investments (passbook, certificate) and disbursement forms (e.g. money market checks) should be properly safeguarded within the bookkeeping department.
- Unless specifically authorized by signed agreement, management approval should be required for transfers of funds between escrow files.

## **Conclusion**

The establishment and maintenance of sound accounting systems and related internal control procedures is essential to properly safeguard the assets of any company and its customers and to assure a prompt, accurate accounting of the business transactions. Management has the responsibility for establishing an escrow control system which should:

- Minimize financial risk,
- Provide an adequate escrow control environment, and
- Satisfy the fiduciary responsibility.

The *Escrow Internal Control Guidelines* should not be considered as “all-inclusive” and as such, the controls implemented should be tailored for the individual escrow system. However, management should exercise prudent judgment in the evaluation of the cost/benefit relationship of proposed controls. Sufficient controls should be implemented and monitored in order to provide reasonable assurance that assets are adequately safeguarded and that the escrow accounting is proper.

# **APPENDIX**

## **ITEM 17**

### **OUTSIDE AUDITOR – MODEL LETTER OF ENGAGEMENT**

This is to confirm the appointment of \_\_\_\_\_ as auditors of \_\_\_\_\_ for the year ending December 31, 20\_\_\_\_. We understand you will also review quarterly reports prior to issue. A formal written report on your quarterly reviews will not be required. Additionally, we have asked you to review the consolidated federal income tax return for the year 20\_\_\_\_.

We will also appreciate your consultation services on tax and accounting systems matters, including any recommendations for improving our financial reports, personnel or any other matter which may come to your attention.

Your audit opinion should be based on an examination made in accordance with generally accepted auditing standards and accordingly, include such tests of the accounting records and other supporting evidence and review of internal accounting controls as you may consider necessary.

We understand such examination and review will not include a detailed audit of transactions, such as would normally be required to disclose defalcations or other irregularities, nor will such review necessarily reveal all significant matters concerning financial information. The responsibilities and functions of the independent auditor in the usual examination and review of financials statements are described in Sections 110 and 150 of Statement of Auditing Standards No. 1 and Paragraph 8 through 18 of the Statement of Auditing Standards No. 10, respectively, issued by the Auditing Standards Executive Committee of the American Institute of Certified Public Accountants.

**20** billings. We understand your estimate of the total billings for the 20\_\_\_\_ audit and the 20\_\_\_\_ tax return review is \$\_\_\_\_\_ (as compared to \$\_\_\_\_\_ last year), as shown in more detail below.

**20\_\_\_\_ audit:**

Regular audit, including escrow .....	\$ _____
Quarterly reviews .....	_____
Subtotal .....	_____
Out-of-pocket expenses, including stenos .....	_____
<b>20____ tax return, review .....</b>	<b>_____</b>
<b>Total .....</b>	<b>\$ _____</b>

Note to office: You should be able to negotiate a discount off standard rates with your outside auditors; for example, billed at 65% of their standard hourly rates.

If your final time charges should be less than the above-estimated total of \$\_\_\_\_\_, we understand that we will be billed the lesser amount.

We want to take any steps practicable to reduce your billings. Please advise us of any savings which would accrue to us by use of our internal audit and accounting staff. Any extended work required by you as a result of lack of cooperation on our part or inadequate records should be brought to my attention immediately.

Except for any additional time we may authorize, as described below, it will be considered highly unusual for your billings to exceed the above estimates. We ask you to make every effort to keep your audit and tax time charges to a minimum.

We understand your estimates do not include any additional time relating to (1) any extension of scope on encountering a significant new matter, (2) FASB and SEC rules, (3) major acquisitions and (4) any significant consultation, research of similar work requested by us which falls outside the scope of your regular examination and review work. Please obtain our written approval, either

in formal letter agreement or as an informal memo to our files, before undertaking any additional work.

**Supporting time schedules.** Please attach a supporting schedule for each amount billed (other than for advances) showing your actual time charges, summarized as to hours and money, stated at standard rates, by staff and classifications.

\* \* \* \* \*

**Management letter.** By no later than \_\_\_\_\_, 20\_\_\_\_ please deliver to me:

- A letter addressed to the board of directors stating clearly that your work disclosed “no material internal control weaknesses we believe might result in material errors in Stewart’s financial statements” or similar wording (assuming this is your finding).
- A memorandum addressed to me detailing any recommendations for improving internal accounting controls.

After we have discussed them and have prepared a response to each recommendation, we will request that the audit committee of the \_\_\_\_\_ board meet with you on or about \_\_\_\_\_, 20 \_\_\_\_\_. Please be prepared to discuss not only your recommendations but any other matters you may feel would be appropriate. The committee will report to the full board, providing each member with a copy of your report.

You will be requested to attend the annual shareholder meeting tentatively scheduled for \_\_\_\_\_, 20\_\_\_\_\_.

Please do not hesitate to request a meeting at any time with the board, its audit committee, or any member or group of executive management for the purpose of reviewing any subject you feel should be initiated by you.

**Deadlines.** We will send you a schedule of time deadlines for the year-end closing of the consolidated accounts to help you plan your audit work. If such deadlines are met, we will expect your opinion date to be no later than \_\_\_\_\_, 20 \_\_\_\_\_.

We expect to complete the tax return and supporting schedules by \_\_\_\_\_, 20\_\_\_\_\_. Your tax review should be completed on or about \_\_\_\_\_, 20\_\_\_\_\_ to permit us to file the return on \_\_\_\_\_, 20\_\_\_\_\_.

Please sign below and send me a copy if this letter adequately described our agreement.

Cordially,

Accepted by: \_\_\_\_\_

# **APPENDIX**

## **ITEM 18**

### **IRS GUIDE TO INFORMATION RULES**

# **APPENDIX**

## **ITEM 19**

### **TAX SHARING AGREEMENT**

**AMENDED AND RESTATED TAX SHARING AGREEMENT**

This Amended And Restated Tax Sharing Agreement (hereinafter referred to as the "Agreement") is effective as of the first day of the consolidated return year beginning January 1, 1997, and is made by and among Stewart Title Company ("Parent") and its currently existing affiliates (the list of affiliates appears in "Exhibit A", attached hereto and incorporated herein by this reference) of Parent domiciled in the United States (collectively, the "Affiliates").

WHEREAS, Parent and Affiliates (sometimes individually referred to herein as "Affiliate") are part of an affiliated group ("Affiliated Group") as defined in Section 1504(a) of the Internal Revenue Code of 1986, as amended ("Code"); and,

WHEREAS, certain of the Affiliates have in the past filed consolidated federal income tax returns under Code Section 1501 and anticipate filing such returns in the future; and,

WHEREAS, certain of the Affiliates have lower tier subsidiaries and such Affiliate and its subsidiaries are to be considered as one consolidated Affiliate; and,

WHEREAS, the Affiliates desire that each Affiliate pay to Parent such amounts equaling each respective Affiliate's federal income tax liability, or receive from Parent such sums equaling the savings in such liability; all to be calculated as if the respective Affiliate had not been a part of the Affiliated Group;

NOW, THEREFORE, in consideration of the premises and mutual promises contained herein, Parents and Affiliates hereto agree as follows:

1. Parent and certain of the Affiliates have previously entered into a certain Agreement for Payment of Federal Income Tax Liability, effective upon the date of acquisition and/or ownership of the Affiliate (the "Prior Agreement"). The Affiliates hereby agree that this Agreement supersedes in all respects the Prior Agreement concerning the periods referred to in Paragraph 2 hereof.
2. Parent which is a part of Stewart Information Services Corporation's (SISCO) affiliated group will be included in SISCO's consolidated U.S. federal income tax return for the taxable year ending December 31, 1997 and for each subsequent taxable year during which this Agreement is in effect and for which the Affiliates are required or permitted to be included in a consolidated U.S. federal income tax return. Each Affiliate shall execute and file such consents, elections and other documents as may be required or deemed appropriate for the proper filing of such returns.
3. The Affiliates desire to allocate each Affiliate's annual federal income tax burden in a manner designed to compensate the Parent for the federal income tax expense of each Affiliate (as defined in Paragraph 4(a) hereof ("Federal Income Tax Expense")) and to compensate each Affiliate for the value of its net operating loss (as defined in Paragraph 4(b) hereof ("Net Operating Loss Value")) and tax credits (as defined in Paragraph 4(c) hereof ("Tax Credits")).
4. The Federal Income Tax Expense, the Net Operating Loss Value and the Tax Credits shall be determined on a monthly basis in the following manner:

(a) The Federal Income Tax Expense shall consist of current tax calculated as if each Affiliate filed a separate federal income tax return; provided, however, that for purposes of computing the Federal Income Tax Expense, each Affiliate shall multiply its separate taxable income by the maximum tax rate as provided in Internal Revenue Code Section 11.

(b) The Net Operating Loss Value shall equal each Affiliate's federal income tax loss multiplied by the maximum tax rate as provided in Internal Revenue Code Section 11. Each Affiliate's federal income tax loss shall be determined as if the Affiliate filed a separate federal income tax return; provided, however, that only those losses which are used by other Affiliates of the Affiliated Group to reduce current federal income taxes payable shall be included for purposes of determining the Net Operating Loss Value.

(c) The Tax Credits shall equal each Affiliate's allocable federal income tax credits determined as if each Affiliate filed a separate federal income tax return; provided, however, that only those credits which are used by other Affiliates of the Affiliated Group to reduce current federal income taxes payable shall be included for purposes of determining the Tax Credits.

(d) Intercompany transactions which are deferred under the consolidated return regulations shall not be recognized in each Affiliate's calculation of its taxable income or loss for purposes of this Agreement.

5. All payments and settlements among Affiliates under the Agreement shall be in cash or by increase or decrease to the appropriate intercompany accounts.

6. All payments required by Paragraph 3 hereof shall be made within 30 days of a calendar month-end. If an Internal Revenue Service ("IRS") settlement includes any amount attributable to interest, such interest shall be allocated to each Affiliate based upon such Affiliate's contribution to the settlement adjustment. Such allocation shall be consistent with the principles set forth in paragraph 3. Payments due under Paragraph 3 shall be paid even if there is no consolidated federal income tax due from the Affiliated Group for any particular taxable year.

7. (a) If the Federal Income Tax Expense, Net Operating Loss Value or Tax Credits are subsequently adjusted for any taxable period, whether by means of an amended return, claim for refund or tax audit by the IRS, the liability of each Affiliate under Paragraph 3 shall be recomputed in order to give effect to such adjustments.

(b) In the case of a decrease in actual consolidated federal income tax liability, the Parent shall pay to each Affiliate such Affiliate's allocable share of such decrease, consistent with the principles set forth in Paragraph 3. In the case of an increase in actual consolidated federal income tax liability, each Affiliate shall pay its respective allocable share of such increased tax liability, consistent with the principles set forth in Paragraph 3.

(c) If any interest (as defined under Code Section 6621) or penalties (as defined in Chapter 68 of the Code) are paid or received as a result of consolidated income tax deficiency or refund, such interest or penalties shall be allocated among the Affiliates consistent with the principles set forth in Paragraph 3.

(d) Any payments under this Paragraph 7 shall be paid within thirty (30) days of the payment of the additional tax or receipt of a refund.

8. This Agreement shall apply to the taxable year beginning January 1, 1997, and to subsequent taxable years, unless (a) Affiliated Group agrees in writing to terminate this Agreement or (b) the Affiliates cease to file consolidated federal income tax returns. Notwithstanding termination hereof, this Agreement shall continue in effect with respect to all payments relating to all taxable periods prior to termination.

9. All materials including but not limited to returns, supporting schedules, work papers, correspondence and other documents relating to the consolidated federal income tax returns filed for a taxable year during the term of the Agreement shall be made available to each Affiliate during regular business hours.

10. In the event that a consolidated, unitary or combined income tax return is filed in any state or local tax jurisdiction by the Affiliated Group, any income tax which is due in connection with such return shall be allocated only to those Affiliates whose activities subjected the Affiliated Group to such filing requirement. Each such Affiliate with a nexus in the state or local tax jurisdiction shall be apportioned tax liability as if that Affiliate filed a tax return in that jurisdiction on a separate basis. In addition, the tax liability on the consolidated income which is attributed to Affiliates without a nexus in that state or local tax jurisdiction shall be apportioned to each Affiliate with such a nexus, on the basis of the ratio that such Affiliate's apportionment factor had to the total apportionment factor of all Affiliates which had taxable activities in that jurisdiction. The payment obligation under Paragraph 3 hereof shall be applied on a rational and consistent basis to such state or local tax jurisdiction in the event that more than one Affiliate has a nexus in a particular jurisdiction and one of the Affiliates has a net operating loss. In the event that state or local income tax liability is subsequently adjusted for any taxable period, whether by means of an amended return, claim for refund or tax audit, the liability of each Affiliate shall be recomputed according to any adjusted apportionment factors.

11. Parent and Affiliates hereto acknowledge that from time to time other corporations may become direct or indirect affiliates of Parent and they hereby agree that Parent will cause such new Affiliates to become parties to this Agreement by executing a written joinder hereto within ninety (90) days of joining the Affiliated Group. Such written joinder need not be executed by any pre-existing Affiliate. The failure of one or more parties hereto to meet the definition of being a "Affiliate" of an "Affiliated Group" for purposes of any applicable income tax shall not result in termination of this Agreement with respect to any other party hereto.

12. Each party hereto hereby agrees to execute, acknowledge and deliver such instruments and take such other responsible actions as any other party hereto may request in order to effectuate the purposes or provisions of this Agreement or of any transaction contemplated hereby. This Agreement contains the entire understanding among the parties with respect to the subject matter hereof, and supersedes all other agreements and understandings among the parties with respect thereto. No amendment or waiver of any provision of this Agreement shall in any event be effective, unless the same shall be in writing and signed by the parties hereto. Should any provision of this Agreement be declared invalid, void or unenforceable for any reason, the remaining provisions hereto shall remain in full force and effect. This Agreement shall inure to the benefit of and be binding upon the parties hereto and their respective successors and assigns. This Agreement shall be governed by and construed in accordance with the laws of the State of Texas, without regard to conflicts of laws provisions.

\_\_\_\_\_  
Name of Affiliate

Stewart Title Company

By: \_\_\_\_\_

By: \_\_\_\_\_

Title: \_\_\_\_\_

Title: \_\_\_\_\_

# **APPENDIX**

## **ITEM 20**

### **EARNINGS MANAGEMENT EXAMPLES**

**Definition of an Asset:** Probable future economic benefits obtained or controlled by a particular entity as a result of past transactions or events.

**Definition of a Liability:** Probable future sacrifices of economic benefits arising from present obligations of a particular entity to transfer assets or provide services to other entities in the future as a result of past transactions or events.

**Note:** Accounting records must adequately document the support for all accrual and prepaid entries. The documentation should include, at a minimum, proof of approval from the appropriate level of management and support for the amount accrued. A schedule of accruals should be maintained so that the actual cost of the event can be compared to the amounts accrued.

**Definition of Revenues:** Inflows or other enhancements of assets of an entity or settlement of liabilities (or a combination of both) during a period from delivering or producing goods, rendering services, or other activities that constitute the entity's ongoing major or central operations.

**Definition of Expenses:** Outflows or other using up of assets or incidences of liabilities (or a combination of both) during a period from delivering or producing goods, rendering services, or carrying out other activities that constitute the entity's ongoing major or central operations.

**Matching Principle:** Efforts (expenses) should be matched with accomplishments (revenues) whenever it is reasonable and practical to do so. Costs that have no future economic benefit or no connection with revenue should be charged to the current period as expenses.

	Example Scenarios	Required Accounting	Unacceptable Accounting	Why?
1	Intentional manipulation of earnings (i.e. recording a transaction that has no basis or support).		X	SEC and accounting standards violation.
2	Recording premium revenue (cash received and/or billing made) on the date of closing, not on the date the commitment is issued or on any other date prior to the actual closing date (i.e., premiums for closings during the first few days of a month recorded as revenue in the previous month).	X		Proper revenue recognition policy.
3	Accruing moving costs if you are only contemplating moving (no new lease signed)		X	No commitment and event could be canceled.
4	Accruing the entire moving costs and lease penalties during the month a new	X		See Definition of a Liability.

	lease is signed.			
5	Accruing monthly the cost of a non-recurring customer function where no commitment has been made.		X	No commitment and event could be canceled.
6	Accruing monthly (or amortizing monthly if paid in advance) the cost of significant customer functions (sponsorship of events) or company events (Christmas party) where a contractual obligation exists. A formal commitment may not be necessary if the function has been approved, announced <u>and</u> it is unlikely there will be a change in the event. Also, you must be able to reasonably estimate the cost.	X		Commitment made. Highly unlikely the event will not happen.
7	Amortizing monthly for prepaid tickets to athletic functions either over the season or as the tickets are used.	X		See Definition of an Asset.
8	Capitalizing the cost of a major repair that extends the useful life of the asset and amortize net book value over remaining useful life.	X		Useful life of asset is extended.
9	Accruing over a 3 month period the estimated cost of a repair that will take place at the end of the 3 month period.		X	No commitment to complete the repair. No future benefit or connection to revenue. Expense in the month of the repair.
10	Accrue for general repairs that typically happen once a year		X	Current period expense; no future benefit, no connection to revenue.
11	Accrue monthly for an annual maintenance contract.	X		Benefits entire year.
12	Accrue for negligent loss billings from STG or expected but unbilled STG amounts.	X		Payable to STG should be recorded.
13	Accrue for estimated escrow losses on known claims.	X		Liability incurred.
14	Accrue for invoices for services and/or invoices <u>received but not paid</u> .	X		Liability incurred.
15	Accrue for a monthly costs such as telephone and insurance expense incurred even though a bill has not been received or has been received but not processed as a payable.	X		Liability incurred.
16	Amortize the cost incurred for large quantities of promotional items (i.e., calendars), office supplies, policy forms and other prepaid expenses over the expected number of months the items will be used.	X		Benefits more than one period.
17	Establishing a receivable for an expected recovery from an escrow shortage.		X	There must be a contractual relationship with debtor (formal note or other binding agreement)
18	Amortize the cost incurred for a placement/recruiting fee over the first year of an associate's employment.		X	Current period expense; no future benefit.

# **APPENDIX**

## **ITEM 21**

### **\* BOOKKEEPING TEST**