

REPORT ON EXAMINATION
OF THE
GENERAL STAR NATIONAL INSURANCE COMPANY
AS OF
DECEMBER 31, 2012

Karen Weldin Stewart, CIR-ML
Commissioner



Delaware Department of Insurance

I, Karen Weldin Stewart, Insurance Commissioner of the State of Delaware, do hereby certify that the attached REPORT OF EXAMINATION, made as of December 31, 2012 of the

GENERAL STAR NATIONAL INSURANCE COMPANY

is a true and correct copy of the document filed with this Department.

Attest By: Brandi Biddle

Date: June 19, 2014

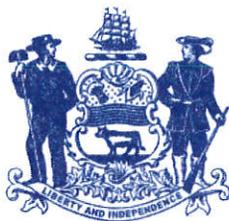


In Witness Whereof, I have hereunto set my hand and affixed the official seal of this Department at the City of Dover, this 19th day of June, 2014.

A handwritten signature in black ink, appearing to read "Karen Weldin Stewart".

Karen Weldin Stewart, CIR-ML
Insurance Commissioner

Karen Weldin Stewart, CIR-ML
Commissioner



Delaware Department of Insurance

REPORT OF EXAMINATION
OF THE
GENERAL STAR NATIONAL INSURANCE COMPANY
AS OF
DECEMBER 31, 2012

The above-captioned report was completed by examiners of the Delaware Department of Insurance.

Consideration has been duly given to the comments, conclusions and recommendations of the examiners regarding the status of the company as reflected in the report.

This report is hereby accepted, adopted and filed as an official record of this Department.

A handwritten signature in black ink, appearing to be "Karen Weldin Stewart".

Karen Weldin Stewart, CIR-ML
Insurance Commissioner

Dated this 19th day of June, 2014

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SALUTATION

May 16, 2014

Honorable Karen Weldin Stewart, CIR-ML
Commissioner
Delaware Department of Insurance
Rodney Building
841 Silver Lake Blvd.
Dover, Delaware 19904

Dear Commissioner:

In compliance with instructions and pursuant to statutory provisions contained in Certificate of Authority No. 13.015, dated March 25, 2013, an examination has been made of the affairs, financial condition and management of the

GENERAL STAR NATIONAL INSURANCE COMPANY

hereinafter referred to as (Company or GSN) and incorporated under the laws of the State of Delaware as a private company with its statutory home office located at 1209 Orange Street, Wilmington, Delaware 19801. The examination was conducted at the administrative office of the Company located at 120 Long Ridge Road, Stamford, CT 06902.

The report of this examination is submitted herewith.

SCOPE OF EXAMINATION

This is the first Delaware regulatory examination of the Company. The Company was an Ohio domiciled insurer until October 1, 2012, at which time the Company re-domesticated to the State of Delaware. GSN was last examined by the Ohio Department of Insurance as of December 31, 2009. This financial examination covers the three (3) year period from January 1, 2010 to December 31, 2012, and encompasses a general review of transactions during the period,

the Company's business policies and practices, as well as management and relevant corporate matters, with a determination of the financial condition of the Company as of December 31, 2012. Transactions subsequent to the examination date were reviewed where deemed necessary.

The examination was conducted concurrently with that of its immediate parent, General Reinsurance Corporation (GRC) and affiliate, General Star Indemnity Company (GSI), all Delaware domestic insurance companies, at its administrative office in Stamford, Connecticut. Separate reports of examination were filed for each company.

We conducted our examination in accordance with the *National Association of Insurance Commissioners (NAIC) Financial Condition Examiners Handbook* (Handbook). The NAIC Handbook requires that we plan and perform the examination to assess the financial condition and identify prospective risks by evaluating Company information including operations, corporate governance, identifying and assessing material inherent risks to which the Company is considered exposed, and evaluating processes, systems, controls and other procedures used to mitigate those risks. The examination also included assessing principles used and significant estimates made by management, as well as evaluating overall financial statement presentation and management's compliance with Statutory Accounting Principles and Annual Statement Instructions.

All accounts and activities of the Company were considered in accordance with the risk focused examination process. The examination report addresses regulatory issues reviewed during the examination process.

During the course of this examination, consideration was given to work performed by the Company's external accounting firm, Deloitte & Touche, LLP (D&T). Certain work papers of their 2012 external audit have been incorporated into the work papers of this examination and

have been utilized principally in the area of risk mitigation and substantive tests of account balances.

Consideration was also given to work performed by General Re Corporation's (GRN) Internal Audit Department on financial, operational and systems compliance and internal control audits performed on the Company's processes during the examination period.

In addition to items hereinafter incorporated as a part of this report, the following areas were reviewed without material exception and made part of the work papers of this examination:

NAIC Ratios
Legal Actions
Regulatory Agency Correspondence
All other Assets and Liabilities not mentioned

SUMMARY OF SIGNIFICANT FINDINGS

There were no material adverse findings, adjustments to the financial statements, or specific recommendations as a result of this examination.

SUBSEQUENT EVENTS

There were no material transactions reported subsequent to the examination date.

COMPANY HISTORY

The Company was incorporated September 10, 1864 under the laws of the State of Ohio as The Eureka Fire & Marine Insurance Company. On February 14, 1922, the company name was changed to The Eureka-Security Fire and Marine Insurance Company. Subsequently, on July 1, 1956, The Monarch Fire Insurance Company and the Eureka-Security Fire and Marine Insurance Company merged and adopted the name to The Monarch Insurance Company of Ohio.

On November 14, 1985, GRC acquired all of the outstanding capital stock of the Company from Pearl American Corporation. The current company name was adopted May 30, 1986.

Effective October 1, 2012, the Company re-domesticated from the State of Ohio to the State of Delaware.

CAPITALIZATION

Common Capital Stock

The Company has 4,000 shares of common stock authorized with a par value of \$1,000 per share. All shares are issued and outstanding and are currently held by the Company's immediate parent, GRC.

Gross Paid-In and Contributed Surplus

As of December 31, 2012, the Company reported \$60,107,585 in gross paid-in and contributed surplus. During the examination period, the company received a \$10.0 million capital contribution from GRC.

Dividends

No dividends were declared or paid during the examination period.

CORPORATE RECORDS

The recorded minutes and written resolutions of the Company's shareholder and Board of Directors were reviewed for the period under examination. The recorded minutes of the Board adequately documented its meetings and approval of Company transactions and events, including the authorization of investments as required by 18 Del.C. §1304 Authorization; record of investments.

A review of the Insurance Holding Company Annual Registration Statement filings (Form B and Form C) made by and on behalf of the Company for all years under examination revealed that the Company had complied with the requirements of 18 Del. Admin. Code §1801 Registration of Insurance Holding Companies.

MANAGEMENT AND CONTROL

Pursuant to the General Corporation Laws of the State of Delaware, as implemented by the Company's Articles of Incorporation and bylaws, all corporate powers and its business, property, and affairs are managed by or under the direction of the Board of Directors.

In accordance with Article 1, Section 1.01 of the Company's bylaws, the annual shareholder's meeting shall be held each year on a date and at such time and place designated by the Board of Directors.

Board of Directors

The business affairs and corporate activities are vested in a Board of Directors. The bylaws provide that the number of directors shall be established by the Board of Directors or by action of the stockholder and shall consist of no less than seven members. Directors are elected annually at the stockholders meeting and serve until a successor is elected and qualified. Currently, the Board is comprised of eight members. A majority of the Board of Directors, but no less than three members, shall constitute a quorum for the transaction of business.

The Board of Directors duly appointed or elected as of December 31, 2012 were as follows:

| <u>Director</u> | <u>Primary Business Affiliation</u> |
|----------------------|--|
| Franklin Montross IV | Chairman, President & Chief Executive Officer General Re Corporation |
| Robert M. Jones | Chief Executive Officer and President General Star National Insurance Company |
| Solan B. Schwab | Vice President General Reinsurance Corporation |
| Gregory J. Diorio | Senior Vice President, General Star Management Vice President, Genesis Management and Insurance Services Corporation |
| John V. Regan | Senior Vice President |

| | |
|--------------------|---|
| | General Reinsurance Corporation |
| Victoria J. Seeger | Senior Vice President and Chief Underwriting Officer, General Star Management Company |
| Damon N. Vocke | General Counsel, Secretary & Senior Vice President General Reinsurance Corporation |
| Daniel K. Lyons | Senior Vice President & Appointed Actuary General Reinsurance Corporation |

Officers

Article 3, Section 3.01 of the Company's bylaws require that the Board of Directors elect a Chairman of the Board, a President, a Treasurer, and a Secretary, all of whom shall be elected by the Board of Directors at the next regular meeting after the annual meeting of the stockholder. The Chief Executive Officer may from time to time appoint other officers.

As of December 31, 2012 the Company's four (4) officers and their respective titles were as follows:

| <u>Officers</u> | <u>Title</u> |
|--------------------------|---------------------------------------|
| Franklin Montross IV | Chairman |
| Robert M. Jones | Chief Executive Officer and President |
| Solan B. Schwab | Secretary |
| William G. Gasdaska, Jr. | Treasurer and Chief Financial Officer |

It was noted that written correspondence was submitted to the Delaware Department of Insurance (DE DOI) in regards to the changes in officers and directors during the period under examination in compliance with 18 Del. C. § 4919 Change of Directors, Officers; Notice.

Committees

The bylaws provide for the Board to appoint such standing committees and/or special committees, to perform such duties and make such investigations and reports as the Board by resolution may determine. The Company has one special committee – the Risk Committee. Several companies within the General Reinsurance Group, which includes General Star National

Insurance Company, have designated the Audit Committee to serve as the oversight function for the legal entity.

Members of committees serving as of December 31, 2012 were as follows:

Risk Committee

Gregory J. Diorio
Janice C. Englesbe
Martin G. Hacala
James Higgins
Robert M. Jones
Florene Kissy Beyniouah
Joseph Majsak
Michael C. McFadden
Cole Palmer
Solan B. Schwab
Victoria J. Seeger

Audit Committee

Franklin Montross IV
Imre John Cholnoky
William Gasdaska, Jr.
Damon N. Vocke
Adrienne Mageras
Salvatore Curiale
Marc Hamburg
Becki Amick

Conflict of Interest

The Company has an established procedure for the disclosure to its Board of Directors of any material interest or affiliation on the part of any of its officers, directors, or responsible employees which is in conflict with or is likely to conflict with the official duties of such person. The disclosures are made annually. Conflict of interest statements completed by all directors and key officers were reviewed and the information contained therein disclosed no evidence of conflicting interests.

Insurance Holding Company System

The Company is a member of an insurance holding company system as defined at 18 *Del. C.* Ch. § 50, Insurance Holding Companies. At December 31, 2012, the Company was owned by GRC, that was in turn owned by GRN, a Delaware insurance holding company. The GRN group of companies provides global reinsurance and financial service operations in over 55 cities in 25

countries, and provides reinsurance worldwide. GRN, in turn, is owned by Berkshire Hathaway Inc., a publicly traded holding company whose subsidiaries overall engage in a number of diverse business activities including property and casualty insurance and reinsurance, freight rail transportation, and a group of utilities and energy generation and distribution businesses, along with finance, manufacturing, services and retailing.

The following is an abbreviated organizational chart which reflects the identities and interrelationships between the Company, parent and all other affiliated insurers of the system as of December 31, 2012:

Berkshire Hathaway Inc.

General Re Corporation

General Reinsurance Corporation

Elm Street Corporation

General Star Indemnity Company

General Star National Insurance Company

General Star Management Company

Genesis Management and Insurance Services Corporation

Genesis Insurance Company

GRC Realty Corporation

General Reinsurance Australia Ltd

General Re Compania de Reaseguros, S.A.

General Reinsurance AG

General Re Holdings Limited

Gen Re Services UK Limited

Faraday Reinsurance Co. Limited

General Star International Indemnity Ltd.

General Reinsurance México S.A.

Gen Re Warsaw Sp. z.o.o.

General Reinsurance Africa Ltd.

General Reinsurance AG Escritório

de Representação no Brasil Ltda.

General Reinsurance Life Australia Ltd.

Gen Re Beirut s.a.l. offshore

General Re Life Corporation

Idealife Insurance Company

Railsplitter Holdings Corporation

Commercial Casualty Insurance Company

International American Group Inc.

American Centennial Insurance Company

International American Management Company

General Re-New England Asset Management, Inc.

GR-NEAM Limited

United States Aviation Underwriters, Incorporated

Canadian Aviation Insurance Managers Ltd.

Gen Re Intermediaries Corporation

Faraday Holdings Limited

GRF Services Limited

Faraday Underwriting Limited

Faraday Capital Limited

GRD Holdings Corporation

General Re Financial Products Corporation

Gen Re Long Ridge, LLC

Fidelity Bond Insurance

The Company's parent, GRC, had a Financial Institution Bond in place, which included the Company as a named insured. The bond coverage limits were \$10.0 million per employee/\$20.0 million aggregate, which meets the NAIC recommended limits.

Pensions, Stock Ownership and Insurance Plans

All production and administrative functions of the Company are performed by General Star Management Company (GSMC), whose costs are charged back to the Company in a cost allocation formula. Pensions and other employee benefits are part of the expenses charged back to the Company.

The Company's share of net expenses under a defined contribution pension plan sponsored by General Re Corporation was \$589,990 for 2012. The Company's share of net expenses for a qualified non-contributory defined benefit pension plan and a non-qualified defined plan sponsored by General Re Corporation, which were frozen in 2005, was \$160,131 and \$267,655 respectively for 2012.

The Company also incurred expenses related to the General Re Corporation Employee Savings and Stock Ownership Plan and Medical/Dental Expense Plan.

The Company does not have an accrual or liability on its balance sheet at December 31, 2012 for pension plan costs. All future liabilities are borne by GRC, charged to GSMC and then charged back to the Company in the cost allocation formula.

Intercompany Management and Service Agreements

The Company was party to various intercompany agreements. The following related party agreements entered into during the examination period:

Underwriting Management Agreement (GSMC)

Effective April 21, 2011, the Company entered into an amended and restated Underwriting Management Agreement with General Star Management Company (GSMC). GSMC shall manage the underwriting activities for liability lines of business and conduct the affairs of the Company, subject to the direction and control of the Company, on a fee for services basis. GSMC agrees to develop sources of production, appoint agents, underwrite risks, issue policies, receive premiums, adjust claims, comply with all applicable laws, and reinsure the risks underwritten. During 2012, the Company paid GSMC \$12,576,967 in fees under this agreement.

Underwriting Management Agreement (GMISC)

Effective April 21, 2011, the Company entered into an amended and restated Underwriting Management Agreement with Genesis Management and Insurance Services Corporation (GMISC). In accordance with the terms of the agreement, GMISC shall manage the underwriting activities for property and liability lines of business and conduct the affairs of the Company, subject to the direction and control of the Company, on a fee for services basis. GMISC agrees to develop sources of production, appoint agents, underwrite risks, issue policies, receive premiums, adjust claims, comply with all applicable laws, and reinsure the risks underwritten. No fees were paid to GMISC under the agreement during 2012.

Cost Allocation Agreement

Effective April 21, 2011, the Company entered into a second amended and restated Cost Allocation Agreement with GRN, whereby each would provide various services for each other.

Tax Allocation Agreement

Effective April 21, 2011, the Company entered into an amended and restated Tax Allocation Agreement with GRN, whereby they agreed to file a consolidated tax return.

The following related party contracts were entered into prior to the current examination period and remained in effect as of December 31, 2012:

- Amended and Restated Investment Management Agreement with Gen Re – New England Asset Management, Inc. (GR-NEAM) effective January 1, 2009, whereby GR-NEAM will make all investment decisions for the Company. The Company paid \$56,452 in fees under this agreement in 2012.
- Amended and Restated Master Loan Agreement dated February 1, 2007, with GRN and certain of its subsidiaries, to create an inter-company short term loan facility to reduce each participant's level of short-term investments while retaining sufficient liquidity to pay current obligations through affiliate borrowing as needed.
- Amended and Restated Joint Asset Agreement dated February 1, 2007 with GRN and

its subsidiaries, whereby the participating companies in the agreement joined together creating a short-term pool, in which each participant contributes cash in excess of general working capital. Each participant jointly owns a percentage of the assets in the pool and shares in the investment income/loss in proportion to its contributed assets.

- General Services Agreement dated September 1, 1998 with GRC and several affiliates, whereby GRC performs certain administrative and general services and is reimbursed for costs, fees, and expenses incurred in the performance of its services.

TERRITORY AND PLAN OF OPERATION

Territory

The Company is authorized as a licensed insurance carrier in all fifty (50) states. In addition, the Company is licensed in the District of Columbia and Puerto Rico.

For the year ending December 31, 2012 the Company wrote approximately 85% of its business in the states of California (32%); New York (26%); Connecticut (12%); New Jersey (10%); and Pennsylvania (5%).

Plan of Operation

GSN currently writes business through wholesale brokers and program administrators. Business is produced through the Excess Casualty Division and Contract E&O Division.

The Excess Casualty Division business includes an entertainment oriented book produced by one appointed producer, and brokerage business written within the New York Free Trade Zone, produced by approximately fifteen (15) appointments.

The Contract E&O Division business includes homogeneous program business produced by four (4) program administrators.

The number of brokers and program administrators varies from year to year but there has been no material change in distribution or number of appointments over the period under examination.

In 2011, the Company entered into an Underwriting Management Agreement with an affiliate, GSMC, under which the Company appointed GSMC as program manager for the purpose of underwriting and administering primarily certain excess commercial casualty insurance coverages on behalf of the Company. Within defined contractual retention and total limitations, the program manager has full authority to act on behalf of the Company to bind risks and manage the business; issue policies; collect premiums; investigate, negotiate, and settle all claims; and place reinsurance when authorized by the Company.

The principal office of GSMC is located in Stamford, Connecticut with underwriting and claims offices in Atlanta, Chicago, Los Angeles, and New York City.

GROWTH OF THE COMPANY

The following information was obtained from the Company's filed Annual Statements and covers the past three years through December 31, 2012:

| Year | Net Admitted Assets | Capital and Surplus | Gross Written Premiums | Net Income (Loss) |
|------|---------------------|---------------------|------------------------|-------------------|
| 2012 | \$250,653,902 | \$181,189,978 | \$18,593,635 | \$7,397,955 |
| 2011 | 251,710,149 | 166,663,218 | 30,374,202 | 7,255,889 |
| 2010 | 279,972,856 | 174,023,811 | 48,178,109 | (509,311) |

Gross written premiums decreased \$29.6 million or 61% during the examination period due to the soft insurance market, during which time the Company maintained its underwriting discipline. The Company exited the following lines during the examination period due to unfavorable market conditions.

- Lawyer's E&O
- Primary Auto
- Physician's and Surgeon's Liability
- Medical Malpractice

Net income increased \$7.9 million during the examination period. In 2011, the Company's investment income was \$8.8 million, of which \$4.4 million was net realized capital gains. The net underwriting loss improved to a loss of \$2.7 million compared to an \$8.5 million underwriting loss in 2010. In 2012, the Company reported a net underwriting gain of \$6.1 million.

LOSS EXPERIENCE

Net loss and expenses unpaid reserves as of December 31, 2011 were \$74.9 million. During 2012, \$10.1 million was paid for incurred loss and loss adjustment expenses attributable to insured events of prior years. Reserves remaining for the prior years are now \$52.2 million as a result of re-estimation of unpaid claims and claim adjustment expenses, principally in 'Other Liability' lines of insurance. Therefore, there has been a \$12.6 million year-to-date favorable development on prior years. The favorable development is generally the result of ongoing analysis of recent loss development trends.

An independent loss reserve review was performed as part of this examination. The findings of that review are discussed in Note (5) of the "Notes to Financial Statements".

REINSURANCE

The Company's reported the following distribution of net premiums written in 2012:

General Star National Insurance Company

| | |
|---|----------------------------|
| Direct and indirect business | \$ 18,592,635 |
| Reinsurance assumed (from affiliates) | 0 |
| Reinsurance assumed (from non-affiliates) | 1,000 |
| Total direct and assumed | <u>\$ 18,593,635</u> |
| Reinsurance ceded (to affiliates) | 9,158,573 |
| Reinsurance ceded (to non-affiliates) | 279,682 |
| Total ceded | <u>\$ 9,438,255</u> |
| Net premiums written | <u><u>\$ 9,155,380</u></u> |

Ceded Reinsurance - Affiliates

Effective January 1, 2005, with the permission of their domestic insurance regulators, the Company and certain of its North American based property and casualty affiliates, entered into a loss portfolio reinsurance contract (the “loss portfolio”) and a quota share reinsurance contract (the “quota share”) with two other affiliates, National Indemnity Company and Columbia Insurance Company. The loss portfolio provides for a 50% reinsurance cover on existing net losses as of December 31, 2004, subject to an overall aggregate limit of \$11.2 billion. The amount of net reserves ceded by the Company on January 1, 2005 was \$60.1 million. Consideration was equal to the amount of net statutory reserves and was reported by the Company as ceded earned premiums in 2005 for the lines of business of the underlying reserves ceded. There was no surplus gain from this retroactive transaction with affiliates and was accounted for as reinsurance. The quota share provides for a 50% reinsurance cover on net losses occurring on or after January 1, 2005, for which the Company ceded premiums earned of \$10.5 million and \$19.5 million in calendar years 2012 and 2011, respectively. At December 1, 2012 the Company reported \$12.7 million of ceded outstanding losses on the loss portfolio, and \$49.1 million of ceded outstanding losses on the quota share.

Ceded Reinsurance - Non Affiliates

Effective July 1, 2009 the Company and GSI entered into a Property Catastrophe Excess of Loss Agreement with various subscribing reinsurers. The coverage was First excess \$12.5 million excess of \$7.5 million and Second excess \$40 million excess of \$20 million. This agreement was last renewed effective May 1, 2012. The Company and GSI paid deposit premiums and deposit premium adjustments in the amount of \$5,854,321 between May 1, 2012 and April 30, 2013 and no losses were reported from this agreement during that period.

The Company did not cede any other material business during the examination period.

Assumed Reinsurance

The Company did not assume any material business during the examination period.

ACCOUNTS AND RECORDS

Accounting Systems and Information

Premium and claims transactions are administered and maintained on GenServe, which is an application developed in-house and first established in 1989. The financial cycle data, principally maintained in the SAP (general ledger) system and its individual modules, is derived from submitted invoices, check requests, purchase orders, manual general journal entries, and automated interfaces from other insurance cycle systems. Personal computers and file servers support financial reporting and analysis. The systems are maintained by personnel located in Trumbull, CT.

The Company's investments are managed and administered by an affiliate, General Re-New England Asset Management, Inc., which utilizes the CAMRA system. The investment related transactions are also posted manually by the Finance Department into the general ledger system.

The accounts and records review included an assessment of the Company's risk management process in identifying and controlling risks in the key operational areas of the Company. In making the assessment in each key area, processes were reviewed, risks were identified, operational and organizational controls were identified and tested, and the Company's methodology for assessing the effectiveness of the established mitigation factors was evaluated.

The primary systems used in the operations of the Company were also evaluated. The Information Systems (IS) portion of the examination was performed by INS Services, Inc. The review was performed in accordance with the NAIC Handbook. The review of IS controls included IS management and organizational controls; application and operating system software change controls, system and program development controls, overall systems documentation, logical and physical security controls, contingency planning, local and wide area networks, personal computers, and mainframe controls. Control testing performed by the Company's SOX and Internal Audit functions and by D&T was evaluated, and testing of end user computing and IS outsourcing controls was performed in making the evaluation. As a result of the procedures performed, the IS Examination Team obtained reasonable assurance that IS general controls and general application controls were functioning as management intended and that an effective system of controls is in place and conducive to the accuracy and reliability of financial information processed and maintained by the Company. There are no reportable items related to the review of IS controls.

Independent Accountants

The Company's financial statements are audited each year by the firm of Deloitte & Touche, LLP. The examiners reviewed the audited statutory financial statements for all years

under examination. For all years under review, D&T issued an unqualified opinion. The examiners reviewed D&T's 2012 work papers, and incorporated their work and findings as deemed applicable into the current examination.

Actuarial Opinion

The Company's loss reserves and related actuarial items were reviewed by Daniel K. Lyons, FSA, MAAA, who issued a statement of actuarial opinion based on the financial information presented by the Company. The opinion stated that the reserves and related actuarial values carried on the balance sheet were computed in accordance with accepted loss reserving standards and principles, and were reasonable in the aggregate for unpaid loss and loss expense obligations and all unearned premium obligations of the Company related to long duration contracts under the terms of its contracts and agreements met the requirements of the insurance laws of the State of Delaware.

The consulting firm of INS Consultants, Inc. (INS), Philadelphia, PA was contracted to perform an independent review of loss reserves. The findings of that review are discussed in Note (5) of the "Notes to Financial Statements".

STATUTORY DEPOSITS

The Company's state statutory deposits are comprised of U.S. Treasury Notes and other bonds. The following statutory deposits were on file with the following states:

| STATE | Deposits For The Benefit of ALL Policyholders | | All Other Special Deposits | |
|-----------------------|---|--------------------|------------------------------|---------------------|
| | Book/Adjusted Carrying Value | Fair Value | Book/Adjusted Carrying Value | Fair Value |
| Arkansas | | | \$ 136,532 | \$ 145,036 |
| Delaware | \$ 3,203,205 | \$3,211,884 | | |
| Florida | | | 106,192 | 112,806 |
| Georgia | | | 96,078 | 102,062 |
| New Mexico | | | 324,620 | 349,713 |
| North Carolina | | | 303,405 | 322,302 |
| TOTAL DEPOSITS | \$ 3,203,205 | \$3,211,884 | \$ 966,827 | \$ 1,031,919 |

Statutory deposits with the State of Delaware were directly confirmed and all statutory deposits were traced back to Schedule D – Part 1 of the 2012 Annual Statement with no exceptions noted.

FINANCIAL STATEMENTS

The following pages contain a statement of assets, liabilities, surplus and other funds as of December 31, 2012, as determined by this examination, along with supporting exhibits as detailed below:

- Assets
- Liabilities, Surplus and Other Funds
- Statement of Income
- Capital and Surplus Account
- Reconciliation of Capital and Surplus

With the exception of invested assets and reserve related balances, narratives on individual accounts are presented on the “exception basis” in the Notes to the Financial Statements section of this Report.

Assets
As of December 31, 2012

| | <u>Assets</u> | Nonadmitted <u>Assets</u> | Net Admitted <u>Assets</u> | <u>Notes</u> |
|--|------------------------------|------------------------------|----------------------------------|--------------|
| Bonds | \$ 35,781,140 | | \$ 35,781,140 | 1 |
| Preferred stocks | 11,200,000 | | 11,200,000 | 2 |
| Common stocks | 11,621,020 | | 11,621,020 | 3 |
| Cash and short-term investments | 185,966,211 | | 185,966,211 | 4 |
| Receivable for securities | 930 | | 930 | |
| Subtotals, cash and invested assets | <u>\$ 244,569,301</u> | <u>\$ -</u> | <u>\$ 244,569,301</u> | |
| Investment income due and accrued | 1,012,760 | | 1,012,760 | |
| Uncollected premiums and agents' balances in course of collection | 1,550,412 | 76,590 | 1,473,822 | |
| Deferred premiums, agents balances and installments booked but deferred and not yet due | 244,519 | 120 | 244,399 | |
| Amounts recoverable from reinsurers | 2,674,368 | | 2,674,368 | |
| Net deferred tax asset | 434,513 | | 434,513 | |
| Aggregate write-ins: | | | | |
| Amounts receivable under high deductible policies | 66,493 | 57,445 | 9,048 | |
| Impress funds | 100,000 | | 100,000 | |
| Contingent commission recoverable | 135,691 | | 135,691 | |
| Total Assets | <u><u>\$ 250,788,057</u></u> | <u><u>\$ 134,155</u></u> | <u><u>\$ 250,653,902</u></u> | |

Liabilities, Surplus and Other Funds
As of December 31, 2012

| | | <u>Note</u> |
|---|-----------------------|-------------|
| Losses | \$ 48,969,061 | 5 |
| Reinsurance payable on paid losses and loss adjustment expenses | | |
| Loss adjustment expenses | 12,832,753 | 5 |
| Current federal and foreign income taxes | 869,269 | |
| Unearned premiums | 3,931,213 | |
| Ceded reinsurance premiums payable | 346,313 | |
| Amounts withheld or retained for the account of others | 53,907 | |
| Remittances and items not allocated | 1,331 | |
| Payable to parent, subsidiaries and affiliates | 2,379,098 | |
| Aggregate write-ins for liabilities: | | |
| Miscellaneous accounts payable - runoff business | 79,458 | |
| Uncashed checks pending escheatment to state | 1,521 | |
| Total Liabilities | <u>\$ 69,463,924</u> | |
| | | |
| Common capital stock | \$ 4,000,000 | |
| Gross paid in and contributed surplus | 60,107,585 | |
| Unassigned funds (surplus) | 117,082,393 | |
| Surplus as regards policyholders | <u>\$ 181,189,978</u> | |
| Total Liabilities, Capital and Surplus | <u>\$ 250,653,902</u> | |

Statement of Income
As of December 31, 2012

| | |
|--|----------------------------|
| UNDERWRITING INCOME | |
| Premiums earned | <u>\$ 10,523,477</u> |
| DEDUCTIONS | |
| Losses incurred | \$ (2,351,952) |
| Loss adjustment expenses incurred | 267,278 |
| Other underwriting expenses incurred | <u>6,540,494</u> |
| Total underwriting deductions | <u>\$ 4,455,820</u> |
| Net underwriting gain or (loss) | <u>\$ 6,067,657</u> |
| INVESTMENT INCOME | |
| Net investment income earned | \$ 3,016,249 |
| Net realized capital gains or (losses) | (503) |
| Net investment gain or (loss) | <u>\$ 3,015,746</u> |
| OTHER INCOME | |
| Net gain or (loss) from agents' or premium balances charged off | \$ (22,359) |
| Aggregate write-ins for miscellaneous income | |
| Miscellaneous income | <u>602</u> |
| Total other income | <u>\$ (21,757)</u> |
| Net income before dividends to policyholders and before federal income taxes | <u>\$ 9,061,646</u> |
| Dividends to policyholders | <u>-</u> |
| Net income after dividends to policyholders but before federal income taxes | \$ 9,061,646 |
| Federal and foreign income taxes incurred | <u>1,663,691</u> |
| Net income | <u><u>\$ 7,397,955</u></u> |

Capital and Surplus Account
As of December 31, 2012

CAPITAL AND SURPLUS ACCOUNT

| | |
|---|------------------------------|
| Surplus as regards policyholders, December 31, 2011 | <u>\$ 166,663,218</u> |
| GAINS AND (LOSSES) IN SURPLUS | |
| Net income | \$ 7,397,955 |
| Change in net unrealized capital gains (losses) | 4,875,709 |
| Change in net deferred income tax | (839,342) |
| Change in non-admitted assets | 2,668,316 |
| Change in provision for reinsurance | 16,000 |
| Cummulative effect of changes in accounting principals | <u>408,122</u> |
| Change in surplus as regards policyholders for the year | <u>\$ 14,526,760</u> |
| Surplus as regards policyholder, December 31, 2012 | <u><u>\$ 181,189,978</u></u> |

Reconciliation of Capital and Surplus
January 1, 2010 through December 31, 2012

The following reconciliation of capital and surplus represents the period since the last examination:

| | Common Capital Stock | Gross Paid-in and Contributed Surplus | Unassigned Surplus | <u>Total</u> |
|---|----------------------------|--|-----------------------|---------------------------|
| December 31, 2009 | \$4,000,000 | \$ 50,107,585 | \$111,004,048 | \$165,111,633 |
| Operations & Investments 2010 Contributed Surplus from GRC | | \$ 10,000,000 | (1,087,822) | (1,087,822) 10,000,000 |
| Operations & Investments 2011 | | | (7,360,593) | (7,360,593) |
| Operations & Investments 2012 | | | 14,526,760 | 14,526,760 |
| Rounding | | | 1 | |
| December 31, 2012 | <u>\$4,000,000</u> | <u>\$ 60,107,585</u> | <u>\$117,082,394</u> | <u>\$181,189,978</u> |

SCHEDULE OF EXAMINATION ADJUSTMENTS

There were no financial adjustments made to the Company's balance sheet as a result of this examination.

NOTES TO FINANCIAL STATEMENTS

Assets

Note 1 – Bonds \$35,781,140

Investments in bonds are reported at values (amortized cost) adopted and approved by the Securities Valuation Office (SVO) of the NAIC. Bonds owned by the Company as of December 31, 2012 were as follows:

| | Statement Value |
|----------------------------|--------------------|
| US Governments | \$ 7,519,775 |
| Special Revenue | 23,261,365 |
| Industrial & Miscellaneous | 5,000,000 |
| | \$ 35,781,140 |

The Company's bond holdings represents 14.6% of the Company's total invested assets and 14.3% of total admitted assets at December 31, 2012, while 100% were categorized as Class 1 or 2 with respect to NAIC credit quality standards.

The Company maintains a conservative investment philosophy with an investment strategy to primarily have adequate fixed income securities in order to meet cash requirements of current operations as well as longer term liabilities. To the extent possible for funds in excess of these requirements, the objective is to maximize returns within a prudent level of risk.

As of December 31, 2012, the Company's custodian was Bank of New York. The agreement was examined to ensure that it contained provisions recommended in the NAIC Handbook.

Note 2 – Preferred Stocks \$11,200,000

The Company's investment in preferred stocks was comprised of shares of Bank of America Corporation preferred stock.

Note 3 – Common Stocks \$11,621,020

The Company's investment in common stocks was comprised of highly rated equities readily traded on the open markets.

Note 4 - Cash, Cash Equivalents and Short Term Investments \$185,966,211

Cash and cash equivalents comprise 74.2% of total admitted assets at December 31, 2012 and were made up of the following:

| | |
|------------------|-----------------------------|
| Cash | \$ 79,521 |
| Cash Equivalents | <u>185,886,690</u> |
| | <u><u>\$185,966,211</u></u> |

Cash on deposit was held at three (3) financial institutions with over 99% or \$78,691 on deposit at First Tennessee Bank, Memphis, TN.

Cash equivalents of \$185,886,690 consisted of Treasury bills acquired in December 2012, and maturing in January and February of 2013.

Liabilities

Note 5 - Losses: \$ 48,969,061

Note 5 - Loss Adjustment Expenses (LAE): \$ 12,832,753

The above-captioned amount, which is the same as that reported by the Company in its 2012 Annual Statement, has been accepted for purposes of this report.

The Delaware Department of Insurance retained the services of INS Consultants, to conduct an independent review of the Company's loss and LAE reserves as of December 31, 2012. The INS analysis was performed using a risk-focused approach according to the guidelines contained in the NAIC Handbook. The review does not address the collectability of reinsurance recoverables.

The conclusions set forth in the INS report are based on information provided by the Company, including the 2012 Annual Statements and the related 2012 Statement of Actuarial Opinion with underlying actuarial work papers.

INS performed an analysis on the Company's book of business by segment of business on both a gross and a net basis for loss, defense and cost containment expense and adjusting and other expense. INS also reviewed the Company's work papers which reconcile the year-end 2012 data to Schedule P. The work papers supported the conclusion that the year-end amounts were closely reconciled to the Schedule P amounts.

Based on work performed, INS concluded the Company's carried net and gross loss and LAE reserves at December 31, 2012, were reasonably stated, and as such, no financial adjustment was required for examination purposes.

COMPLIANCE WITH PRIOR EXAMINATION RECOMMENDATIONS

This was the first financial examination by the Delaware Department of Insurance; therefore, there are no prior examination recommendations.

CONCLUSION

The following schedule shows the results of this examination and the results of the prior examination with changes between the examination periods:

| <u>Description</u> | <u>December 31, 2009</u> | <u>December 31, 2012</u> | <u>Increase (Decrease)</u> |
|--|--------------------------|--------------------------|--------------------------------|
| Assets | \$ 268,023,450 | \$ 250,653,902 | \$ (17,369,548) |
| Liabilities | 102,911,817 | 69,463,924 | (33,447,893) |
| Special Surplus Funds | - | - | - |
| Common Capital Stock | 4,000,000 | 4,000,000 | - |
| Gross Paid In and Contributed Surplus | 50,107,585 | 60,107,585 | 10,000,000 |
| Unassigned Funds (Surplus) | 111,004,048 | 117,082,393 | 6,078,345 |
| Total Surplus as Regards Policyholders | <u>\$ 165,111,633</u> | <u>\$ 181,189,978</u> | <u>\$ 16,078,345</u> |
| Totals | <u>\$ 268,023,450</u> | <u>\$ 250,653,902</u> | <u>\$ (17,369,548)</u> |

The assistance of Delaware's consulting actuarial firm, INS Consultants, Inc. is acknowledged. In addition, the assistance and cooperation of the Company's outside audit firm, Deloitte & Touche, LLP, and the Company's management and staff were appreciated and are acknowledged.

Respectfully submitted,


 Don Hollier, CFE
 Examiner-In-Charge
 State of Delaware