

**REPORT ON EXAMINATION**

**AS TO THE CONDITION OF THE**

**ARI CASUALTY INSURANCE COMPANY**

**LAWRENCEVILLE, NEW JERSEY 08648**

**AS OF DECEMBER 31, 2007**

**N.A.I.C. GROUP CODE 0848**

**N.A.I.C. COMPANY CODE 37680**

**F I L E D**

**JUN 29 2009**

**COMMISSIONER  
NJ DEPT OF BANKING & INSURANCE**

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**State of New Jersey**  
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STEVEN M. GOLDMAN  
*Commissioner*

Sir:

In accordance with the authority vested in you by the Revised Statutes of New Jersey (N.J.S.A.) an examination has been made of assets, liabilities, methods of conducting business and other affairs of the

**ARI Casualty Company  
133 Franklin Corner Road  
Lawrenceville, NJ 08648  
N.A.I.C. Group Code 0848  
N.A.I.C. Company Code 37680**

hereinafter referred to as the "Company" or "ARI Casualty".

**SCOPE OF EXAMINATION**

The New Jersey Commissioner of Banking and Insurance called this Examination in compliance with the requirements of N.J.S.A. 17:23-22. The examination was a full scope comprehensive examination and was conducted at the Company's home office located at 133 Franklin Corner Road, Lawrenceville, New Jersey.

The present examination covers the three-year period from January 1, 2005 through December 31, 2007. During the three-year examination period, the Company's reported admitted assets increased from \$23,513,450 to \$39,153,971. Reported liabilities increased from \$14,019,792 to \$23,087,256. Reported surplus as regards to policyholders increased from \$9,493,658 to \$16,066,715. The conduct of the examination was governed in accordance with the procedures of the National Association of Insurance Commissioners (NAIC) and followed regulatory procedures prescribed or permitted by the New Jersey Department of Banking and Insurance.

The following criteria were used in determining the emphasis to be placed on each specific account:

- Adequacy of the Company's system of internal control
- Materiality of each account and its relationship to the Company's solvency
- Analytical reviews performed under the review of the Examiner-In-Charge.

The material balance sheet accounts in significant cycles specific to the Company and the emphasis placed on those accounts for this examination are as follows:

**Bonds (Medium Emphasis)**

**Preferred & Common Stocks (Medium Emphasis)**

**Cash and Short-Term Investments (Medium Emphasis)**

**Interest, Dividends and Real Estate Income Due and Accrued (Medium Emphasis)**

**Premiums in Course of Collection (Medium Emphasis)**

**Reinsurance Recoverable on Loss and Loss Adjustment Expense Payments (Medium Emphasis)**

**Deferred Income Tax (Medium Emphasis)**

**Loss Reserves (Medium Emphasis)**

**Loss Adjustment Expense Reserves (Medium Emphasis)**

**Unearned Premiums (Medium Emphasis)**

**Amounts Withheld or Retained by Company (Medium Emphasis)**

**Payable to Parent, Subsidiaries and Affiliates (Medium Emphasis)**

All the remaining accounts, which are not mentioned here, are having a Low Emphasis.

In addition to the items hereinafter incorporated as part of the written report, the following items were reviewed and made part of the examination work papers:

**Advertising**

**Policy Forms and Underwriting Practices**

**Commitments and Contingencies**

## **COMPLIANCE WITH PRIOR REPORT RECOMMENDATIONS**

The following is a list of prior report recommendations and a review of the Company's compliance with those recommendations:

### **Accounts and Records:**

**Recommendation:** It is recommended the Company do a full restore of its systems from time to time on a regularly scheduled basis and test its Business Continuation Plan.

**Company Response and Review:** The Company is in the process of reviewing back-up and restoration alternatives that will allow the Company automatically back-up business transactions to a remote protected, dedicated and vaulted server. Regularly scheduled restoration testing will be performed on the remote server once the automated back-up is established. Upon review it was determined while there was evidence that the Company has run tests for their most important systems, the Company has not presented a fully tested Business Continuity Plan. It will be recommended that the company continue to work on upgrading the recovery process of all their important systems and that they continue developing and testing a full Business Continuity Plan.

### **Bonds and Stocks:**

**Recommendation:** During our examination of bonds and stocks it was noted the Company used the settlement date for recording bond acquisitions. In accordance with SSAP 26-4 all bond acquisitions (other than the acquisition of private placement bonds) are to be recorded on the trade date. It is recommended the Company record all bond acquisitions on the trade date, rather than the settlement date in accordance with SSAP 26-4.

**Company Response and Review:** The Company has reported all bond acquisitions on the trade date in accordance with SSAP 26-4 as of December 31, 2005, and has been continuing to do so during this examination also.

### **Advanced Premiums**

**Recommendation:** It is recommended the Company report advance premiums as a liability in all future financial filings in accordance with SSAP 53-13.

**Company Response and Review:** The Company reported all advance premiums collected in accordance with SSAP 53-13 at December 31, 2005, and has continued to do so in this examination also.

### **Ceded Reinsurance Balances Payable**

**Recommendation:** It is recommended the Company properly segregate all inter-company reinsurance transactions including assumed and ceded reinsurance recoverables on paid losses and loss adjustment expenses and assumed and ceded reinsurance premium balances due to or from its Affiliate ARI Mutual Insurance Company in Schedule F in accordance with SSAP 64-3 and NAIC Annual Statement instructions.

**Company Response and Review:** The Company segregated all reinsurance transactions including assumed and ceded reinsurance recoverables and payables on paid loss and loss adjustment expenses and assumed and ceded reinsurance balances payable due to or from its Parent, ARI Mutual in Schedule F in accordance with SSAP 64-3 and NAIC annual statement instructions at December 31, 2005, and has continued to do so in this examination also.

#### **Net Deferred Tax Asset**

**Recommendation:** The Company did not limit its calculation of its deferred tax asset by ten percent of adjusted surplus as defined in SSAP 10-10(b)(ii). It is recommended the Company limit its deferred tax asset by ten percent of adjusted surplus (as recorded in its most recent financial filing with the NJDOBI Commissioner) as indicated in SSAP 10-10(b)(ii).

**Company Response and Review:** The Company has again reviewed the requirements of SSAP 10-10(b)(ii) and has applied the requirements to the deferred tax asset limits which was verified during our examination.

#### **Loss and Loss Adjustment Expense Reserves**

**Recommendation:** Although net reserves were accepted for examination purposes in total, the NJDOBI Actuarial Unit did note that the Company's reserve methodology for ULAE resulted in an understatement of ULAE reserves. This was offset by a subrogation recovery. Subsequently in 2005 the Company did revise its reserve methodology for ULAE reserves and ULAE reserves appear to be adequate. It is recommended the Company continue to adequately reserve for ULAE reserves.

**Company Response and Review:** The Company has reviewed the methodology for developing ULAE reserves as the reserves develop and are paid over time. The methodology was reviewed by the NJDOBI Actuarial Unit and no exceptions were noted.

#### **Other Expenses and Taxes, Licenses and Fees**

**Recommendation:** It is recommended the Company establish accruals for the following liabilities:

- Property Liability Insurance Guaranty Assessment (PLIGA)-This accrual can be offset by the expected recoupment from policyholder surcharges
- Unsatisfied Claim and Judgment Fund (UCJF)
- Motor Vehicle Security Responsibility and Insurance Fraud Assessments

**Company Response and Review:** The Company has established the accruals for PLIGA, UCJF and the Motor Vehicle Security Responsibility Assessments as of December 31, 2007. However, it appeared that the Company did not set up an accrual for fraud assessments. It will be recommended again that the Company report an accrual for fraud assessment.

**Cash and Short-Term Investments:**

**Recommendation:** The Company continued to report the Evergreen Money Mutual Fund as cash in its financial statements. It is again recommended the Company properly report balances from the Evergreen Money Mutual Fund as short-term investments and record them in Schedule DA in accordance with SSAP 2-10.

**Company Response and Review:** The Company has reported the Evergreen Money Mutual Funds as short-term investments and recorded them in Schedule DA in accordance with SSAP 2-10 as of December 31, 2005, and the review of this examination also confirmed having done so by the Company.

**Reinsurance and Retention:**

**Recommendation:** The NJDOBI Actuarial Unit determined risk transfer on the 2004 multi-line quota share reinsurance contract to be minimal. Subsequently 2005 and 2006 reinsurance contracts were reviewed and were found to have higher levels of risk transfer. It is recommended the Company continue to assess and document adequate risk transfer on all future reinsurance contracts.

**Company Response and Review:** The Company annually scrutinizes the transfer of risk in all reinsurance contracts and has worked with the Company's auditors and reinsurers to ensure adequate levels of risk transfer exist in each year's contracts. The multi-line quota share contract was eliminated on December 31, 2005. During this examination, NJDOBI Actuarial Unit determined that all the reinsurance contracts pass "10/10" risk transfer test.

**COMPANY HISTORY AND KIND OF BUSINESS**

On August 27, 1979 the Company submitted a Certificate of Incorporation to the New Jersey Department of Banking and Insurance which was filed with the Department of Banking and Insurance on November 9, 1979.

Pursuant to N.J.S.A. 17:17-10 a Certificate of Authority was issued to the Company on December 4, 1979 by the Commissioner of Insurance of the State of New Jersey. The current Certificate of Authority dated December 18, 1995 allows the Company to write the kinds of insurance specified in paragraphs "a", "b", "d", "e", "f", "g", "j", "k", "l" and "o-1" and "o-3" of N.J.S.A. 17:17-1 et seq. \*(except that authority granted by N.J.S.A.

17:17-1(d) shall not include authority to write individual or group health insurance as defined in the “Life and Health Insurance Code” N.J.S.A. 17B:17-4).

On January 1, 1992 the New Jersey Department of Banking and Insurance approved a Plan of Reorganization to transfer the Company’s New Jersey personal automobile business to American Reliance Indemnity, a wholly owned subsidiary of the Company. Under the Plan, all premium and losses incurred in 1992 and later are the responsibility of American Reliance Indemnity Company. The Company distributed its ownership in American Reliance Indemnity Company to American Reliance Group, Inc..

On June 30, 1993 the Company, in collaboration with American Reliance Insurance Company, hereinafter referred to as “Mutual”, sold the bulk of their insurance business written to VIK Brothers Insurance, Inc. and affiliates pursuant to an Asset Purchase Agreement dated February 12, 1993 which was approved by the New Jersey Department of Banking and Insurance on June 21, 1993.

Effective December 18, 1995, the Company’s name was changed to ARI Casualty Company.

On February 1, 1996 the Company moved its principal office and operations to 133 Franklin Corner Road, Lawrenceville, New Jersey 08648. Additionally, during 1996 the Company developed a detailed feasibility study and plan for recommencement of operations. This plan was filed with the State of New Jersey with the request that the Company be permitted to recommence writing insurance. The State of New Jersey approved the Company’s request in August. In April 1997 the Company recommenced issuing insurance policies in the State of New Jersey.

On February 19, 1999 the New Jersey Department of Banking and Insurance approved a capital contribution of \$ 2,000,000 to the Company from its parent, ARI Mutual Insurance Company. The contribution was made to the Company in the form of a transfer of 709,220 shares of ARI Indemnity common stock with a statement value of \$2.82 per share. The Indemnity Insurance Company was sold on October 1, 2005. ARI Casualty owns 100% of ARI Services Inc., which is a “shell” Company.

The registered agent upon whom process may be served is the Company itself.

### **TERRITORY AND PLAN OF OPERATION**

A review of the Company's Schedule T indicated the Company is licensed and authorized to write business in the states of: Delaware, Maryland, New Jersey, Pennsylvania and Virginia and District of Columbia as of December 31, 2007.

The Company conducts its business operations from its home office at 133 Franklin Corners Road, Lawrenceville, New Jersey.

All underwriting and administrative business is conducted at this office; and all accounting books of record are maintained at this office. The Company has no other locations of business.

The Company intends to concentrate on mono-line auto rather than an entire account basis. The Company's concentration is on smaller "mom and pop" businesses with a small percentage of riskier businesses (vehicles over 20,000 pounds).

The Company markets its products exclusively through approximately 170 independent agents and brokers.

The Company places reinsurance through one reinsurance intermediary broker AON, Re Inc. AON began as the Company's Intermediary on August 15, 2005. The Intermediary is authorized to act in the state of New Jersey under N.J.S.A. 17:22E-2(b).

A summary of direct written premiums written over the past three years is summarized below:

<u>Year</u>	<u>Direct Premiums Written</u>
2005	\$600,267
2006	\$500,324
2007	\$297,924

Gross direct written premiums written in 2007 are allocated among the following lines of business:

<u>Line of Business Written</u>	<u>Direct Premiums Written</u>
Commercial Automobile Liability	\$244,419
Automobile Physical Damage	<u>53,505</u>
Total	<u>\$297,924</u>

The Company's accounting, claim, underwriting and administrative functions are conducted at the Company's home office.

#### REINSURANCE AND RETENTION

The Company had the following reinsurance in force as of December 31, 2007:

**Business Type and Contract**

**Reinsurance Limits**

**Commercial Auto Liability**

1 <sup>st</sup> Excess of Loss	\$375,000 excess of \$125,000 Company retention
2 <sup>nd</sup> Excess of Loss	\$500,000 excess of \$500,000
3 <sup>rd</sup> Excess of Loss	\$4,000,000 excess \$1,000,000

**Commercial Auto Physical**

1 <sup>st</sup> Excess of Loss	\$65,000 each insured excess of \$35,000 Company retention; \$195,000 maximum per occurrence
Excess of Loss Catastrophe	95% excess \$250,000 of any catastrophe loss; \$1,662,500 Maximum per occurrence; cannot exceed \$3,325,000 per reinsurance term

Once the above reinsurance is calculated the Company cedes 100% of its retained loss exposures to its Parent ARI Mutual Insurance Company (ARI Mutual) under an Inter-company Reinsurance Pooling Treaty. Loss exposures are then returned to the Company per an inter-company quota share reinsurance treaty with ARI Mutual. Under this Treaty ARI Casualty assumes 35% of total net consolidated losses of the combined Companies. These inter-company Agreements are explained in detail under the examination report section "Holding Company System".

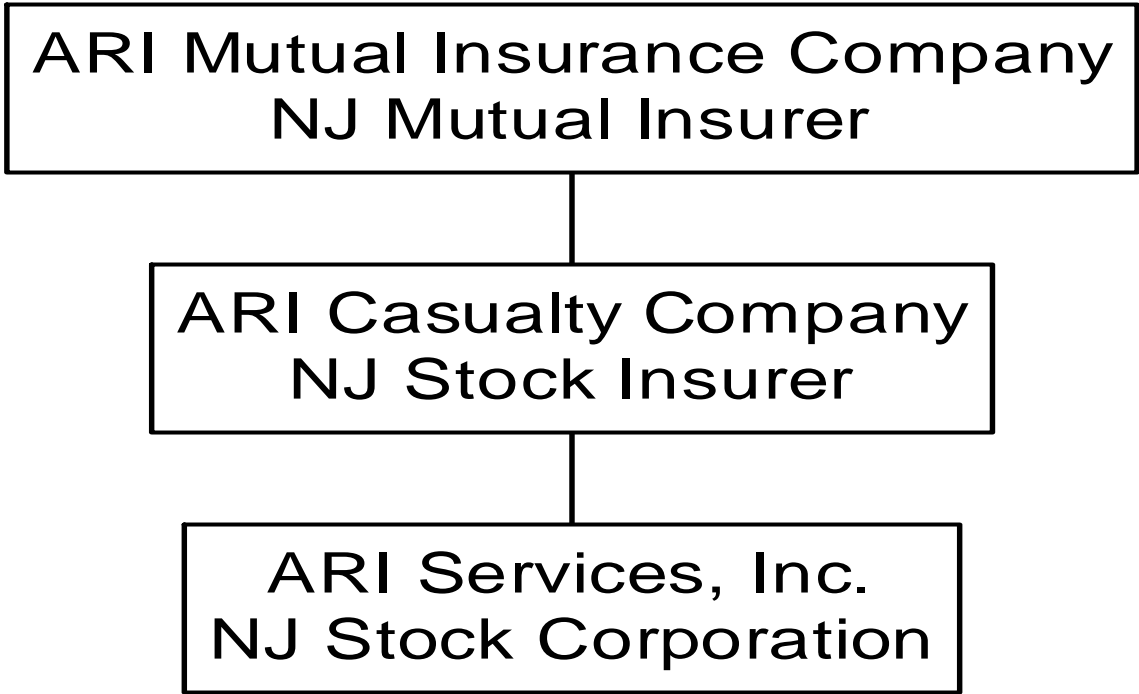
In addition to the above mentioned reinsurance the Company is also a participant in mandatory Pools and Associations. The Company assumes reinsurance from the National Workers Compensation Pool and the New Jersey Commercial Automobile Insurance Procedure and cedes reinsurance to the New Jersey Unsatisfied Claim and Judgment Fund.

The Company did report reinsurance in dispute of \$9,000 as of December 31, 2007 and has not written off any amount in reinsurance balances in 2007.

Reinsurance Agreements were reviewed to ensure contracts had acceptable clauses and conditions. The NJDOBI Actuarial Unit determined that all the reinsurance contracts pass "10/10" risk transfer test.

**INSURANCE HOLDING COMPANY SYSTEM**

The Company is a member of a holding company system as defined within N.J.S.A. 17:27A-1 as illustrated below:



The Company is operating under a number of inter-company agreements, which are described below:

**Inter-Company Quota Share Reinsurance Pooling Agreements**-The Company and ARI Mutual Insurance Company participate in two reinsurance pooling agreements. Under the Agreements ARI Casualty cedes 100% of its premiums and losses to ARI Mutual. ARI Mutual combines this business with its own premiums and losses and cedes 35% back to ARI Casualty. Prior to March 1, 1997, ARI Mutual assumed 40% and ARI Casualty assumed 60% of the combined premiums and losses.

**Management Agreement**-Under the Agreement, ARI Mutual provides the Company use of the following:

- Executive, management, administrative and other employee services
- Office facilities
- Data processing systems and services
- Equipment, supplies, communications and other systems

In exchange ARI Casualty is to share in the cost of such services through the same respective prorated percentage (35%) as indicated in the Pooling Agreement.

**Tax Allocation Agreement**-ARI Mutual files a consolidated income tax return with ARI Casualty Company. The Agreement stipulates ARI Mutual should account for all tax payments and tax refunds and share all payments and refunds based upon each Company's

proportionate share of tax liability (including credit for tax losses) as if the Company filed independently. All agreements have been approved by the NJDOBI in accordance with N.J.S.A. 17:27A-4.

### **CORPORATE RECORDS**

Minutes of meetings held by the Board of Directors revealed adequate approval of the Company's transactions and events including the review and approval of the prior statutory financial examination report.

The Company's adherence to its Certificate of Incorporation and Bylaws was validated without exception.

### **MANAGEMENT AND CONTROL**

#### **Stockholders**

Stockholder meetings are held annually at a place and time as determined by the Board of Directors.

A majority of shareholders shall constitute a quorum for the transaction of any business. Each stockholder is entitled to one vote.

The election of the Board Directors is accomplished by the Shareholders at the shareholders annual meeting.

#### **Directors**

In accordance with the Company's By-laws, the business and affairs of the Company are governed under the management of the Board of Directors.

The By-laws indicate the number of Directors serving the Company should be no less than three or more than five. Directors are to remain in office for a term of three years except in the case of death, resignation or removal. A majority of Directors shall constitute a quorum on any business transactions.

The following Directors were serving as of December 31, 2007:

<b>Director</b>	<b>Current Occupation</b>
<b>George L. Bielitz, Jr.</b>	<b>Independent Financial Consultant Chairman of the Board</b>
<b>Barry W. Blank</b>	<b>Commercial Banking Consultant</b>
<b>William G. Vowteras</b>	<b>President and Full Partner of Fraser Brothers, Inc. an independent insurance agency</b>
<b>Karen S. Fulton</b>	<b>President of ARI Companies and Chief Executive Officer</b>

In accordance with N.J.S.A. 17:27A-4(d)(3) the Company is required to maintain 1/3 outside directors. All Directors other than Karen S. Fulton are outside directors.

In accordance with the By-laws the Company is required to maintain an audit committee consisting of Directors who are neither Officers nor employees of the Company. The audit committee shall perform the following functions:

- Annually arrange an audit of the Company's books by an independent public accountant
- Review the annual report and present the report and its finding to the Board of Directors
- Access to the accounts, books and records of the Company and the cooperation and assistance of the Officers maintaining such corporate and accounting records

Directors of the audit committee serving as of December 31, 2007 were as follows:

**George Leonard Bielitz Jr.  
William George Vowteras  
Barry William Blank**

In accordance with the Company By-laws the Board of Directors may create additional committees and appoint Directors to serve on them. Under this resolution the Board of Directors created a Compensation Committee comprised of the following Directors:

**George Leonard Bielitz Jr.  
William George Vowteras  
Barry William Blank**

As indicated above all Directors serving on both the audit and compensation committees are considered outside directors. As indicated in N.J.S.A. 17:27A-4(d)(4) any committee selecting and reviewing the work performed by the Company's CPA auditors, nominating candidates

for director, or evaluating the performance and determining the compensation of Company officers, shall be comprised solely of outside Directors. Both the compensation and audit committee encompass such functions.

### Officers

As designated in the Company's By-laws the Officers of the Company shall be a President, a Secretary, a Treasurer and additional Officers as designated by the Board. Officers are annually elected and hold one-year terms.

Officers serving the Company as of December 31, 2007 are indicated below:

Karen S. Fulton-President  
John T. Ericson-Secretary  
David A. Gerth-Treasurer

### POLICY ON CONFLICT OF INTEREST

The Company maintains a "Code of Conduct" policy statement for all employees regardless of position. The Code of Conduct stipulates the various conditions and actions that are and or may be deemed by the Company to be inappropriate, potential conflicts of interest and or violations of said policy statement.

Conflict of interest questionnaire are completed annually by each Company employee. Potential conflicts are brought to the attention of the Company's President and questionnaires are annually presented to the Board of Directors for review.

### FIDELITY BONDS AND OTHER INSURANCE COVERAGES

The Company maintains an insurance program on a consolidated basis with Company affiliates designed to protect their assets arising out of property and casualty risks. Coverage's include protection on property, general liability, directors and officers, fiduciary liability, workers compensation, insurance company professional liability, employment practices liability insurance, system breakdown and financial institution bond.

At December 31, 2007, the ARI Insurance Companies maintained Commercial Umbrella Coverage in the amount of \$10,000,000 with deductible of \$10,000.

The Company also maintained fidelity bond with the aggregate limit of \$4,000,000, with insuring clause of a single loss limit of \$2,000,000 and deductible of \$25,000 that include coverage for fidelity, loss of property on premises or in transit and forgery on deposits and securities, counterfeit currency, servicing contractors/third party administrators and

computer theft. The amount of fidelity bond coverage as measured by the NAIC's formula and exposure index was deemed adequate.

### **ACCOUNTS AND RECORDS**

Financial information needed in conjunction with the verification of assets and the determination of liabilities was made available in detail and summary form. The general ledger system was tested and reconciled to the annual statement. The Company's accounting books and records are maintained at the Company's home office. The general books of account are maintained on a Freedom general ledger software package (Freedom).

The Company uses Freedom to record accounts payable, which has a direct feed into the general ledger package.

Premium billing and accounts receivable are recorded using the Company's Phoenix System. Approximately 70% of all premium receipts by volume are received in a lock box and are deposited directly in the bank. The bank issues detail to the Company and the Company records the deposits daily through the Phoenix System. The remaining 30% of receipts are received by the Company directly. Premiums billed are recorded in Phoenix, and are interfaced with Freedom and posted to the general ledger. Written premiums are manually recorded (through journal entries) into Freedom and posted to the general ledger on a monthly basis through reports generated by Phoenix. Commissions are recorded in the same manner with commission payments fully automated and the recording of commissions manually recorded on a monthly basis.

Claim reserves and payments are entered in the Company's Phoenix System on a daily basis and recorded manually (through journal entries) onto Freedom and posted to the general ledger.

Investment transactions are recorded through the use of Excel spreadsheets. The Company records the activity to their investment accounts on a monthly basis. All reconciled monies are then posted to the general ledger through journal entries.

### **CONTINUITY OF OPERATIONS:**

A review was made of the Company's Business Continuity Plan and ImageRight System which holds all the images for claims, underwriting and billing. The review determined that the Company has run tests for their ImageRight System, when they upgraded from their original server to a new server. However, the Company has not presented a fully tested Business Continuity Plan. It is recommended that the company continue to work on upgrading the recovery process of all their important systems and continue developing and testing a full Business Continuity Plan.

## **TREATMENT OF POLICYHOLDERS**

The Company's complaint handling procedures as well as its complaint log were reviewed during the examination.

Upon review of the Company's complaint file it was determined that the Company was in compliance with N.J.S.A. 17:29B-4(10) which states: "This record shall indicate the total number of complaints, their classification by line of insurance, the nature of each complaint, the disposition of these complaints, and the time it took to process each complaint".

## **FINANCIAL STATEMENTS AND OTHER EXHIBITS**

**Exhibit A- Balance Sheet at December 31, 2004 and December 31, 2007**

**Exhibit B- Summary of Operations for the Three Year Period Ending  
December 31, 2007**

**Exhibit C- Capital and Surplus Account for the Three Year Period Ending  
December 31, 2007**

EXHIBIT A

ARI CASUALTY COMPANY  
BALANCE SHEET AT DECEMBER 31, 2007 AND DECEMBER 31, 2004

	Current Examination at 12/31/07	Balance per Company at 12/31/07	Examination Note Change Number	Balance per Company at 12/31/04
<u>Assets</u>				
Bonds	\$28,704,585	\$28,704,585		\$13,606,408
Preferred Stocks	2,282,409	2,282,409		1,237,110
Common Stocks	731,050	731,050		2,063,128
Cash and Short-Term Investments	313,986	313,986		647,515
Investment Income Due and Accrued	399,637	399,637		188,649
Agents' Balances or Uncollected Premiums:				
Uncollected Premiums and Agents' Balances In Course of Collection	5,802,561	5,802,561		2,632,742
Amounts Recoverable From Reinsurers	275,081	275,081		2,195,381
Other Amounts Receivable Under Reinsurance Contracts	76,688	76,688		246,517
Current Federal and Foreign Tax receivable	21,739	21,739		0
Net Deferred Tax Asset	497,798	497,798		521,293
Guarenty Funds on deposit	11,411	11,411		23,374
Electronic Data Processing Equipment	0	0		17,884
Receivable from Parent, Subsidiaries and Affiliates	37,026	37,026		0
Aggregate Write-ins for Other Than Invested Assets	0	0		133,449
<b>Total Admitted Assets</b>	<b>\$39,153,971</b>	<b>\$39,153,971</b>		<b>\$23,513,450</b>
<u>Liabilities</u>				
Losses	\$10,456,776	\$10,456,776		\$6,712,846
Reinsurance Payable on Paid Losses	1,408,830	1,408,830		0
Loss Adjustment Expenses	3,088,562	3,088,562		1,701,182
Commissions Payable	70,201	70,201		66,217
Other Expenses	1,695,853	1,695,853		525,175
Taxes, Licenses and Fees	359,306	359,306		49,489
Current Federal and Foreign Income Taxes	0	0		28,079
Unearned Premiums	5,518,552	5,518,552		3,952,834
Advance Premium	8,565	8,565		0
Ceded Reinsurance Premiums Payable	185,159	185,159		83,305
Amounts Withheld or Retained by Company for Account of Others	18,214	18,214		525,886
Provision for Reinsurance	2,200	2,200		2,000
Payable to Parent Subsidiaries and Affiliates	275,038	275,038		372,779
<b>Total Liabilities</b>	<b>\$23,087,256</b>	<b>\$23,087,256</b>		<b>\$14,019,792</b>
<u>Surplus and Other Funds</u>				
Common Stock	\$3,525,000	\$3,525,000		\$3,525,000
Gross Paid and Contributed Surplus	11,085,186	11,085,186		11,085,186
Unassigned Funds	1,456,529	1,456,529		(5,116,528)
<b>Surplus as Regards Policyholders</b>	<b>\$16,066,715</b>	<b>\$16,066,715</b>		<b>\$9,493,658</b>
<b>Total Liabilities, Surplus and Other Funds</b>	<b>\$39,153,971</b>	<b>\$39,153,971</b>		<b>\$23,513,450</b>

**EXHIBIT B**

**ARI CASUALTY COMPANY**  
**SUMMARY OF OPERATIONS FOR THE**  
**THREE YEAR PERIOD ENDING DECEMBER 31, 2007**

<u>UNDERWRITING INCOME</u>	<u>2007</u>	<u>2006</u>	<u>2005</u>	<u>2004</u>
Premiums Earned	\$11,880,576	\$11,757,694	\$9,479,378	\$7,665,220
<b>Deductions:</b>				
Losses Incurred	6,031,643	5,168,048	2,478,935	3,894,754
Loss Expenses Incurred	1,506,621	1,312,573	1,703,030	1,390,881
Other Underwriting Expenses Incurred	3,713,957	4,156,789	3,567,434	2,125,902
<b>Total Deductions</b>	<b>\$11,252,221</b>	<b>\$10,637,410</b>	<b>\$7,749,399</b>	<b>\$7,411,537</b>
<b>Net Underwriting gain or (Loss)</b>	<b>\$628,355</b>	<b>\$1,120,284</b>	<b>\$1,729,979</b>	<b>\$253,683</b>
 <u>INVESTMENT INCOME</u>				
Net Investment Income Earned	\$1,462,530	\$1,186,252	\$747,752	\$635,634
Net Realized Capital Gains or (-) Losses	117,873	1,598	(31,802)	0
<b>Net Investment Gain</b>	<b>\$1,580,403</b>	<b>\$1,187,850</b>	<b>\$715,950</b>	<b>\$635,634</b>
 <u>OTHER INCOME</u>				
Net Gain or Loss (-) From Agents' Balances Charged Off	(\$106,825)	(\$116,511)	(\$26,733)	(\$26,347)
Finance or Service Charge not Included in Premiums	65,653	65,426	61,956	49,869
Aggregate Write-ins for Miscellaneous Income	0	0	0	0
<b>Total Other Income</b>	<b>(\$41,172)</b>	<b>(\$51,085)</b>	<b>\$35,223</b>	<b>\$23,522</b>
<b>Net Income Before Dividends To Policyholders and Before Federal and Foreign Income Taxes</b>	<b>\$2,167,586</b>	<b>\$2,257,049</b>	<b>\$2,481,152</b>	<b>\$912,839</b>
<b>Dividends To Policyholders</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>8</b>
<b>Net Income Before Federal Income Taxes</b>	<b>\$2,167,586</b>	<b>\$2,257,049</b>	<b>\$2,481,152</b>	<b>\$912,831</b>
<b>Federal and Foreign Income Taxes Incurred</b>	<b>17,784</b>	<b>72,260</b>	<b>81,067</b>	<b>18,624</b>
<b>Net Income</b>	<b>\$2,149,802</b>	<b>2,184,789</b>	<b>\$2,400,085</b>	<b>\$894,207</b>

**EXHIBIT C****ARI CASUALTY COMPANY  
CAPITAL AND SURPLUS ACCOUNT FOR  
THREE YEAR PERIOD ENDING DECMEBER 31, 2007**

	<u>2007</u>	<u>2006</u>	<u>2005</u>	<u>2004</u>
Net Income	<u>\$2,149,802</u>	<u>\$2,184,790</u>	<u>\$2,400,085</u>	<u>\$894,223</u>
<b><u>OTHER SURPLUS GAINS OR (-) LOSSES</u></b>				
Change In Net Unrealized Capital Gains or (-) Losses	(\$183,394)	\$15,743	\$96,608	(\$16,168)
Change in Net Deferred Income Tax	131,507	(564,716)	(2,062,762)	(296,099)
Change in Non Admitted Assets	(290,986)	489,041	2,207,540	393,782
Change in Provision for Reinsurance	<u>18,400</u>	<u>(13,200)</u>	<u>(5,400)</u>	<u>84,200</u>
Total Other Surplus Gains or (-) Losses	<u>(\$324,473)</u>	<u>(\$73,133)</u>	<u>\$235,986</u>	<u>\$165,715</u>
Increase or (-) Decrease as Regards Policyholders	\$1,825,329	\$2,111,657	\$2,636,071	\$1,059,938
Surplus as Regards Policyholders December 31, Previous Year	<u>\$14,241,386</u>	<u>\$12,129,729</u>	<u>\$9,493,658</u>	<u>\$8,433,720</u>
Surplus as Regards Policyholders December 31, Current Year	<u>\$16,066,715</u>	<u>\$14,241,386</u>	<u>\$12,129,729</u>	<u>\$9,493,658</u>

## **NOTES TO THE FINANCIAL STATEMENTS**

### **NOTE 1-BONDS AND STOCKS**

At December 31, 2007 the Company reported assets for bonds of \$ 28,704,585, Preferred Stocks of \$ 2,282,409 and common stocks of \$ 731,050. The assets were accepted as stated.

#### **Statutory Deposits:**

At December 31, 2007 the Company held an U.S. Treasury note of \$ 250,000 with New Jersey, a U.S. Treasury Note of \$ 250,000 with Delaware and a U.S. Treasury Note of \$ 250,000 with Virginia.

### **NOTE 2-LOSS AND LOSS ADJUSTMENT EXPENSE RESERVES**

At December 31, 2007 the Company reported a net liability for Losses and Loss Adjustment Expenses of \$ 13,545,338.

A review of the reserves for losses and loss adjustment expenses was completed by the Property and Casualty Actuarial Division of the New Jersey Department of Banking and Insurance. On the basis of this review, it was determined that the Company's reserves were reasonable and the balances be accepted as stated.

The liabilities consisted of Net Loss Reserves, as reported by the Company and as determined by this examination, totaled \$10,456,776. Net Loss Adjustment Expense Reserves, as reported by the Company and as determined by this examination, totaled \$3,088,562.

### **NOTE 3 – OTHER EXPENSES**

The Company reported a liability for "Other Expenses" of \$ 1,695,853 at December 31, 2007. The liability has been accepted as stated. However, it was determined that the Company did not report an accrual for insurance fraud assessments. It is recommended the Company include insurance fraud assessments in their future accruals.

#### **NOTE 4: SURPLUS AS REGARDS POLICYHOLDERS**

A summary of the Surplus as Regards Policyholders as a result of this examination is summarized below:

Common Capital Stock	\$ 3,525,000
Gross Paid-In and Contributed Surplus	11,085,186
Unassigned Funds	<u>1,456,529</u>
<b>Total Surplus as Regards Policyholders</b>	<b>\$ 16,066,715</b>

The Surplus as Regards Policyholders as determined by this examination amounted to \$ 16,066,715 which is above the minimum needed surplus level of \$ 4,500,000 as required by statutes to write policies without contingent liability.

#### **Gross Paid-In and Contributed Surplus**

At December 31, 2007 the Company reported a balance of \$ 11,085,186 for Gross Paid-In and Contributed Surplus.

#### **Unassigned Funds**

The Exchange reported an amount for unassigned funds at December 31, 2007 of \$ 1,456,529 which has been accepted as stated by this examination report.

#### **REPORT RECOMMENDATIONS**

##### **Continuity of Operations (Page 13)**

It will be recommended that the company continue to work on upgrading the recovery process of all their important systems and that they continue developing and testing a full Business Continuity Plan.

##### **Other Expenses (Page 18)**

It was determined that the Company did not report an accrual for insurance fraud assessments. It is recommended the Company include insurance fraud assessments in their future accruals.





