

**REPORT ON EXAMINATION AS TO THE CONDITION OF  
MERCER INSURANCE COMPANY OF NEW JERSEY, INC.**

**PENNINGTON, NEW JERSEY 08534**

**AS AT DECEMBER 31, 2008**

**N.A.I.C. GROUP CODE 1114**

**N.A.I.C. COMPANY CODE 43540**

**FILED**

**June 24, 2010**

Commissioner  
Department of Banking & Insurance

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JUNE 7, 2010

Honorable Thomas B. Considine  
Commissioner of Banking and Insurance  
State of New Jersey  
20 West State Street  
Trenton, New Jersey 08625-0325

Commissioner:

Pursuant to instructions and in accordance with N.J.S.A. 17:23-22, an examination as of December 31, 2008 was made of the financial condition and affairs of

MERCER INSURANCE COMPANY OF NEW JERSEY, INC.  
NAIC GROUP CODE 1114 NAIC COMPANY CODE 43540

a domestic insurer duly authorized to transact the business of insurance in the State of New Jersey, hereinafter referred to as the "Company" or "Mercer" or "MICNJ".

## **SCOPE OF EXAMINATION**

The comprehensive examination covered the period January 1, 2005 through December 31, 2008 and included any material transactions or events occurring subsequent to the examination date and noted during the course of this examination. The examination was conducted at the Company's home office located at 10 Route 31, Pennington, New Jersey.

The examination took place concurrently with the other affiliated companies of Mercer Group which was lead by the Pennsylvania Insurance Department, being primary state of domicile of the parent Company Mercer Insurance Company (MIC).

The examination was made as at December 31, 2008, and addressed the four-year period from December 31, 2004, the date of the last Financial Condition Examination. During this four-year period under examination, the Company's reported assets increased from \$45,998,876 to \$69,911,114, Company's reported liabilities increased from \$30,361,968 to \$50,550,430 and MICNJ's reported surplus as regards policyholders increased from \$15,636,908 to \$19,360,684.

This examination was conducted in accordance with the risk focus examination approach as adopted by the National Association of Insurance Commissioners (NAIC) and followed regulatory procedures prescribed or permitted by the New Jersey Department of Banking and Insurance. The format of this report is consistent with the current practices of the NJ Department of Banking and Insurance (NJDOBI) and the examination format prescribed by the National Association of Insurance Commissioners (NAIC). It is limited to a description of the Company, a discussion of financial items that are of specific regulatory concern, and a factual disclosure of other significant regulatory information.

The overall objectives of the examination are:

1. To identify significant deviations from statutory accounting practices and procedures that impact solvency,
2. To identify significant deviations from New Jersey insurance laws, regulations and department directives.
3. To comply with the standards prescribed in the revised NAIC Financial Condition Examiners Handbook, NAIC accreditation/codification standards and procedures and with New Jersey Laws and Regulations.
4. To identify and report significant operational and internal control deficiencies.
5. To assess the quality and reliability of corporate governance to identify, assess and manage the risk environment facing the insurer in order to identify current or prospective solvency risk area.
6. To assess the risks that the Company's surplus is materially misstated.
7. To provide a foundation for a profile of the Company's operations, risks and results to be utilized by regulatory authorities.

The specific asset and liability accounts comprising, in part, the various examination phases that are "generally material" were determined to require substantive procedures to be performed during the examination were:

- Bonds
- Preferred and Common Stocks
- Cash and Short-term Investments
- Losses
- Loss Adjustment Expenses
- Receivable from Parent, Subsidiaries and Affiliates

Additional areas reviewed during this examination were as follows:

- History and Kind of Business
- Territory and Plan of Operation
- Reinsurance
- Management and Control
- Fidelity Bond and Other Insurance Coverages
- Policy on Conflict of Interest
- Parent, Subsidiaries and Affiliates
- Inter-Company Agreements
- Accounts and Records
- Advertising and Sales Material
- Treatment of Policyholders/Claimants
- Continuity of Operations

The examination report, contained herein, will address significant balance sheet accounts and, if necessary, comments on those accounts which involve departures from laws, regulations or rules, or which are deemed to require special explanation or description. All other accounts were either tested by Analytical Review or Control Procedures.

## **COMPLIANCE WITH PRIOR EXAMINATION RECOMMENDATIONS**

### **Accounts and Records**

MIC business continuity plan (disaster recovery plan) which includes all subsidiaries and affiliates has not been tested since December 31, 1999. It is recommended that the Company update the business continuity plan (disaster recovery plan) and schedule an annual testing of the plan.

The Company updated the business continuity plan (disaster recovery plan) but the plan has yet to be tested.

### **Cash and Short-Term Investments**

It is recommended that in the future, the Company report all long-term certificates of deposit as bonds in accordance with Statement of Statutory Accounting Principle No. 26, paragraph 2 of the NAIC Accounting Practices and Procedures Manual.

The Company no longer owns any long term certificates of deposit as of December 31, 2008.

### **Agents' Balances or Uncollected Premiums**

It is recommended that the Company change its aging method of premiums receivable to conform to the requirement of Statement of Statutory Accounting Principle No. 6, paragraph 7(d) of the NAIC Accounting Practices and Procedures Manual.

The Company complied with the recommendation.

### Other Expenses

It is recommended that in the future the Company establish and report an accrual for the annual statement liability item Other Expenses when a liability exists in accordance with Statement of Statutory Accounting Principle No. 5, paragraph 3 of the NAIC Accounting Practices and Procedures Manual so as not to understate the Company's true liabilities.

The company is in compliance through the use of the inter-company account.

### **HISTORY AND KIND OF BUSINESS**

The Company was incorporated under the laws of New Jersey dated October 14, 1981 and commenced business on September 15, 1982.

The Company's initial certificate of authority permitted the Company to write the kinds of insurance specified in paragraphs "a", "b", "e", "j" "k" "l" and "o" of **N.J.S.A.** 17:17-1 of the Revised Statutes of New Jersey.

MICNJ's Certificate of Amendment to the Certificate of Incorporation dated January 16, 1996 enabled the Company to write the kinds of insurance authorized by paragraph "e" of **N.J.S.A.** 17:17-1 et seq. except only that authority granted under paragraph "e" to write automobile bodily injury liability and automobile property damage liability, is specifically excluded.

MICNJ's Certificate of Amendment to the Certificate of Incorporation dated December 17, 1997 occurred due to a name change from Mercer Insurance Company to Mercer Insurance Company of New Jersey, Inc. (MICNJ).

MICNJ's Certificate of Amendment to the Certificate of Incorporation dated August 12, 1998, fifth paragraph of **N.J.S.A.** 17:17-1 increased the common capital stock and gross paid in and contributed surplus from \$1,000,000 to \$3,500,000 and \$400,000 to \$600,000 respectively.

MICNJ's Certificate of Amendment to the Certificate of Incorporation dated August 12, 1998, third paragraph of **N.J.S.A.** 17:17-1 granted the Company authorization to transact the kinds of business specified in paragraph "a", "b", "e", "f", "g", "j", "k", "l", "m", "n", "o-1" and "o-3ii".

The authorized capital stock of the Company is \$3,500,000 divided into 350,000 shares of common stock having a par value of \$10 per share. All authorized shares are issued and outstanding, and owned by Queenstown Holding Company, Inc.

The Company's gross paid in and contributed surplus increased \$5,596,657 from \$600,000 to \$6,196,657 for the period ending December 31, 2003. This amount of gross paid in and contributed surplus of \$6,196,657 is as of December 31, 2008.

## **MANAGEMENT AND CONTROL**

The directors and officers of the Company as of the examination date were as follows:

### **Directors and Address**

### **Principal Occupation**

Ronald D. Boehm  
10 North Highway 31  
Pennington, NJ 08534

Self Employed Business Consultant

William V. R. Fogler  
10 North Highway 31  
Pennington, NJ 08534

Owner  
Van Rensselaer Ltd.

William C. Hart  
10 North Highway 31  
Pennington, NJ 08534

Retired

George T. Hornyak, Jr.  
10 North Highway 31  
Pennington, NJ 08534

Self Employed Private Investor

Richard U. Niedt  
10 North Highway 31  
Pennington, NJ 08534

Retired

Richard G. Van Noy  
10 North Highway 31  
Pennington, NJ 08534

Retired

Andrew R Speaker  
10 North Highway 31  
Pennington, NJ 08534

President, Chief Executive Officer  
Mercer Insurance Group, Inc.

Samuel J. Malizia

Managing Partner

10 North Highway 31  
Pennington, NJ 08534

Mazilia Spidi & Fisch, PC

Henry T. Davis  
10 North Highway 31  
Pennington, NJ 08534

Sr. Vice President  
Mercer Insurance Group, Inc

**Officers:**

**Title**

Andrew R. Speaker

President, Chief Executive Officer

David B. Merclean

Sr. Vice President and CFO

Paul D. Ehrhardt

Sr. Vice President Underwriting &  
Secretary

Henry T. Davis, Jr.

Sr. Vice President

Richard Chichester

Vice President Marketing

Gordon A. Coleman

Treasurer

Lawrence Crawford

Vice President Claims

Paul Corkey

Chief Information Officer

Raymond Dudonis

Vice President

In accordance with N.J.S.A. 17:27A-4d(3) the company is required to have a Board of Directors (Board) comprised of no less than 1/3 outside directors. All of the seven Board members are considered "outside" directors with the exception of Andrew Speaker, who is the President, Chief Executive Officer Mercer Insurance Group, Inc.

In accordance with N,J,S.A. 17:27A-4d(4) any committee selecting and reviewing the work performed by the Company's CPA firm, nominating candidates for director or evaluating the performance and determining the compensation of Company officers shall be comprised solely of outside directors. These functions are under the direction of the audit and compensation committee. In accordance with the Corporate By-Laws the audit and compensation committees or any other committee designated by the majority of the Board.

Members of the audit and compensation committees are as follows:

**Audit Committee:**

George T. Hornyak, Jr.  
William C. Hart  
Richard Neidt  
Richard G. Van Noy

**Compensation Committee**

William Hart  
George Hornyak  
Richard Neidt  
Richard G. Van Noy

In accordance with N.J.S.A. 17:27A-4d(3) the company is required to have committees of the Board of Directors comprised of no less than 1/3 outside directors. Additional committees maintained by the Company in compliance with N.J.S.A. 17:27A-4(d)(3) are as follows:

Investment Committee  
Nominating/Governance Committee

All the Committees are for the benefit of Mercer Insurance Group, Inc..

**CONFLICT OF INTEREST**

The Company, as part of the Mercer Insurance Group, Inc. and its ultimate parent, has a formal code of “Conduct and Ethics Policy”, which includes a conflicts of interest policy.

Annually all officers and employees of the company are required to certify in writing that they have read and understand their responsibility to comply with the policy, execute the related questionnaire and disclose any potential conflicts.

A review of senior management and the Board of Directors questionnaires for the examination period revealed no conflicts of interests.

**CORPORATE RECORDS**

The review of the minutes of the Board of Directors, Stockholders and Audit Committee adequately support Company transactions, events and operations. MICNJ operates under common management with the Mercer Insurance Company.

The review of the agreements and the minutes of the board and committee meetings determined the Services Allocation Agreement and the Consolidated Tax Sharing Agreement were not submitted and approved by the Board of Directors. It is recommended that the Company establish procedures for all affiliated agreements

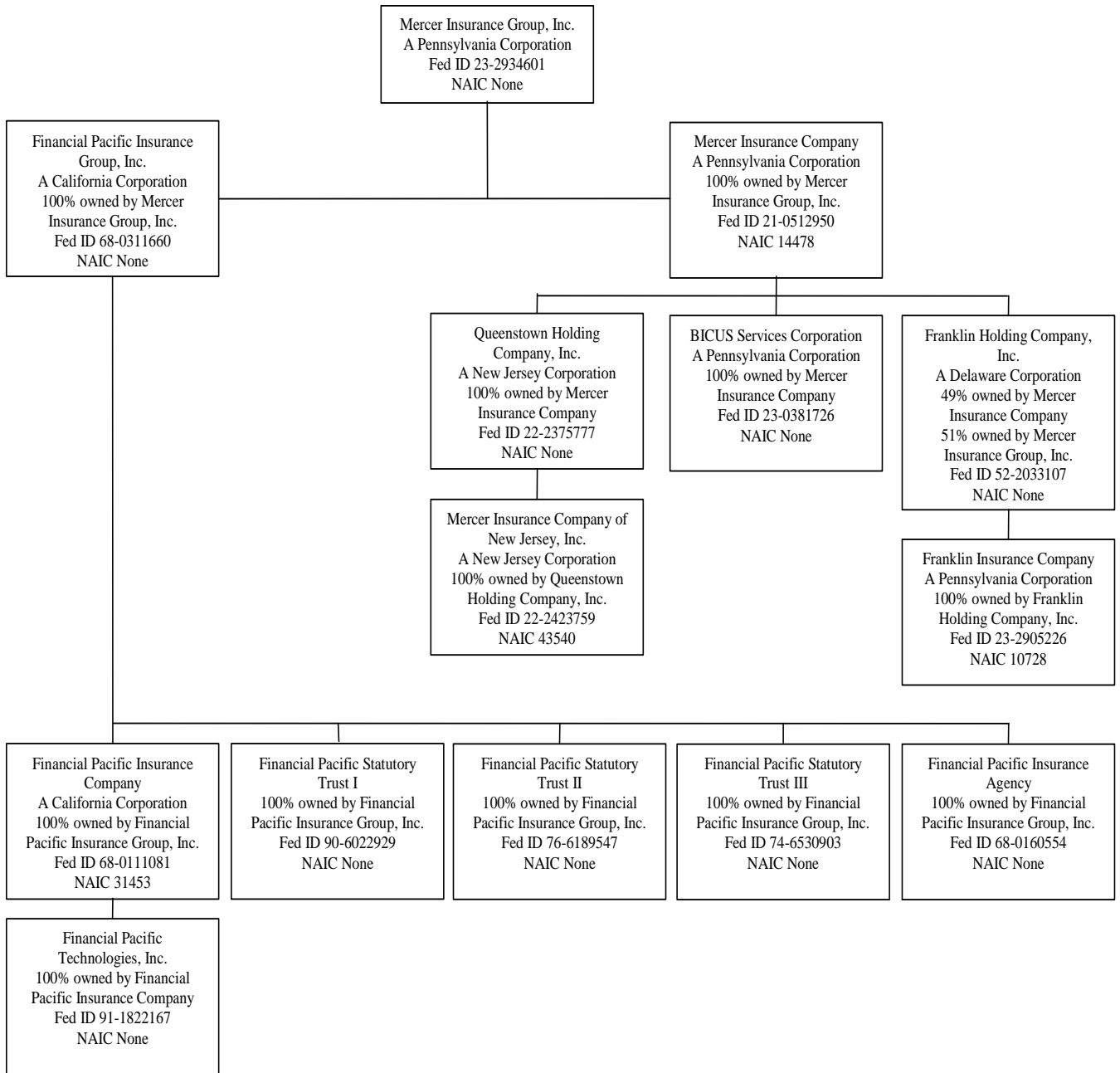
and transactions are properly reviewed and approved by the board of directors to ensure good corporate compliance.

### **REGULATION OF INSURANCE HOLDING COMPANY SYSTEMS**

The Company is a wholly owned subsidiary of Queenstown Holding Company, Inc. a New Jersey Corporation, which is a 100% owned subsidiary of the Mercer Insurance Company, a Pennsylvania corporation.

The Mercer Insurance Group, Inc. (MIG) also a Pennsylvania corporation and the Company's ultimate parent, owns 100% of the MIC. The Company is a member of an insurance holding company system as defined under **N.J.S.A.** 17:27A-1 and a registration statement by MIG has been filed on behalf of its subsidiaries in accordance with **N.J.S.A.** 17:27A-3.

The following is an organizational chart of the Mercer Insurance Company of New Jersey, Inc. and its affiliated companies:



## **INTER-COMPANY AGREEMENTS**

The Company participated in several agreements with its parent and or affiliates. The agreements are as follows:

### **Reinsurance Pooling Agreement**

The Group operates under an inter-company pooling agreement whereby all business acquired by the participants is pooled. This pooling arrangement was updated January 1, 2006 after the acquisition of Financial Pacific Insurance Company (FPIC) in 2005. The current pooling percentages are as follows: MIC (the lead Company) maintains 42%, FPIC maintains 40%, Franklin Insurance Company (FIC) maintains 5% and MICNJ maintains 13%. Premiums and losses from FIC and MICNJ are ceded 100% to Mercer before non-affiliated reinsurance cessions. FPIC, however, cedes premiums and losses after non-affiliated reinsurance cessions. The percentage that Mercer Insurance Company retro-cedes business back to the Companies is based upon each Company's prior year surplus.

The Company's affiliated reinsurance pooling agreement stipulates balances are to be settled on a quarterly basis within forty-five days of the quarter end. It was determined the Company failed to settle balances reported as of December 31, 2008, by the stipulated due date. The Company is not in compliance with the terms of the affiliated reinsurance pooling agreement. It is recommended that the Company settle all balances covered by the affiliated pooling agreement by the stipulated due date.

### **Service Allocation Agreement**

Mercer Insurance Group, Inc., Mercer Insurance Company, Financial Pacific Insurance Group, Inc., Financial Pacific Insurance Company, Financial Pacific Technologies, Inc., Queentown Holding Company, Inc., Mercer Insurance Company of New Jersey, Inc., Franklin Holding Company, Inc.; and Franklin Insurance Company are parties to a Service Allocation Agreement which stipulates that certain services and functions for all of the parties will be performed by BICUS Services Corporation, a wholly owned subsidiary of the Mercer Insurance Company. The parties reimburse BICUS for their respective shares of such services and functions.

The Company's Services Allocation agreement does not comply with the requirements of SSAP No. 25 and No.96 as it contains no provision for timely settlements of intercompany balances. It is recommended that the Company amend its affiliated Service Agreements to include provisions for timely settlements, with specific due dates, as required under the provisions of SSAP No. 25 and No. 96.

## **Tax Allocation Agreement**

Effective October 1, 2005 Mercer Insurance Group, Inc., Mercer Insurance Company, Financial Pacific Insurance Group, Inc., Financial Pacific Insurance Company, Financial Pacific Technologies, Inc., Financial Pacific Insurance Agency, BICUS Services Corporation, Queenstown Holding Company, Inc., Mercer Insurance Company of New Jersey, Inc., Franklin Holding Company, Inc., and Franklin Insurance Company are parties to a consolidated tax agreement.

Under the agreement each company is allocated a pro-rata share of the consolidated income tax expense based upon its contribution of taxable income to the consolidated tax return. Additionally, allocation is based upon separate return calculations with current credit for net losses.

Inter-company tax balances are settled within forty-five days of finalization of each company's tax liability.

## **FIDELITY BOND AND OTHER INSURANCE COVERAGES**

The company's and its affiliates are covered under a financial institution bond maintained by the ultimate parent with a single loss of limit liability of \$1,000,000 and a single loss deductible of \$25,000. This coverage is adequate for an individual Company basis based on the minimum levels recommended by the NAIC.

Other Insurance Policies include:

- Commercial Automobile
- Special Multi Peril
- Employer Liability
- Commercial Crime Policy - Fidelity
- Surety Bond- Commercial Crime - Fidelity (For ESOP)
- Directors and Officers Liability
- Financial Institution Bond
- Workers' Compensation

## **EMPLOYEE WELFARE AND PENSION PLANS**

The Company has no employees and, therefore, has no retirement, deferred compensation, or other post retirement benefit plan liabilities. All employees are employed directly by BICUS Services Corporation. BICUS provides management services to all of the insurance companies.

## **STATUTORY DEPOSITS**

The following securities were held by the State of New Jersey as special deposits on behalf of the Company:

Goldman Sachs ILA Federal Portfolio	\$ 122
US Treasury Notes 4.625% 11/15/2009	100,000

## **POLICY FORMS AND UNDERWRITING GUIDELINES**

MICNJ, through its parent Mercer Insurance Group, Inc., maintains an underwriting guide. A review of the underwriting guideline manual indicated that MICNJ writes their personal and commercial lines by evaluating each risk with consistently applied standards. The Company maintains information on all aspects of their business, which is regularly reviewed to determine product line profitability.

MICNJ through the Mercer Insurance Group, Inc. maintains access to numerous underwriters, who generally specialize in either personal or commercial lines, and have many years of experience as underwriters. Specific information is monitored with regard to individual insureds to assist the Company in making decisions about policy renewals or modifications. New risks are frequently inspected to insure they are as desirable as suggested by the application process.

The Company relies on information provided by independent agents. Subject to certain guidelines, producers also pre-screen policy applicants. The producers have the authority to sell and bind insurance coverages in accordance with pre-established guidelines.

Producers' results are continuously monitored. On occasion, producers with historically poor loss ratios have had their binding authority removed until more profitable underwriting results were achieved. Continued poor loss ratios often result in agency termination.

## **TERRITORY AND PLAN OF OPERATION**

The Company is licensed only to write insurance within the confines of the State of New Jersey. The Company is located at 10 North Highway 31, Pennington, NJ 08534. The Company's accounts and data are maintained at this address.

The Company's is authorized to write homeowners and commercial lines coverages, including workers' compensation, commercial automobile and a religious institution package policy. Commercial products target mercantile, light manufacturing business owners, artisans and contractors coverage.

The Company utilizes independent agents to write its business and is not producer controlled. Broker and agents commissions are authorized in accordance with their respective agreements.

## **REINSURANCE**

In the ordinary course of business the Company seeks to limit its exposure to loss on individual claims and from the effects of catastrophes by entering into reinsurance contracts with other insurance companies. Reinsurance is ceded on excess of loss and on a pro rata basis with the Company's retention not exceeding \$850,000 (excluding workers' compensation) per occurrence for year ending December 31, 2008.

As of December 31, 2008 the Mercer Insurance Company retro-ceded 13%, 5% and 40% back to Mercer Insurance Company of New Jersey, Franklin Insurance Company and Financial Pacific Insurance Company, respectively. The following summary identifies the various coverages by treaty;

<b><u>Treaty</u></b>	<b><u>Coverage</u></b>
Multi-Line Excess	\$150,000 x \$850,000 per occurrence All lines except umbrella
WC First Excess	\$1,000,000 X \$1,000,000 per occurrence
WC Second Catastrophe Excess	\$3,000,000 X \$2,000,000 per occurrence
Property Per Risk First	\$4,000,000 X \$1,000,000 per occurrence Occurrence Limit \$8,000,000
Property Per Risk Second	\$2,500,000 X \$5,000,000 per occurrence
First Excess Catastrophe	100 % of \$5,000,000 X \$5,000,000
Second Excess Catastrophe	100 % of \$10,000,000 X \$10,000,000
Third Excess Catastrophe	100 % of \$35,000,000 X \$20,000,000

First Casualty Contingency Excess of Loss	\$1,000,000 X \$1,000,000 per occurrence
Second Casualty Contingency Excess of Loss	\$3,000,000 X \$2,000,000 per occurrence
Commercial Umbrella Excess	75% of \$1,000,000 100% of \$4,000,000 X \$1,000,000 Additional w/ approval
Personal Umbrella Excess	75% of \$1,000,000 100% of \$2,000,000 X \$1,000,000 Additional \$2,000,000 w/ approval
American Re Facultative	Excess of \$4,000,000 subject to American Re approval.
Boiler & Machinery Quota Share	100% of Boiler and Machinery Losses and LAE -.0065% churches/ .024% Business Operating policy, of total insurable value Policy of Boiler and Machinery Premiums
Terrorism Excess of Loss	\$10,000,000 X \$3,000,000 in the aggregate

In accordance with N.J.S.A. 17:18-9 (Risk Limitations), “No insurance company transacting business in this State shall expose itself to any loss on any one risk or hazard in an amount exceeding ten per centum (10%) of its net assets as of December 31 next preceding, . . . , EXCEPT that for the kind of business specified in subsection “e” of N.J.S.A. 17:17-1, the exposure shall not exceed five per centum (5%) of the insurer’s net assets as of December 31 next preceding.” MICNJ is in compliance with N.J.S.A. 17:18-9 on Risk Limitations.

The Company maintains reinsurance intermediaries-brokers, AON RE Inc./ Benefield Inc. as liaisons between the Company and its reinsurers. The reinsurance intermediaries are authorized to transact business in the State of New Jersey under N.J.S.A. 17:22E-2(b). The Company maintains agreements with Benefield Inc. conforming to the reinsurance intermediary contract requirements as stipulated in and in accordance with N.J.S.A. 17:22E-6. The agreement with AON Re Inc. does not meet N.J.S.A. 17:22-6. It is recommended that the Company modify the agreement to be in compliance with N.J.S.A. 17:22E-6. The Company is party to one reinsurance agreement with Factory Mutual Insurance Company

and three reinsurance agreements with Munich Reinsurance America which did not include language for an entire agreement clause. The missing information is "The agreement shall constitute the entire contract between the parties and must provide no guarantee of profit, directly or indirectly, from the reinsurer to the ceding entity or from the ceding entity to the reinsurer".

It is recommended that the Company amend its reinsurance agreement to an entire agreement clause to ensure compliance with SSAP 62 paragraph 8c.

It was determined that the agreement with General Reinsurance Corporation included a provision for a Mortgagee Reinsurance Endorsement which allows certain policy beneficiaries to obtain payment directly from the reinsurer. This cut-through provision limits the effectiveness of the insolvency clause and the reinsurance agreement's compliance with SSAP 62, paragraph 8a.

It is recommended that the company amend its reinsurance agreement to remove any provisions which allows cut-through for its policyholders to ensure compliance with the NAIC Accounting Practices and Procedures Manual SSAP 62, paragraph 8a.

### **CONTINUITY OF OPERATIONS**

The Company, as part of the Mercer Insurance Group, Inc. group of companies, has developed and maintains a formal disaster recovery plan for the purpose of continuing its business operations in the event of a natural or man made disaster. The plan provides for and each department has an individual department preparation plan identifying its responsibility.

The information systems plan requires a complete backup of data each night. The most recent backup tape is taken off-site by a designated Information Systems employee. Each week the prior week's backup tapes are stored off-site in a bank deposit box. Plans are in place to replicate data between the Lock Haven, Pennsylvania and Pennington, New Jersey offices as much as possible.

The Company's disaster recovery Emergency Team meets semi-annually to review the plan and is responsible for the Company becoming operational and conducting business as efficiently as possible under the circumstances.

It was noted that the disaster recovery plan has not been tested and or the Company has not performed a mock recovery drill so as to identify any potential deficiencies, which could potentially impede the process necessary to establish either a basic or critical systems restoration and the specific recovery time associated with each critical system restoration.

It is recommended the Company perform a mock disaster recovery test to further identify and document essential deficiencies that might exist which could potentially impede the process necessary to establish either a basic or critical systems restoration or the specific recovery time associated with each critical system restoration.

### **ACCOUNTS AND RECORDS**

The Company's accounting, investment, policy and claim records are available at the Company's administrative office.

The Company utilizes the Phoenix software for its policy management system, to process all transactions including claims, accounting, billing and policy administration and inquiry. Custom reports used to analyze and interpret that data are created using Actuate, a reporting tool. All accounting transactions are fed into Oracle Financials. The Oracle financial system allows for the processing of accounts Payable and General Ledger transactions as well as the payment of claims or refunds.

### **AUDITED FINANCIALS**

Pursuant to **N.J.A.C.** 11:2-26.4 an annual audit was performed by the CPA firm of KPMG LLP, located at 1601 Market Street Philadelphia, Pa. 19103-2499 and an audited financial CPA report with the qualification letter was filed with the Commissioner of Banking and Insurance of the State of New Jersey for the examination period.

The report contains a synopsis of the major audit activities and the results of these activities on the Company's financial statements.

### **ADVERTISEMENT MATERIALS**

A review of the Company's advertisements indicated that it is in compliance with **N.J.S.A.** 17:18-10.

### **TREATMENT OF POLICYHOLDERS**

The Company maintains a complaint register, which is in general compliance with **N.J.S.A.** 17:29B-4(10).

## **FINANCIAL STATEMENTS AND OTHER EXHIBITS**

The financial statements consist of the following exhibits and notes to financial statements showing the financial condition as of December 31, 2008, as shown in the annual statement:

EXHIBIT A: Comparative Statement of Assets, Liabilities, Surplus, and Other Funds at December 31, 2008.

EXHIBIT B: Summary of Operations for the Four-Year Period Ending December 31, 2008.

EXHIBIT C: Capital and Surplus Account for the Period Ended December 31, 2004 through December 31, 2008.

The financial statements, schedules, and other exhibits shown in the following pages are based upon the annual statements as reported by the Mercer Insurance Company of New Jersey, Inc. Failure of items to add to the totals in certain schedules is due to rounding.

MERCER INSURANCE COMPANY OF NEW JERSEY					
STATEMENT OF ASSETS, LIABILITIES AND SURPLUS FUNDS					
AS OF DECEMBER 31, 2008			EXHIBIT A		
	Balance Per		Balance Per		
	Examination		Company	Examination	Note
<u>Assets</u>	<u>December 31,2008</u>		<u>December 31,2008</u>	<u>Change</u>	<u>Number</u>
Bonds	\$38,527,187		\$38,527,187	\$0	1)
Preferred stocks	537,750		537,750	0	
Common stocks	623,165		623,165	0	(1)
Cash and short-term investments	6,485,794		6,485,794	0	
Investment income due and accrued	441,723		441,723	0	
Agents' balances and uncollected premiums In Course of Collection	4,857,849		4,857,849	0	
Agents' balances and uncollected premiums Deferred and Not Yet Due	5,744,073		5,744,073	0	
Amounts recoverable from reinsurers	4,966,416		4,966,416	0	
Net deferred tax asset	1,013,938		1,013,938	0	
Receivable from parent, subsidiaries and affiliates	6,471,894		6,471,894	0	
Agg. Write-in for other than invested assets	241,325		241,325	0	
<b>Total Assets</b>	<b>\$69,911,114</b>		<b>\$69,911,114</b>	<b>\$0</b>	
<u>Liabilities</u>					
Losses	\$28,335,036		\$28,335,036	\$0	(2)
Reinsurance payable on paid loss and LAE	1,817,799		1,817,799	0	
Commissions payable	383		383	0	
Other Expenses	-		-	0	
Taxes, licenses and fees	104,886		104,886	0	
Federal and foreign income taxes	514,180		514,180	0	
Unearned premiums	9,530,645		9,530,645	0	
Ceded reinsurance premiums payable	9,976,723		9,976,723	0	
Amounts withheld by company for others	270,778		270,778	0	
<b>Total Liabilities</b>	<b>\$50,550,430</b>		<b>\$50,550,430</b>	<b>\$0</b>	
Common capital stock	\$3,500,000		\$3,500,000	\$0	
Gross paid in and contributed surplus	6,743,060		6,743,060	0	
Unassigned funds (surplus)	9,117,624		9,117,624	0	
Surplus as regards policyholders	\$19,360,684		\$19,360,684	\$0	(3)
<b>Total Liabilities and Surplus</b>	<b>\$69,911,114</b>		<b>\$69,911,114</b>	<b>\$0</b>	

MERCER INSURANCE COMPANY OF NEW JERSEY				
UNDERWRITING AND INVESTMENT EXHIBIT				
FOUR PERIOD ENDED DECEMBER 31, 2008				
				<u>EXHIBIT B</u>
	<u>2005</u>	<u>2006</u>	<u>2007</u>	2008
<u>Underwriting Income</u>				
Premiums earned	<u>\$ 11,565,611</u>	<u>\$18,533,394</u>	<u>\$19,067,695</u>	<u>\$19,835,014</u>
Deductions:				
Losses incurred	\$4,456,667	\$8,826,880	\$8,768,337	\$8,368,299
Loss adjustment expenses incurred	883,439	2,576,449	3,090,120	4,014,652
Other underwriting expenses	5,334,946	6,378,246	6,681,463	6,919,598
Total underwriting deductions	\$10,675,052	\$17,781,575	\$18,539,920	\$19,302,549
Net underwriting gain or (loss)	<u>\$890,559</u>	<u>\$751,819</u>	<u>\$527,775</u>	<u>\$532,465</u>
<u>Investment Income</u>				
Net investment income earned	\$739,894	\$1,170,542	\$1,516,456	\$1,661,531
Net realized capital gains	(115,911)	(18,193)	(10,629)	(203,951)
or (losses)				
Net investment gain or (loss)	<u>\$623,983</u>	<u>\$1,152,349</u>	<u>\$1,505,827</u>	<u>\$1,457,580</u>
<u>Other Income</u>				
Net gain from agents or premium balances recovered	(\$65,962)	(\$156,529)	(\$170,310)	(\$208,529)
Finance and service charge	175,791	176,468	172,923	169,063
Aggregate write-in for mis income	-	-	-	-
Total Other Income	<u>\$109,829</u>	<u>\$19,939</u>	<u>\$2,613</u>	<u>(\$39,466)</u>
Net income before dividends to policyholders and before federal and foreign income taxes	\$1,624,371	\$1,924,107	\$2,036,215	\$1,950,579
Dividends to policyholders	-	-	-	
Net income after dividends to policyholders but before federal income taxes	\$1,624,371	\$1,924,107	\$2,036,215	\$1,950,579
Federal and foreign income taxes incurred	428,624	1,207,204	780,967	<u>619,246</u>
Net income	<u>\$1,195,747</u>	<u>\$716,903</u>	<u>\$1,255,248</u>	<u>\$ 1,331,333</u>



## **NOTES TO THE FINANCIAL STATEMENTS**

### **(NOTE 1) Bonds and Stocks**

The custodial agreement is for Commerce Bank whereas the bank was purchased from TD Bank. The custodial agreement does not meet the NAIC requirements for custodial agreements. It is recommended that the company enter into a custodial agreement that will meet the NAIC Provisions and Safeguards with TD Bank as custodian.

### **(NOTE 2) LOSSES**

MICNJ's loss and loss adjustment expense reserves, as reported by the Company totaled \$28,335,036 for the period ending December 31, 2008.

The New Jersey Department of Banking and Insurance Managing Property and Casualty Actuary determined that MICNJ's overall reserves as of December 31, 2008 were reasonable and acceptable to meet future loss and loss adjustment expenses. This review was based on an actuarial analysis by California and approved by the lead state, Pennsylvania.

Kevin C. McAllister, FCAS, MAAA of KPMG LLP has certified the adequacy of the Company's loss and loss adjustment expense reserves as of December 31, 2008. His review of these reserves concluded that the Company makes a reasonable provision, in the aggregate, for all unpaid loss and loss adjustment expense obligations of the Company under the terms of its contracts and agreements.

### **(NOTE 3) SURPLUS AS REGARDS POLICYHOLDERS**

MICNJ's Surplus as Regards Policyholders as determined by this examination and reported in the Company's 2008 Annual Statement, is \$19,360,684. This amount consisted of common capital stock of \$3,500,000, gross paid in and contributed surplus of \$6,743,060 and unassigned funds (surplus) \$9,117,624.

## **EXAMINATION RECOMMENDATIONS**

### **CORPORATE RECORDS (Page 8)**

It is recommended that the Company establish procedures for all affiliated agreements and transactions are properly reviewed and approved by the board of directors to ensure good corporate compliance.

### **INTERCOMPANY AGREEMENTS (Page 11 )**

It is recommended that the Company settle all balances covered by the affiliated pooling agreement by the stipulated due date.

It is recommended that the Company amend its affiliated Service Agreements to include provisions for timely settlements, with specific due dates, as required under the provisions of SSAP No. 25 and No.96.

### **REINSURANCE (Page 14 )**

It is recommended that the Company modify the AON reinsurance intermediary agreement to be in compliance with NJSA 17:22E-6.

It is recommended that the Company amend its reinsurance agreements to include an entire agreement clause to ensure compliance with SSAP 62, 8c.

It is recommended that the company amend its reinsurance agreement to remove any provisions which allows cut-through for its policyholders to ensure compliance with the NAIC Accounting Practices and Procedures Manual SSAP 62, paragraph 8a.

### **CONTINUITY OF OPERATIONS (Page 16 )**

It is recommended the Company perform a mock disaster recovery test to further identify and document essential deficiencies that might exist which could potentially impede the process necessary to establish either a basic or critical systems restoration and the specific recovery time associated with each critical system restoration.

### **BONDS AND STOCKS (Page 22)**

It is recommended that the company enter into a custodial agreement that will meet the NAIC Provisions and Safeguards with TD bank as custodian.

## **SIGNIFICANT SUBSEQUENT EVENTS**

Richard G. Van Noy, a member of the Board of Directors and various committees died in the summer of 2009. Presently, he has not been replaced on the Board of Directors.

Queenstown Holding Company was liquidated on December 31, 2009. As a result, the Company is now directly owned by the Mercer Insurance Company.



