

REPORT ON EXAMINATION

OF THE

COMMERCIAL MUTUAL INSURANCE COMPANY

AS OF

DECEMBER 31, 2006

DATE OF REPORT

JANUARY 28, 2008

EXAMINER

WAYNE LONGMORE

TABLE OF CONTENTS

<u>ITEM NO.</u>		<u>PAGE NO.</u>
1.	Scope of Examination	4
2.	Description of Company	4
	A. Management	7
	B. Territory and plan of operation	10
	C. Reinsurance	11
	D. Holding company system	14
	E. Significant operating ratios	16
	F. Loans to Officers	17
	G. Accounts and records	17
3.	Financial Statements	25
	A. Balance sheet	25
	B. Underwriting and investment exhibit	27
4.	Other amounts receivable under reinsurance contracts	28
5.	Net Deferred Tax Asset	29
6.	Losses and loss adjustment expenses	30
7.	Market conduct activities	31
8.	Compliance with prior report on examination	33
9.	Summary of comments and recommendations	37



STATE OF NEW YORK
INSURANCE DEPARTMENT
ONE COMMERCE PLAZA
ALBANY, NEW YORK 12257

January 28, 2008

Honorable Eric R. Dinallo
Superintendent of Insurance
Albany, New York 12257

Sir:

Pursuant to the requirements of the New York Insurance Law, and in compliance with the instructions contained in Appointment Number 22617 dated March 9, 2007, attached hereto, I have made an examination into the condition and affairs of Commercial Mutual Insurance Company as of December 31, 2006, and submit the following report thereon.

Wherever the designations "the Company" or "CMIC" appear herein without qualification, they should be understood to indicate Commercial Mutual Insurance Company.

Wherever the term "Department" appears herein without qualification, it should be understood to mean the New York Insurance Department.

The examination was conducted at the Company's home offices located at 15 Joys Lane, Kingston, New York, 12401.

1. SCOPE OF EXAMINATION

The previous examination was conducted as of December 31, 2001. This examination covered the five-year period from January 1, 2002 through December 31, 2006. Transactions occurring subsequent to this period were reviewed where deemed appropriate by the examiner.

The examination comprised a verification of assets and liabilities as of December 31, 2006. The examination included a review of income, disbursements and company records deemed necessary to accomplish such analysis or verification and utilized, to the extent considered appropriate, work performed by the Company's independent certified public accountants. A review or audit was also made of the following items as called for in the Examiners Handbook of the National Association of Insurance Commissioners:

- History of Company
- Management and control
- Corporate records
- Fidelity bond and other insurance
- Territory and plan of operation
- Growth of Company
- Business in force by states
- Loss experience
- Reinsurance
- Accounts and records
- Financial statements

A review was also made to ascertain what action was taken by the Company with regard to comments and recommendations contained in the prior report on examination.

This report on examination is confined to financial statements and comments on those matters, which involve departures from laws, regulations or rules, or which are deemed to require explanation or description.

2. DESCRIPTION OF COMPANY

The Company was incorporated under the laws of New York as The Co-operative Fire Insurance Company of Greene, Schoharie and Delaware Counties on April 12, 1886. The Company was organized for the purpose of transacting business as a co-operative fire insurance company in said counties.

In November 1922, a certificate was issued by the Insurance Department authorizing the Company to change its name to The Co-operative Fire Insurance Company of Catskill, New York. Subsequently, the Company's charter was amended permitting it to extend its territory to include the entire State of New York and, wherever authorized by law, any other state of the United States of America and the District of Columbia.

On June 1, 1935, the Company assumed all of the assets and liabilities of the Commercial Mutual Fire Insurance Company of Greene County pursuant to a reinsurance agreement approved by the Insurance Department.

Under the terms of a reinsurance and assumption agreement approved by the Insurance Department in July 1956, with three other advance premium companies participating equally, the entire in-force business of the Oneida Co-operative Fire Insurance Association, Rome, New York was ceded over. The corporate existence of the latter company was terminated and subsequent to an Order of Liquidation and Distribution signed December 8, 1959, the Insurance Department approved distribution of the balance in the Oneida bank account to the four participating companies in March 1960.

The Company filed with the Superintendent of Insurance, a Certificate of Amendment of Charter, as amended, in compliance with Section 1206 of the New York Insurance Law. Such certificate amends the Company's charter and license to reflect the name change from The Co-operative Fire Insurance Company of Catskill, New York to Commercial Mutual Insurance Company. This amendment was approved by the Insurance Department on April 20, 1976.

Under the terms of the Articles of Agreement dated and adopted July 1, 1976 the Company participated on a 1/3 share basis in non-assessable combination policies issued under the name of New York Mutual Underwriters. The participating companies assume equal proportions of liability arising out of any combination policies issued and share equally all expenses and premiums in connection with said combination policies. Effective October 31, 1997, Commercial Mutual Insurance Company withdrew its membership in that facility, however, the Company is still running off its' participation.

Commercial Mutual Insurance Company was deemed by this Department to have become a controlled insurer of the Robert Plan Corporation ("RPC") on April 1, 1998 when Eagle Insurance Company ("Eagle", a wholly owned subsidiary of the RPC) obtained controlling interest of the Company by investing \$3 million in the Company in the form of a surplus note carrying an interest rate of the lesser

of: (a) 8.5% per annum (b) the prime rate charged by Citibank, N.A. (c) the rate permitted pursuant to the provisions of Section 5-501 of the General Obligations Law of the State of New York. On March 12, 1999, Eagle purchased another surplus note in the amount of \$750,000 with similar interest and terms.

On January 31, 2006 the aforementioned Section 1307 surplus notes in the amount of \$3,750,000 were transferred from Eagle to DCAP Group, Inc.

The beneficial owners of DCAP Group, Inc. based upon the review of Securities and Exchange Commission Form 10KSB filing dated 3/29/07 were as follows:

<u>Name and Address of Beneficial Owner</u>	<u>Number of Shares Beneficially Owned</u>	<u>Approximate Percent of Class</u>
Barry B. Goldstein 1158 Broadway Hewlett, New York	393,400	13.3%
AIA Acquisition Corp 6787 Market Street Upper Darby, Pennsylvania	361,600	11.1%
Eagle Insurance Company [c/o The Robert Plan Corporation 999 Stewart Avenue Bethpage, New York]	297,378	10.0%
Jack D. Seibald 1336 Boxwood Drive West Hewlett Harbor, New York	274,750	9.2%
Infinity Capital Partners, L.P. 767 Third Avenue, 16th Floor New York, New York	292,597	9.9%
Jay M. Haft 69 Beaver Dam Road Salisbury, Connecticut	182,278	6.1%
Morton L. Certilman 90 Merrick Avenue East Meadow, New York	170,248	5.8%
David A. Lyons 252 Brookdale Road Stamford, Connecticut	20,000	Less than 1%

<u>Name and Address of Beneficial Owner</u>	<u>Number of Shares Beneficially Owned</u>	<u>Approximate Percent of Class</u>
All executive officers and directors as a group (5 persons)	1,040,676	34.5%

The Insurance Department had considered RPC to be in control of CMIC through its majority representation on the Board of Directors of CMIC, the interlocking of officers between the RPC affiliates and CMIC, the service agreements between the RPC affiliates and CMIC, the reinsurance agreements between the RPC affiliates and CMIC and the surplus notes of CMIC owned by Eagle, a wholly owned subsidiary of RPC. On April 4, 2006, an application pursuant to Section 1501(c) of the New York Insurance Law for a determination that CMIC is no longer a controlled insurer was submitted to this Department based on the following: 1) all of the CMIC directors employed by RPC had resigned from the Board of Directors of CMIC, 2) only one CMIC officer/director was still employed part-time by RPC, 3) some of the service agreements between the RPC affiliates and CMIC had been terminated, 4) the reinsurance agreements between the RPC affiliates and CMIC had been terminated and 5) all of the CMIC Surplus notes owned by Eagle were purchased by the DCAP Group, Inc.

After considering the information presented by the Company in the application, on May 4, 2006 the Department determined that CMIC was no longer a controlled insurer and no longer subject to Article 15 of the Insurance Law.

A. Management

Pursuant to the Company's by-laws, as amended, management of the Company is vested in a board of directors consisting of not less than eleven nor more than thirteen members. As of the examination date, the board of directors was comprised of eleven members. Each of the director's qualifications, as set forth in Article II, Section I of the by-laws was reviewed and it appears that each Director was duly qualified.

At least four board meetings were held in each of the years during the period under examination, thereby complying with Section 6624(b) of the New York Insurance Law.

The Company reported that the directors as of December 31, 2006, were as follows:

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Barry B. Goldstein Hewlett Harbor, NY	Chairman of the Board, Commercial Mutual Insurance Company President and CEO of the DCAP Group, Inc.
Karl J. Houseknecht Kingston, NY	Treasurer and Chief Financial Officer, Commercial Mutual Insurance Company
Dwight S. Landberg Huntington Station, NY	Director of Marketing, Commercial Mutual Insurance Company
John D. Reiersen Port Jefferson, NY	President and Chief Executive Officer, Commercial Mutual Insurance Company
Jeffrey C. Schwartz Brooklyn, NY	Vice President, Payments Inc. (premium finance company wholly owned by the DCAP Group, Inc.)
Jack D. Seibald Hewlett, NY	Managing Director, Sanders Morris Harris Managing Member of Whitehead Advisors Member of the Board of Directors of DCAP Group, Inc.
Steven Shapiro Dix Hills, NY	Sales/management, Sandlar, Inc. (real estate business)
David C. Smith East Greenbush, NY	Retired
Floyd R. Tupper, CPA New York, NY	Certified Public Accountant Private Practice
Sally A. Udalovas Eatons Neck, NY	Retired
Samuel Yedid Hewlett Harbor, NY	Attorney Lazer, Aptheker, Rosella and Yedid

A review of the minutes of the board of directors' meetings held during the examination period indicated that the meetings were generally well attended with the exception of Robert M. Wallach who attended less than 50% of the meetings for which he was eligible to attend. Mr. Wallach served as Chairman of CMIC's board of directors and resigned as a member of the board effective January 31, 2006.

By-law Compliance

Article III - Officers - Section 1 of the Company's by-laws states that the officers shall be a President, a Secretary, and a Treasurer to be chosen by the Board of Directors from among its members at the annual meeting for a term of one year. Review of the Annual Meeting minutes indicated that this requirement was not complied with for 2006. It is recommended that the Company complies with the requirements of Article III, Section 1 of its by-laws henceforth and ensure that the position of President, Secretary, and Treasurer are chosen by the Board of Directors from among its members at the annual meeting for a term of one year. The performance of this act should be clearly documented in the relevant Board of Directors meeting minutes.

Article III - Officers- Section 2 of the Company's by-laws states that the compensation of officers shall be fixed by the Board of Directors. For the period under examination: 2002 through 2006; no approval or review of officers' salaries was apparent during the examination of the minutes of the board of directors meetings for the corresponding timeframe. The only exception noted was the approval in 2006 of Company President John Reiersen's Employment Contract. It is recommended that the Company complies with the requirements of Article III, Section 2 of its by-laws henceforth and ensure that the compensation of all officers is fixed by the Board of Directors.

As of December 31, 2006, the principal officers of the Company were as follows:

<u>Name</u>	<u>Title</u>
Barry B. Goldstein	Chairman of the Board
John D. Reiersen	President and Chief Executive Officer
Karl J. Houseknecht	Chief Financial Officer and Treasurer
William J. Muller	Vice President- Claims
Marilyn B. More	Secretary

Conflict of Interest Statements

The previous report on examination included a recommendation that the Company exercise due care in obtaining and maintaining signed conflict of interest statements from its board of directors, officers and employees.

The Company has in place a procedure to distribute conflict of interest questionnaires to its board of directors and executive officers annually. Based upon the review of signed conflict of interest

statements for the period under examination: 2002 through 2006, directors and officers were noted to be completing conflict of interest statements for each of the years 2002, 2003 and 2004. However, no signed conflict of interest statements, consistent with the Company's existing procedure, were generated for directors and officers in the years 2005 and 2006.

It is again recommended that the Company exercise due care in obtaining and maintaining signed conflict of interest questionnaires from its board of directors, officers and key employees.

B. Territory and Plan of Operation

As of December 31, 2006, the Company was licensed to write business in New York State only and was authorized to transact the kinds of insurance as defined in the following numbered paragraphs of Section 1113(a) of the New York Insurance Law:

<u>Paragraph</u>	<u>Line of Business</u>
4	Fire
5	Miscellaneous property
6	Water damage
7	Burglary and theft
8	Glass
12	Collision
13	Personal injury liability
14	Property damage liability
19	Motor vehicle and aircraft physical damage
20	Marine and inland marine (inland only)

Commercial Mutual Insurance Company writes primarily commercial auto liability, auto physical damage and homeowners risks in New York State. CMIC introduced private passenger physical damage coverage in 2003 and in 2004 started a Black Car program (physical damage only coverage for livery vehicles). In 2005 the Company also commenced writing both Yellow Car (physical damage only coverage on Yellow Medallion Cars) and Silver Car (physical damage only coverage for livery vehicles over 4 years old). During 2006, CMIC added a 3-4 family package policy to the existing product line. Business is written through more than 400 independent agents and brokers.

The following schedule shows the direct premiums written by the Company both in total and in New York for the period under examination:

<u>Calendar Year</u>	<u>Direct Premiums Written (000's)</u>
2002	\$11,903
2003	\$11,419
2004	\$14,858
2005	\$17,634
2006	\$20,645

Based upon the lines of business for which the Company is licensed, and pursuant to the requirements of Articles 13, 41 and 66 of the New York Insurance Law, as of December 31, 2006, the Company is required to maintain a minimum surplus to policyholders in the amount of \$650,000.

C. Reinsurance

Assumed reinsurance accounted for less than 1% of the Company's gross premium written at December 31, 2006. Since the last examination, and throughout the period covered by this examination, the Company's assumed reinsurance business has remained stable. The assumed reinsurance as of the examination date represents business obtained through mandatory pool participation in the New York Special Risk Distribution Program.

The Company utilizes reinsurance accounting as defined in the National Association of Insurance Commissioners ("NAIC") Accounting Practices & Procedures Manual Statement of Statutory Accounting Principles ("SSAP") No. 62 for all of its assumed reinsurance business.

The Company has structured its ceded reinsurance program to limit its maximum exposure to any one risk as follows:

Homeowners Dwelling Fire

For the period July 1, 2006 through June 30, 2007 all business is covered by three treaties designed to cap CMIC's per occurrence limit at \$175,000. The treaties are as follows:

- 75% quota share of the Company's net liability;
- 25% of \$800,000 in excess of \$700,000 as respects any one risk, each loss; and
- Catastrophe coverage of \$3,165,750 per occurrence in excess of \$500,000.

Motor Vehicle Physical Damage Insurance

For the period January 1, 2006 through December 31, 2006 a 60% quota share treaty covers the Black and Yellow Car Programs.

Commercial Auto Insurance

For the period January 1, 2006 through December 31, 2006 commercial auto business is covered by two treaties in order to cap CMIC's per occurrence limit at \$150,000. The treaties are as follows:

- 60% quota share of the Company's net liability; and
- Excess of loss treaty providing \$375,000 ultimate net loss in excess of \$375,000 each occurrence.

As of the examination date the Company ceded the majority of its business to authorized reinsurers.

It is the Company's policy to obtain the appropriate collateral for its cessions to unauthorized reinsurers. The Letter of Credit obtained by the Company to take credit for cessions to unauthorized reinsurers was reviewed for compliance with Department Regulations 133. No exceptions were noted.

All ceded reinsurance agreements in effect as of the examination date were reviewed and found to contain the required clauses, including an insolvency clause meeting the requirements of Section 1308 of the New York Insurance Law.

Examination review of the Schedule F data reported by the Company in its filed Annual Statement was found to accurately reflect its reinsurance transactions with the following exception. Review of the 2006 filed Annual Statement Schedule F- Part 3 indicated that in some instances the reinsurers named by the Company did not correspond to the reinsurer identified by the NAIC assigned Company Code. It is recommended that the Company comply with the Annual Statement Instructions when completing Schedule F Part 3 and show the correct name and NAIC Company Code numbers for its reinsurers.

Additionally, management has represented that all material ceded reinsurance agreements transfer both underwriting and timing risk as set forth in SSAP No. 62. On examination, the Company could not provide sufficient analytic documentation to substantiate that the transfer of risk analysis on its ceded

reinsurance contracts was performed prior or subsequent to entering into those contracts. Representations were made by an attestation from the Company's Chief Executive and Chief Financial officers that all of these contracts contained "self-evident risk transfer." Additionally, examination review indicated that the Company's ceded reinsurance contracts did not contain clauses indicating that they were a party to finite reinsurance agreements. All ceded reinsurance agreements were accounted for utilizing reinsurance accounting as set forth in paragraphs 42 to 46 of SSAP No. 62.

It is recommended that the Company obtain and retain documentation of the risk transfer analyses performed in accordance with SSAP No. 62 paragraphs 14 and 15 on each of its reinsurance contracts. Such analysis should be kept in the respective reinsurance underwriting file.

During the period covered by this examination, the Company commuted various ceded reinsurance agreements, resulting in surplus gains on commutations in the amount of \$127,658 as follows:

<u>Company</u> <u>(year)</u>	<u>CASE LOSS</u> <u>AND LAE</u> <u>RESERVES</u> <u>COMMUTED</u>	<u>IBNR LOSS</u> <u>AND LAE</u> <u>RESERVES</u> <u>COMMUTED</u>	<u>RETURN</u> <u>OF CEDED</u> <u>UNEARNED</u> <u>PREMIUM</u>	<u>CONTINGENT</u> <u>COMMISSION</u> <u>RECEIVED</u> <u>(ALREADY</u> <u>ACCRUED</u> <u>PRIOR TO</u> <u>COMMUTATION)</u>	<u>CEDED</u> <u>PAID</u> <u>LOSSES</u> <u>AND/OR</u> <u>LAE DUE</u> <u>CMIC</u>	<u>TOTAL</u> <u>AMOUNT</u> <u>RECEIVED</u>	<u>GAIN OR LOSS</u> <u>ON</u> <u>COMMUTATION</u>
Vesta Fire Insurance Corporation (2004)	17,100	-		8,213	4,172	29,485	(0)
Eagle Insurance Company (2005)	156,091	78,045		-	-	234,136	0
Alea North America Insurance Company (2006)	616,073	426,942	142,608	511,719	(58,795)	1,766,205	127,658
Total	789,264	504,987	142,608	519,932	(54,623)	2,029,826	127,658

D. Holding Company System

As previously mentioned in the “Description of the Company” section of this report, after considering the information presented by CMIC in their application dated April 4, 2006, the Department determined, on May 4, 2006, that CMIC is no longer a controlled insurer and no longer subject to Article 15 of the Insurance Law.

CMIC Subsidiaries

The Company has two subsidiaries in its holding company system at December 31, 2006. A description of the system is as follows:

CMIC Properties, Inc. (“CPI”)

CMIC Properties, Inc. (“CPI”) was organized in 2003 and is a wholly owned subsidiary of Commercial Mutual Insurance Company. CPI was organized for the purpose of managing the Company’s interest in 15 Joys Lane, LLC and to reap the benefits of the Empire Zone Tax credit. 15 Joys Lane, LLC is the owner of the Company’s Office building located at 15 Joys Lane, Kingston, New York and was organized in 2003 through an Operating Agreement made effective February 21, 2003 by, between and among Commercial Mutual Insurance Company, Peter T. Demetriou, Joseph J. Deegan and Robert J. Ryan. The initial funding of 15 Joys Lane LLC was derived from \$350,000 in capital contributions from the members as follows:

<u>Member</u>	<u>Contribution Amount</u>	<u>Percentage</u>
Commercial Mutual Insurance Company	\$175,000	50%
Peter T. Demetriou	70,000	20%
Joseph J. Deegan	35,000	10%
Robert J. Ryan	<u>70,000</u>	<u>20%</u>
Total	<u>\$350,000</u>	<u>100%</u>

The initial funding of CPI was CMIC’s purchase of 100 shares of no-par value common stock in exchange for CMIC’s 50% ownership in 15 Joys Lane LLC. In 2006 the Company subsequently purchased through CPI, for \$171,525, an additional 20% share of 15 Joys Lane, LLC from the Estate of Peter Demetriou.

The Company is noted to be reporting a book value of its subsidiary CPI at a cost of \$346,525, which represents a per share value of \$3,465.25 for 100 shares. Unrealized gains from the operation of the entity are being reported as part of the asset 'Investment income due and accrued'.

It is noted that since inception, no independent certified public accountant report has been issued for the CPI subsidiary. However, during the annual audit of the Company, the certified public accountant did review of the Company's valuation of the entity.

Correspondence dated February 6, 2004 from the Department directed the Company to file with the New York State Insurance Department, within 30 days after the organization of the CPI subsidiary, the relevant information identifying the basis of valuation used in accordance with section 78.3 of Department Regulation 59. During the current examination Company management indicated in correspondence dated May 29, 2007 that such a filing was not made. The Company did, however, provide on examination a letter dated July 17, 2007 wherein it was indicated that CPI has consistently been valued on the basis of the actual investment in CPI with the undistributed increase in the net worth of CPI being reflected in CMIC's Annual Statement as dividends due and accrued. This basis is not one of those identified in section 78.3 of Department Regulation 59. The Company subsequently advised this Department via a letter dated December 19, 2007 that CPI will be valued at the net worth of CPI determined in accordance with generally accepted accounting principles, as detailed in section 78.3(b)(1) of Department Regulation 59.

A review of the meeting minutes of the board of directors of CPI revealed that the directors met for the first time on December 22, 2004 and the first dividend payment, to CMIC, was only approved on April 28, 2005 yet CMIC reflected as dividends due and accrued amounts prior to that date. As of December 31, 2006, dividends due and accrued reflected on CMIC's Annual Statement as 'Investment income due and accrued', and reflected on CPI's books as Dividends declared and unpaid amounted to \$112,553. It is noted that although the CMIC Properties, Inc. board of directors did make blanket approvals of the declaration of dividends at each quarter end in the amount of CPI's share of the profit from 15 Joys Lane LLC (meeting dates April 28, 2005, December 13, 2005, and December 27, 2006), payment of such dividends required further approval of the board of directors. Despite the dividends being declared, there was no specified payment date, plus the actual payment of the dividend by CPI to CMIC required further approval by CPI's board of directors. Therefore, these dividends do not appear to be legally due to CMIC and should not be reflected by CMIC as 'Investment income due and accrued'.

Instead, they appear to represent an increase in the retained earnings or net worth of CMIC's investment in CPI and should be properly accounted for as such.

It is recommended that the Company complies with Department Regulation 59 henceforth.

Since the Company did not comply with the 30 day directive from the Department included in the February 6, 2004 correspondence, relative to the reporting of a valuation base, it is recommended that the Company complies fully with all future Department directives unless there exists a valid reason for not doing so.

Department Regulation 53 requires the reporting of all transactions entered into during the next preceding calendar year by the Company with any of its subsidiaries. Company Management was asked for supporting documentation of Commercial Mutual Insurance Company's compliance with the reporting requirements outlined in section 81-1.2 of Regulation 53. Note particularly the filings required on or before March 1st of each year. Based upon the correspondence from the Company's President dated May 17, 2007, this requirement was not complied with.

It is recommended that the Company complies with the filing requirements of section 81-1.2 of Department Regulation 53 as it pertains to its current subsidiary, CMIC Properties Inc., as well as any future subsidiaries formed.

Comutual Services, LLC. ("Comutual")

In letter dated November 28, 2006, the Department did not take exception to CMIC's organization of the entity known as Comutual Services, LLC. Comutual was organized to conduct business as an insurance broker for CMIC producers to place business with licensed insurers. As of the examination date Comutual had yet to commence operations.

E. Significant Operating Ratios

The following ratios have been computed as of December 31, 2006, based upon the results of this examination:

Net premiums written to surplus as regards policyholders	154.52%
Liabilities to liquid assets (cash and invested assets less investments in affiliates)	85.87%
Premiums in course of collection to surplus as regards policyholders	8.26%

All of the above ratios fall within the benchmark ranges set forth in the Insurance Regulatory Information System of the National Association of Insurance Commissioners.

The underwriting ratios presented below are on an earned/incurred basis and encompass the five-year period covered by this examination:

	<u>Amounts</u>	<u>Ratios</u>
Losses and loss adjustment expenses incurred	\$11,954,638	59.54%
Other underwriting expenses incurred	7,459,260	37.15%
Net underwriting gain (loss)	<u>665,688</u>	<u>3.32%</u>
Premiums earned	<u>\$20,079,586</u>	<u>100.00%</u>

F. Loans to Officers

In April of 2004 the Company sold an automobile to an officer of CMIC. That officer paid \$6,000 for the automobile on an installment basis via payroll deductions with the final payment being made in 2006.

This type of transaction is considered a loan to an officer and is in violation of Section 1411(f)(1) of the New York Insurance Law.

In addition, since the arrangement was not approved by the board of directors this transaction is also a violation of Section 1411(a) of the New York Insurance Law.

Given the above observations, it is recommended that the Company comply with Sections 1411(a) as well as 1411(f)(1) of the New York Insurance Law, henceforth.

G. Accounts and Records

During the period covered by this examination, the examiner noted the following deficiencies in the Company's system of accounts and records:

i. Written Contract with independent CPA

The written agreement with the Company's independent certified public accountant was reviewed and was determined not to be in full compliance with the wording and requirements of Department Regulation 118, section 89.2 which states, in part:

“Every insurer subject to this Part shall retain an independent Certified Public Accountant (CPA) who agrees by written contract with such insurer to comply with the provisions of section 307(b) of the Insurance Law, this Part and the Code of Professional Conduct adopted by the American Institute of Certified Public Accountants (AICPA). Such contract must specify that:

(a) on or before May 31st, the CPA shall provide an audited financial statement of such insurer and of any subsidiary required by section 307(b)(1) of the Insurance Law together with an opinion on the financial statements of such insurer and any such subsidiary for the prior calendar year and an evaluation of the insurer's and any such subsidiary's accounting procedures and internal control systems as are necessary to the furnishing of the opinion;...”

It is recommended that the Company ensures that the written contract with its independent certified public accountant incorporates the requirements and specific wording of Department Regulation 118, henceforth.

ii. Trustco Bank Resolution

It is noted that the Trustco Bank banking resolution provided by Management during this current examination is the same one that was reviewed during the previous examination as of December 31, 2001. That resolution was noted during the previous examination to not accurately reflect the current officers authorized to act on the Company's behalf.

It is again recommended that Company Management amend its corporate resolutions with Trustco Bank in order to accurately reflect the current officers authorized to act on the Company's behalf.

iii. Custodial Agreements -- Trustco Bank and Sanders Morris Harris

As of the examination date, the Company is noted to have a brokerage account with Sanders Morris Harris as well as a custodial account with Trustco Bank. Signed affidavits received show Pershing

LLC as the custodian of the securities for the Sanders Morris Harris account. Based upon documentation provided by Company Management, the Company did not have in place a custodial agreement for assets held with Pershing LLC (custodians per affidavits received) which incorporates the requirements of Part 1- General, Section IV. J of the NAIC Financial Condition Examiners Handbook. A similar deficiency was apparent from the review of the Company's "non-discretionary" custodial account agreement at Trustco Bank.

In addition it does not appear that the Company accurately completed item 24 of the General Interrogatories included in the 2006 filed Annual Statement since neither the agreement with Trustco Bank (non-discretionary) nor Pershing LLC (Sanders Morris Harris) were held pursuant to a custodial agreement with a qualified bank or trust company in accordance with the requirements specified in Part 1- General, Section IV. J of the NAIC Financial Condition Examiners Handbook.

It is recommended that the Company complies with Insurance Department recommendations and obtain agreements for its custodial accounts that include the safeguards and controls as set forth in the NAIC Financial Condition Examiner Handbook.

It is also recommended that the Company correctly complete the Annual Statement interrogatories relative to its custodial agreements, henceforth.

iv. IDP Premium Receivable Aging

The previous report on examination, as of December 31, 2001, included a recommendation as follows:

"It is recommended that the Company comply with the guidelines pursuant to SSAP No. 6 of the NAIC Accounting Practices and Procedures Manual for determining premiums over 90 days past due."

Review during the previous examination of the asset "Agents' Balances or Uncollected Premiums" indicated that the Company's guidelines for determining premiums over 90 days past due is based on the percentage of premium outstanding at year-end. This method is not in accordance with the guidelines set forth in SSAP No. 6 of the NAIC Accounting Practices and Procedures Manual.

During the current examination period it appears that an attempt was made at aging the receivables in accordance with the requirements of SSAP No. 6, however, Company Management was unable to

generate a policy level report showing a receivable consistent with the bulk of the premium receivable balance being reported in the 2006 filed Annual Statement. Since the aging of the receivable is based on the aforementioned receivable report, the accuracy of the over 90 day non-admitted amount reported in the 2006 filed Annual Statement is questionable. Company Management has indicated that the inaccurate receivable report was a programming issue which was apparently corrected during the course of the current examination. Nonetheless, it is recommended that the Company obtains and maintains documentation sufficient to support the Annual Statement reporting of premium receivable balances as well as the aging of those balances, henceforth.

v. Advance Premium vs. Remittances and items not allocated

The Company is noted to be reporting Advance premiums in the amount of \$4,205 in the 2006 filed Annual Statement. In accordance with SSAP No. 67, paragraph 9, the \$4,205 amount was determined to be “Remittances and Items not allocated” and not “Advance premium” since the policies included in the underlying report represented for the most part premiums received in December 2006 on policies that were effective in 2006 but were not issued or the cash was not posted to the policy until 2007.

During the course of current examination, Company Management provided a system report dated September 11, 2007 entitled “cash received in one month and policy effective in another month” which shows advance premiums totaling \$146,446. That \$146,446 amount represented premiums received in December 2006 on policies effective in 2007.

SSAP No. 53 Paragraph 13 states that “advance premiums result when the policies have been processed, and the premium has been paid prior to the policy effective date. These advance premiums are reported as a liability in the statutory financial statement and not considered income until due. Such amounts are not included in written premium or the unearned premium reserve”. Given the above observations, it was determined that the Company was not correctly reporting the amounts for Advance premiums or Remittances and items not allocated in the 2006 filed Annual Statement lines. In as much as this is a classification issue no exam change was made to the financial statements.

It is recommended that the Company complies with the Annual Statement Instructions as well as SSAP No.’s 67 and 53 relative to the reporting of Remittances and items not allocated and Advance premiums, henceforth.

vi. Subrogation Partners Agreement

CMIC is noted to have a business relationship with Subrogation Partners under which the Company forwards certain claims cases for them to attempt to pursue subrogation recoveries. Subrogation Partners is compensated in the amount of 25% of any recoveries made on behalf of CMIC on the subject claim. In as much as it is a good business practice to have executed agreements for business relationships of this nature, it is recommended that the Company executes a written contract specifying the terms of its business relationship with Subrogation Partners.

vii. Prior Affiliations

The following is a summary of the observations made relative to certain intercompany agreements effective during the examination period 2002 through 2006 between CMIC and RPC (and affiliated entities):

a) CMIC and Colonial Indemnity Insurance Company (“CIIC”) Policy Administration and Servicing Agreement

On January 1, 1999, the Company originally entered into a policy administration and servicing agreement with its then affiliate CIIC, which was not objected to by the Department in letter dated October 15, 1999. Under the terms of the agreement, CIIC agreed to provide administration and services, including underwriting, for all policies written by the Company, processing applications for insurance, collecting premium balances, rating, quoting and issuing policies, developing and maintaining proper underwriting files.

In the previous report on examination, as of December 31, 2001, it was recommended that the Company amend the Policy Administration and Servicing Agreement with CIIC to include a provision for the settlement of accounts. Such provision should provide for billing periods on at least a quarterly basis, with settlement being within thirty days of the end of the billing period.

The Company is noted to have amended and restated the above agreement effective January 1, 2002 and renamed it an expense sharing agreement. Pursuant to the amended agreement the Company agreed to provide policy administration on CIIC’s run-off business as well as claims administration services for certain claims. Sections 2.3 of this new “Amended and Restated Expense Sharing

Agreement” calls for settlements to be done on a quarterly basis, however, semiannual billing settlements were observed in 2006, 2005, and 2004.

CIIC was placed in rehabilitation by the New York State Insurance Department on September 6, 2007. Nonetheless, it is recommended that the Company complies henceforth with the settlement provisions of this as well as any future intercompany agreements entered into.

It was also noted in a letter from the Company dated August 29, 2002 to the Department that certain commitments were made as follows relative to the aforementioned “Amended and Restated Expense Sharing Agreement” between CMIC and CIIC:

- I. The agreement will be amended to include the scope and authority limiting CMIC's claim settlement ability and to list what activities are included in policy administration.
- II. Company Management stated that the following would be added to the agreement: CMIC claims staff is to make an estimate of the time they spend handling CMIC and CIIC claims. The salaries and fringe benefits of these employees are billed to CIIC based on its share of their time.
- III. Management indicated that specific language relative to the provisions for the settlement of accounts to be determined in accordance with Regulation 30 (11 NYCRR 105-109) would be added to the agreement.

The Company was unable to provide a copy of the amended agreement including the provisions documented in correspondence with the Department.

It is recommended that the Company obtains and retains documentation of compliance with any and all future commitments made to the New York State Insurance Department.

In accordance with Department Regulation 152 every insurer is required to maintain records in accordance with the specific standards set forth in the regulation. It is recommended that copies of all contracts and amendments thereto be retained by Company Management in accordance with the record retention requirements of Department Regulation 152, section 243.2.

b) Expense Allocation -- CMIC and CIIC Salary allocation Time Studies

Company Management was requested to provide documentation supporting compliance during the current examination period with the following recommendations made in the previous report on examination:

- It is recommended that the Company adhere to the provisions of Department Regulation 30 regarding the allocation of expenses between insurance companies and to the major expense groups.
- It is recommended that the Company keep in clear and legible form, records of all bases of allocation. Such records should fully disclose the bases and be readily available for examination.

Based upon the review of the documentation provided by Company management the allocation to the major expense groups is based on the actual salaries paid the claims department as a percentage of total salaries adjusted in some instances for salary expense allocations made to CIIC. No formal time studies are done in support of the allocation percentages being used. In as much as the Company failed to generate studies, compliance with the prior report recommendation is not evident.

It is again recommended that the Company adhere to the provisions of Department Regulation 30 regarding the allocation of expenses between insurance companies and to the major expense groups (support for the allocation percentages needs to be obtained i.e. time studies need to be generated).

c) Claims Service Agreement (Post May 1, 1998 Claims)

On May 1, 1998, the Company entered into a claims service agreement with its then affiliated Robert Plan Company, Material Damage Adjustment Corp. ("MDA"). Such agreement was non-objected to by the Insurance Department on September 13, 1999. Under the terms of the agreement, MDA agreed to handle claims and claims legal administration for claims on losses occurring on or after May 1, 1998. MDA shall provide complete claims administration and claims legal administration services for all claims made under insurance policies issued by the Company and which are incurred on or after May 1, 1998. MDA shall bear and pay all allocated and unallocated expenses of providing such services.

Such agreements were cancelled effective December 31, 2001 with MDA still responsible for handling claims with accident dates prior to January 1, 2002. In accordance with the terms of the MDA-CMIC claims service agreement, the compensation to be earned by MDA was 13.5% of gross earned

premiums. That amount was subsequently adjusted to 10% of the Company's gross earned premiums and was not paid immediately, but pursuant to a deferral pattern contained in the agreement. Documentation provided by Company Management shows that a liability for \$548,413 was established at December 31, 2001 on the books of the Company for unpaid loss adjustment expense reserves relative to this arrangement. In 2002, that liability was reduced by amounts categorized as "claim service fees" paid to MDA by CMIC during 2002. Subsequent to 2002, the liability was further reduced by allocated loss adjustment expense payments made directly by CMIC (which apparently should have been handled by MDA directly). At December 31, 2006 the unpaid reserve was reduced to zero. The Company keeps track of payments made on the underlying claims and at December 31, 2006, \$45,691 was deemed due from MDA but not booked as a receivable since the likelihood of payment was deemed to be remote. CMIC physically took possession of all remaining open files from MDA during the summer of 2006. At September 2007, two files remained open that would have been subject to the agreement.

d) CMIC and The Robert Plan Corporation ("RPC")

Pursuant to an agreement between the Company and RPC, effective January 1, 2002, RPC made certain payments on behalf of CMIC including the compensation to the Company's President, John Reiersen, as well as employee benefits for the Company's President and its employees. RPC also provided support services to CMIC including payroll administration, human resources administration and regulatory support as needed. CMIC reimbursed RPC for such payments actually made and paid for services actually provided.

Although the agreement terminated, effective December 31, 2005, it is noted that in correspondence from the Company dated September 16, 2002 to this Department (paragraph 3) that Management indicated certain specific changes were to be made to the aforementioned expense sharing agreement between CMIC and RPC. Specifically the terms "make certain payments" and "including without limitation" would be deleted from the underlying agreement. These changes were not apparent from the documentation provided by the Company on this examination. In a letter dated August 29, 2002 Management also indicated the agreement would be amended to include the Regulation 30 provisions. The Company was unable to provide a copy of the amended agreement including the provisions documented in correspondence with the Department. Recommendations relative to compliance with record retention requirements have already been made in this report and are not being repeated.

3. FINANCIAL STATEMENTS

A. Balance Sheet

The following shows the assets, liabilities and surplus as regards policyholders as of December 31, 2006 as determined by this examination and as reported by the Company:

<u>Assets</u>	<u>Examination</u>		<u>Company</u>		Surplus Increase <u>(Decrease)</u>
	<u>Assets</u>	Assets Not <u>Admitted</u>	Net Admitted <u>Assets</u>	Net Admitted <u>Assets</u>	
Bonds	\$ 3,755,397	\$ 0	\$3,755,397	\$ 3,755,397	\$ 0
Preferred stocks	251,042	0	251,042	251,042	0
Common stocks	780,925	200	780,725	780,725	0
Cash, cash equivalents and short-term investments	3,012,372	0	3,012,372	3,012,372	0
Investment income due and accrued	146,199	0	146,199	146,199	0
Uncollected premiums and agents' balances in the course of collection	428,635	74,934	353,701	353,701	0
Deferred premiums, agents' balances and installments booked but deferred and not yet due	3,493,730	0	3,493,730	3,493,730	0
Amounts recoverable from reinsurers	451,131	0	451,131	451,131	0
Other amounts receivable under reinsurance contracts	1,531,668	255,929	1,275,739	1,531,668	(255,929)
Net deferred tax asset	469,002	46,054	422,948	469,002	(46,054)
Electronic data processing equipment and software	182,090	153,938	28,152	28,152	0
Receivables from parent, subsidiaries and affiliates	3,494	0	3,494	3,494	0
Aggregate write-ins for other than invested assets	<u>402,454</u>	<u>73,537</u>	<u>328,917</u>	<u>328,917</u>	<u>0</u>
Totals	<u>\$14,908,139</u>	<u>\$604,592</u>	<u>\$14,303,547</u>	<u>\$14,605,530</u>	<u>\$(301,983)</u>

<u>Liabilities, surplus and other funds</u>	<u>Examination</u>	<u>Company</u>	Surplus Increase <u>(Decrease)</u>
Losses and Loss adjustment expenses	\$ 4,752,336	\$4,373,336	\$ (379,000)
Commissions payable, contingent commissions and other similar charges	162,747	162,747	0
Other expenses (excluding taxes, licenses and fees)	339,069	339,069	0
Taxes, licenses and fees (excluding federal and foreign income taxes)	0	0	0
Current federal and foreign income taxes	29,896	29,896	0
Unearned premiums	3,649,224	3,649,224	0
Advance premium	4,205	4,205	0
Ceded reinsurance premiums payable (net of ceding commissions)	855,711	855,711	0
Amounts withheld or retained by company for account of others	15,303	15,303	0
Payable to parent, subsidiaries and affiliates	1,541	1,541	0
Aggregate write-ins for liabilities	<u>209,443</u>	<u>209,443</u>	<u>0</u>
Total liabilities	<u>\$10,019,475</u>	<u>\$9,640,475</u>	<u>\$(379,000)</u>
Aggregate write-ins for special surplus funds	\$728,102	\$728,102	0
Surplus notes	3,750,000	\$3,750,000	0
Unassigned funds (surplus)	<u>(194,033)</u>	<u>\$486,951</u>	<u>(680,984)</u>
Surplus as regards policyholders	<u>\$ 4,284,069</u>	<u>\$ 4,965,053</u>	<u>\$(680,984)</u>
Totals	<u>\$14,303,544</u>	<u>\$14,605,528</u>	

Note: The Internal Revenue Service did not audit the Company's federal income tax returns for the period under examination. Audits covering subsequent tax years have yet to commence. The examiner is unaware of any potential exposure of the Company to any further tax assessment and no liability has been established herein relative to such contingency.

B. Underwriting and Investment Exhibit

Surplus as regards policyholders increased \$2,550,051 during the five-year examination period January 1, 2002 through December 31, 2006, detailed as follows:

Statement of Income

Underwriting Income

Premiums earned		\$20,079,586
Deductions:		
Losses and Loss adjustment expenses incurred	\$11,954,638	
Other underwriting expenses incurred	7,459,260	
Aggregate write-ins for underwriting deductions	<u>0</u>	
Total underwriting deductions		<u>19,413,898</u>
Net underwriting gain or (loss)		\$ 665,688

Investment Income

Net investment income earned	\$1,042,092	
Net realized capital gain	<u>(36,992)</u>	
Net investment gain or (loss)		1,005,100

Other Income

Net gain or (loss) from agents' or premium balances charged off	\$ (288,848)	
Finance and service charges not included in premiums	786,520	
Aggregate write-ins for miscellaneous income	<u>115,869</u>	
Total other income		<u>613,541</u>
Net income before dividends to policyholders and before federal and foreign income taxes		\$2,284,329
Dividends to policyholders		0
Net income after dividends to policyholders but before federal and foreign income taxes		\$2,284,329
Federal and foreign income taxes incurred		<u>56,023</u>
Net Income		<u>\$2,228,306</u>

Surplus as regards policyholders per report on examination as of December 31, 2001				\$1,734,018
		<u>Gains in Surplus</u>	<u>Losses in Surplus</u>	
Net income	\$2,228,306			
Net unrealized capital gains or (losses)	68,226			
Change in net deferred income tax	422,948			
Change in nonadmitted assets			\$522,229	
Change in provision for reinsurance	602,800			
Aggregate write-ins for gains and losses in surplus	<u>0</u>		<u>250,000</u>	
Net increase (decrease) in surplus	\$3,322,280		\$772,229	<u>2,550,051</u>
Surplus as regards policyholders per report on examination as of December 31, 2006				<u>\$4,284,069</u>

4. OTHER AMOUNTS RECEIVABLE UNDER REINSURANCE CONTRACTS

The examination net admitted asset of \$1,275,739 is \$255,929 less than the \$ 1,531,668 reported by the Company in its December 31, 2006, filed Annual Statement. The reasons for the examination change are as follows:

85% Quota Share contract

The Company is reporting \$758,267 in accrued profit commission recoverable under the 85% quota share reinsurance agreement for the period July 1, 2004 -2005. Per the Company's calculation, the incurred loss ratio under this treaty blended with the 95% contract results in a "blended rate" of 37.96%. Addendum 4 to the treaty, effective July 1, 2004, states, in part that "the adjusted commission rate shall be calculated as follows and be applied to premiums earned for the period under consideration:...4. If the ratio of losses incurred to premiums earned is less than 44.50%, but not less than 35.65%, the adjusted commission rate for the period under consideration shall be 36.25%, plus 65% of the difference in percentage points between 44.50% and the actual ratio of losses incurred to premiums earned;..." The Company is noted to have calculated the adjusted rate at 42%. This results in an overstatement of the additional commission due to CMIC in the amount of \$113,749 per examination.

2006 Physical Damage Quota Share Treaty

The Company is reporting \$142,180 in accrued profit commission under the 2006 Physical Damage Quota Share Reinsurance Treaty. Addendum 3, effective January 1, 2006, deleted Contingent Commissions from this contract. In as much as the contract addendum allowing the Contingent Commission was not effective at December 31, 2006, the profit sharing accrual under this contract has been eliminated. It should be noted, however, that the addendum allowing the profit sharing was made effective subsequent to the examination date: January 1, 2007. In order to allow the receivable of \$142,180, reported by the Company as of December 31, 2006 unearned premium reserves would have to be increased by \$146,084 with a corresponding decrease in ceded balances payable of \$87,302.50. The net effect would be a decrease to surplus, of \$58,781.50.

5. **NET DEFERRED TAX ASSET ("DTA")**

The examination net admitted asset of \$422,948 is \$46,054 less than the \$469,002 reported by the Company in its December 31, 2006, filed Annual Statement. The Company is noted to be taking asset credit for ten percent of the unadjusted surplus reported on the September 2006 quarterly statement filed with this Department. Reported surplus shown by the Company in its' 2006 quarterly statement was \$4,690,022. Based upon the review of documentation provided by Company Management it appears that a deferred tax asset balance of \$1,732,384 existed as of the examination date. Applying a tax rate 34% amounts to \$589,010 in available DTA which is then subject to the admissibility test included in SSAP No. 10. Applying that test the net DTA was determined on examination to be \$422,948.

The examination review of the Company's method of calculating the DTA revealed inconsistencies when compared with the requirements of SSAP No. 10 as adopted by Part 83.4 (b) of Department Regulation 172.

It is recommended that Company Management complies with SSAP No. 10, the Annual Statement Instructions as well as Part 83.4 (b) of Regulation 172 in computing and reporting the Deferred Tax Asset, henceforth.

6. LOSSES AND LOSS ADJUSTMENT EXPENSES

The examination liability for the captioned items of \$4,752,336 is \$379,000 more than the \$4,373,336 reported by the Company in its December 31, 2006, filed annual statement. The examination change reflects an increase in loss reserves of \$37,000 and an increase in loss adjustment expenses of \$342,000.

The examination analysis of the loss and loss adjustment expense reserves was conducted in accordance with generally accepted actuarial principles and was based on statistical information contained in the Company's internal records and in its filed annual statements.

The examination review identified the following anomalies in the Company's 2006 Annual Statement Schedule P filing:

- a. For most lines, the Company fails to establish defense and cost containment ("DCC") known case reserves; and
- b. An apparent misallocation of loss adjustment expense reserves by accident year was observed in the Commercial Multiple Peril line of business. It is noted from the 2006 Schedule P, that the Company has reported a total of \$410,000 of loss reserves and 14 open claims for accident years 1997 and prior. The Company also reported \$115,000 and 2 open claims for accident years 1998 to 2006. However, the Company's booked loss adjustment expense reserves were \$12,000 for accident years 1997 and prior and \$80,000 for accident years 1998 to 2006 respectively. This observation reflects that the allocation of loss adjustment expense reserves by accident year is not in line with the amount of loss reserves and the anticipated number of claims to be closed in the future.

It is recommended that the Company establish DCC known case reserves and segregate them from the known case pure losses when filing their Schedule P data in the future.

It is recommended that the Company allocate its loss adjustment expense reserves more appropriately to each accident year when filing their Schedule P data in the future.

7. MARKET CONDUCT ACTIVITIES

In the course of this examination, a review was made of the manner in which the Company conducts its business and fulfills its contractual obligations to policyholders and claimants. The review was general in nature and is not to be construed to encompass the more precise scope of a market conduct investigation, which is the responsibility of the Market Conduct Unit of the Property Bureau of this Department.

Except as noted below, no unfair practices were encountered.

Agent or Broker Terminations

The previous report on examination included the following recommendation:

It is recommended that the Company indicate the specific reason for terminating an agent or broker as set forth in Section 218.4 of Department Regulation 90.

The Examiner reviewed the termination letters issued by the Company in 2006 and noted that the Company is using the generalized statements "low volume" and "poor loss ratio" as reasons included in termination letters sent an agent or broker. It should be noted that Management has provided a copy of a producer termination letter issued in 2007 and that letter was more specific in the reason for the contract termination. It was also observed that the redlining notice in use at the Company needs to be updated to reflect the revised State Insurance Department address and to show the web address.

It is again recommended that the Company complies fully with Section 218.4 of Department Regulation 90 and indicate in the termination letters sent to agents and brokers the specific reason(s) for terminating the agreement and not use generalized states like "low volume" or "poor loss ratio."

It is recommended that the Company complies fully with Section 218.5 of Department Regulation 90 and update the redlining notice used in its producer termination letters so as to reflect the website address as well as the accurate mailing address for the State Insurance Department.

Complaint Log

The Company's complaint log was reviewed to determine if this log was in compliance with Circular Letter No. 11 (1978). This review indicates that the log did not contain the data or the structure required by Circular Letter No. 11 (1978).

On examination it was determined that the Company's complaint log did not include the following columns:

- The person in the company with whom the complainant has been dealing.
- The person within the company to whom the matter has been referred for review.
- The date of such referral.
- Bearing in mind the appropriate regulation mandating timely substantive replies, the dates of correspondence to the Insurance Department's Consumer Services Bureau.
 - A. The acknowledgment (if any).
 - C. The chronology of further contacts with this Department.
- The subject matter of the complaint.
- The results of the complaint investigation and the action taken.
- Remarks about internal remedial action taken as a result of the investigation.

It is recommended that the Company revise its complaint log to incorporate the data with the requisite column headings as required by Circular Letter No. 1978-11.

8. COMPLIANCE WITH PRIOR REPORT ON EXAMINATION

The prior report on examination contained 19 recommendations as follows (page numbers refer to the prior report):

<u>ITEM</u>	<u>PAGE NO.</u>
A. <u>Management</u>	
i. Members of the board have a fiduciary responsibility and must evince an ongoing interest in the affairs of the insurer. It is essential that board members attend meetings consistently and set forth their views on relevant matters so that appropriate policy decisions may be reached by the board. Individuals who fail to attend at least one-half of the regular meetings do not fulfill such criteria. Board members who are unable or unwilling to attend meetings consistently should resign or be replaced.	5
Although the Company did not comply with this recommendation during the examination period, the director noted to have poor attendance, Robert M. Wallach, resigned from the board effective January 31, 2006. As a result a similar recommendation will not be repeated in this report on examination.	
ii. It is recommended that the board of directors hold the requisite number of regular meetings as set forth in the Company's by-laws and pursuant to the provisions of Section 6624 (b)(1) of the New York Insurance Law.	6
The Company has complied with this recommendation.	
iii. It is recommended that the Company exercise due care in obtaining and maintaining signed conflict of interest questionnaires from its board of directors, officers and employees.	7
The Company has not complied with this recommendation. A similar recommendation will be made in this report on examination.	

B. Reinsurance

- i. It is recommended that the Company comply with the requirements of Section 1308(e)(1)(A) of the New York Insurance Law. 10

The Company has complied with this recommendation.

- ii. It is recommended that the Company comply with Section 6611(a)(1) of the New York Insurance Law and maintain complete copies of all reinsurance contracts to which it is a party. Such contracts should be readily available upon examination. 11

The Company has complied with this recommendation.

C. Holding Company System

- i. It is recommended that the Company adheres to the provisions of Sections 1505(c) and 1505(d) of the New York Insurance Law and Section 80-1.5 of Department Regulation No. 52 with respect to reporting transactions with affiliated companies. 12

The Company has complied with this recommendation.

- ii. It is recommended that going forward the Company comply with all conditional non-disapprovals of the Insurance Department. 13

The Company has complied with this recommendation.

- iii. It is recommended that the Company adhere to the provisions of the Claims Service Agreement with MDA and adjust the fees payable to MDA to actual cost on an annual basis. 15

Although the Company did not comply with this recommendation, a repeat recommendation is not being made since CMIC took back possession of the all remaining open files from MDA in 2006.

- iv. It is recommended that the Company settle these accounts in a timely manner pursuant to the provisions of such agreements. 15

Although the Company did not comply with this recommendation, a repeat recommendation is not being made since CMIC took back possession of the all remaining open files from MDA in 2006.

D. Accounts and Records

- i. It is recommended that the Company amends its corporate resolutions with the Trustco Bank to accurately reflect the current officers authorized to act on the Company's behalf. 17

The Company has not complied with this recommendation. A similar recommendation will be made in this report on examination.

- ii. It is recommended that the Company comply with the provisions of Section 1307(c) of the Insurance Law, with respect to the loan and the accrued interest being disclosed as part of the standard footnote. 18

The Company has complied with this recommendation.

- iii. It is recommended that the Company adhere to the terms of the surplus note agreements when calculating accrued interest on the outstanding principal amount. 18

The Company has complied with this recommendation.

- iv. It is recommended that the Company calculate and accumulate the special contingent surplus pursuant to the provisions of Section 4109 (b) of the New York Insurance Law. 19

The Company has complied with this recommendation.

- v. It is recommended that the Company adjust its books and records to reflect the special contingent surplus in the amount of \$503,726 as determined by this examination. 19

The Company has complied with this recommendation.

- vi. It is recommended that the Company comply with the guidelines pursuant to SSAP No. 6 of the NAIC Accounting Practices and Procedures Manual for determining premiums over 90 days past due. 20

The Company has not complied with this recommendation. A similar recommendation will be made in this report on examination.

- vii. It is recommended that the Company adhere to the provisions of Department Regulation 30 regarding the allocation of expenses between insurance Companies and to the major expense groups. 20

The Company has not complied with this recommendation. A similar recommendation will be made in this report on examination.

20

- viii. It is recommended that the Company keep in clear and legible form, records of all bases of allocation. Such records should fully disclose the bases and be readily available for examination.

The Company has not complied with this recommendation. A similar recommendation will be made in this report on examination.

E. Market Conduct Activities

- i. It is recommended that the Company indicate the specific reason for terminating an agent or broker as set forth in Section 218.4 of Department Regulation 90.

25

The Company has not complied with this recommendation. A similar recommendation will be made in this report on examination.

- ii. It is recommended that the Company institute procedures that adequately define their criteria for low volume and poor loss ratio and apply it consistently to all agents and brokers.

25

The Company has complied with this recommendation.

9. SUMMARY OF COMMENTS AND RECOMMENDATIONS

<u>ITEM</u>	<u>PAGE NO.</u>
A. <u>Management</u>	
i. It is recommended that the Company complies with the requirements of Article III, Section 1 of its by-laws henceforth and ensure that the position of President, Secretary, and Treasurer are chosen by the Board of Directors from among its members at the annual meeting for a term of one year.	9
ii. It is recommended that the Company complies with the requirements of Article III, Section 2 of its by-laws henceforth and ensure that the compensation of all officers is fixed by the Board of Directors.	9
iii. It is again recommended that the Company exercise due care in obtaining and maintaining signed conflict of interest questionnaires from its board of directors, officers and key employees.	10
B. <u>Reinsurance</u>	
i. It is recommended that the Company comply with the Annual Statement Instructions when completing Schedule F Part 3 and show the correct name and NAIC Company Code numbers for its reinsurers.	12
ii. It is recommended that the Company obtains and retains documentation of the risk transfer analyses performed in accordance with SSAP No. 62 paragraphs 14 and 15 on each of its reinsurance contracts. Such analysis should be kept in the respective reinsurance underwriting file.	13
C. <u>Holding Company</u>	
i. It is recommended that the Company complies with Department Regulation 59 henceforth.	16
ii. It is recommended that the Company complies fully with all future Department directives unless there exists a valid reason for not doing so.	16
iii. It is recommended that the Company complies with the filing requirements of section 81-1.2 of Department Regulation 53 as it	16

pertains to its current subsidiary, CMIC Properties Inc., as well as any future subsidiaries formed.

D. Loans to Officers

It is recommended that the Company comply with Sections 1411(a) as well as 1411(f)(1) of the New York Insurance Law, henceforth. 17

E. Accounts and Records

- i. It is recommended that the Company ensures that the written contract with its certified public accountant incorporates the requirements and specific wording of Department Regulation 118, henceforth. 18
- ii. It is again recommended that the Company amend its corporate resolutions with Trustco Bank in order to accurately reflect the current officers authorized to act on the Company's behalf. 18
- iii. It is recommended that the Company complies with Insurance Department recommendations and obtain agreements for its custodial accounts that include the safeguards and controls as set forth in the NAIC Financial Condition Examiner Handbook. 19
- iv. It is recommended that the Company correctly completes the Annual Statement interrogatories relative to its custodial agreements, henceforth. 19
- v. It is recommended that the Company obtains and maintains documentation sufficient to support the Annual Statement reporting of premium receivable balances as well as the aging of these balances, henceforth. 20
- vi. It is recommended that the Company complies with the Annual Statement Instructions as well as SSAP No.'s 67 and 53 relative to the reporting of Remittances and items not allocated and Advance premiums, henceforth. 20
- vii. It is recommended that the Company executes a written contract specifying the terms of its business relationship with Subrogation Partners. 21
- viii. It is recommended that the Company complies henceforth with the settlement provisions of this as well as any future intercompany agreements entered into. 22

- ix. It is recommended that the Company obtains and retains documentation of compliance with any and all future commitments made to the New York State Insurance Department. 22
 - x. It is also recommended that copies of all contracts and amendments thereto be retained by Company Management in accordance with the record retention requirements Department Regulation 152, section 243.2. 22
 - xi. It is again recommended that the Company adhere to the provisions of Department Regulation 30 regarding the allocation of expenses between insurance companies and to the major expense groups (support for the allocation percentages needs to be obtained i.e. time studies need to be generated). 23
- F. Net Deferred Tax Asset (“DTA”)
- It is recommended that the Company complies with SSAP No. 10, Annual Statement Instructions as well as Part 83.4 (b) of Regulation 172 in computing and reporting the Deferred Tax Asset, henceforth. 29
- G. Losses and Loss Adjustment Expense
- i. It is recommended that the Company establish DCC known case reserves and segregate them from the known case pure losses when filing their Schedule P data in the future. 30
 - ii. It is recommended that the Company allocate its loss adjustment expense reserves more appropriately to each accident year when filing their Schedule P data in the future. 30
- H. Market Conduct Activities
- i. It is again recommended that the Company complies fully with Section 218.4 of Department Regulation 90 and indicate in the termination letters sent to agents and brokers the specific reason(s) for terminating the agreement and not use generalized states like "low volume" or "poor loss ratio." 31
 - ii. It is recommended that the Company complies fully with Section 218.5 of Department Regulation 90 and update the redlining notice used in its producer termination letters so as to reflect the website address as well as the accurate mailing address for the State Insurance Department. 31
 - iii. It is recommended that the Company revise its complaint log to incorporate the data with the requisite column headings as required by Circular Letter No. 1978-11. 32

Respectfully submitted,

_____/S/
Wayne Longmore
Senior Insurance Examiner

STATE OF NEW YORK)
)SS:
)
COUNTY OF ALBANY)

Wayne Longmore, being duly sworn, deposes and says that the foregoing report, subscribed by him, is true to the best of his knowledge and belief.

_____/S/
Wayne Longmore

Subscribed and sworn to before me
this _____ day of _____, 2008.

Appointment No 22617

STATE OF NEW YORK
INSURANCE DEPARTMENT

I, ERIC DINALLO, Superintendent of Insurance of the State of New York,
pursuant to the provisions of the Insurance Law, do hereby appoint:

Wayne Longmore

as proper person to examine into the affairs of the

Commercial Mutual Insurance Company

and to make a report to me in writing of the condition of the said

Company

with such other information as he shall deem requisite.

In Witness Whereof, I have hereunto subscribed by the
name and affixed the official Seal of this Department, at
the City of New York,

this 9th day of March 2007



A handwritten signature in cursive script, appearing to read "Eric Dinallo", written over a horizontal line.

ERIC DINALLO

Acting Superintendent of Insurance