

REPORT ON EXAMINATION
OF THE
UTICA FIRST INSURANCE COMPANY
AS OF
DECEMBER 31, 2002

DATE OF REPORT:

NOVEMBER 19, 2003

EXAMINER:

WARREN YOUNGS

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

George E. Pataki
Governor

Howard Mills
Superintendent

November 19, 2003

Honorable Howard Mills
Superintendent of Insurance
Albany, New York 12257

Pursuant to the requirements of the New York Insurance Law, and in compliance with the instructions contained in Appointment Number 22010, dated March 7, 2003, attached hereto, I have made an examination into the condition and affairs of the Utica First Insurance Company as of December 31, 2002 and submit the following report thereon.

The examination was conducted at the Company's home office located at 5981 Airport Road, Oriskany, New York 13424.

Wherever the designations "the Company" or "UFIC" appear herein without qualification, they should be understood to indicate the Utica First Insurance Company.

1. SCOPE OF EXAMINATION

The previous examination was conducted as of December 31, 1998. This examination covered the four-year period from January 1, 1999 through December 31, 2002. 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, 2002, a review of income and disbursements deemed necessary to accomplish such 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 bonds and other insurance
- Territory and plan of operation
- Growth of Company
- Business in force by states
- Loss experience
- Reinsurance
- Accounts and records
- Financial statements
- Market conduct activities

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 organized in 1903 for the purpose of transacting business as a co-operative fire insurance corporation in Oneida County, New York.

On March 1, 1942, the Company was authorized to issue non-assessable policies.

Under Agreements of Merger approved by this Department, the Company merged with the Colonial Co-operative Fire Insurance Company, of Newburgh, New York and the Dwelling Insurance Association of Central New York, of Ilion, New York in 1941 and 1956, respectively, under the title and charter of the Utica Fire Insurance Company of Oneida County, N.Y.

Effective January 1, 1994, the Company was authorized by this Department to change its name to the "Utica First Insurance Company".

A. Management

Pursuant to the Company's charter and by-laws, management of the Company is vested in a board of directors consisting of eleven members. As of the examination date, the board of directors was comprised of ten members.

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 directors as of December 31, 2002, were as follows:

<u>Director</u>	<u>Principal Business Affiliation</u>
Frederick Edwin Bangs Barneveld, NY	Retired
Dominick Donald Carbone Boonville, NY	President and Chief Executive Officer, Don-Al Management Company, Inc.
Alan Remy Leist New Hartford, NY	Chief Executive Officer, Strategic Investment Advisors, Inc.

<u>Director</u>	<u>Principal Business Affiliation</u>
Joseph Kemper Matt Fayetteville, NY	Chairman of the board, UFIC; President, Dupli Envelope & Graphics Corporation
John Bradford Millet, Jr. Clinton, NY	President, Mohawk Metal Products Company, Inc.
Don Philip Murnane Utica, NY	General Counsel, UFIC; Partner in the law firm Rossi & Murnane
Earle Clifford Reed Utica, NY	Chief Executive Officer, ECR International, Inc.
Dwight Earle Vicks, Jr. Utica, NY	President, Vicks Lithograph & Printing Corporation
John Alan Zawadzki New Hartford, NY	President and Chief Executive Officer, SBU Bank
Richard James Zick Rome, NY	President and Chief Executive Officer, UFIC; Director and President, UFIC Agency, Inc.

At the annual meeting of members (policyholders) held March 4, 2002, the terms of four directors expired; however, only three directors were elected. Article III Section 2 of the Company's by-laws and Article VI of its Charter indicates that "At each annual meeting of members there shall be elected a sufficient number of directors to fill the places of those whose terms expire at any such annual meeting." By not electing four directors at such meeting the Company became in violation of Article III Section 2 of its by-laws, which requires that there be eleven directors, but the Company only had ten.

At the September 11, 2002 board meeting the board appointed a director to a term expiring March 2005. However, inasmuch as Article III Section 2 of the Company's by-laws and Article VI of its Charter required the policyholders to fill the expiring term, it appears that this

person was not properly elected to the board of directors. However, this person has been functioning as a director of the Company since the September 11, 2002 board meeting.

In view of the above, it is recommended that the Company take the steps necessary to ensure that it is in compliance with its charter and by-laws related to the election of directors and the number of directors. In addition, it is recommended that the Company only allow individuals that have been properly elected to function as a director.

The minutes of all of the Board of Directors' meetings and the committees thereof held during the examination period were reviewed. Such review indicated that all of the meetings were well attended. Each of the directors had a satisfactory attendance record for the board meetings held.

Each of the director's qualifications, as set forth in Article VI of the Company's charter and Article III Section 1 of its by-laws, was reviewed and it appears that each director was duly qualified.

At December 31, 2002, the officers of the Company were as follows:

Chairman of the Board	Joseph Kemper Matt
President and Chief Executive Officer	Richard James Zick
Senior Vice President	William Clarence Bowers
Vice President/Chief Financial Officer/ Treasurer	Scott Andrew Shatraw
Vice President-Director of Information Systems Operations	Richard R. Shlotzhauer
Secretary	Carol Monica Vangura
General Counsel	Don Philip Murnane

B. Territory and Plan of Operation

The Company is licensed to transact business within the States of Connecticut, New Jersey, New York, Ohio, Pennsylvania and Rhode Island.

Approximately 98.5% of the Company's 2002 direct writings were concentrated in Connecticut, New York and Pennsylvania. The following schedule compares direct premiums written during the examination period in New York State with the total direct premiums written in the United States.

<u>Calendar Year</u>	<u>DIRECT PREMIUMS WRITTEN (000s)</u>		Percentage of U.S. Premiums Written in <u>New York State</u>
	<u>New York State</u>	<u>Total United States</u>	
1999	\$33,123	\$39,687	83.5%
2000	37,532	44,598	84.2%
2001	45,534	53,217	85.6%
2002	58,284	67,901	85.8%

As of December 31, 2002, the Company 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>Kind of Insurance</u>
4	Fire
5	Miscellaneous property
6	Water Damage
7	Burglary and theft
8	Glass
9	Boiler and machinery
10	Elevator
12	Collision
13	Personal injury liability
14	Property damage liability
16	Fidelity and surety
19	Motor vehicle and aircraft physical damage
20	Marine and inland marine (inland marine only)

The Company was also licensed as of December 31, 2002, to accept and cede reinsurance as provided in Section 6606 of the Insurance Law of the State of New York.

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, 2002, the Company is required to maintain a minimum surplus to policyholders in the amount of \$1,200,000.

The review of all the Company's licenses in effect as of December 31, 2002 revealed that the Company has been licensed in other states for lines of business for which it does not have authority in its New York license, as follows: Connecticut-ocean marine; Ohio-ocean marine and workers compensation.

Section 1102(b) of the New York Insurance Law does not permit the Company to do an insurance business outside of New York unless licensed to do such business in New York. The Company is in the process of having its licenses outside this state conform to its New York license. Therefore, it is recommended that the Company complete the steps necessary to conform its licenses outside this state to its New York license.

At December 31, 2002, the Company wrote insurance through independent agents. The Company's predominate lines of business are homeowners multiple peril and commercial multiple peril, which accounted for 16.87% and 77.69%, respectively, of the Company's 2002 direct written business.

C. Reinsurance

The Company assumed a minor volume of business during the examination period, from the NAMICO Reinsurance Facility and the "FAIR" Plans of several states.

The examiner reviewed all ceded reinsurance contracts effected during the examination period that were provided. These contracts all contained the required standard clauses including insolvency clauses meeting the requirements of Section 1308 of the New York Insurance Law.

As of December 31, 2002 the Company had the following general excess of loss reinsurance program in place:

Property 3 layers	\$925,000 in excess of \$75,000 each risk, Each layer has a limit for all risks involved in one occurrence as follows: First--\$225,000; Second--\$450,000 and Third--\$1,400,000.
Casualty 4 layers	\$1,925,000 in excess of \$75,000 each occurrence.
Combination (occurrence involves the liability business and one property risk reinsured in combination)	\$75,000 in excess of \$75,000 each combination occurrence.
Property	\$1,000,000 in excess of \$1,000,000 each risk. Related to adjustment expense and/or extra contractual obligations incurred by the Company on an individual risk. Reinsurer's limit of liability, \$1,000,000 on all risks involved in one occurrence. Reinsurer's limit of liability for losses in excess of policy limits and extra contractual obligations combined arising out of occurrences taking place during each agreement year, \$2,000,000.
Casualty Clash (policies with a limit of \$1,000,000 or less)	\$1,000,000 in excess of \$1,000,000 each occurrence. Related to adjustment expense and/or loss in excess of policy limits and/or extra contractual obligations incurred by the Company on an individual policy; and/or where two or more policies are involved in the same occurrence. Reinsurer's limit of liability for losses in excess of policy limits and extra contractual obligations combined arising out of occurrences taking place during each agreement year, \$2,000,000.
Casualty Clash (Commercial multiple peril including business owners policies, with \$2,000,000 policy limits)	\$1,000,000 in excess of \$2,000,000 each occurrence. Related to adjustment expense and/or loss in excess of policy limits and/or extra contractual obligations incurred by the Company on an individual policy; and/or where two or more policies are involved in the same occurrence. Reinsurer's limit of liability for losses in excess of policy limits and extra contractual obligations combined arising out of occurrences taking place during each agreement year, \$2,000,000.
Fire	\$150,000 in excess of \$75,000 of net loss sustained by the

Company each occurrence involving two or more property risks that are less than 25 feet apart, with respect to the peril of fire. Coverage is after all other reinsurance recoveries, including catastrophe reinsurance.

Terrorism (covers loss under policies classified as property)	\$2,000,000 in excess of \$2,000,000 each loss occurrence, subject to a limit of \$4,000,000 for all loss occurrences during the term of the contract.
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As of December 31, 2002, the Company also maintained catastrophe excess of loss coverage on a per occurrence (two or more risks involved) basis:

Property 4 layers	\$25,500,000 in excess of \$1,500,000, subject to a limit of two times the reinsurers limit of liability on each separate layer during the term of the agreement as follows: First--\$3,000,000; Second--\$4,000,000; Third--\$10,000,000 and Fourth--\$34,000,000.
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One each of the first three layers only 95% of the limit is ceded with 5% retained by the Company.

The Company also had the following facultative excess of loss program in place as of December 31, 2002:

Property	\$4,000,000 in excess of \$1,000,000 each risk.
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The Company also had available, as of the examination date, an umbrella program as follows:

Quota Share	95% of the first \$1,000,000 of ultimate net loss, any one policy, any one loss.
Excess of Loss	100% of up to an additional \$4,000,000 in excess of \$1,000,000 each loss occurrence.

At December 31, 2002 the Company had reinsurance coverage of 100% of the equipment breakdown liability under the Company's policies to which the systems breakdown coverage form is attached up to a limit of \$20,000,000 for any one accident.

The Company ceded to authorized and unauthorized reinsurers during the period under examination. Bona fide letters of credit covered the unauthorized reinsurance portion of any recoveries as of December 31, 2002.

The Company's retention for property and casualty decreased from \$120,000 as of the last examination to \$75,000 as of December 31, 2002. Starting January 1, 2003 the Company's property and casualty retention increased to \$100,000.

Section 1308(e)(1)(A) of the New York Insurance Law states that "During any period of twelve consecutive months, without the superintendent's permission: no domestic insurer, except life, shall by any reinsurance agreement or agreements cede an amount of its insurance on which the total gross reinsurance premiums are more than fifty percent of the unearned premiums on the net amount of its insurance in force at the beginning of such period ..."

The Department granted approval for the Company to cede an amount in excess of the 50% limitation prescribed by Section 1308(e)(1)(A) of the New York Insurance Law, on July 16, 1982. However, the Company has failed to submit any subsequent amendments to its reinsurance contracts since November 1984, nor did it submit any additional reinsurance treaties that it became a party to subsequent to that date, for our review in accordance with Section 1308(e)(1)(A).

In view of the above, it is recommended that the Company submit its currently effective reinsurance contracts to this Department, and any subsequent amendments thereto, as well as any

new contracts it becomes a party to, for our review in accordance with Section 1308(e)(1)(A) of the New York Insurance Law.

D. Holding Company System

As of December 31, 2002, the Company had a wholly owned subsidiary, UFIC Agency, Inc. During the first half of 2003 the subsidiary was dissolved.

E. Significant Operating Ratios

The following ratios have been computed as of December 31, 2002, based upon the results of this examination:

Net premiums written in 2002 to Surplus as regards policyholders	1.70 to 1
Liabilities to liquid assets (cash and invested assets less investments in affiliates)	74.52%
Premiums in course of collection to Surplus as regards policyholders	7.02%
Surplus aid to policyholder surplus	17.52%
Investment yield	4.29%

The above ratios fall within the benchmark ranges set forth in the Insurance Regulatory Information System of the National Association of Insurance Commissioners, except for the Surplus aid to policyholder surplus ratio and the Investment yield ratio.

The benchmark range for the Surplus aid to policyholder surplus ratio is less than 15%. The benchmark range for the Investment yield ratio is over 4.5% and less than 10%. The underwriting ratios presented below are on an earned-incurred basis and encompass the four-year period covered by this examination:

	<u>Amounts</u>	<u>Ratios</u>
Losses and loss expenses incurred	\$109,187,964	77.77%
Other underwriting expenses incurred	40,647,264	28.95%
Aggregate write-ins for underwriting deductions	1,332,652	0.95%
Net underwriting gain (loss)	<u>(10,765,136)</u>	<u>(7.67)%</u>
 Premiums earned	 <u>\$140,402,744</u>	 <u>100.00%</u>

F. Abandoned Property

During the period covered by this examination, the Company filed reports with the state comptroller although not always in accordance with the requirements of the New York Abandoned Property Law. In correspondence during April 2003, Company management indicated that it would follow the requirements of the New York Abandoned Property Law in the future.

It is noted that during this examination the Company provided written procedures related to the handling of unclaimed funds.

G. Accounts and Records

i. Advance premiums

During the review of the amount reported as Agents' balances or uncollected premiums in the Company's 2002 annual statement it was found that the Company was including premiums received prior to the effective date of the contract as an offset to such asset.

Statement of Statutory Accounting Principles ("SSAP") No. 53 paragraph 13 indicates that advance premiums result when the policies have been processed, and the premium has been paid prior to the effective date. These advance premiums are reported as a liability in the statutory financial statement and not considered income until due.

The 2002 annual statement instructions require premiums received prior to the effective date of the contract to be included on Page 3 line 10 "Advance premiums" of such statement.

In correspondence dated June 20, 2003 the Company agreed to take corrective action regarding this matter.

Nevertheless, it is recommended that the Company comply with SSAP No. 53 paragraph 13 and the annual statement instructions and show premiums received prior to the effective date of the contract as a liability and not as an offset to agents' balances or uncollected premiums.

ii. Remittances and items not allocated

During the review of the amount reported as Agents' balances or uncollected premiums in the Company's 2002 annual statement it was found that the Company was including cash receipts that could not be identified for a specific purpose or, for other reasons, could not be applied to a specific account when received as an offset to such asset.

SSAP No. 67 paragraph 9 indicates that cash receipts cannot always be identified for a specific purpose or, for other reasons, applied to a specific account when received. The reporting entity shall record a liability for these cash receipts when the funds are received. These liability accounts are generally referred to as suspense accounts. Examples include:

- a. Premium payments received with the application for policies, which have not yet been issued;
- b. Premium payments in an amount different than the amount billed by the reporting entity; and
- c. Unidentified cash receipts.

The 2002 annual statement instructions require cash receipts that cannot be identified for a specific purpose or, for other reasons, cannot be applied to a specific account when received to be included on Page 3 line 15 "Remittances and items not allocated" of such statement.

In correspondence dated June 20, 2003 the Company agreed to take corrective action regarding this matter.

Nevertheless, it is recommended that the Company comply with SSAP No. 67 paragraph 9 and the annual statement instructions and show cash receipts that cannot be identified for a specific purpose or, applied to a specific account when received, under the liability caption "Remittances and items not allocated" instead of as an offset to agents' balances or uncollected premiums.

iii. CPA Contracts

The CPA contracts for the years under examination did not meet all the requirements of Department Regulation 118 and New York Insurance Law Section 307(b). After bringing such requirements to the attention of Company management, the 2002 agreement was brought into compliance. In correspondence dated May 19, 2003, the Company indicated that future agreements with its CPA firm would comply with Regulation 118 and Section 307(b) of the New York Insurance Law.

Nevertheless, it is recommended that the Company ensure that its contracts with its CPA firm covering all future audit years meet the requirements of Department Regulation 118 and Section 307(b) of the New York Insurance Law.

iv. Allocation of Expenses

This Department's Regulation No. 30 (11NYCRR105-109) sets forth the rules and methods governing the allocation of expenses among the major expense groups (loss adjustment,

other underwriting and investment). This regulation also requires insurers to maintain detailed worksheets on file, supporting percentages used in allocating expenses to the various expense groups.

Management could not provide detailed worksheets to support the allocation of each expense category to a particular expense group. Thus, there was no viable way to determine whether the Company correctly allocated expenses, as per the rules found in the regulation.

Management is directed to establish and maintain written documentation supporting the allocation of each expense category to the major expense groups as required by this Department's Regulation No. 30.

3. FINANCIAL STATEMENTS

A. Balance sheet

The following shows the assets, liabilities and surplus as regards policyholders as determined by this examination as of December 31, 2002. This statement is the same as the balance sheet filed by the Company. The figures included in these financial statements have been rounded.

<u>Assets</u>	<u>Ledger</u> <u>Assets</u>	<u>Non Admitted</u> <u>Assets</u>	<u>Net Admitted</u> <u>Assets</u>
Bonds	\$60,683,091	\$	\$60,683,091
Preferred stocks	237,500		237,500
Common stocks	2,650,203		2,650,203
Real estate	392,066		392,066
Cash on hand and on deposit	5,914,087		5,914,087
Short-term investments	7,123,290		7,123,290
Agents' balances or uncollected premiums	14,840,901	178,075	14,662,826
Reinsurance recoverables on loss and loss adjustment expense payments	724,140		724,140
Federal and foreign income tax recoverable and interest thereon	1,537,000		1,537,000
Electronic data processing equipment	202,233		202,233
Interest, dividends and real estate income due and accrued	918,606		918,606
Equities and deposits in pools and associations	637,641	1,158	636,483
Other assets non-admitted	468,643	468,643	
Key man life insurance	<u>262,353</u>	—	<u>262,353</u>
Total assets	<u>\$96,591,754</u>	<u>\$647,876</u>	<u>\$95,943,878</u>

Liabilities & Surplus

Losses and Loss adjustment expenses		\$42,843,140
Commissions payable, contingent commissions and other similar charges		901,276
Other expenses (excluding taxes, licenses and fees)		1,161,202
Taxes, licenses and fees (excluding federal and foreign income taxes)		206,243
Unearned premiums		22,006,286
Ceded reinsurance premiums payable (net of ceding commissions)		3,428,370
Amounts withheld or retained by company for account of others		918
Outstanding stale dated checks written off		108,215
Reinsurers in liquidation-amounts held		5,241
Drafts outstanding		<u>(11)</u>
 Total liabilities		 \$70,660,880
 Required surplus	\$1,200,000	
Surplus notes	7,000,000	
Unassigned funds (surplus)	<u>17,082,998</u>	
 Surplus as regards policyholders		 <u>\$25,282,998</u>
 Total liabilities and surplus as regards policyholders		 <u>\$95,943,878</u>

The Company issued a \$7,000,000 surplus note dated December 4, 2002 that was purchased by I-Preferred Term Securities I, LTD., a Cayman Island limited liability corporation. The note has a thirty-year maturity. The interest rate will be set each quarter based upon the 3-month LIBOR plus 4%; however, prior to December 4, 2007, the interest rate shall not exceed 12.50%. The terms of the surplus note were approved by the New York Insurance Department on November 27, 2002.

The surplus note is subject to the provisions of Section 1307 of the New York Insurance Law and as such the payment of principal and interest under the note requires the prior approval of the Superintendent of the New York Insurance Department. The amount of the surplus note shall not be part of the legal liabilities of the Company.

The Company paid a one-time placement fee of 3% of the face amount of the surplus note in December 2002.

The Internal Revenue Service did not audit the Company's federal income tax returns for the years under examination. Audits covering subsequent tax years have yet 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 by \$9,779,893 during the four-year examination period, January 1, 1999 to December 31, 2002, detailed as follows:

Statement of Income

Underwriting Income

Premiums earned		\$140,402,744
Losses and loss expenses incurred	\$109,187,964	
Other underwriting expenses incurred	40,647,264	
Aggregate write-ins for underwriting deductions	<u>1,332,652</u>	
Total underwriting deductions		<u>151,167,880</u>
Net underwriting gain (loss)		\$(10,765,136)

Investment Income

Net investment income earned	\$ 11,233,964	
Net realized capital gains or (losses)	<u>1,938,993</u>	
Net investment gain or (loss)		13,172,957

Other Income

Net loss from agents' or premium balances charged off	\$(789,892)	
Finance and service charges not included in premiums	1,355,762	
Aggregate write-ins for miscellaneous income	<u>150,099</u>	
Total other income		<u>715,969</u>
Net income before federal income taxes		3,123,790
Federal income taxes incurred		<u>337,000</u>
Net income (loss)		<u>\$2,786,790</u>

Capital and Surplus Account

Surplus as regards policyholders, December 31, 1998, per prior report on examination			\$15,503,105
	<u>Gains in Surplus</u>	<u>Losses in Surplus</u>	
Net income or loss	\$2,786,790	\$ 0	
Net unrealized capital gains or (losses)	0	907,965	
Change in non-admitted assets	0	422,651	
Cumulative effect of changes in accounting principles	83,600	0	
Change in net deferred income tax	1,234,000	0	
Change in surplus notes	7,000,000	0	
Aggregate write-ins	<u>6,119</u>	<u>0</u>	
Total gains and losses	<u>\$11,110,509</u>	<u>\$1,330,616</u>	
Net increase in surplus as regards policyholders			<u>9,779,893</u>
Surplus as regards policyholders, December 31, 2002 per report on examination			<u>\$25,282,998</u>

4. LOSSES AND LOSS ADJUSTMENT EXPENSES

The examination liability of \$42,843,140 is the same as the amount reported by the Company in its 2002 filed annual statement.

The Department's analysis was conducted in accordance with generally accepted actuarial principles and practices and was based on statistical information contained in the Company's internal records and in its filed annual statements. Based upon such analysis it appears that the Company's loss and loss adjustment expense reserves were not adequate as of December 31, 2002. However while the examination increase in loss and loss adjustment expense reserves was material, when combined with all other examination changes the net

amount of the change was not material enough to make an examination change for report on examination purposes.

Section 1303 of the New York Insurance Law states, in part, that “Every insurer shall ... maintain reserves in an amount estimated in the aggregate to provide for the payment of all losses or claims incurred on or prior to the date of statement, whether reported or unreported, which are unpaid as of such date and for which such insurer may be liable, and also reserves in an amount estimated to provide for the expenses of adjustment or settlement of such losses or claims.”

Therefore, it is recommended that the Company provide an adequate reserve for unpaid losses and loss adjustment expenses in all future financial statements filed with this Department in order to comply with the requirements of Section 1303 of the New York Insurance Law.

5. MARKET CONDUCT ACTIVITIES

In the course of this examination, a review was made of the manner in which the Company conducts its business practices and fulfills its contractual obligations to policyholders and claimants.

The review was general in nature and is not to be construed to encompass the generally more precise scope of a market conduct investigation.

The general review was directed at practices of the Company in the following areas:

- 1) Sales and advertising
- 2) Underwriting
- 3) Rating
- 4) Treatment of policyholders and claimants

Except as noted below, no unfair practices were encountered.

Section 3425 of the Insurance Law

During the review of cancellation notices issued by the Company it was found that the Company issued personal line mid-term cancellation notices for other than statutory reasons in violation of Section 3425(c) of the New York Insurance Law.

In correspondence dated July 24, 2003, the Company indicated that it has taken corrective action regarding this matter. Nevertheless, it is recommended that the Company comply with Section 3425(c) of the New York Insurance Law and not issue mid-term cancellations for other than statutory reasons.

Department Regulation 90

During the review of agent termination notices issued by the Company it was found that the termination notices sent to some agents contained unsupported general statements as the reason for termination. This violates Regulation 90 Part 218.4(a), which requires that all notices to agents that their contract is to be terminated shall state the specific reason or reasons for termination, which can not be an unsupported general statement. In addition, it was found that the agent termination notices issued by the Company did not contain the redlining wording required by Regulation 90 Part 218.5(b).

In correspondence dated June 2, 2003, the Company indicated that it would take corrective action regarding these matters. Nevertheless, it is recommended that the Company comply with Department Regulation 90 Parts 218.4(a) and 218.5(b) when terminating agent's contracts.

Mortgagee Clause and Department Circular Letter No. 17 (1976)

During the review of cancellations it was found that the Company failed to give mortgagees ten days advance notice that an insurance policy was being cancelled at the insured's

request in some cases. The New York Standard Mortgagee Clause, as reaffirmed by Department Circular Letter No. 17 (1976), requires that such notice be given to mortgagees before their interest in such policies is cancelled.

In correspondence dated July 28, 2003, the Company indicated that it has taken corrective action regarding this matter. Nevertheless, it is recommended that the Company comply with the provisions of the New York Standard Mortgagee Clause and Department Circular Letter No. 17 (1976).

6. COMPLIANCE WITH PRIOR REPORT ON EXAMINATION

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

<u>Item</u>	<u>Page No.</u>
A. Recommendation that the Company comply with Section 1209(f) of the Insurance Law and cease compensating its officers based upon its profitability.	8
The Company was in compliance with Section 1209(f) of the New York Insurance Law as of December 31, 2002.	
B. Recommendation that the Company comply with Section 1414(g) of the Insurance Law by filing the required SAR forms within the time frame specified in the Purposes and Procedures Manual of the NAIC Securities Valuation Office.	8

The Company was in compliance with the NAIC Securities Valuation Office rules in effect as of December 31, 2002 regarding filing SAR forms.

<u>Item</u>		<u>Page No.</u>
C.	Recommendation that the Company maintain copies of its advertisements so that compliance with Sections 1313 and 2403 of the Insurance Law can be determined. The Company has complied with this recommendation.	12
D.	Recommendation that the Company, at least quarterly, review its premium receivable accounts for credits and possibly, return premiums. The Company has complied with this recommendation.	12

7. SUMMARY OF COMMENTS AND RECOMMENDATIONS

The following is a summary of comments and recommendations made in the body of this report:

<u>Item</u>	<u>Page No.</u>
<p>A. <u>Management</u></p> <p>It is recommended that the Company take the steps necessary to ensure that it is in compliance with its charter and by-laws related to the election of directors and the number of directors. In addition, it is recommended that the Company only allow individuals that have been properly elected to function as a director.</p>	5
<p>B. <u>Territory and plan of operation</u></p> <p>It is recommended that the Company complete the steps necessary to conform its licenses outside this state to its New York license.</p>	7
<p>C. <u>Reinsurance</u></p> <p>It is recommended that the Company submit its currently effective reinsurance contracts to this Department, and any subsequent amendments thereto, as well as any new contracts it becomes a party to, for our review in accordance with Section 1308(e)(1)(A) of the New York Insurance Law.</p>	10-11

<u>Item</u>	<u>Page No.</u>
D. <u>Accounts and Records</u>	
i. <u>Advance Premiums</u>	13
<p>It is recommended that the Company comply with SSAP No. 53 paragraph 13 and the annual statement instructions and show premiums received prior to the effective date of the contract as a liability and not as an offset to agents' balances or uncollected premiums.</p>	
ii. <u>Remittances and items not allocated</u>	14
<p>It is recommended that the Company comply with SSAP No. 67 paragraph 9 and the annual statement instructions and show cash receipts that cannot be identified for a specific purpose or, applied to a specific account when received under the liability caption "Remittances and items not allocated" instead of as an offset to agents' balances or uncollected premiums.</p>	
iii. <u>CPA Contracts</u>	14
<p>It is recommended that the Company ensure that its contracts with its CPA firm covering all future audit years meet the requirements of Department Regulation 118 and Section 307(b) of the New York Insurance Law.</p>	

<u>Item</u>	<u>Page No.</u>
iv. <u>Allocation of Expenses</u>	15
<p>Management is directed to establish and maintain written documentation supporting the allocation of each expense category to the major expense groups as required by this Department's Regulation No. 30.</p>	
E. <u>Losses and loss adjustment expenses</u>	21
<p>It is recommended that the Company provide an adequate reserve for unpaid losses and loss adjustment expenses in all future financial statements filed with this Department in order to comply with the requirements of Section 1303 of the New York Insurance Law.</p>	
F. <u>Market Conduct Activities</u>	
i. It is recommended that the Company comply with Section 3425(c) of the New York Insurance Law and not issue mid-term cancellations for other than statutory reasons.	22
ii. It is recommended that the Company comply with Department Regulation 90 Parts 218.4(a) and 218.5(b) when terminating agent's contracts.	22
iii. It is recommended that the Company comply with the provisions of the New York Standard Mortgagee Clause and Department Circular Letter No. 17 (1976).	23

Appointment No 22010

STATE OF NEW YORK
INSURANCE DEPARTMENT

I, GREGORY V. SERIO, Superintendent of Insurance of the State of New York, pursuant to the provisions of the Insurance Law, do hereby appoint:

Warren Youngs

as proper person to examine into the affairs of the

Utica First 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 Albany,

this 7th day of March, 2003



A handwritten signature in black ink, appearing to read "Gregory V. Serio", written over a horizontal line.

GREGORY V. SERIO
Superintendent of Insurance