

REPORT ON EXAMINATION

OF THE

TSI INSURANCE, INC.

AS OF

DECEMBER 31, 2011

DATE OF REPORT

March 29, 2013

EXAMINER

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NEW YORK STATE
DEPARTMENT *of*
FINANCIAL SERVICES

Andrew M. Cuomo
Governor

Benjamin M. Lawsky
Superintendent

March 29, 2013

Honorable Benjamin M. Lawsky
Superintendent of Financial Services
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 30905 dated December 27, 2012, attached hereto, I have made an examination into the condition and affairs of TSI Insurance, Inc. as of December 31, 2011, and submit the following report thereon.

Wherever the designation “the Company” appears herein without qualification, it should be understood to indicate TSI Insurance, Inc. Wherever the designations “Parent” or “Town Sports” appear herein without qualification, they should be understood to refer to Town Sports International, LLC. Wherever the designation “the Ultimate Parent” appears herein without qualification, it should be understood to indicate Town Sports International Holdings, Inc.

Wherever the term “Department” appears herein without qualification, it should be understood to mean the New York State Department of Financial Services.

1. SCOPE OF EXAMINATION

The examination covers the period from January 1, 2007 through December 31, 2011, and was limited in its scope to a review or audit of only those balance sheet items considered by this Department to require analysis, verification or description, including invested assets, and losses and loss adjustment expense reserves. The examination included a review of income, disbursements and Company records deemed necessary to accomplish such analysis or verification. Additionally, a review was performed to determine whether the captive insurer was operating within its by-laws, conforming with its plan of operation, as submitted to the New York State Department of Financial Services, and was in compliance with Article 70 of the New York Insurance Law.

Comments and recommendations are limited to those items requiring financial adjustment, procedural recommendations, or instances where the Company was not conforming to the application submitted to the Department or Article 70 of the New York Insurance Law.

The report utilized work performed by the Company's independent certified public accountants and its opining actuary to the extent considered appropriate.

2. DESCRIPTION OF COMPANY

TSI Insurance, Inc. was incorporated under the laws of New York State as a pure captive insurance company on December 20, 2002, and commenced operations on December 31, 2002. The Company is a wholly-owned subsidiary of Town Sports International, LLC, a New York corporation, which is wholly-owned by Town Sports International Holding, Inc., a Delaware holding company.

A. Articles of Incorporation

The Company is organized to transact the kinds of insurance specified in Section 1113 of the New York Insurance Law, subject at all times to the limitation on the business of a captive insurance company set forth in Article 70 of the New York Insurance Law.

B. By-Laws

It appears that the Company is in compliance with its by-laws in all material respects.

C. Capital Structure

The Company initially issued 100,000 authorized shares of \$1.00 par value Common Stock to Town Sports International, LLC (the “Parent”) in exchange for \$250,000.

As of December 31, 2011, the Company’s paid in capital was \$100,000 and its surplus as regards policyholders was \$54,369,669.

D. Corporate Records

The corporate records reviewed appear to be substantially accurate and complete in all material respects.

E. Management and Control

(i) Captive Manager

Section 7003(b)(4) of the New York Insurance Law provides that no captive insurer shall do any captive insurance business in this state unless it utilizes a captive manager resident in the State of New York that is licensed as an agent or broker under the provisions of the Article 21 of the New York Insurance Law or any other person approved by the Superintendent.

The Company is managed by Aon Insurance Managers, the captive management arm of AON Risk Consultant, an insurance consultant licensed by the New York Department of Financial Services. Pursuant to the Management Agreement between the Company and Aon Insurance Managers, Aon Insurance Managers shall have the following authority and duties:

- Prepare statistical and other reports;
- Maintain the Company’s books and records;
- Prepare for the Company’s review and approval tax statements;
- Act as principal representative and communicate with regulatory authorities;
- Provide administrative assistance in the implementation of any insurance program;
- Assist in the maintenance of the Company’s bank accounts.

(ii) Board of Directors

At December 31, 2011, the board of directors was comprised of the following four members:

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Robert Giardina Edison, NJ	President & CEO, TSI Insurance, Inc
Kieran Sikso New York, NY	Vice President of Finance, TSI Insurance, Inc
Daniel G. Gallagher Upper Saddle River, NJ	CFO & Treasury & Assistant Secretary TSI Insurance, Inc
Nitin Ajmera Baldwin, NY	Vice President of Accounting, Town Sports International, LLC

Pursuant to Article III Section 1 of the Company's By-laws, a director need not be a shareholder or resident of the state of New York, provided that a minimum of two directors shall at all times be residents of the State of New York. As of December 31, 2011, two of four directors are residents of New York State. Therefore, the Company is in compliance with its by-laws and Section 7005(g) of the New York Insurance Law.

During the period covered by this examination, the board met once each year. A review of the meeting minutes during the examination period indicated that all the board meetings were generally well attended.

(iii) Officers

As of December 31, 2011, the principal officers of the Company were as follows:

<u>Name</u>	<u>Title</u>
Robert Giardina	President & CEO
Daniel G. Gallagher	Vice President & Treasurer & CFO
David Kastin	Vice President & Secretary
Kieran Sikso	Vice President & Assistant Secretary

F. Certified Public Accountant (“CPA”) and Actuarial Services

The Company was audited by the independent CPA firm Saslow, Lufkin & Buggy, LLP for the years covered by this examination. The Company’s opening actuary as of December 31, 2011 was AON Risk Consultants, Inc.

G. Growth of Company

The following schedule sets forth a summary of the Company’s significant financial information for the period covered by this examination:

<u>Year</u>	<u>Net Premiums Earned</u>	<u>Net Income</u>	<u>Assets</u>	<u>Shareholders’ Equity</u>
2007	\$12,670,500	\$19,742,743	\$42,957,394	\$42,379,802
2008	14,635,500	23,227,260	61,208,322	60,484,637
2009	16,635,500	23,796,329	46,587,059	45,458,541
2010	19,510,500	26,270,091	66,130,517	64,899,957
2011	15,150,000	19,772,212	58,480,662	54,369,669

3. FINANCIAL STATEMENTS

The financial statements of the Company have been prepared in conformity with accounting principles generally accepted in the United States of America that differ from statutory accounting practices prescribed or permitted for insurance companies by the New York State Department of Financial Services. The Company's independent accounting firm concluded that the following financial statements, present fairly, in all material respects, the financial position TSI Insurance, Inc. as of December 31, 2011.

A Balance Sheet

Assets

Cash	\$ 273,514
Investment in and advances to affiliates	<u>58,207,148</u>

Total Assets	<u>\$58,480,662</u>
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Liabilities

Losses and loss adjustment expenses	\$2,334,463
Accounts payable and accrued expenses	43,560
Other payables to the Parent	<u>1,732,970</u>

Total liabilities	\$ 4,110,993
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Capital and Surplus

Paid in capital (par value)	\$ 100,000
Contributed surplus	213,099
Surplus (accumulated earnings)	<u>54,056,570</u>

Total capital and surplus	<u>\$54,369,669</u>
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Total liabilities, capital and surplus	<u>\$58,480,662</u>
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B. Statement of Income

The Company's capital and surplus increased \$27,431,820 during the five-year period detailed as follows:

STATEMENT OF INCOME

Underwriting Income

Net premiums earned		\$ 78,602,000
Deductions:		
Net losses and net loss adjustment expense incurred	\$ 2,432,767	
Maintenance fee expenses	18,025,474	
Policy acquisition expenses	314,408	
General and administrative	<u>941,778</u>	
Total underwriting deductions		<u>21,714,427</u>
Net underwriting gain or (loss)		\$ 56,887,573

Investment Income

Royalty income	\$70,811,278	
Interest income on notes receivable	4,825,476	
Miscellaneous Income	<u>10,793</u>	
Investment income		<u>75,647,547</u>
Net income before tax		\$132,535,120
Federal income tax expenses	<u>\$19,726,485</u>	
Net income		<u>\$112,808,635</u>

C. Capital and Surplus Account

	<u>Gains in Surplus</u>	<u>Losses in Surplus</u>	
Capital and surplus as of December 31, 2006			\$26,937,849
Net income	\$112,808,635		
Adjustment to Federal income tax		\$ 72,300	
Adjustment to income on note receivable	206,185		
Dividend to Parent	<u>0</u>	<u>85,510,700</u>	
Total gains and losses in surplus	<u>\$113,014,820</u>	<u>\$85,583,000</u>	<u>27,431,820</u>
Capital and surplus as of December 31, 2011			<u>\$54,369,669</u>

4. LOSSES AND LOSS ADJUSTMENT EXPENSES

As of December 31, 2011, the Company did not record loss and loss adjustment expenses (“LAE”) on its annual statement. The Company’s CPA, Saslow Lufkin & Buggy, LLP believed that reserves for losses and loss adjustment expenses should have been established and the amount of \$2,334,463 estimated to be necessary or appropriate to settle losses incurred on occurrence-based general liability coverage. The Company’s opining actuary stated the following in its “Statement of Actuarial Opinion” based on the audited financial statement:

“In my opinion, the amounts of Loss and Loss Adjustment Expenses of \$2,334,463:

- Meet the requirements of the insurance laws of the State of New York;
- Are computed in accordance with accepted loss reserving standards and principles;
- Make a reasonable provision for all unpaid loss and loss adjustment expense obligations under the terms of its contracts and agreements, subject to the discussion of major risk factors.”

TSI Insurance, Inc. did not re-file the 2011 annual statement. However, the review of the 2012 annual statement indicated that the Company reflected the revised Losses and loss adjustment expenses of \$2,334,463 in the “Prior Year” column.

5. ARTICLE 70 COMPLIANCE

Article 70 of the New York State Insurance Law is the governing section of the law for the formation and continued operation of captive insurers in New York State. A review was performed to test the Company’s compliance with all applicable parts of Article 70 of the New York Insurance Law. No significant areas of non-compliance were found.

6. ORGANIZATIONAL STRUCTURE

TSI Insurance, Inc. is ultimately owned by New York based Town Sports International Holdings, Inc. Town Sports International Holding, Inc. is the largest owner and operator of fitness clubs in the Northeast and Mid-Atlantic regions of the United States and the third largest fitness club operator in the United States.

7. INSURANCE PROGRAM

The Company provides various underlying insurance coverage to the Ultimate Parent and its subsidiaries. During the examination period, the Company provided varying commercial coverage including the following: Property Insurance, Employment Practices Liability, Excess/Umbrella, Director & Officers Liability, Fiduciary Liability, Blanket Crime, International Liability, Pollution Liability, Sabotage and Terrorism coverages. In 2011, the Company discontinued all the coverages except for Property Coverage. The Property Policy also covers certified terrorism losses as defined under the Terrorism Risk Insurance Act of 2007 (“TRIA”). As of December 31, 2011, the Property Coverage has a limit of \$75,000,000 in excess of \$25,000,000 each occurrence with a deductible of \$25,000 per occurrence. The limit for Sabotage and Terrorism including War Risk Coverage remains \$200,000,000 each occurrence with a deductible of \$25,000 per occurrence. The General Liability policy provided coverage limit of \$500,000 per occurrence with no deductible.

8. COMPLIANCE WITH PRIOR REPORT ON EXAMINATION

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It is recommended that the Company maintain a board of directors that fulfills the residency requirements of its charter, by-laws and Section 7005(g) of the New York Insurance Law.

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The Company has complied with this recommendation.

9. SUMMARY OF COMMENTS AND RECOMMENDATIONS

There are no comments or recommendations in this report.

Respectfully submitted,

_____/s/_____
Wei Cao
Senior Insurance Examiner

STATE OF NEW YORK)
)ss:
COUNTY OF NEW YORK)

WEI CAO, being duly sworn, deposes and says that the foregoing report, subscribed by her, is true to the best of her knowledge and belief.

_____/s/_____
Wei Cao

Subscribed and sworn to before me
this _____ day of _____, 2012.

APPOINTMENT NO. 30905

NEW YORK STATE
DEPARTMENT OF FINANCIAL SERVICES

I, **BENJAMIN M. LAWSKY**, Superintendent of Financial Services of the State of New York, pursuant to the provisions of the Financial Services Law and the Insurance Law, do hereby appoint:

Wei Cao

as a proper person to examine the affairs of the

TSI INSURANCE, INC.

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

COMPANY

with such other information as he shall deem requisite.

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

this 27th day of December, 2012

BENJAMIN M. LAWSKY
Superintendent of Financial Services



By:

Jean Marie Cho
Deputy Superintendent