

REPORT ON EXAMINATION

OF THE

CAPITAL MARKETS ASSURANCE CORPORATION

AS OF

DECEMBER 31, 2003

DATE OF REPORT

SEPTEMBER 30, 2005

EXAMINER

JAMES MURPHY

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STATE OF NEW YORK
INSURANCE DEPARTMENT
25 BEAVER STREET
NEW YORK, NEW YORK 10004

September 30, 2005

Honorable Howard Mills
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 22414 dated September 22, 2005 attached hereto, I have made an examination into the condition and affairs of the Capital Markets Assurance Corporation as of December 31, 2003, and submit the following report thereon.

Wherever the designations "the Company" or "CapMac" appear herein without qualification, they should be understood to indicate the Capital Markets Assurance Corporation.

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 113 King Street, Armonk, New York 10504.

1. **SCOPE OF EXAMINATION**

The previous examination was conducted as of December 31, 1999. This examination covered the four-year period from January 1, 2000 through December 31, 2003. Transactions occurring subsequent to this period were reviewed where deemed appropriate by the examiner.

The examination comprised a complete verification of assets and liabilities as of December 31, 2003. 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 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 (NAIC):

- 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 in 1938 under the laws of New York as the Jersey Insurance Company of New York. It was established to provide the means of transferring the corporate domicile of the New Jersey Insurance Company from Jersey City, New Jersey to New York. In 1972, the Company's name was changed to Mohawk Insurance Company.

In 1973, H.F. Ahmanson & Co. acquired control of the Company and its name was changed to National American Insurance Company of New York in 1976.

On December 24, 1987, the Company was sold to CapMac Holdings Inc., a Delaware insurance holding company and a wholly-owned subsidiary of Citibank. The Company's name was changed to Capital Markets Assurance Corporation on December 29, 1987.

Effective June 25, 1992, Citibank sold CapMac Holdings Inc. to CapMac Acquisition Corp, a newly formed corporation owned by a group of investors. On June 26, 1992, CapMac Holdings Inc. was merged into CapMac Acquisition Corp. Concurrently, the latter changed its name to CapMac Holdings Inc.

On February 17, 1998, the Company became an indirect wholly-owned subsidiary of MBIA Inc., through the merger of its subsidiary, MBIA Insurance Corporation, with CapMac Holdings Inc. Currently, all outstanding shares of the Company are owned by MBIA Insurance Corporation.

Capital paid in is \$17,460,000 consisting of 5,820,000 shares of \$3 par value per share common stock. Gross paid in and contributed surplus is \$57,540,000.

A. Management

Pursuant to the Company's charter and by-laws, management of the Company is vested in a board of directors consisting of not less than thirteen nor more than twenty-one members. The board met four times during each calendar year. At December 31, 2003, the board of directors was comprised of the following fifteen members:

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Joseph W. Brown Bedford Corners, NY	Chairman and Chief Executive Officer, MBIA Insurance Corporation
W. Thacher Brown Devon, PA	Managing Director, MBIA Insurance Corporation
Neil G. Budnick New Canaan, CT	Vice Chairman and Chief Financial Officer, MBIA Insurance Corporation
John B. Caouette Pound Ridge, NY	Vice Chairman, MBIA Insurance Corporation
Clifford D. Corso Katonah, NY	Managing Director and Chief Investment Officer, MBIA Insurance Corporation
Gary C. Dunton Ridgefield, CT	President and Chief Operating Officer, MBIA Insurance Corporation
Douglas C. Hamilton Armonk, NY	Managing Director and Controller, MBIA Insurance Corporation
John S. Pizzarelli Pleasantville, NY	Managing Director and Head of Public Finance, MBIA Insurance Corporation
Joseph L. Sevely Manhasset, NY	Managing Director and Treasurer, MBIA Insurance Corporation
Kevin D. Silva Manhasset, NY	Managing Director and Chief Administrative Officer, MBIA Insurance Corporation
Richard L. Weill Mt. Kisco, NY	Vice Chairman and Secretary, MBIA Insurance Corporation
Ram D. Wertheim Westport, CT	Managing Director, General Counsel and Assistant Secretary, MBIA Insurance Corporation
Ruth M. Whaley Scarsdale, NY	Managing Director and Chief Risk Officer, MBIA Insurance Corporation

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Robert T. Wheeler Waccabuc, NY	Managing Director and Chief Technology Officer, MBIA Insurance Corporation
Mark S. Zucker Westport, CT	Managing Director and Head of Structured Finance, MBIA Insurance Corporation

A review of the minutes of the board of directors' meetings held during the examination period indicated that the meetings were generally well attended and each board member has an acceptable record of attendance.

As of December 31, 2003, the principal officers of the Company were as follows:

<u>Name</u>	<u>Title</u>
Joseph W. Brown	Chairman and Chief Executive Officer
Gary C. Dunton	President and Chief Operating Officer
Richard L. Weill	Vice Chairman and Secretary
John B. Caouette	Vice Chairman
Neil G. Budnick	Vice Chairman and Chief Financial Officer
Joseph L. Sevely	Managing Director and Treasurer
Ram D. Wertheim	Managing Director, General Counsel and Assistant Secretary
Douglas C. Hamilton	Managing Director and Controller

B. Territory and Plan of Operation

As of December 31, 2003, the Company was licensed to write business in all fifty states, the District of Columbia, Guam and Puerto Rico.

As of the examination date, 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>Line of Business</u>
16(C,D,E,F)	Fidelity and surety
25	Financial guaranty

Based on the lines of business for which the Company is licensed and the Company's current capital structure, and pursuant to the requirements of Article 13 and 41 of the New York Insurance Law, the Company is required to maintain a minimum surplus to policyholders in the amount of \$66,400,000.

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

DIRECT PREMIUMS WRITTEN

<u>Calendar Year</u>	<u>New York State</u>	<u>Total United States</u>	<u>Premiums Written in New York State as a Percentage of United States Premium</u>
2000	\$21,320,594	\$28,400,926	75.07%
2001	\$16,944,335	\$21,167,174	80.05%
2002	\$11,285,070	\$13,427,354	84.05%
2003	\$10,293,129	\$11,849,346	86.87%

The Company is not currently writing any new business. All business written in 2003 is renewal business.

C. Reinsurance

Assumed

The Company assumes a relatively minor volume of business from both affiliated and unaffiliated companies as compared to its direct writings.

Ceded

The Company's policies outstanding as of December 31, 2003 were 25.4% reinsured through a few specialized treaties but primarily facultative agreements of which 49% were authorized and 51% were unauthorized.

Effective April 1, 1998, the Company and MBIA Insurance Corporation entered into a reinsurance agreement under which MBIA Insurance Corporation agreed to reinsure 100% of CapMac's net portfolio exposure and its related contingency reserves and unearned premium liability.

The Schedule F data as contained in the Company's filed annual statement was found to accurately reflect its reinsurance transactions.

The examiner reviewed all ceded reinsurance contracts in effect at December 31, 2003. The contracts all contained the required standard clauses including insolvency clauses meeting the requirements of Section 1308 of the New York Insurance Law.

Unauthorized Reinsurance

The trust agreements and letters of credit obtained by the Company in order to take credit for cessions made to unauthorized reinsurers were reviewed for compliance with Department Regulations 114 and 133, respectively.

D. Holding Company System

A review of the holding company registration statements filed with this Department indicated that such filings were complete and were filed in a timely manner pursuant to Article 15 of the New York Insurance Law and Department Regulation 52.

The Company is a wholly-owned subsidiary of MBIA Insurance Corporation. The chart of the holding company system at December 31, 2003, is attached to this report as Exhibit A.

At December 31, 2003, the Company was party to the following agreements with other members of its holding company system:

Tax Allocation Agreement

The Company participates in a tax allocation agreement with its parent company and members of its holding company group. A formal agreement was executed and submitted to the Department, pursuant to Department Circular Letter No. 33 (1979). The agreement was effective January 1, 1987, and was amended numerous times to add various participants and to change various terms and conditions.

Management Agreement between CapMac and MBIA Insurance Corporation

The Company entered into a management agreement with MBIA Corp. effective January 31, 2000. Pursuant to the terms of the agreement, MBIA Insurance Corporation provides all administrative, production, accounting and claim services on behalf of CapMac. The agreement was submitted to the Department pursuant to Section 1505 of the New York Insurance Law.

Reinsurance Agreement with MBIA Insurance Corporation

Effective April 1, 1998, the Company entered into a reinsurance agreement with MBIA Insurance Corporation. Pursuant to the terms of the agreement, MBIA Insurance Corporation assumed 100% of the Company's net insured exposure as well as its unearned premiums and contingency reserves. The agreement was filed with the Department pursuant to Section 1505 of the New York Insurance Law.

E. Abandoned Property Law

Section 1316 of the New York Abandoned Property Law provides that amounts payable to a resident of this state from a policy of insurance, if unclaimed for three years, shall be deemed to be abandoned property. Such abandoned property shall be reported to the comptroller on or before the first day of April each year. Such filing is required of all insurers regardless of whether or not they have any abandoned property to report.

The Company's abandoned property reports for the period of this examination were all filed on a timely basis pursuant to the provisions of Section 1316 of the New York Abandoned Property Law.

F. Significant Operating Ratios

These ratios were not calculated because the Company cedes 100% of its business to MBIA Insurance Corporation; therefore, these ratios are not relevant. Additionally, the Company has discontinued writing new business.

3. FINANCIAL STATEMENTS

A Balance Sheet

The following shows the assets, liabilities and surplus as regards policyholders as of December 31, 2003 as determined by this examination and as reported by the Company:

<u>Assets</u>	<u>Assets</u>	<u>Assets Not Admitted</u>	<u>Net Admitted Assets</u>
Bonds	\$106,118,730	\$	\$106,118,730
Cash, cash equivalents and short-term investments	2,434,637		2,434,637
Other invested assets	646,390		646,390
Investment income due and accrued	1,577,396		1,577,396
Uncollected premiums and agents' balances in the course of collection	844,206		844,206
Amounts recoverable from reinsurers	(5,712)		(5,712)
Electronic data processing equipment and software	121,981		121,981
Leasehold improvements		912,871	
Aggregate write-ins for other than invested assets	<u>33,000</u>		<u>33,000</u>
Total assets	<u>\$112,683,499</u>	<u>\$912,871</u>	<u>\$111,737,628</u>

Liabilities, Surplus and Other FundsLiabilities

Losses and loss adjustment expenses	\$	0
Taxes, licenses and fees (excluding federal and foreign income taxes)		123,685
Current federal and foreign income taxes		35,956
Net deferred tax liability		(105,326)
Ceded reinsurance premiums payable (net of ceding commissions)		388,419
Amounts withheld or retained by company for account of others		126,176
Payable to parent, subsidiaries and affiliates		<u>5,880,426</u>
Total liabilities		\$6,449,336

Surplus and Other Funds

Common capital stock	\$17,460,000	
Gross paid in and contributed surplus	57,540,000	
Unassigned funds (surplus)	<u>30,321,292</u>	
Surplus as regards policyholders		<u>105,321,292</u>
Total liabilities, surplus and other funds		<u>\$111,770,628</u>

B. Underwriting and Investment Exhibit

Surplus as regards policyholders increased \$13,062,906 during the four-year examination period January 1, 2000 through December 31, 2003, detailed as follows:

Statement of Income

Underwriting Income

Premiums earned		\$0
Deductions:		
Losses incurred	\$0	
Loss adjustment expenses incurred	0	
Other underwriting expenses incurred	7,290,764	
Aggregate write-ins for underwriting deductions	<u>0</u>	
Total underwriting deductions		<u>7,290,764</u>
Net underwriting gain or (loss)		\$(7,290,764)

Investment Income

Net investment income earned	\$22,647,715	
Net realized capital gain	<u>(793,219)</u>	
Net investment gain or (loss)		21,854,496

Other Income

Net gain or (loss) from agents' or premium balances charged off	\$0	
Finance and service charges not included in premiums	0	
Aggregate write-ins for miscellaneous income	<u>1,323,732</u>	
Total other income		<u>1,323,732</u>
Net income before dividends to policyholders and before federal And foreign income taxes		\$15,887,464
Dividends to policyholders		<u>0</u>
Net income after dividends to policyholders but before federal and foreign income taxes		\$15,887,464
Federal and foreign income taxes incurred		<u>1,532,496</u>
Net Income		<u>\$14,354,968</u>

C. Capital and Surplus Account

Surplus as regards policyholders per report on examination as of December 31, 1999			\$92,258,386
	<u>Gains in</u>	<u>Losses in</u>	
	<u>Surplus</u>	<u>Surplus</u>	
Net income	\$14,354,968		
Change in net unrealized foreign exchange capital gain	2,001,023		
Change in net deferred income tax	105,326		
Change in non-admitted assets	1,148,716		
Dividends to stockholders		\$4,500,000	
Aggregate write-ins for gains and losses in Surplus		<u>47,127</u>	
Total gains & losses	<u>\$17,610,033</u>	<u>\$4,547,127</u>	
Net increase (decrease) in surplus			<u>13,062,906</u>
Surplus as regards policyholders per report on examination as of December 31, 2003			<u>\$105,321,292</u>

4. LOSSES AND LOSS ADJUSTMENT EXPENSES

The examination liability for the captioned items of \$0 is the same as the amount reported by the Company as of December 31, 2003. Effective April 1998, the Company and MBIA Insurance Corporation entered into a reinsurance agreement under which MBIA Insurance Corporation agreed to reinsure 100% of the Company's net unearned premium, loss reserves and related contingency reserves.

5. MARKET CONDUCT ACTIVITIES

A review of the Company's market conduct activities was not performed due to the run-off status of the company.

6. COMPLIANCE WITH PRIOR REPORT ON EXAMINATION

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

<u>ITEM</u>	<u>PAGE NO.</u>
A. <u>Management</u>	6
i. It was recommended that the Company amend Section 2.07 of its by-laws, Action Without Meeting, to include the required specific language that would limit its use to emergency situations. The Company has complied with this recommendation.	
ii. Further, although the Company's by-laws allows its directors to take action without a meeting, they also require that an annual meeting following the shareholders' meeting should be held and thereafter regular meetings should be held at least once every quarter. By not holding annual meetings or regular meetings, the Company appears to be acting in violation of its by-laws. It is recommended that the Company comply with its by-laws by holding annual and regular meetings of its board of directors as stated therein. The Company has complied with this recommendation.	7

<u>ITEM</u>	<u>PAGE NO.</u>
iii. It is recommended that the Company comply with Section 1411(a) of the New York Insurance Law, which requires that investments be approved and authorized by the Company's board of directors or any committee thereof.	7
The Company has complied with this recommendation.	
iv. It is recommended that the Company exercise care when answering general interrogatories of its filed and sworn annual statement.	13
The Company has complied with this recommendation.	
B. <u>Reinsurance-Schedule F-Part 8</u>	13
It is recommended that the Company restate its contingency reserve account to reflect the reinsurance credit taken on such liability.	
The Company has complied with this recommendation.	
C. <u>Holding Company System</u>	
<u>Tax Allocation Agreement</u>	
(i) It is recommended that the Company comply with Section 4(b) and (c) of its tax allocation agreement.	16
The Company has complied with this recommendation.	
(ii) It is further recommended that the tax allocation agreement be revised to specifically indicate the names of all participating entities and their direct responsibilities.	16
The Company has complied with this recommendation.	
<u>Investment Manager</u>	
It is recommended that the Company establish a written investment agreement with its affiliate CMC. This agreement should be written in a manner that is in compliance with Section 1505(a) and be submitted to the Department pursuant to Section 1505(d) of the New York Insurance Law.	16
The Company has complied with this recommendation.	

ITEMPAGE NO.Loan to MBIA Assurance

It is recommended that the Company comply with Section 1411(a) and Section 1505(d)(1) of the New York Insurance Law. 17

The Company has complied with this recommendation.

Sale of CapMac Assurance

The Company did not request prior approval before selling its subsidiary. It is recommended that the Company comply with Section 1505(c) of the New York Insurance Law whenever its transactions with members of its holding company group subject to such section involve more than 5% of its admitted assets at year-end. 17

The Company has complied with this recommendation.

Management Agreement

- (i) It is recommended that the Company comply with Department Regulation 30, Part 106.6. 18

The Company has complied with this recommendation.

- (ii) It is recommended that the Company comply with Department Regulation 30, Part 105.4. 19

The Company has complied with this recommendation.

- (iii) It is also recommended that the Company comply with the annual statement instructions when completing its Underwriting and Investment Exhibit Part – 4 Expenses and allocate its management fee to the appropriate expense items. 19

The Company has complied with this recommendation.

D. Abandoned Property Law.

It is recommended that the Company annually submit abandoned property reports to the State Comptroller in accordance with Section 1316 of the New York Abandoned Property Law. 20

The Company has complied with this recommendation.

<u>ITEM</u>		<u>PAGE NO.</u>
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E.	<u>Accounts and Records</u>	
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	<u>Notes to the Financial Statements</u>	
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|-----|---|----|
| (i) | It is recommended that the Company ensure that the financial statement disclosures made in its filed and sworn to annual statements be accurately stated. | 21 |
|-----|---|----|

The Company has complied with this recommendation.

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|------|--|----|
| (ii) | It is further recommended that the Company be included in the expense allocation agreement that is currently in effect between MBIA Inc., its ultimate parent, and members of the holding company group. | 21 |
|------|--|----|

The Company has complied with this recommendation.

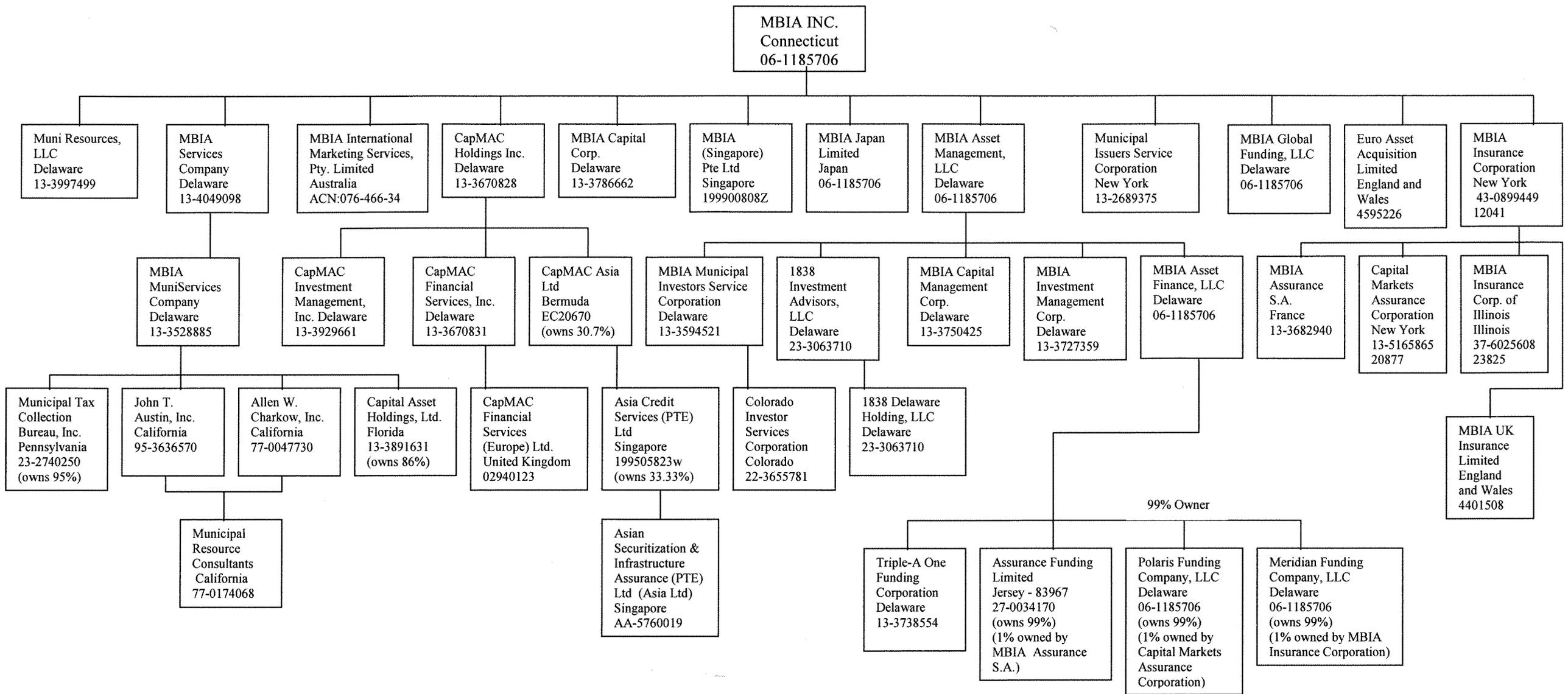
	<u>Disaster Recovery Plan</u>	
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	It is recommended that the Company establish and implement a disaster recovery plan.	21
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The Company has complied with this recommendation.

7. SUMMARY OF COMMENTS AND RECOMMENDATIONS

There are no comments or recommendations in this report on examination.



Appointment No 22397

STATE OF NEW YORK
INSURANCE DEPARTMENT

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

James Murphy

as proper person to examine into the affairs of the

CAPITAL MARKET ASSURANCE CORPORATION

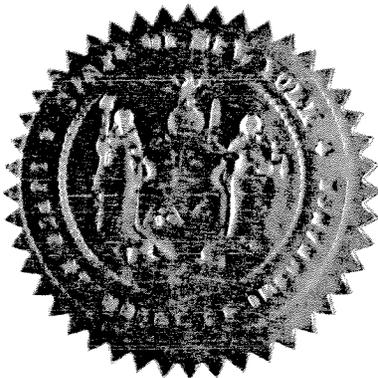
and to make a report to me in writing of the condition of the said

Corporation

with such other information as she 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 8th day of August, 2005



A handwritten signature in cursive script, appearing to read "Howard Mills".

HOWARD MILLS
Superintendent of Insurance