

REPORT ON EXAMINATION

OF THE

MIDROX INSURANCE COMPANY

AS OF

DECEMBER 31, 2009

DATE OF REPORT

AUGUST 20, 2010

EXAMINER

WAYNE A. LONGMORE

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

August 20, 2010

Honorable James J. Wrynn
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 30506 dated April 5, 2010 attached hereto, I have made an examination into the condition and affairs of Midrox Insurance Company as of December 31, 2009, and submit the following report thereon.

Wherever the designation "the Company" appears herein without qualification, it should be understood to indicate Midrox 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 office located at 56 Hillcrest Drive, Roxbury, New York 12474.

1. SCOPE OF EXAMINATION

The Department has performed a single-state examination of Midrox Insurance Company. The previous examination was conducted as of December 31, 2004. This examination covered the five-year period from January 1, 2005 through December 31, 2009. Transactions occurring subsequent to this period were reviewed where deemed appropriate by the examiner.

This examination was conducted in accordance with the National Association of Insurance Commissioners (“NAIC”) Financial Condition Examiners Handbook (“Handbook”), which requires that we plan and perform the examination to evaluate the financial condition and identify prospective risks of the Company by obtaining information about the Company including corporate governance, identifying and assessing inherent risks within the Company and evaluating system controls and procedures used to mitigate those risks. This examination also includes assessing the principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation, management’s compliance with Statutory Accounting Principles and annual statement instructions when applicable to domestic state regulations.

All financially significant accounts and activities of the Company were considered in accordance with the risk-focused examination process. The examiners also relied upon audit work performed by the Company’s independent public accountants when appropriate.

This examination report includes a summary of significant findings for the following items as called for in the Financial Condition Examiners Handbook of the NAIC:

- Significant subsequent events
- Company history
- Corporate records
- Management and control
- Fidelity bonds and other insurance
- Territory and plan of operation
- Growth of Company
- Loss experience
- Reinsurance
- Accounts and records
- Financial statements
- Summary of recommendations

This examination report also includes a summary of significant findings regarding 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 that involve departures from laws, regulations or rules, or that are deemed to require explanation or description.

2. DESCRIPTION OF COMPANY

The Company was organized in May of 1936, for the purpose of transacting business as an assessment cooperative insurance company in the counties of Delaware, Greene, Otsego, Schoharie and Ulster of this state. Subsequently the territorial limits were extended to cover all of the counties of this State, excluding the counties of New York, Kings, Queens, Bronx and Richmond.

In 1988, a certificate was issued by this Department authorizing the Company to change its name from the Midrox Co-Operative Fire Insurance Company to the Midrox 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 not less than nine nor more than fifteen members. The board of directors and the executive committee meets at least four times during each calendar year. At December 31, 2009, the board of directors was comprised of the following nine members:

| <u>Name and Residence</u> | <u>Principal Business Affiliation</u> |
|--------------------------------------|--|
| Alton James Brandow Schenevus, NY | Retired |
| Eugene David Cole Edmeston, NY | Officer and Insurance Agent, Gates-Cole Associates |
| William Richard Finch Roxbury, NY | Owner and President, Brookside Hardware, Ltd. |
| Dawnette Marie Giesse Delhi, NY | Senior Vice President, National Bank of Delaware County |

| <u>Name and Residence</u> | <u>Principal Business Affiliation</u> |
|---|---|
| Hugh Irvin Henderson Oneonta, NY | Farmer and Insurance Agent |
| Charles Frank McIntosh Bovina Center, NY | Owner, McIntosh Market and Auction Service |
| Frederick John Morse Margaretville, NY | President of Midrox Insurance Company, Insurance Agent and Owner of the Morse-Wilson Agency Inc |
| Joseph Charles Ranc Otego, NY | Certified Public Accountant, Comptroller, Fraiziers Nursery & Landscape, Inc. |
| Carol Morse Wilson Roxbury, NY | Secretary and Treasurer of Midrox Insurance Company, Insurance Agent, President and Owner of Morse-Wilson Agency Inc. |

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, 2009, the principal officers of the Company were as follows:

| <u>Name</u> | <u>Title</u> |
|----------------------|-------------------------|
| Frederick John Morse | President |
| Carol Morse Wilson | Secretary and Treasurer |

The jurat page of the Company's filed 2009 annual statement included Lindon Morse as Vice President and director of the Company even though he had passed away in July 2009. Article III – Section 1 of the by-laws states that the officers of the Company shall be President, Vice President, Secretary and Treasurer and such other officers as may be deemed necessary, to be chosen by the board of directors from among its members at the annual meeting for a term of one year. The Company filled the vacancy in the Vice President position at its June 2010 annual meeting; however, it is recommended that the Company correctly complete the annual statement jurat page and not list deceased individuals as officers and board members.

B. Territory and Plan of Operation

As of December 31, 2009, the Company was licensed to write business only in the State of New York, excluding the counties of New York, Kings, Queens, Bronx and Richmond.

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> |
|------------------|---|
| 4 | Fire |
| 5 | Miscellaneous property |
| 6 | Water damage |
| 7 | Burglary and theft |
| 8 | Glass |
| 12 | Collision |
| 13 | Personal injury liability |
| 14 | Property damage liability |
| 15 | Workers' compensation and employers' liability (excluding workers' compensation) |
| 19 | Motor vehicle and aircraft physical damage (excluding aircraft physical damage) |
| 20 | Marine and inland marine (inland marine only) |

Paragraphs 5, 6, 7, 8, 13, 14 and 15 can be written solely in conjunction with fire insurance written under the same policy and covering the same premises. The Company is also licensed to accept and cede reinsurance as provided in Section 6606 of the New York Insurance Law.

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

| <u>Calendar Year</u> | <u>Direct Premiums Written</u> |
|----------------------|--------------------------------|
| 2005 | \$4,827,395 |
| 2006 | \$4,298,410 |
| 2007 | \$4,057,342 |
| 2008 | \$3,847,729 |
| 2009 | \$3,641,532 |

Based on the lines of business for which the Company is licensed and pursuant to the requirements of Articles 13 and 66 of the New York Insurance Law, the Company is required to maintain a minimum surplus to policyholders in the amount of \$100,000.

At December 31, 2009 the Company wrote business through approximately ninety-nine independent agents.

The Company's predominant lines of business are commercial multiple peril, farmowners multiple peril and fire, which accounted for 36.10%, 29.52% and 20.48%, respectively, of the Company's direct written premiums in 2009.

C. Reinsurance

During the period covered by this examination the Company did not assume any reinsurance business.

As of December 31, 2009, the Company had the following ceded reinsurance program in place:

| <u>Type of Treaty</u> | <u>Cession</u> |
|--|---|
| <u>Property</u> 2 layers | \$445,000 in excess of \$55,000 each loss, each risk; liability of the reinsurer not to exceed \$190,000 and \$700,000 ultimate net loss any one loss occurrence for the first and second layers, respectively. |
| <u>Property Catastrophe</u> Specifically named Catastrophe Perils (Windstorm, Hail, Tornado, Cyclone, Flood, Earthquake, Volcanic Eruption) | \$110,000 in excess of \$38,000. |
| <u>Property Catastrophe</u> Excess of loss 4 layers | Layer 1: 95% of \$350,000 in excess of \$150,000 each loss occurrence. Layers 2 through 4: 100% in excess of \$500,000 each loss occurrence. |
| <u>Casualty</u> Excess of loss 3 layers | \$960,000 in excess of \$38,000 per loss occurrence. |

| <u>Type of Treaty</u> | <u>Cession</u> |
|----------------------------------|---|
| <u>Casualty</u> | |
| Special excess of loss | \$500,000 in excess of \$500,000 each loss occurrence. |
| Facultative Excess of Loss | \$1 million in excess of \$1 million in ultimate net loss in any one loss occurrence, each policy. |
| Property and Casualty Occurrence | \$55,000 in excess of \$38,000 per occurrence- in the event the property and casualty business covered under the first excess layer are both involved in the same loss. |
| Casualty Clash | \$500,000 in excess of \$1,000,000 each occurrence. With respect to workers compensation insurance subject to Section 3420 of the New York Insurance Law no claim shall be made unless the Company sustains an ultimate net loss in excess of \$1.5 million, then the reinsurer will reimburse the whole excess amount. |
| Aggregate excess of loss | 95% of \$300,000 of the amount of the ultimate net loss in the aggregate over an amount equal to 70% of net earned premium income for the contract year. |
| Property Facultative | Cession hereunder shall be limited to an amount equal to 5 times the Company's net retention plus the amount ceded under the Company's working reinsurance contracts subject to a minimum net retention of \$100,000 and a maximum cession of \$500,000 on any one risk. |

Examination review of the property and casualty combination excess of loss reinsurance contract effective January 1, 2009 determined that the Company was in violation of Section 6610(d) of the New York Insurance Law. The Company's retention on the subject casualty business was found to be greater than the 2% of surplus limitation of Section 6610(d) of the New York Insurance Law.

Section 6610(d) of the New York Insurance Law states, in part, that:

“The maximum amount of insurance (including the obligation to pay outside loss adjustment expense) less reinsurance in other authorized insurers or accredited reinsurers as defined in subsection (a) of section one hundred seven of this chapter which may be assumed by an assessment corporation on a single risk for the kinds of insurance . . . shall not exceed two percent of its surplus as shown in its last sworn statement filed with the superintendent.”

Upon being informed of this observation, the Company amended the contract in order to correct the deficiency by reducing the casualty retention level to \$38,000 from \$40,000. Nonetheless,

it is again recommended that the Company comply with Section 6610(d) of the New York Insurance Law and not exceed the limitations specified.

Section 1308(e)(1)(A) of the New York Insurance Law (“NYIL”) states, in part, 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 previously granted approval for the Company to cede an amount in excess of the fifty percent limitation prescribed by Section 1308(e)(1)(A) of the NYIL. However, in 2009 the Company failed to submit additional reinsurance treaties that it became a party to for review in accordance with Section 1308(e)(1)(A). Therefore, it is recommended that, in the future, the Company submit its reinsurance contracts in effect as well as any new contracts and any amendments thereto for review in accordance with Section 1308(e)(1)(A) of the New York Insurance Law.

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. Additionally, management has represented that all material ceded reinsurance agreements transfer both underwriting and timing risk as set forth in the NAIC Accounting Practices and Procedures Manual Statements of Statutory Accounting Principles (“SSAP”) No. 62. Representations were supported by appropriate risk transfer analyses and an attestation from the Company's chief executive and chief financial officers pursuant to the NAIC Annual Statement Instructions. Additionally, examination review indicated that the Company was not a party to any finite reinsurance agreements. All ceded reinsurance agreements were accounted for utilizing reinsurance accounting as set forth in paragraphs 26 and 27 of SSAP No. 62.

D. Holding Company System

Statewide Underwriters Agency, Inc.

As of December 31, 2009, the Company is in control of a subsidiary known as Statewide Underwriters Agency, Inc. (“Statewide”). The subsidiary was formed to provide agents of Midrox Insurance Company access to markets that the Company was unable to write. The Company and its subsidiary share the use of personnel, property and services. A management agreement, made effective January 1, 2009 and expiring December 31, 2009, calls for the Company to provide management, underwriting and clerical services deemed necessary for the operation of the Agency. Said management agreement is subject to managerial review and is renewed annually.

Department Regulation 53 filings

Department Regulation 53, Part 81-1.2(f), states that:

“Every insurer owning a subsidiary pursuant to article 16 of the Insurance Law shall file a report containing the following information with the superintendent on or before March 1st of each year, or within such longer period as the superintendent, on good cause shown, may permit:

(f) A brief description of all transactions entered into during the next preceding calendar year with any of such subsidiaries (other than any transactions otherwise reported to or approved by the superintendent under any provision of the Insurance Law) inclusive of arrangements for common management or cooperative or joint use of personnel, property or services. (Transactions not deemed material, transactions in series, or numerous similar transactions, may be reported in the aggregate provided that they are reasonably described.) The issuance of contracts of insurance issued in the normal course of business other than contracts of reinsurance shall not be deemed transactions hereunder. Descriptions of transactions, other than those reported in the aggregate, shall include at least the following:

- (1) the nature and purpose of the transaction;
- (2) the nature and amounts of any payments or transfers of assets between the parties;
- (3) the identities of all parties to such transaction;
- (4) whether any officers or directors of a party are pecuniarily interested therein; and
- (5) copies of any contracts, agreements or memoranda of understanding between the parties relating to the transaction.”

The Company has not been filing its agreements with the Department regarding its Statewide Underwriters Agency, Inc. subsidiary in accordance with the aforementioned requirements of Department Regulation 53.

It is recommended that the Company comply fully with the filing requirements of Department Regulation 53, and include in those filings all transactions between the Company and its subsidiary.

Correct Reporting of Subsidiary Investments/Article 16 Compliance

The Company was authorized by the Department in June of 1991 to invest \$5,000 in 5,000 shares of its subsidiary, Midrox Agency, Inc. "Class A voting stock" with a par value of \$1.00 per share. Subsequent to that date, the name of Midrox Agency, Inc was changed to Statewide Underwriters Agency, Inc. ("Statewide"). The Company is reporting ownership of 100 shares of Midrox Agency, Inc. per Schedule D - Part 2 - Section 2 of its 2009 filed Annual Statement. Upon examination, it was determined that the Company actually owns 6,800 shares at a cost of \$6,800. The Company was asked to provide evidence of Department approval to invest an additional \$1,800 in Statewide in accordance with the directive in the Department's initial approval to invest in this subsidiary. The Company was unable to provide documentation of compliance with this directive from the Department.

The Company is also noted to have left Note No. 10 (Information concerning parent, subsidiaries, affiliates, and other related parties) to the 2009 filed Annual Statement blank despite them having a subsidiary.

It was also noted that the share certificates issued by the subsidiary all stated "non-voting." This appears to be in violation of Section 1602 of the New York Insurance Law which states that:

"A domestic insurer shall own not less than fifty-one percent of the issued and outstanding voting shares of each of its subsidiaries."

Given the foregoing, the following recommendations are being made:

- 1) It is recommended that the Company comply fully with directives from this Department.
- 2) It is recommended that the Company correctly complete its investment schedules as well as the notes to the filed Annual Statements with information pertaining to its subsidiary, Statewide Underwriters Agency, Inc.

- 3) It is recommended that the Company comply with Section 1602 of the New York Insurance Law.

Tax Allocation Agreement

Circular Letter No. 33 (1979) Guideline No. 1 states that:

"Every domestic insurer which is a party to a consolidated federal income tax filing must have a definitive written agreement, approved by its Board of Directors, governing its participation therein."

The Company files a consolidated tax return with its subsidiary, Statewide; however, the Company was not able to provide an executed tax allocation agreement pursuant to the directives of Circular Letter No. 33 (1979).

It is recommended that the Company comply with Department Circular Letter No. 33 (1979) by preparing and submitting its inter-company tax allocation agreement to the board of directors for approval and then to the Department for non-disapproval pursuant to the guidelines of Circular Letter No. 33 (1979).

Morse-Wilson Agency, Inc. ("agency")

The Company has both a real estate lease agreement and an expense sharing agreement with the Morse-Wilson Agency, Inc. The agency is owned by the president and the secretary-treasurer of the Company. The agency maintains its own office staff and shares office space with the Company. The entities share the cost of a receptionist.

Lease Agreement

The Company ("Landlord") and the Morse-Wilson Agency, Inc. ("Tenant") entered into a lease agreement effective July 1, 2009. The Landlord, in consideration of the lease payments called for in the agreement, leases office space totaling 1,324 square feet of the home office to the Tenant. The lease agreement is renewed on an annual basis.

Expense Sharing Agreement

The expense sharing agreement was made effective January 1, 2009 and expires December 31, 2009 and is renewed on an annual basis. The agreement calls for the reimbursement of the Company for actual usage by the Morse-Wilson Agency of postage, broadband costs and telephone.

The agreement calls for postage and telephone cost to be reimbursed based on actual usage, while broadband costs will be split equally.

E. Significant Operating Ratios

The following ratios have been computed as of December 31, 2009, based upon the results of this examination:

| | |
|--|--------|
| Net premiums written to surplus as regards policyholders | 1.16:1 |
| Liabilities to liquid assets (cash and invested assets less investments in affiliates) | 66% |
| Premiums in course of collection to surplus as regards policyholders | 4% |

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 | \$7,865,585 | 65.74% |
| Other underwriting expenses incurred | 4,951,955 | 41.38 |
| Net underwriting loss | <u>(852,349)</u> | <u>(7.12)</u> |
| Premiums earned | <u>\$11,965,191</u> | <u>100.00%</u> |

F. Accounts and Records

Approval of Investments

Section 1411(a) of the New York Insurance Law states, in part, that:

“No domestic insurer shall make any loan or investment . . . unless authorized or approved by its board of directors or a committee thereof responsible for supervising or making such investment or loan. The committee's minutes shall be recorded and a report submitted to the board of directors at its next meeting.”

It was determined that the board of directors did not approve all investment transactions during the examination period.

It is recommended that the Company comply with the investment authorization requirements of Section 1411(a) of the New York Insurance Law.

Levy of Assessment by the Board of Directors

The Company, as an assessment cooperative, is not required to file its rates. However, the Company's board of directors was not approving rate changes. Section 6615(a)(1) of the New York Insurance Law states that:

"Every assessment corporation may, if so directed by its board of directors levy an assessment upon all of its members. Such assessment shall be sufficient to provide for the payment of losses, expenses, and other obligations, incurred, or likely to be incurred during the fiscal year for which the assessment is levied."

It is recommended that the Company comply with Section 6615(a)(1) of the New York Insurance Law and have its rates of assessment approved by its board of directors.

Rent Charges - Compliance with SSAP 40

Statement of Statutory Accounting Principles ("SSAP") No. 40 paragraph 15 states that:

"A reporting entity shall include in both its income and expenses an amount for rent relating to its occupancy of its own building. The amount recorded shall be at a rate comparable to rent received from others and/ or rental rates of like property in the same area. If this is unavailable, it shall be derived from consideration of the repairs, expenses, taxes, and depreciation incurred, plus interest added at an average fair rate on the carrying value of the reporting entity's investment in its home office building."

The rent the Company charged itself for 2009 was insufficient and not consistent with the aforementioned requirements.

It is recommended that the Company comply with the requirements of SSAP No. 40 paragraph 15 when determining the rental charge for the occupancy of its own building.

Allocation of Expenses

SSAP No. 70 sets forth the rules and methods governing the allocation of certain expenses among three categories: loss adjustment expenses, other underwriting expenses, and investment expenses. Paragraph 6 of SSAP 70 requires that allocation should be based on a method that yields the most accurate results. Where specific identification is not feasible, “allocation of expenses should be based upon pertinent factors or ratios such as studies of employee activities, salary ratios or similar analyses.”

The Company was unable to provide current time studies supporting the allocation percentages being used in allocating expenses to the three expense categories.

It is recommended that the Company establish and maintain written documentation supporting the allocation of each type of expense to the three expense groups as required by SSAP No. 70.

G. Risk Management and Internal Controls

Succession Planning

The Company was unable to present a formalized succession plan which addresses the key officers of the entity.

It is recommended that the Company implement and keep updated a formal succession plan in order to protect the best interests of the Company and its policyholders.

3. FINANCIAL STATEMENTS

A. Balance Sheet

The following shows the assets, liabilities and surplus as regards policyholders as of December 31, 2009 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 | \$3,579,688 | \$ 0 | \$3,579,688 |
| Common stocks | 715,972 | | 715,972 |
| Real Estate: Properties occupied by the company | 177,878 | | 177,878 |
| Cash, cash equivalents and short-term investments | 174,230 | | 174,230 |
| Investment income due and accrued | 45,958 | | 45,958 |
| Uncollected premiums and agents' balances in course of collection | 74,286 | 2,767 | 71,519 |
| Deferred premiums, agents' balances and installments booked but deferred and not yet due | 673,873 | | 673,873 |
| Reinsurance: Amounts recoverable from reinsurers | 39,625 | | 39,625 |
| Net deferred tax asset | 560,379 | 475,379 | 85,000 |
| Furniture and equipment, including health care delivery assets | 15,309 | 15,309 | 0 |
| Receivables from parent, subsidiaries and affiliates | 55 | | 55 |
| Other receivables | <u>782</u> | <u>0</u> | <u>782</u> |
| Total assets | <u>\$6,058,035</u> | <u>\$493,455</u> | <u>\$5,564,580</u> |

Liabilities, Surplus and Other FundsLiabilities

| | | |
|---|--|----------------|
| Losses and loss adjustment expenses | | \$1,270,970 |
| Commissions payable, contingent commissions and other similar charges | | 175,922 |
| Other expenses (excluding taxes, licenses and fees) | | 12,837 |
| Taxes, licenses and fees (excluding federal and foreign income taxes) | | 2,977 |
| Borrowed money and interest thereon | | 190,000 |
| Unearned premiums | | 1,448,246 |
| Advance premium | | 22,428 |
| Ceded reinsurance premiums payable (net of ceding commissions) | | 182,996 |
| Amounts withheld or retained by company for account of others | | 419 |
| Pension liability | | <u>319,186</u> |
| Total liabilities | | \$3,625,981 |

Surplus and Other Funds

| | | |
|--|----------------|--------------------|
| Unassigned funds (surplus) | \$1,838,600 | |
| Required surplus | <u>100,000</u> | |
| Surplus as regards policyholders | | <u>1,938,600</u> |
| Total liabilities, surplus and other funds | | <u>\$5,564,581</u> |

NOTE: The Internal Revenue Service did not audit the Company's consolidated 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 decreased \$185,694 during the five-year examination period January 1, 2005 through December 31, 2009, detailed as follows:

Underwriting Income

| | | |
|--|------------------|-------------------|
| Premiums earned | | \$11,965,191 |
| Deductions: | | |
| Losses and loss adjustment expenses incurred | \$7,865,585 | |
| Other underwriting expenses incurred | <u>4,951,955</u> | |
| Total underwriting deductions | | <u>12,817,540</u> |
| Net underwriting gain or (loss) | | \$ (852,349) |

Investment Income

| | | |
|-------------------------------|---------------|---------|
| Net investment income earned | \$ 630,875 | |
| Net realized capital gain | <u>16,052</u> | |
| Net investment gain or (loss) | | 646,927 |

Other Income

| | | |
|---|---------------|------------------|
| Net gain or (loss) from agents' or premium balances charged off | \$ 10,077 | |
| Finance and service charges not included in premiums | 201,449 | |
| Aggregate write-ins for miscellaneous income | <u>42,274</u> | |
| Total other income | | <u>253,800</u> |
| Net income | | \$ <u>48,378</u> |

| | | | |
|--|-------------------|------------------|--------------------|
| Surplus as regards policyholders per report on examination as of December 31, 2004 | | | \$2,124,294 |
| | <u>Gains in</u> | <u>Losses in</u> | |
| | <u>Surplus</u> | <u>Surplus</u> | |
| Net income | \$ 48,378 | | |
| Net unrealized capital losses | | \$ 75,066 | |
| Change in net deferred income tax | 375,429 | | |
| Change in nonadmitted assets | | 307,510 | |
| Aggregate write-ins for gains and losses in surplus | <u> </u> | <u>226,925</u> | |
| Total gains or losses in surplus | <u>\$423,807</u> | <u>\$609,501</u> | |
| Net increase (decrease) in surplus | | | <u>(185,694)</u> |
| Surplus as regards policyholders per report on examination as of December 31, 2009 | | | <u>\$1,938,600</u> |

4. LOSSES AND LOSS ADJUSTMENT EXPENSES

The examination liability for the captioned items of \$1,270,970 is the same as reported by the Company as of December 31, 2009. The examination 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.

5. 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.

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.

Specificity of non-renewal reasons and three-year policy period on Personal Lines policies

During the review of a sample of non-renewals, the following observations were made:

1. The Company is using "Losses" and "Loss history" as reasons for non-renewal.
2. The Company is not honoring the three-year policy period on personal lines policies.

Section 3425(d)(1) of the New York Insurance Law states, in part, that:

“Unless the insurer, at least forty-five but not more than sixty days in advance of the end of the policy period, mails or delivers to the named insured, at the address shown in the policy, a written notice of its intention not to renew a covered policy, or to condition its renewal upon change of limits or elimination of any coverages, the named insured shall be entitled to renew the policy upon timely payment of the premium billed to the insured for the renewal. The specific reason or reasons for nonrenewal or conditioned renewal shall be stated in or shall accompany the notice...”

Section 3425(e) of the New York Insurance Law states, in part, that:

“With respect to personal lines insurance policies, no notice of nonrenewal or conditional renewal of a covered policy shall be issued to become effective during the required policy period unless it is based upon a ground for which the policy could have been cancelled...”

Section 3425(c)(2) of the New York Insurance Law outlines the specific statutory reasons for which a personal lines policy may be terminated after the first sixty days of coverage.

Given the foregoing, the following recommendations are made:

1. It is recommended that the Company provide a specific reason for policy non-renewal as required by Section 3425(d)(1) of the New York Insurance Law.
2. It is recommended that the Company comply with the requirements of Section 3425(e) of the New York Insurance Law and not non-renew personal lines policies midterm for other than the statutory reasons put forth in Section 3425(c)(2) of the New York Insurance Law.

Department Regulation No. 64 - Denial Letters

Department Regulation 64 Part 216.6 states the following:

“(h) Any notice rejecting any element of a claim involving personal property insurance shall contain the identity and the claims processing address of the insurer, the insured's policy number, the claim number, and the following statement prominently set out:

"Should you wish to take this matter up with the New York State Insurance Department, you may file with the Department either on its website at www.ins.state.ny.us/complhow.htm or you may write to or visit the Consumer Services Bureau, New York State Insurance Department, at: 25 Beaver Street, New York, NY 10004; One Commerce Plaza, Albany, NY 12257; 200 Old Country Road, Suite 340, Mineola, NY 11501; or Walter J. Mahoney Office Building, 65 Court Street, Buffalo, NY 14202."

The notices in the denial letters reviewed were not consistent with the above requirement.

It is recommended that the Company comply with all the requirements of Part 216.6(h) of Department Regulation 64 when issuing notices rejecting any element of a claim involving personal property insurance.

Property Insurance Loss Register (“PILR”) filing Timelines and Evidence of Filing Retention

The examiner requested that the Company provide evidence of compliance with the recommendation from the previous examination which stated:

"It is recommended that the Company comply with Section 318(a) of the New York Insurance Law and Regulation 96 (NYCRR Part 62-2.2) and report all fire losses in excess of \$1,000 to the PILR."

The Company provided examples of claims that met the threshold and it was noted that despite appearing to make the PILR filings as was recommended, evidence of that was not consistently being included in the claim files nor were those filings being made within five business days of the Company receiving the loss notice.

It is recommended that the Company comply with the timelines specified by Department Regulation 96 when reporting fire losses in excess of \$1,000 to the PILR.

It is recommended that the Company comply with the documentation requirements of Department Regulation 64 Part 216.11 and maintain within each claim file all transactions relating to the claim.

6. COMPLIANCE WITH PRIOR REPORT ON EXAMINATION

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

| <u>ITEM</u> | <u>PAGE NO.</u> |
|---|-----------------|
| A. <u>Management</u> | |
| i. Although the Company complied with Section 6624(b) of the New York Insurance Law for four of the five years of the examination period, it was still recommended that the Company must be in compliance with the Section 6624(b) of the New York Insurance Law and have four board meetings in each calendar year. A similar recommendation was made in the previous examination report. | 4 |
| | |
| The Company has complied with this recommendation. | |
| ii. It was recommended that board members who are unable or unwilling to attend meetings consistently should resign or be replaced. | 5 |
| | |
| The Company has complied with this recommendation. | |
| iii. It was recommended that the Company comply with Article II Section 1 of its by-laws by having all members of the board maintain a policy with the Company. | 5 |
| | |
| The Company has complied with this recommendation. | |
| iv. It was recommended that, henceforth, the directors of Midrox Insurance Company remain mindful of their fiduciary responsibilities to the Company and its policyholders, as set forth in Section 717 of the New York Business Corporation Law. In addition, the policyholders should replace any director of the Company who cannot or does not fulfill his/her duties in good faith and with that degree of care which an ordinarily prudent person in a like position would use under similar circumstances. | 6 |
| | |
| The Company has complied with this recommendation. | |

| <u>ITEM</u> | <u>PAGE NO.</u> |
|---|-----------------|
| | |
| B. <u>Reinsurance</u> | |
| i. It was recommended that in the future, the Company comply with Sections 6610(c) and 6610(d) and not exceed any of the limitations specified in the above cited Sections of the Insurance Law. | 9 |
| | |
| The Company has not complied fully with this recommendation. A similar recommendation is made in this report. | |
| ii. It was recommended that the Company comply with the requirements of Section 1308(e)(1)(A) of the New York Insurance Law. A similar recommendation was made in the previous examination report. | 10 |
| | |
| The Company has not complied fully with this recommendation. A similar recommendation is made in this report. | |
| iii. It was recommended that the Company comply with Sections 6606 and 6610 of the Insurance Law and only have authorized reinsurers participating in its reinsurance agreements. | 11 |
| | |
| The Company has complied with this recommendation. | |
| iv. It was recommended that the Company comply with Regulation 98 (11NYCRR Part 32.1(b)(1) and (2)) and obtain written evidence from its intermediary that the assuming insurer or insurers agreed to assume the risks or that such insurer or insurers had given authority to the reinsurance intermediary to bind risks in their name and the scope of such authority. | 12 |
| | |
| The Company has complied with this recommendation. | |
| | |
| C. <u>Accounts and Records</u> | |
| | |
| It was recommended that the Company comply with Department guidelines, as set forth by NAIC guidelines and reinforced by Circular Letter No. 2 of 1977, and obtain a custodial agreement that includes the suggestions specified by the New York Insurance Department. | 14-15 |
| | |
| The Company has complied with this recommendation. | |
| | |
| D. <u>Market Conduct Activities</u> | |
| i. It was recommended that the Company comply with Section 318(a) of the New York Insurance Law and Regulation 96 (NYCRR Part 62-2.2) and report all fire losses in excess of \$1,000 to the PILR. | 20 |
| | |
| The Company has not complied with this recommendation. A similar | |

| <u>ITEM</u> | <u>PAGE NO.</u> |
|--|-----------------|
| recommendation is made in this report. | |
| ii. It was recommended that the Company comply with Section 331 of the New York Insurance Law and Circular Letter 34 of 1999 and before payment is made on fire losses send written notice to Tax Districts who have informed the Department of their intent to claim against fire insurance proceeds. | 20-21 |

The Company has complied with this recommendation.

7. SUMMARY OF COMMENTS AND RECOMMENDATIONS

| <u>ITEM</u> | <u>PAGE NO.</u> |
|--|-----------------|
| A. <u>Management</u> | |
| It is recommended that the Company correctly complete the annual statement jurat page and not list deceased individuals as officers and board members. | 4 |
| B. <u>Reinsurance</u> | |
| i. It is recommended that the Company comply with Section 6610(d) of the New York Insurance Law and not exceed the limitations specified. | 8 |
| ii. It is recommended that, in the future, the Company submit its reinsurance contracts in effect as well as any new contracts and any amendments thereto for review in accordance with Section 1308(e)(1)(A) of the New York Insurance Law. | 8 |
| C. <u>Holding Company</u> | |
| i. It is recommended that the Company comply fully with the filing requirements of Department Regulation 53 and include in those filings all transactions between the Company and its subsidiary. | 10 |
| ii. It is recommended that the Company comply fully with directives from this Department. | 10 |
| iii. It is recommended that the Company correctly complete its investment schedules as well as the notes to the filed Annual Statements with information pertaining to its subsidiary, Statewide Underwriters Agency, Inc. | 10 |
| iv. It is recommended that the Company comply with Section 1602 of the New York Insurance Law. | 11 |

| <u>ITEM</u> | <u>PAGE NO.</u> | |
|-------------|---|----|
| v. | It is recommended that the Company comply with Department Circular Letter No. 33 (1979) by preparing and submitting its inter-company tax allocation agreement to the board of directors for approval and then to the Department for non-disapproval pursuant to the guidelines of Circular Letter No. 33 (1979). | 11 |
| | | |
| D. | <u>Accounts and Records</u> | |
| i. | It is recommended that the Company comply with the investment authorization requirements of Section 1411(a) of the New York Insurance Law. | 13 |
| ii. | It is recommended that the Company comply with Section 6615(a)(1) of the New York Insurance Law and have its rates of assessment approved by its board of directors. | 13 |
| iii. | It is recommended that the Company comply with the requirements of SSAP No. 40 paragraph 15 when determining the rental charge for the occupancy of its own building. | 13 |
| iv. | It is recommended that the Company establish and maintain written documentation supporting the allocation of each type of expense to the three expense groups as required by SSAP No. 70. | 14 |
| | | |
| E. | <u>Risk Management and Internal Controls</u> | |
| | It is recommended that the Company implement and keep updated a formal succession plan in order to protect the best interest of the Company and the policyholders. | 14 |
| | | |
| F. | <u>Market Conduct</u> | |
| i. | It is recommended that the Company provide a specific reason for policy non-renewal as required by Section 3425(d)(1) of the New York Insurance Law. | 19 |
| ii. | It is recommended that the Company comply with the requirements of Section 3425(e) of the New York Insurance Law and not non-renew personal lines policies midterm for other than the statutory reasons put forth in Section 3425(c)(2) of the New York Insurance Law. | 19 |
| iii. | It is recommended that the Company comply with all of the requirements of Part 216.6(h) of Department Regulation 64 when issuing notices rejecting any element of a claim involving personal property insurance. | 20 |

| <u>ITEM</u> | | <u>PAGE NO.</u> |
|-------------|---|-----------------|
| iv. | It is recommended that the Company comply with the timelines specified by Department Regulation 96 when reporting fire losses in excess of \$1,000 to the PILR. | 20 |
| v. | It is recommended that the Company comply with the documentation requirements of Department Regulation 64 Part 216.11 and maintain within each claim file all transactions relating to the claim. | 21 |

Respectfully submitted,

/s/
Wayne A. Longmore
Senior Insurance Examiner

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

WAYNE A. 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 A. Longmore

Subscribed and sworn to before me

this _____ day of _____, 2010.

STATE OF NEW YORK
INSURANCE DEPARTMENT

I, James J. Wrynn 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

Midrox Insurance Company

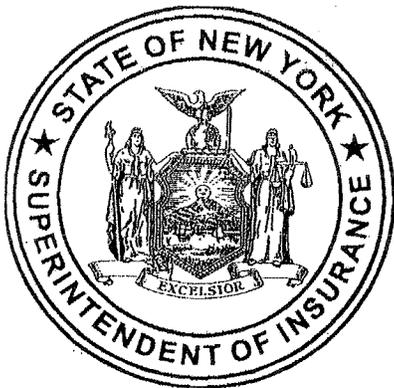
and to make a report to me in writing of the condition of the said

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 5th day of April 2010



A handwritten signature in cursive script, reading "James J. Wrynn".

James J. Wrynn
Superintendent of Insurance