

REPORT ON EXAMINATION

OF THE

CONSTITUTION INSURANCE COMPANY

AS OF

DECEMBER 31, 2006

DATE OF REPORT

FEBRUARY 15, 2008

EXAMINER

MARC ALLEN

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

February 15, 2008

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

Sir:

Pursuant to the requirements of the New York Insurance Law, and in compliance with the instructions contained in Appointment Number 22593 dated February 16, 2007 attached hereto, I have made an examination into the condition and affairs of Constitution Insurance Company as of December 31, 2006, and submit the following report thereon.

Wherever the designation "the Company" appears herein without qualification, it should be understood to indicate Constitution Insurance Company.

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

The examination was initially conducted at the Company's home office located at 1345 Avenue of the Americas, New York, NY 10105. The Company relocated its home office in November 2007, to Seven Times Square, New York, NY 10036.

1. SCOPE OF EXAMINATION

The previous filed examination report for the Company was as of December 31, 1998. In 2003, the Department commenced a financial examination of the Company as of December 31, 2002. The Company's parent, from which the Company assumed business through a quota share agreement, commuted a large number of its assumed reinsurance contracts subsequent to the December 31, 2002 examination date. These commutations had a substantial and material impact on the financial position of the Company. The Department chose not to file the December 31, 2002 examination report as the subsequent commutations rendered the December 31, 2002 report irrelevant and obsolete.

This examination covered the four year period from January 1, 2003 through December 31, 2006. Transactions occurring subsequent to this period were reviewed where deemed appropriate by the examiner.

The examination comprised a verification of assets and liabilities as of December 31, 2006. The examination included a review of income, disbursements and company records deemed necessary to accomplish such analysis or verification and utilized, to the extent considered appropriate, work performed by the Company's independent certified public accountants ("CPA"). 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"):

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

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 on February 10, 1992 as the Folksamerica National Reinsurance Company ("FNRC"). On December 31, 1992, substantially all of the assets and liabilities of FNRC and its underwriting and investment activities were transferred to Folksamerica Reinsurance Company.

In July 1996, 100% of the outstanding stock of the Company was purchased by Gerling Konzern Rueckversicherungs Aktiengesellschaft ("GKG"), of Cologne, Germany (now known as Globale Ruckversicherungs-AG ("Globale")). GKG was owned by Gerling Konzern Versicherungs-Beteiligungs ("GKB") of Cologne, Germany (now known as Winsor Vermaltungen-AG ("Winsor")), which at the time was owned 70% by the private group of Dr. Rolf Gerling and 30% by Deutsche Bank. Since 1963, GKG conducted reinsurance operations in the United States through its United States branch, Gerling Global Reinsurance Corporation-United States Branch (now known as the United States Branch of Global Reinsurance Company ("US Branch")). In December 1996, the Company's name was changed to Gerling Global Reinsurance Corporation of America ("GGRCA").

At January 1, 1997, the Company entered into a 100% quota share agreement with the US Branch whereby, all of its reinsurance contracts that were in force as of January 1, 1997, were assumed by the Company. Under this agreement, premiums assumed by the Company in 1998 and 1997 amounted to \$7,757,000 and \$44,136,000, respectively.

On October 27, 1998, the Company's parent acquired EXOR-CRC Inc. (later renamed Gerling Global Holdings Inc.), a Delaware investment holding company, which owned Constitution Holding Inc. ("CHI"), a United States insurance holding company, which in turn owned Constitution Reinsurance Corporation ("CRC"). The Gerling Group intended to integrate the operations of CRC with the Company's operations. To that end, the Company entered into an assumption agreement with CRC, whereby the Company transferred all of its policy obligations to CRC. Simultaneously,

the Company entered into a quota share agreement with CRC in which CRC ceded 3% of all its policies in force, issued or renewed to the Company.

In connection with the restructuring of Gerling's US operations the Company's name was changed to Constitution Insurance Company and Constitution Reinsurance Corporation's name was changed to the Company's previous name of Gerling Global Reinsurance Corporation of America ("GGRCA"). The name changes were effective May 21, 1999.

On September 22, 1999, the Department approved a stock redemption plan whereby the Company redeemed its 500 shares of \$10,000 par value per share common capital stock and issued 20,000,000 shares of \$1 par value per share common capital stock, thereby increasing its capital stock from \$5,000,000 to \$20,000,000. As part of the restructuring, the Company then redeemed 15,800,000 of the newly issues shares for \$158,449,469. In 2001, the remaining 4,200,000 outstanding shares were contributed to GGRCA, making GGRCA the direct parent of the Company.

In 2000, the Company began writing direct business in addition to the business it assumed from GGRCA per the quota share agreement between the two companies. In the third quarter of 2002, the Company voluntarily went into run-off and ceased writing new or renewal business as did its direct parent, GGRCA. In addition, the Company's ultimate insurance parent, GKG ceased writing business in the fourth quarter of 2002.

On November 9, 2005, the Company's parent, GGRCA, changed its name to Global Reinsurance Corporation of America ("GRCA"). The Department approved the name change on November 15, 2005.

At December 31, 2006, Capital paid in was \$4,200,000 consisting of 4,200,000 shares of common stock at \$1 par value per share. Gross paid in and contributed surplus was \$47,972,137. Gross paid in and contributed surplus increased by \$3,217,974 during the examination period, as follows:

<u>Year</u>	<u>Description</u>	<u>Amount</u>
1/1/2003	Beginning gross paid in and contributed surplus	\$ 44,754,163
2003	Surplus contribution	<u>3,217,974</u>
12/31/2006	Ending gross paid in and contributed surplus	<u>\$ 47,972,137</u>

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 meets four times during each calendar year. At December 31, 2006, the board of directors was comprised of the following thirteen members:

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Michael Bluzer Bayside, NY	Vice President and Actuary, Global Reinsurance Corporation of America
Bard Bunaes Irvington, NY	President and Chief Executive Officer, Global Reinsurance Corporation of America
Wei Chez Brooklyn, NY	Vice President and Corporate Accounting Manager, Global Reinsurance Corporation of America
Dr. Jan Eickstaedt Cologne, Germany	External Director, Globale Ruckversicherungs- AG
James Fletcher Darien, CT	Senior Vice-President and Chief Actuary Global Reinsurance Corporation of America
Thomas Freudenstein Alfter, Germany	External Director, Globale Ruckversicherungs- AG
Burton Henry North Caldwell, NJ	Executive Vice President and Chief Financial Officer, Global Reinsurance Corporation of America
Thomas Hill Monmouth Junction, NJ	Senior Vice President Human Resources/Administration, Global Reinsurance Corporation of America
Dr. Achim Kann Munich, Germany	Chairman, Globale Ruckversicherungs- AG
Barry Keogh Hillsdale, NJ	Senior Vice President Claims, Global Reinsurance Corporation of America
Vincent Potts Long Valley, NJ	Senior Vice President Underwriting, Global Reinsurance Corporation of America
James Ready Syosset, NY	Vice President and Investment Accounting Manager, Global Reinsurance Corporation of America
David Smith Glen Head, NY	Executive Vice President and General Counsel, Global Reinsurance Corporation of America

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, 2006, the principal officers of the Company were as follows:

<u>Name</u>	<u>Title</u>
Bard Bunaes	President and Chief Executive Officer
James Fletcher	Senior Vice President and Chief Actuary
Burton Henry	Executive Vice President and Chief Financial Officer
David Smith	Executive Vice President and General Counsel

B. Territory and Plan of Operation

As of December 31, 2006, the Company was authorized to transact business in the District of Columbia and all states of the United States except Connecticut, Maine, Massachusetts, Minnesota, North Carolina and Wyoming. The Company voluntarily ceased writing all new and renewal business in 2002.

At December 31, 2006, the Company was licensed 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>
3	Accident and health
4	Fire
5	Miscellaneous property
6	Water damage
7	Burglary and theft
8	Glass
9	Boiler and machinery
10	Elevator
11	Animal
12	Collision
13	Personal injury liability
14	Property damage liability
15	Workers' compensation and employers' liability
16	Fidelity and surety
17	Credit
19	Motor vehicle and aircraft physical damage
20	Marine and inland marine
21	Marine protection and indemnity

The Company is also empowered to transact such workers' compensation insurance as may be incidental to the lines of business contemplated under paragraphs 20 and 21 of Section 1113(a) of the New York Insurance Law, including insurances described in the Longshoremen's and Harbor Workers' Compensation Act (Public Law No. 803, 69th Congress as amended; 33 USC Section 901 et seq. as amended).

Further, the Company is authorized, subject to statutory exception and charter exclusion, to reinsure risks of every kind or description, and to insure property or risks of every kind or description located outside of the United States, its territories and possessions, as provided in Section 4102(c) of the New York Insurance Law.

Based upon the lines of business for which the Company is licensed, and the Company's current capital structure, and pursuant to the requirements of Articles 13 and 41 of the New York Insurance Law, the Company is required to maintain a minimum surplus to policyholders in the amount of \$35,000,000.

The Company went into voluntary run-off in 2002. Beginning in 1999, the Company assumed business from its parent GRCA per a quota share agreement described in the reinsurance section of this report. Beginning in 2000 and ending in 2002, before the Company went into run-off, the Company wrote direct business concentrated in commercial multi-peril, other liability, private passenger auto liability, and auto physical damage lines. The Company ceded most of this business to its parent GRCA per a quota share agreement described in the reinsurance section of this report.

C. Reinsurance

The Company utilizes reinsurance accounting as defined in the NAIC Accounting Practices and Procedures Manual, Statements of Statutory Accounting Principles ("SSAP") No. 62 for all of its assumed reinsurance business. The Schedule F data as contained in the Company's annual statements filed for the years covered by this examination was found to properly reflect its reinsurance transactions.

Effective January 1, 1999, the Company entered into an assumption agreement with GRCA (then known as Constitution Reinsurance Corporation), whereby it transferred 100% of its in-force business as of the effective date to GRCA. As a result of this transfer and upon the advice from the

Department, GRCA's Schedule P was recast to reflect the assumption of the Company's insurance liabilities from January 1, 1997, (the effective date the Company commenced operations) going forward. Similarly, the Company's Schedule P has been recast removing all of the business assumed by GRCA. The Department approved this agreement on April 27, 1999.

Additionally, effective January 1, 1999, the Company entered into a quota share agreement with GRCA, whereby the Company assumed 3% of all policies in force, issued or renewed by GRCA during the contract term. The Department approved this agreement on April 27, 1999.

Effective January 1, 2000, the Company entered into a quota share agreement with GRCA, whereby the Company ceded 97% of its direct business written as of the effective date. The Department approved this agreement on June 21, 2000.

At December 31, 2006, the Company had a small amount of ceded external reinsurance in run-off. The total reinsurance recoverables under these treaties, at December 31, 2006, was \$3,180,000.

It should be noted that effective January 1, 2007, the 3% quota share assumption agreement with GRCA was cancelled and the liability assumed by the Company for the period of the agreement was returned to the books of the GRCA. Furthermore, the agreement whereby the Company ceded 97% of its direct business to GRCA was amended so that GRCA would assume 100% of the Company's direct business.

D. Holding Company System

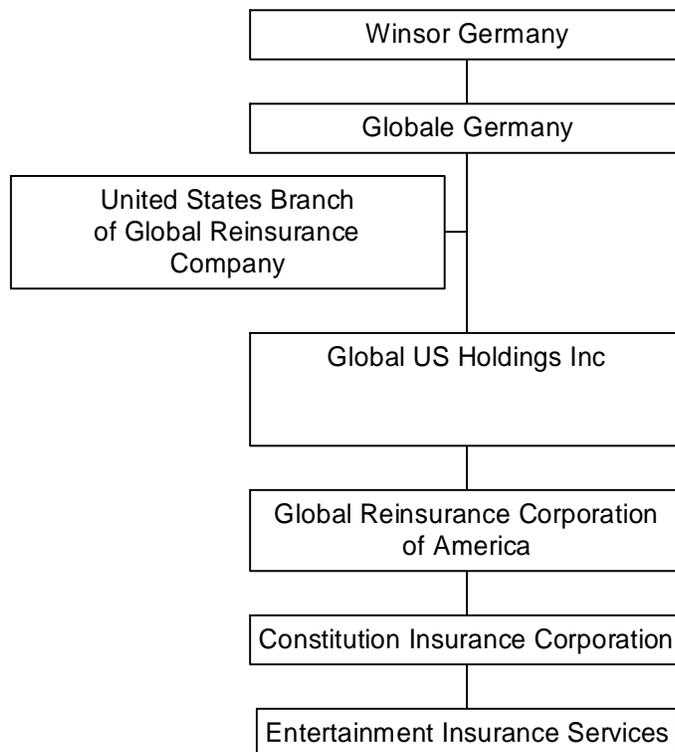
The Company is a member of a German holding company system known as the Globale Group. The group is comprised of a large number of related entities in Germany, as well as throughout the world. At December 31, 2006, ultimate control was held by the private group of Dr. Rolf Gerling. At December 31, 2006, the primary holding company was Winsor Vermaltungs-AG ("Winsor"). Winsor owns Globale Ruckversicherungs-AG ("GR"). Both are located in Cologne, Germany.

GR in turn owned Global U.S. Holdings, Incorporated ("GUSHI"). GUSHI served as the holding company for the group's United States reinsurance operations and is the direct parent Global Reinsurance Corporation of America ("GRCA"). GRCA is the direct parent of the Company.

The Company owned a shell subsidiary with no value called Entertainment Insurance Services ('EIS'). EIS was obtained as a result of legal action against a general agent who failed to remit premiums owed to the Company. EIS was subsequently dissolved as of September 21, 2007.

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 following is an abridged chart of the holding company system at December 31, 2006:



At December 31, 2006, the Company was party to the following agreements with other members of its holding company system:

Investment Service Agreement

The Company and its direct parent, GRCA, are party to an investment service agreement with Global U.S. Holdings, Incorporated (“GUSHI”). GUSHI is a New York corporation and the ultimate United States parent of the Company. Under the terms of the agreement, GUSHI provides investment management services to the Company and GRCA.

Expense Sharing Agreements

The Company is party to an expense sharing agreement, which was restated at November 1, 2005. The other parties to the agreement are the Company’s ultimate United States parent, GUSHI, its direct parent, GRCA, and affiliates the US Branch and Global International Reinsurance Company, Ltd., a Barbados Company. The agreement provides for GRCA to make available to the other companies the employees and facilities necessary for the conduct of their business which include but is not limited to: claims and underwriting services; accounting, legal, and IT services; assistance with report preparation; assistance with retrocessional programs; and human resource services.

Tax Sharing Agreement

The Company is party to a tax sharing agreement with its ultimate United States parent, GUSHI and direct parent GRCA. The agreement became effective August 3, 1999.

E. Significant Operating Ratios

As the Company has been in run-off status since mid 2002 many of the standard ratios involving premiums written or premiums earned do not provide relevant information and therefore have not been presented. The following ratios have been computed as of December 31, 2006, based upon the results of this examination:

Liabilities to liquid assets (cash and invested assets less investment in affiliates)	25.38%
Premiums in course of collection to surplus as regards policyholders	3.97%

The above ratios are within the bench mark ranges set forth in the Insurance Regulatory Information System of the National Association of Insurance Commissioners.

F. Accounts and Records

It was noted that the Company failed to meet the requirements of Section 1402(a) of the New York Insurance Law for each of the four years of the examination period. This section states:

“Before investing its funds in any other investments, every domestic insurer shall invest and maintain an amount equal to the greater of the minimum capital required by law or the minimum surplus to policyholders required to be maintained by law for a domestic stock corporation authorized to transact the same kinds of insurance, only in investments of the type specified in this section which are not in default as to principal or interest...”

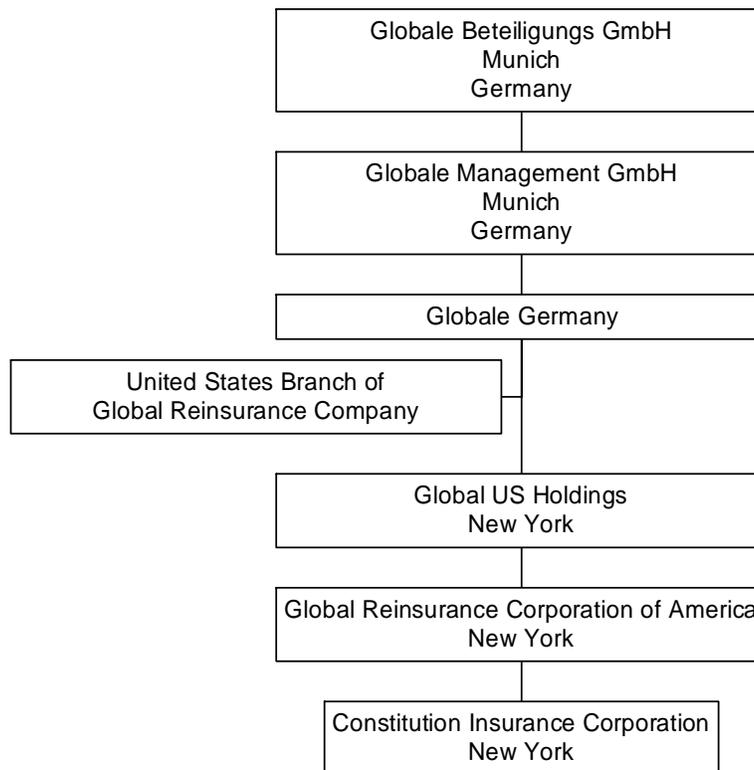
It is recommended that the Company take the necessary steps to ensure future compliance with Section 1402(a) of the New York Insurance Law.

G. Subsequent Events

There were significant events that have taken place subsequent to the examination period. A summary of these events is presented below;

1. On December 28, 2007, the Department approved a change of control, whereby Globale Beteiligungs GmbH (“GBG”) became the ultimate holding company replacing Winsor. Dr. Achim Kann maintains a controlling 51% interest in GBG. At the end of 2007 GBG is the ultimate holding company and is the owner of GR, who continues to own GUSHI, who owns GRCA, who is the 100% owner of the Company.

The following is an abridged chart of the holding company system at December 31, 2007, incorporating the changes described above:



2. The quota share agreement, effective January 1, 2000 whereby the Company ceded 97 percent of its net direct business to GRCA was amended with the ceding percentage adjusted to 100 percent. In effect all of the net direct business written by the Company has now been assumed by its parent, GRCA. This amendment took effect on January 1, 2007, and was approved by the Department in May 2007.
3. The quota share agreement, effective January 1, 1999, whereby the Company assumed three percent of GRCA's net assumed business was cancelled. All business assumed by the Company under this treaty was transferred back to GRCA. The result of the cancellation of this agreement and the amendment to the January 1, 2000 quota share agreement is to bring to zero the net loss liabilities of the Company as of January 1, 2007.
4. In March 2008 the Company received approval for an assumption agreement whereby GRCA would directly assume the Company's direct business. It should be noted that the assumption of a particular policy will not take place if it is objected to by any former policyholder with an open claim.

The overall purpose in altering the quota share agreements and implementing the assumption agreement is to reduce the Company to shell status in order to facilitate the sale of the Company.

3. Balance Sheet

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

	<u>Assets</u>	<u>Nonadmitted Assets</u>	<u>Net Admitted Assets</u>
Bonds	\$38,755,537		\$38,755,537
Cash, cash equivalents and short-term investments	2,112,605		2,112,605
Other invested assets	3,427,994		3,427,994
Receivable for securities	1,688		1,688
Investment income due and accrued	214,456		214,456
Uncollected premiums and agents' balances in the course of collection	2,612,064	\$1,170,558	1,441,506
Amounts recoverable from reinsurers	199,886		199,886
Net deferred tax asset	6,299,917	6,299,917	0
Receivables from parent, subsidiaries and affiliates	447,308		447,308
Accounts receivable miscellaneous	<u>176,793</u>	<u>0</u>	<u>176,793</u>
 Total assets	 <u>\$ 54,248,248</u>	 <u>\$7,470,475</u>	 <u>\$ 46,777,773</u>
 <u>Liabilities, Surplus and Other Funds</u>	 <u>Examination</u>	 <u>Company</u>	 Surplus Increase <u>(Decrease)</u>
Losses and loss adjustment expenses	\$11,646,000	\$ 9,343,583	\$(2,302,417)
Reinsurance payable on paid losses and loss adjustment expenses	(2,576,382)	(2,576,382)	
Commissions payable, contingent commissions and other similar charges	11,772	11,772	
Other expenses (excluding taxes, licenses and fees)	200,400	200,400	
Taxes, licenses and fees (excluding federal and foreign income taxes)	(52,500)	(52,500)	
Current federal and foreign income taxes	505,658	505,658	
Unearned premiums	51,231	51,231	
Provision for reinsurance	<u>641,053</u>	<u>641,053</u>	_____
 Total liabilities	 <u>\$10,427,232</u>	 <u>\$ 8,124,815</u>	 <u>\$(2,302,417)</u>
 <u>Surplus and Other Funds</u>			
Common capital stock	\$ 4,200,000	\$ 4,200,000	
Gross paid in and contributed surplus	47,972,137	47,972,137	
Unassigned funds (surplus)	<u>(15,821,596)</u>	<u>(13,519,179)</u>	<u>\$(2,302,417)</u>
 Surplus as regards policyholders	 <u>\$36,350,541</u>	 <u>\$38,652,958</u>	 <u>\$(2,302,417)</u>
 Total liabilities and surplus and other funds	 <u>\$46,777,773</u>	 <u>\$46,777,773</u>	

NOTE: The Internal Revenue Service has not performed any audits of the Company's federal income tax returns. The examiner is unaware of any potential exposure of the Company to any tax assessment and no liability has been established herein relative to such contingency.

4. LOSSES AND LOSS ADJUSTMENT EXPENSES

The examination liability for the captioned items of \$11,646,000 is \$2,302,417 more than the \$9,343,583 reported by the Company in its December 31, 2006 filed annual statement.

The examination liability stated above took into account the commutation by the Company's parent, GRCA of several assumed reinsurance contracts from January 1, 2007 through October 31, 2007. As indicated previously the Company had a quota share agreement in place under which it assumes three percent of GRCA's business.

Before consideration of the 2007 commutations, the examination's estimate of the Company's net loss and loss adjustment expenses ("LAE") was \$12,312,000. The consideration of the 2007 commutations resulted in lowering the estimated deficiency by \$666,000.

A revision in the unallocated loss adjustment expense reserve ("ULAE") represented \$456,436 of the overall deficiency of \$2,302,417. The ULAE represents a significant component of the Company's overall loss reserve deficiency.

The Company's filed ULAE in its 2006 annual statement was \$281,000. The analysis of this item determined that this figure was inadequate given the general expenses reported by the Company as well as CIC's run-off status. This was brought to the attention of the Company which revised its December 31, 2006 ULAE to \$737,436. This revision was reflected in the Company's September 30, 2007 quarterly statement. The Department accepted the Company's revised ULAE and incorporated it into the overall reserve analysis.

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

5. SUMMARY OF COMMENTS AND RECOMMENDATIONSITEMPAGE NO.A. Investments

It is recommended that the Company take the necessary steps to ensure future compliance with Section 1402(a) of the New York Insurance law.

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Respectfully submitted,

_____/s/_____
Marc Allen
Principal Insurance Examiner

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

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

_____/s/_____
Marc Allen

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

STATE OF NEW YORK
INSURANCE DEPARTMENT

I, Eric R. Dinallo, Acting Superintendent of Insurance of the State of New York, pursuant to the provisions of the Insurance Law, do hereby appoint:

Marc Allen

as proper person to examine into the affairs of the

CONSTITUTION INSURANCE COMPANY

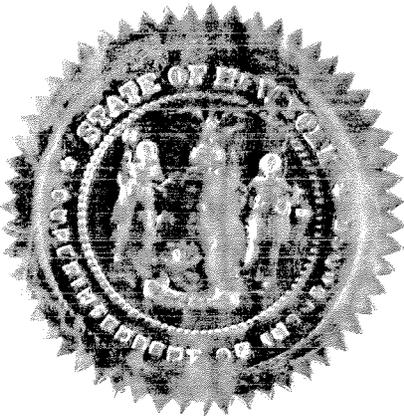
and to make a report to me in writing of the condition of the said

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 16th day of February, 2007



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

ERIC R. DINALLO
Acting Superintendent of Insurance