

REPORT ON EXAMINATION

OF THE

NIC INSURANCE COMPANY

AS OF

DECEMBER 31, 2004

DATE OF REPORT

JULY 7, 2006

EXAMINER

JAMES MURPHY

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

July 7, 2006

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 22425 dated October 13, 2005 attached hereto, I have made an examination into the condition and affairs of NIC Insurance Company as of December 31, 2004, and submit the following report thereon.

Wherever the designations "the Company" or "NIC" appear herein without qualification, they should be understood to indicate NIC 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 administrative offices located at 6 International Drive, Rye Brook, New York 10573.

1. SCOPE OF EXAMINATION

The previous examination was conducted as of December 31, 2000. This examination covered the four-year period from January 1, 2001 through December 31, 2004. 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, 2004. 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 under the laws of the State of New York on December 1, 1988 as the Pilot Insurance Company. It commenced business on October 17, 1989 and was renamed NIC Insurance Company effective January 23, 1990.

Capital paid in is \$5,000,000 consisting of 250 shares of \$20,000 par value per share common stock. Gross paid in and contributed surplus is \$36,000,000. Gross paid in and contributed surplus increased by \$25,000,000 during the examination period, as follows:

<u>Year</u>	<u>Description</u>	<u>Amount</u>
2001	Beginning gross paid in and contributed surplus	\$11,000,000
2003	Surplus contribution	<u>\$25,000,000</u>
	Total surplus contributions	<u>25,000,000</u>
2004	Ending gross paid in and contributed surplus	<u>\$36,000,000</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, 2004, the board of directors was comprised of the following sixteen members:

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Michael L. Civisca West Nyack, NY	President, Marine Division Navigators Management Company, Inc.
Terence N. Deeks Summit, NJ	Chairman, Navigators Insurance Company
Christopher C. Duca Rockville Centre, NY	President, Navigators Pro
Richard S. Eisdorfer Trumbull, CT	Senior Vice President and Chief Information Officer, Navigators Insurance Company
Stanley A. Galanski Ridgefield, CT	President, Navigators Insurance Company

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Noel Higgitt Menlo Park, CA	President, Navigators California Insurance Services
David E. Hope Ansty Sussex, Great Britian	Director, Navigators Management UK, Ltd.
Christopher A. Johnson Oakland, CA	Executive Vice President, Navigators California Insurance Services
Russell J. Johnson Seaford, NY	Senior Vice President, Navigators Management Company
John W. Jones Kingwood, TX	President, Navigators Insurance Services of Texas
Jane E. Keller Southport, CT	Senior Vice President and Chief Claims Officer, Navigators Insurance Company
Paul J. Malvasio Westport, CT	Executive Vice President and Chief Financial Officer, Navigators Insurance Company
Salvatore A. Margarella Staten Island, NY	Vice President and Treasurer, Navigators Insurance Company
Gregory D. Olson Seattle, WA	President, Navigators Insurance Services of Washington
Richard C. Rea Ockley, Surrey, Great Britian	Managing Director, Navigators Management UK, Ltd.
Bradley D. Wiley Ringwood, NJ	Senior Vice President and Corporate Secretary Navigators Insurance Company

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, 2004, the principal officers of the Company were as follows:

<u>Name</u>	<u>Title</u>
Stanley A. Galanski	President
Bradley D. Wiley	Senior Vice President and Secretary
Salvatore A. Margarella	Vice President and Treasurer
Paul J. Malvasio	Executive Vice President and Chief Financial Officer
Richard S. Eisdorfer	Senior Vice President
Jane E. Keller	Senior Vice President
Ramona L. Eiseman	Vice President
Christopher M. Steinbach	Vice President

B. Territory and Plan of Operation

As of December 31, 2004, the Company was licensed to write business in New York. The Company underwrites its business on a surplus lines basis in various states. 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>
3	Accident & health
4	Fire
5	Miscellaneous property damage
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 empowered to transact such workers' compensation insurance as may be incident to coverages 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.

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 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 \$4,400,000.

The Company did not write any business in New York during the exam period. The following schedule shows the direct premiums written by the Company for the period under examination:

<u>Calendar Year</u>	<u>Total United States</u>
2001	\$ 15,553,772
2002	\$ 68,461,490
2003	\$120,111,390
2004	\$140,751,488

C. Reinsurance

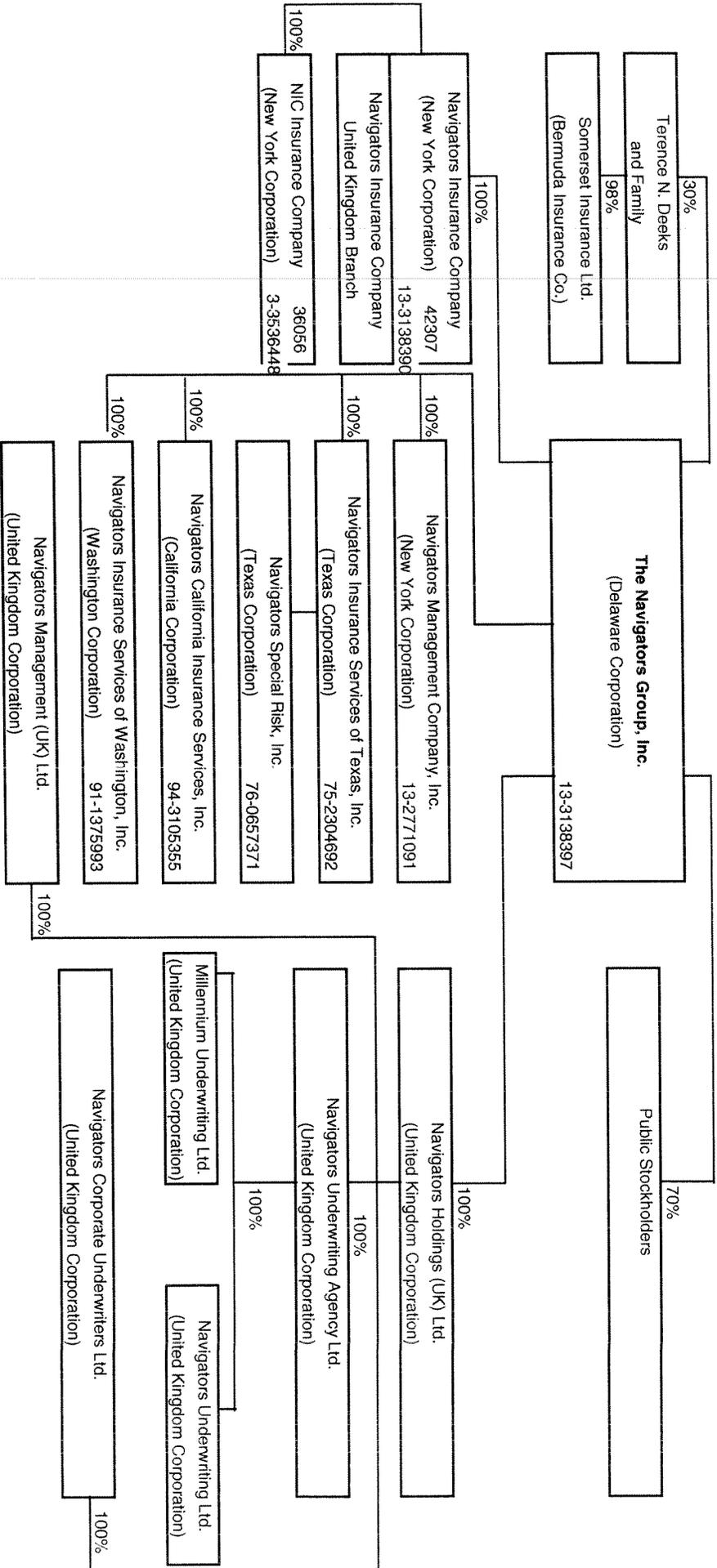
The Company did not assume any business during the examination period. The Company cedes 100% of its business to its parent, Navigators Insurance Company pursuant to the terms of an inter-company reinsurance agreement. Effective January 1, 1999, the Company transferred all of its outstanding losses, loss adjustment expenses and unearned premiums to Navigators Insurance Company pursuant to a commutation agreement. The agreement was approved by the Department.

D. Holding Company System

The Company is a member of the Navigators Group, Inc. The Company is a wholly-owned subsidiary of Navigators Insurance Company, a New York corporation, which is ultimately controlled by the Navigators Group, Inc., which in turn is 30% owned by Terence N. Deeks and family.

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 a chart of the holding company system at December 31, 2004:



At December 31, 2004, 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 the provisions of Department Circular Letter No. 33 (1979). The agreement was effective December 31, 1983 and was amended numerous times to add various participants and to amend various terms and conditions.

Inter-Company Reinsurance Agreement

As noted in Section 2C of this report, the Company participates in an inter-company reinsurance agreement whereby the Company cedes 100% of its written premiums to its parent company, Navigators Insurance Company. The agreement was effective January 1, 1999 and was approved by the Department pursuant to the provisions of Section 1505 of the New York Insurance Law.

Agency Agreement

The Company participates in an agency agreement with Navigators Management Company (“NMC”). Pursuant to the terms of the agreement NMC underwrites and services various lines of business on behalf of the Company. The agreement was effective January 1, 2002 and was approved by the Department pursuant to the provisions of Section 1505 of the New York Insurance Law.

Agency Agreement

The Company participates in an agency agreement with Navigators California Insurance Services (“NCIS”). Pursuant to the terms of the agreement NCIS underwrites and services business on behalf of the Company. NCIS specializes in construction liability insurance. The agreement was effective January 1, 2002 and was approved by the Department pursuant to the provisions of 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 its parent, Navigators Insurance Company. Therefore these ratios are not relevant.

3. FINANCIAL STATEMENTS

A. Balance Sheet

The following shows the assets, liabilities and surplus as regards policyholders as of December 31, 2004 as determined by this examination and as reported by the Company:

<u>Assets</u>	<u>Assets</u>	Assets Not <u>Admitted</u>	Net Admitted <u>Assets</u>
Bonds	\$43,855,266	\$0	\$43,855,266
Cash, cash equivalents and short-term investments	8,639,158	0	8,639,158
Investment income due and accrued	473,766	0	473,766
Uncollected premiums and agents' balances in the course of collection	16,876,257	0	16,876,257
Receivables from parent, subsidiaries and affiliates	<u>3,934</u>	<u>0</u>	<u>3,934</u>
Total assets	<u>\$69,848,381</u>	<u>\$0</u>	<u>\$69,848,381</u>

Liabilities, Surplus and Other FundsLiabilities

Losses and loss adjustment expenses	\$	0
Other expenses (excluding taxes, licenses and fees)		21,250
Current federal and foreign income taxes		1,128,257
Ceded reinsurance premiums payable (net of ceding commissions)		16,876,257
Payable for securities		<u>230,729</u>
Total liabilities		\$18,256,494

Surplus and Other Funds

Common capital stock	\$ 5,000,000	
Gross paid in and contributed surplus	36,000,000	
Unassigned funds (surplus)	<u>10,591,887</u>	
Surplus as regards policyholders		<u>51,591,887</u>
Total liabilities, surplus and other funds		<u>\$69,848,381</u>

NOTE: The Internal Revenue Service has completed its audits of the Company's consolidated federal income tax returns through tax year 1994. All material adjustments, if any, made subsequent to the date of examination and arising from said audits, are reflected in the financial statements included in this report. The Internal Revenue Service has not yet begun to audit tax returns covering tax years 1995 through 2004. 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.

B. Underwriting and Investment Exhibit

Surplus as regards policyholders increased \$28,676,738 during the four-year examination period January 1, 2001 through December 31, 2004, detailed as follows:

Underwriting Income

Premiums earned		\$0
Deductions:		
Losses incurred	\$0	
Loss adjustment expenses incurred	0	
Other underwriting expenses incurred	0	
Total underwriting deductions		<u>0</u>
Net underwriting gain or (loss)		\$0

Investment Income

Net investment income earned	\$6,368,336	
Net realized capital gain	<u>(797,280)</u>	
Net investment gain or (loss)		5,571,056

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>938</u>	
Total other income		<u>938</u>
Net income before dividends to policyholders and before federal and foreign income taxes		\$5,571,994
Dividends to policyholders		<u>0</u>
Net income after dividends to policyholders but before federal and foreign income taxes		\$5,571,994
Federal and foreign income taxes incurred		<u>1,895,257</u>
Net Income		<u>\$3,676,737</u>

C. Capital and Surplus Accounts

Surplus as regards policyholders per report on examination as of December 31, 2000			\$22,915,150
	<u>Gains in</u>	<u>Losses in</u>	
	<u>Surplus</u>	<u>Surplus</u>	
Net income	\$3,676,739	\$0	
Capital paid in	<u>\$25,000,000</u>	<u>0</u>	
Total losses	<u>\$28,676,739</u>	<u>\$0</u>	
Net increase (decrease) in surplus			<u>28,676,739</u>
Surplus as regards policyholders per report on examination as of December 31, 2004			<u>\$51,591,889</u>

4. LOSSES AND LOSS ADJUSTMENT EXPENSES

The examination liability of \$0 is the same as the amount reported by the Company in its 2004 filed annual statement. As noted in Section 2C of this report, the Company cedes 100% of its business to its parent company, Navigators Insurance Company.

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:

- A. Sales and advertising
- B. Underwriting
- C. Rating
- D. Claims and complaint handling

No problem areas were encountered.

6. COMPLIANCE WITH PRIOR REPORT ON EXAMINATION

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

<u>ITEM</u>		<u>PAGE NO.</u>
A	<u>Holding Company System</u>	
i.	It was recommended that the Company file all of the required parts of its annual holding company registration statements in a timely manner pursuant to the provisions of Part 80-1.4 of Department Regulation 52. The Company has complied with this recommendation.	8
ii.	It is recommended that the Company submit all inter-company agreements and their amendments to this Department for our on-disapproval in a timely manner pursuant to the provisions of Section 1505(d)(3) of the New York Insurance Law. The Company has complied with this recommendation.	10-12

7. SUMMARY OF COMMENTS AND RECOMMENDATIONS

There are no comments or recommendations as a result of this examination.

Appointment No 22425

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

NIC INSURANCE COMPANY

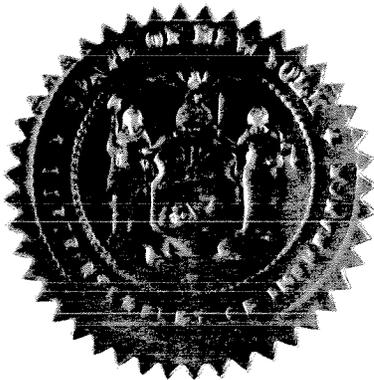
and to make a report to me in writing of the condition of the said

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 13th day of October, 2005



A handwritten signature in cursive script, appearing to read "Howard Mills", written over a horizontal line.

HOWARD MILLS
Superintendent of Insurance