

REPORT ON EXAMINATION
OF THE
STEWART TITLE INSURANCE COMPANY
AS OF
DECEMBER 31, 2003

DATE OF REPORT

JUNE 18, 2004

EXAMINER

MOSES EGBON, C.F.E.

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

June 18, 2004

Honorable Gregory V. Serio
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 22136 dated January 30, 2004 attached hereto, I have made an examination into the condition and affairs of the Company as of December 31, 2003, and submit the following report thereon.

The examination was conducted at the Company's administrative office located at 300 East 42nd Street, New York, New York 10017.

Wherever the designations "Stewart Title" or "the Company" appear herein without qualification, they should be understood to indicate Stewart Title Insurance Company.

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

1. SCOPE OF EXAMINATION

The previous examination was conducted as of December 31, 1998. This examination covered the covered five-year period from January 1, 1999 through December 31, 2003. Transactions 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 certified 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:

- History of the Company
- Management and control
- Corporate records
- Fidelity bonds and other insurance
- Officers' and employees' welfare and pension plans
- Territory and plan of operation
- Market conduct activities
- Growth of Company
- Business in force
- Loss experience
- Reinsurance
- Accounts and records

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 provisions of Article 64 of the New York Insurance Law on October 26, 1987. It became licensed on December 2, 1987 and commenced business on the same date.

As of the examination date, the Company's paid in capital was \$1,100,000, comprised of 100,000 shares of Class A common stock with a par value of \$2 per share and 90,000 shares of Class B common stock with a par value of \$10 per share. Gross paid in and contributed surplus increased by \$250,000 during the examination period as follows:

<u>Year</u>	<u>Description</u>	<u>Amount</u>
1998	Beginning gross paid in and contributed surplus	\$11,862,500
1999	Surplus contribution	<u>250,000</u>
2003	Ending gross paid in and contributed surplus	<u>\$12,112,500</u>

During the examination period, the Company paid \$9,080,020 cash dividends to its parent and such dividends were in compliance with Section 6407 of the New York Insurance Law.

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 seven or more than eleven members. The Board met four times during each calendar year. As of December 31, 2003, the board of directors was comprised of the following nine members:

<u>Name and Residence</u>	<u>Principal Occupation</u>
Peter C. Haeffner, Jr. Garden City, NY	Partner and Managing Director, Real Estate Trade Advisor LLC

<u>Name and Residence</u>	<u>Principal Occupation</u>
James I. Hisiger, Esq. Armonk, NY	Partner, Latham and Watkins
Malcolm Morris Houston, TX	President and CEO, Stewart Title Guaranty Company
Carlross Morris Houston, TX	Executive Committee Chairman, Stewart Title Guaranty Company
Stewart Morris, Jr. Houston, TX	Chairman, Stewart Title Guaranty Company
Paul A. Mucci Manhasset, NY	Senior Vice President, Lend Lease Real Estate Investments, Inc.
Richard A. Nardi, Esq. Armonk, NY	Partner, Brown Raysman Millstein Felder and Steiner LLP
Michael B. Skalka Katy, TX	Senior Vice President and General Counsel, Stewart Title Guaranty Company
John F. Welling Rye, NY	President and Chief Operating Officer, Stewart Title Insurance Company

A review of the minutes of all meetings of the board of directors' meetings held during the examination period indicated that the meetings were generally well attended and each board member had 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>
John F. Welling	President
Julie A. Curlen	Secretary
Emily Thai De Rago	Treasurer

B. Territory and Plan of Operation

As of December 31, 2003, the Company was authorized to transact title insurance as defined in the numbered paragraph 18 of Section 1113(a) of the New York Insurance Law. The Company was authorized to write title insurance business in the states of New York and California.

During the examination period, the Company issued title insurance policies in New York State only. The following schedule shows the direct premiums written by the Company during the examination period:

DIRECT PREMIUMS WRITTEN

<u>Calendar Year</u>	<u>New York State</u>
1999	\$ 69,308,202
2000	\$ 63,870,989
2001	\$ 75,224,686
2002	\$106,080,692
2003	\$141,782,087

Based upon the kind of insurance for which the Company is licensed, and the current capital structure, and pursuant to the requirements of Articles 13 and 64 of the New York Insurance Law, the Company is required to maintain a minimum surplus to policyholders in the amount of \$500,000.

The Company writes most of its business through title agents, who are compensated at a commission rate ranging from 80% to 85% of gross premiums written.

C. Reinsurance
Assumed

During the examination period, the Company assumed minimal reinsurance business on a facultative basis. It is mainly a direct writer, and most of its direct business is generated through title agents.

Ceded

The Schedule F data contained in the Company's annual statements filed for the years within the examination period was found to accurately reflect the reinsurance transactions.

The examiner reviewed all ceded reinsurance contracts in effect at December 31, 2003. The agreements meet the requirements of Section 1308 of the New York Insurance Law. All reinsurance is on a facultative basis.

D. Holding Company System

The Company is a wholly-owned subsidiary of Stewart Title Guaranty Company, a State of Texas domicile, which is ultimately controlled by Stewart Information Services Corp., a Delaware holding company.

A review of the holding company registration statements filed with the 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.

As of the examination date, the Company was a party to the following agreements with affiliated entities:

1. Consolidated Federal Income Tax Return Settlement Agreement

Effective January 1, 1974, the holding company entered into a consolidated federal income tax return settlement agreement. The agreement was subsequently amended on January 1, 1987. After Stewart Title Insurance Company was incorporated on October 26, 1987, it became a party to the above tax agreement. However, the Company could not provide any documentation to indicate that the agreement was filed with the Department pursuant to Department Circular Letter 33 (1979) which provides that:

“...every domestic insurer is directed to notify this Department within 60 days of this circular letter if it participates in a consolidated tax return and to submit a copy of its tax allocation agreement with such notification. Any domestic insurer which currently does not participate in a consolidated tax return shall file a copy of its tax allocation agreement with this Department within 30 days of electing to do so. Furthermore, notification to this Department should be given within 30 days of any amendment to or termination of a tax allocation agreement.”

It is recommended that the Company file its consolidated federal income tax return settlement agreement with the Department in compliance with the provisions of Department Circular Letter #33 (1979).

2. Facultative Reinsurance Agreements.

In 1996 and 1997, the Company entered into two facultative reinsurance agreements with affiliated entities. The agreements allow the Company to cede title insurance business to and assume such business from affiliates. The agreements were filed in accordance with 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

The following ratios have been computed as of December 31, 2003, based upon the results of this examination:

Net premiums written in 2003 to surplus as regards policyholders	9.1
Liabilities to liquid assets (cash and invested assets less investments in affiliates)	71.17%
Premiums in course of collection to surplus as regards policyholders	10.18%

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	\$ 26,350,663	5.68%
Other underwriting expenses incurred	433,984,764	93.57
Net underwriting gain	<u>3,465,852</u>	<u>.75</u>
Premiums earned	<u>\$463,801,279</u>	<u>100.00%</u>

G. Contingent Liabilities

In November 2002, the Company was served as a defendant in a class action lawsuit alleging that the Company, along with some other underwriters, directly and through its agents, routinely collected

excess premiums in connection with refinance transactions. Management indicated that the Company's potential exposure cannot be reasonably estimated at this time.

H. Agent Defalcations

Management indicated that some improprieties were committed by a few agents, resulting in agent defalcations. These acts resulted in losses totaling approximately \$1.6 million during 1999 through 2001. Company management indicated that it is actively pursuing each case to recover the losses involved, including litigation, voluntary repayment agreements from agents, and filing complaints with law enforcement authorities.

3. FINANCIAL STATEMENTS

A Balance Sheet

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

<u>Ledger Assets</u>	<u>Assets</u>	Non-Admitted <u>Assets</u>	Net-Admitted <u>Assets</u>
Bonds	\$40,317,494	\$	\$ 40,317,494
Cash on hand and on deposit	5,948,441		5,948,441
Other invested assets	344,472	214,868	129,604
Premiums and agents balances	1,686,498	59,000	1,627,498
Net deferred tax asset	2,447,806	2,057,502	390,304
Electronic data processing equipment	268,625		268,625
Interest income due and accrued	669,405		669,405
Receivables from parent, subsidiaries and affiliates	41,721		41,721
Other assets non-admitted	1,588,798	1,588,798	
Prepaid expenses	290,174	290,174	
Title plant	67,131		67,131
Deposits	170,816		170,816
Accounts receivable	13,118	3,453	9,665
Notes receivable	<u>9,576</u>	<u>9,576</u>	<u>0</u>
Totals	<u>\$53,864,075</u>	<u>\$ 4,223,371</u>	<u>\$ 49,640,704</u>

Liabilities

Known claim reserve	\$ 9,490,249
Statutory premium reserve	15,956,870
Other expenses	2,867,590
Taxes, licenses and fees	86,592
Federal and foreign income taxes	4,878,635
Amounts withheld or retained by company for account of others	697
Payable to parent, subsidiaries and affiliates	160,645
Other liabilities	<u>206,943</u>
Total liabilities	\$ 33,648,221

Surplus and Other Funds

Common capital stock	\$ 1,100,000
Gross paid in and contributed surplus	12,112,500
Unassigned funds (surplus)	<u>2,779,983</u>
Surplus as regards policyholders	<u>15,992,483</u>
Total liabilities, surplus and other funds	<u>\$ 49,640,704</u>

NOTE: The Company has never been audited by the Internal Revenue Service. 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. Operations and Investment Exhibit

Surplus as regards policyholders increased \$1,056,001 during the five-year examination period from January 1, 1999 through December 31, 2003, detailed as follows:

Statement of Income

Operating Income

Title insurance and related income	\$446,927,774	
Escrow and settlement services	470,610	
Other title fees and service charges	<u>16,402,895</u>	
Total operating income		\$463,801,279

Deductions:

Losses and loss adjustment expenses incurred	\$ 26,350,663	
Operating expenses incurred	<u>433,984,764</u>	
Total operating deductions		<u>460,335,427</u>
Net operating gain		\$3,465,852

Investment Income

Net investment income earned	\$9,213,240	
Net realized capital gains	<u>372,119</u>	
Net investment gain		9,585,359
Other miscellaneous income		<u>333,704</u>
Net income before federal and foreign income taxes incurred		\$13,384,915
Federal and foreign income taxes incurred		<u>5,888,774</u>
Net income		<u>\$7,496,141</u>

Capital and Surplus Account

Surplus as regards policyholders, per report on examination as of December 31, 1998			\$14,936,482
	<u>Gains in Surplus</u>	<u>Losses in Surplus</u>	
Net income	\$7,496,141	\$	
Net unrealized capital gain	2,534,678		
Change in non-admitted assets		2,677,453	
Change in net deferred tax	391,828		
Paid in surplus	250,000		
Dividends to stockholders		9,080,020	
Extra-ordinary amount of tax	150,702		
Cumulative effect of change in accounting principles	<u>1,990,125</u>	<u>0</u>	
Total increases and decreases	<u>\$12,813,474</u>	<u>\$11,757,473</u>	
Net increase to surplus as regards policyholders			<u>1,056,001</u>
Surplus as regards policyholders, per report on examination as of December 31, 2003			<u>\$15,992,483</u>

4. KNOWN CLAIMS RESERVE

The examination liability for the captioned item of \$9,490,249 is the same as reported by the Company as of December 31, 2003. 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 practices and fulfills its contractual obligations to policyholders and claimants. The review was general in nature and is not to be construed to encompass the generally more precise scope of a market conduct investigation.

A general review was directed at the Company's underwriting practices. The examiner reviewed a sample of title insurance policies issued to determine if the premiums charged to insured were in compliance with filed rates. Based on this review, it appears that some of the Company's agents might have charged an incorrect title insurance premiums rate on some mortgage refinance transactions. It appears that the rate manual is unclear in this area. It is recommended that the Company establish procedures to ensure that the premiums charged by its agents are accurate.

6. COMPLIANCE WITH PRIOR REPORT ON EXAMINATION

The prior report on examination contained no comments or recommendations.

7. SUMMARY OF COMMENTS AND RECOMMENDATIONS

<u>ITEM</u>	<u>PAGE NO.</u>
<p>A. <u>Holding Company System</u></p> <p>It is recommended that the Company file its consolidated federal income tax return settlement agreement with the Department in compliance with the provisions of Department Circular Letter # 33 (1979).</p>	7
<p>B. <u>Contingent Liabilities</u></p> <p>In November 2002, the Company was served as a defendant in a class action lawsuit alleging that the Company along with some other underwriters directly and through its agents routinely collected excess premiums in connection with refinance transactions. Management indicated that the Company's potential exposure cannot be reasonably estimated at this time.</p>	8
<p>C. <u>Agent Defalcations</u></p> <p>Improprieties were committed by a few of the Company's agents. These acts resulted in the Company's title insurance losses. The Company's management indicated that it is actively pursuing each case to recover the losses involved.</p>	9
<p>D. <u>Market Conduct Activities</u></p> <p>It appears that the rate manual is unclear in the mortgage refinance area.</p> <p>It is recommended that the Company establish procedures to ensure that the premiums charged by its agents are accurate.</p>	14 14

Respectfully submitted,

_____/S/_____
Moses Egbon, C.F.E.
Senior Insurance Examiner

STATE OF NEW YORK)
)SS.
)
COUNTY OF NEW YORK)

MOSES EGBON, being duly sworn, deposes and says that the foregoing report submitted by him is true to the best of his knowledge and belief.

_____/S/_____
Moses Egbon

Subscribed and sworn to before me

this _____ day of _____ 2004.

STATE OF NEW YORK
INSURANCE DEPARTMENT

I, GREGORY V. SERIO, Superintendent of Insurance of the State of New York,
pursuant to the provisions of the Insurance Law, do hereby appoint:

Moses Egbon

as proper person to examine into the affairs of the

STEWART TITLE INSURANCE COMPANY

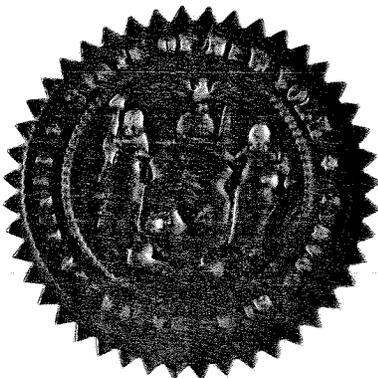
and to make a report to me in writing of the condition of the said

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 30th day of January, 2004




GREGORY V. SERIO
Superintendent of Insurance