

REPORT ON EXAMINATION
OF THE
NIC INSURANCE COMPANY
AS OF
DECEMBER 31, 2000

DATE OF REPORT

JULY 1, 2003

EXAMINER

ERWIN ROCA

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

George E. Pataki
Governor

Gregory V. Serio
Superintendent

July 1, 2003

Honorable Gregory 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 21804 dated November 27, 2001, attached hereto, I have made an examination into the financial condition and affairs of NIC Insurance Company as of December 31, 2000, and submit the following report.

The examination was conducted at the Company's home office located at One Penn Plaza, New York, New York 10119-0002.

Where the designations "Company" and "NIC" appears herein without qualification, they should be understood to indicate the NIC Insurance Company.

Where the designation "the Department" appears herein without qualification, it should be understood to indicate the New York Insurance Department.

1. SCOPE OF EXAMINATION

The previous examination of the Company was conducted as of December 31, 1995. This examination covered the five-year period from January 1, 1996 through December 31, 2000. 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, 2000, a review of income and disbursements deemed necessary to accomplish 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 Company
- Management and control
- Corporate records
- Fidelity bond and other insurance
- Territory and plan of operation
- Growth of Company
- Business in force by states
- Reinsurance
- Accounts and records
- Financial statements

A review was made to ascertain what action was taken by the Company with regard to the 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 New York on December 1, 1988, as the Pilot Insurance Company and began business on October 17, 1989. Active underwriting operations commenced in 1990 and effective January 23, 1990, the Company was renamed NIC Insurance Company.

All outstanding capital stock of the Company is owned 100% by Navigators Insurance Company, which in turn is owned by the Navigators Group, Inc., a publicly traded holding company, 51% owned by Terence N. Deeks and family.

At December 31, 2000, the Company's paid in capital was \$5,000,000, consisting of 250 shares of common stock at \$20,000 par value per share, and its gross paid in and contributed surplus was \$11,000,000. On December 18, 1997, the Company amended its charter to increase its paid in capital from \$2,500,000 to \$5,000,000 and to change its capital structure from 150 shares of common stock of \$10,000 par value per share, and 100 shares of preferred stock at \$10,000 par value per share, to its present capital structure. The increase in paid in capital was offset by a decrease in paid in and contributed surplus.

A. Management

Pursuant to the Company's charter and by-laws, a board of directors consisting of not less than thirteen but not more than twenty-one members shall exercise corporate powers. As of December 31, 2000, the board of directors was comprised of the following thirteen members:

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Michael L. Civisca New City, NY	Vice President, Somerset Marine, Inc.

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
John A. Cooper Kent, UK	Managing Director, Mander, Thomas & Cooper
Brian R. Deans Berkeley, CA	President, SIS of California, Inc.
Terence N. Deeks Summit, NJ	Chairman of the Board, President and Chief Executive Officer Navigators Insurance Company and NIC Insurance Company
Richard S. Eisdorfer Trumbell, CT	Senior Vice President, Navigators Insurance Company and NIC Insurance Company
Noel Higgitt Menlo Park, CA	President, Anfield Insurance Services, Inc.
Christopher A. Johnson Martinez, CA	Vice President, SIS of California, Inc.
Russel J. Johnson Seaford, NY	Senior Vice President, Somerset Marine, Inc.
John W. Jones Kingwood, TX	President, SIS of Texas, Inc.
Salvatore A. Margarella Staten Island, NY	Vice President and Treasurer, Navigators Insurance Company and NIC Insurance Company
James V. McGuire Essex Falls, NJ	Senior Vice President, Somerset Marine, Inc.
Gregory D. Olson Seattle, WA	President, SIS of Washington, Inc.
Bradley D. Wiley Ringwood, NJ	Senior Vice President, Chief Financial Officer and Secretary Navigators Insurance Company NIC Insurance Company

The board met four times during each calendar year under examination. The minutes of all meetings of the board of directors held during the examination period were reviewed. The meetings were generally well attended and each of the directors had a satisfactory attendance record.

The principal officers of the Company as of December 31, 2000 were as follows:

<u>Name</u>	<u>Title</u>
Terence N. Deeks	Chairman of the board, President and Chief Executive Officer
Richard S. Eisdorfer	Senior Vice President
Bradley D. Wiley	Senior Vice President, Chief Financial Officer and Secretary
Salvatore Margarella	Vice President and Treasurer

B. Territory and Plan of Operation

As of December 31, 2000, the Company is licensed to conduct business in New York. The Company underwrites a small book of surplus lines business in various states and pursuant to an intercompany reinsurance agreement, cedes 100% of its gross writings to Navigators Insurance Company.

As of December 31, 2000, 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>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

<u>Paragraph</u>	<u>Kind of Insurance</u>
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), including insurances described in the Longshoremen's and Harbor Workers' Compensation Act (Public Law No. 803, 69 Cong. as amended; 33 USC Section 901 et seq. as amended).

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

<u>Year</u>	<u>Direct Premiums Written</u>
1996	\$3,708,583
1997	\$4,612,596
1998	\$3,278,923
1999	\$2,613,569
2000	\$4,210,846

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, NIC Insurance Company is required to maintain a surplus to policyholders in the amount of \$4,400,000. Surplus to policyholders as of December 31, 2000 was \$22,915,149.

NIC's direct writings are acquired through an affiliated entity, Anfield Insurance Services, Inc., which produces property and inland marine business for the Company.

C. Reinsurance

Effective January 1, 1999, NIC ceded 100% of its business written to Navigators Insurance Company (“Navigators”). Concurrent with the effective date of this reinsurance agreement, NIC transferred all of its outstanding losses, loss adjustment expenses and unearned premiums as of December 31, 1998 to Navigators pursuant to a commutation agreement, which was approved by this Department.

Prior to January 1, 1999, NIC and Navigators were party to a pooling agreement whereby NIC ceded 100% of its business written or assumed to Navigators. Navigators, in turn, ceded 10% of its net business (including the business it assumed from NIC) to NIC.

For the year ended December 31, 2000, NIC ceded to Navigators gross direct premiums written in the amount of \$4,210,846.

The Company is not a party to any other reinsurance agreements.

D. Holding Company System

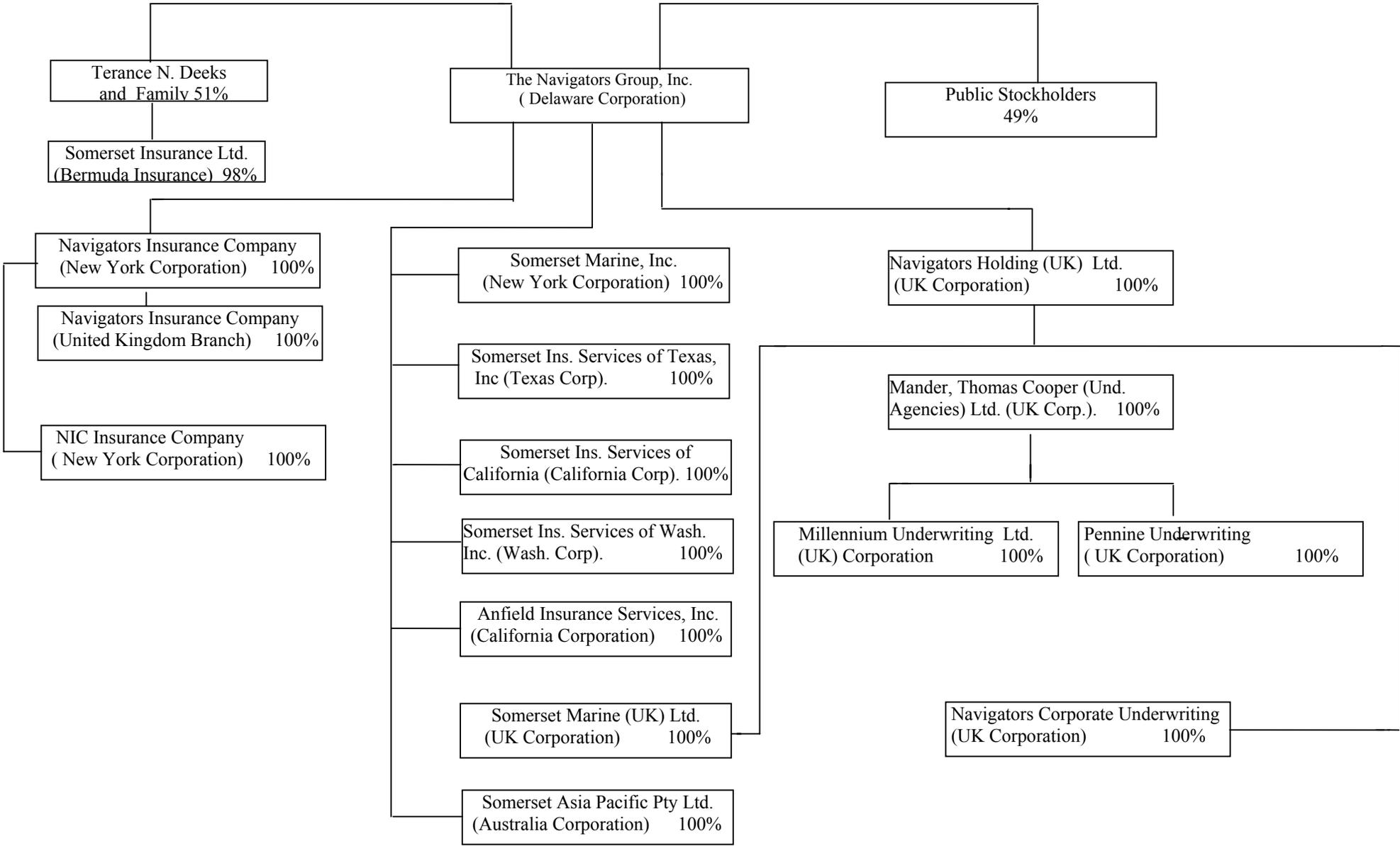
The Company is a wholly-owned subsidiary of Navigators Insurance Company, a New York domiciled insurer. Navigators, in turn, is a wholly-owned subsidiary of the Navigators Group, Inc., a publicly traded holding company domiciled in the State of Delaware. The Navigators Insurance Group, Inc. is 51% owned by Terence N. Deeks and family, who have been deemed by the Department as the ultimate owners.

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 except for the 2000 statement. Pursuant to Part 80-1.4 of Department Regulation 52:

“All controlled insurers are required to file an annual holding company registration statement (Form HC-1) within 120 days following the end of its ultimate holding company’s fiscal year, including an audited consolidated balance sheet and related consolidated statements of income and surplus for the ultimate holding company and each significant person within the holding company system”

The Company did not file an audited consolidated balance sheet as of December 31, 2000 for the ultimate owners until June 7, 2001. It is 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 following chart sets forth the interrelationships among the members of the holding company system at December 31, 2000:



At December 31, 2000, NIC participated in the following agreements with member of the holding company system:

1. Underwriting Management Agreement

Effective January 1, 1995, the Company was a party to an underwriting management agreement with Anfield Insurance Services Incorporated (“Anfield”). Anfield is a non-marine underwriting agency, which is based in San Francisco. This agency specializes in underwriting general liability coverage to small artisan and general contractors on the West Coast. On April 2, 1999, Anfield was purchased by the Navigators Group, Inc. and therefore became an affiliate of the Company. This agreement was not submitted to this Department upon the acquisition of Anfield by the Navigators Group, Inc.

Section 1505(d)(3) of the New York Insurance Law provides that:

“Transactions involving the rendering of services on a regular or systematic basis between a domestic controlled insurer and any person in its holding company system may not be entered into unless the insurer has notified the superintendent in writing of its intention to enter into any such transaction at least thirty days prior thereto, or such shorter period as he may permit, and he has not disapproved it within such period.”

Subsequent to the date of this examination, the Company submitted the underwriting management agreement to this Department and it was non-disapproved by letter dated July 19, 2002. It is recommended that the Company submit all inter-company agreements to this Department for our non-disapproval in a timely manner pursuant to the provisions of Section 1505(d) of the New York Insurance Law.

It is noted that on April 25, 2001, Anfield changed its name to Navigators California Insurance Services, Inc.

2. Reinsurance Agreements with Affiliated Entities

The Company cedes 100% of its business written to Navigators pursuant to a reinsurance agreement, as described in Section 2C herein. The reinsurance agreement was submitted to this Department and was non-disapproved pursuant to the provisions of Section 1505(d)(2) of the New York Insurance Law.

3. Tax Allocation Agreement (“Agreement”)

Effective December 31, 1983, the Company files a consolidated federal income tax return with its parent, The Navigators Group, Inc. pursuant to a tax allocation agreement. The tax allocation agreement was submitted to this Department and was non-disapproved pursuant to the provisions of Section 1505(d) of the New York Insurance Law.

Effective January 2, 2000, the tax allocation agreement was amended to add the names of two affiliates; however, this amendment was not submitted to this Department for non-disapproval prior to implementation. Subsequent to the date of this examination, the Company submitted the amendment to the tax allocation agreement to this Department and it was non-disapproved by letter dated April 6, 2002. It is recommended that the Company submit all amendments to its inter-company agreements to this Department for our non-disapproval in a timely manner pursuant to the provisions of Section 1505(d) of the New York Insurance Law.

E. Abandoned Property Law

Section 1316 of the New York State 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 State Abandoned Property Law.

F. Significant Operating Ratios

The following ratios have been computed as of December 31, 2000, based upon the results of this examination:

Net premiums written in 2000 to surplus as regards policyholders	0.0 to 1
Liabilities to liquid assets (cash and invested assets less investment in affiliates)	4.0%
Premiums in course of collection to Surplus as regards policyholders	3.0%

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 examination period from January 1, 1996 through December 31, 2000:

	<u>Amounts</u>	<u>Ratios</u>
Losses incurred	\$11,107,314	54.67%
Loss adjustment expenses incurred	1,707,166	8.40
Other underwriting expenses incurred	6,436,811	31.68
Net underwriting gain	<u>1,066,627</u>	<u>5.25</u>
Premiums earned	<u>\$20,317,918</u>	<u>100.00%</u>

3. FINANCIAL STATEMENTS

A. Balance Sheet

The following exhibit shows the assets, liabilities and surplus as regards policyholders as determined by this examination as of December 31, 2000. The statement is the same as the balance sheet filed by the Company.

<u>Assets</u>	<u>Ledger Assets</u>	<u>Non-Ledger Assets</u>	<u>Not- Admitted Assets</u>	<u>Net-Admitted Assets</u>
Bonds	\$22,123,887	\$	\$	\$22,123,887
Cash and short-term investments	785,167			785,167
Interest, dividends and real estate income due and accrued		377,370		377,370
Receivable from parent, subsidiaries and affiliates	<u>2,934</u>	_____	_____	<u>2,934</u>
Total assets	<u>\$22,911,988</u>	<u>\$377,370</u>	<u>0</u>	<u>\$23,289,358</u>
<u>Liabilities</u>				
Other expenses			\$	30,000
Federal and foreign income taxes				<u>344,208</u>
Total liabilities				\$374,208
<u>Surplus as Regards Policyholders</u>				
Common capital stock			\$5,000,000	
Gross paid in and contributed surplus			11,000,000	
Unassigned funds (surplus)			<u>6,915,150</u>	
Surplus as regards policyholders				<u>22,915,150</u>
Total liabilities and surplus				<u>\$23,289,358</u>

Note: The Internal Revenue Service has completed its audits of the Company's consolidated Federal income tax returns through tax year 1993. 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. An audit covering tax year 1994 is currently under examination. The Internal Revenue Service has not yet begun to audit tax returns covering tax years 1995 through 2000. 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 \$6,645,764 during the period of January 1, 1996 through December 31, 2000, detailed as follows:

Statement of Income

Underwriting Income

Premiums earned		\$20,317,916
Deductions:		
Losses incurred	\$11,107,314	
Loss adjustment expenses incurred	1,707,165	
Other underwriting expenses incurred	<u>6,436,811</u>	
Total underwriting deductions		<u>19,251,290</u>
Net underwriting gain or (loss)		\$ 1,066,626

Investment Income

Net investment income earned	\$ 8,986,006	
Net realized capital gain	<u>566,747</u>	
Net investment gain or (loss)		9,552,753

Other Income

Aggregate write-ins for miscellaneous income	\$ <u>13,081</u>	
Total other income		<u>13,081</u>
Net income before federal and foreign income taxes		\$10,632,460
Federal and foreign income taxes incurred		<u>1,486,696</u>
Net income		<u>\$ 9,145,764</u>

Surplus as regards policyholders per report on examination as of December 31, 1995			\$16,269,386
	<u>Gains in Surplus</u>	<u>Losses in Surplus</u>	
Net income	\$9,145,764		
Capital changes paid in	2,500,000		
Surplus adjustments paid in		\$2,500,000	
Dividends to stockholders	<u> </u>	<u>2,500,000</u>	
Total gains and losses	<u>\$11,645,764</u>	<u>\$5,000,000</u>	
Net increase (decrease) in surplus			<u>6,645,764</u>
Surplus as regards policyholders per report on examination as of December 31, 2000			<u>\$22,915,150</u>

4. LOSSES AND LOSS ADJUSTMENT EXPENSES

The examination liability of \$0 is the same as the amount reported by the Company in its 2000 filed annual statement. As mentioned previously in this report, the Company cedes all of its losses to its parent pursuant to the terms of a reinsurance agreement approved by this Department.

5. COMPLIANCE WITH PRIOR REPORT ON EXAMINATION

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

<u>ITEM</u>	<u>PAGE NO.</u>
A. <u>Management</u>	
i. It is recommended that the Company comply with the provisions of Section 624 of the Business Corporation Law and Section 325(a) of the New York Insurance Law. The Company has complied with this request.	5
ii. It is recommended that all payments of dividends be declared by the board of directors before the payment is made. The Company has complied with this request.	5-6
iii. It is recommended that the board of directors establish practices which assure that all material matters affecting the Company's operations are presented to the board of directors for its consideration. The Company has complied with this request.	6
B. <u>Territory and Plan of Operation</u>	
It is recommended that NIC Insurance Company immediately cease assuming surety insurance business until it amends its license to include such line of business. Subsequent to the prior examination date, the Company amended its New York license to include the authority to write surety business. The Company has complied with this request.	8-9
C. <u>Reinsurance</u>	
It is recommended that the Company amend its pooling agreement to reflect the name change of Pilot Insurance Company to NIC Insurance Company. The Company has complied with this request.	9

<u>ITEM</u>	<u>PAGE NO.</u>
D. <u>Holding Company System</u>	
i. It is recommended that the Company make its Regulation 52 filings in a timely manner.	12
The Company has not complied with this comment and recommendation. A similar comment is made in this report.	
ii. It is recommended that the Company comply with the provisions of Section 1505 of the New York Insurance Law.	12
The Company has not complied with this comment and recommendation. A similar comment is made in this report.	
E. <u>Abandoned Property Law</u>	
It is recommended that, in the future, the Company comply with the provisions of Section 1316 of the New York Abandoned Property Law and file the report that is mandated by such law.	13
The Company has complied with this recommendation.	

6. SUMMARY OF COMMENTS AND RECOMMENDATIONS

<u>ITEM</u>	<u>PAGE NO.</u>
A. <u>Holding Company System</u>	
i. It is 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.	8
ii. It is recommended that the Company submit all inter-company agreements and their amendments to this Department for our non-disapproval in a timely manner pursuant to the provisions of Section 1505(d)(3) of the New York Insurance Law.	10-12

Respectfully submitted,

_____/S/_____
Erwin Roca
Senior Insurance Examiner

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

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

_____/S/_____
Erwin Roca

Subscribed and sworn to before me
this _____ day of _____ 2003.

Appointment No. 21804

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:

ERWIN ROCA

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

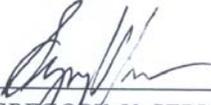
Company

with such other information as she shall deem requisite.

*In Witness Whereof, I have hereunto subscribed by the
name and affixed the official Seal of this Department, at
the City of New York,*

this 27th day of November 2001





GREGORY V. SERIO
Superintendent of Insurance