

REPORT ON EXAMINATION

OF

BERKSHIRE HATHAWAY ASSURANCE CORPORATION

AS OF

DECEMBER 31, 2017

DATE OF REPORT

OCTOBER 23, 2018

EXAMINER

SHEIK H. MOHAMED

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## Department of Financial Services

**ANDREW M. CUOMO**  
Governor

**LINDA A. LACEWELL**  
Acting Superintendent

February 8, 2019

Honorable Linda A. Lacewell  
Acting Superintendent  
New York State Department of Financial Services  
Albany, New York 12257

Madam:

Pursuant to the requirements of the New York Insurance Law, and in compliance with the instructions contained in Appointment Number 31770 dated May 30, 2018, attached hereto, I have made an examination into the condition and affairs of Berkshire Hathaway Assurance Corporation as of December 31, 2017, and submit the following report thereon.

Wherever the designation “the Company” appears herein without qualification, it should be understood to indicate Berkshire Hathaway Assurance Corporation.

Wherever the term “Department” appears herein without qualification, it should be understood to mean the New York State Department of Financial Services.

The examination was conducted at the Company’s administrative office located at 1314 Douglas Street, Omaha, Nebraska 68102.

## **1. SCOPE OF EXAMINATION**

The Department has performed an examination of the Company, a multi-state insurer. The previous examination was conducted as of December 31, 2012. This examination covered the five-year period from January 1, 2013 through December 31, 2017. 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 current and 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 New York laws, statutory accounting principles, and annual statement instructions.

This examination report includes, but is not limited to, the following:

- Company history
- Management and control
- Territory and plan of operation
- Holding company description
- Reinsurance
- Loss review and analysis
- Financial statement presentation
- 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 that involve departures from laws, regulations or rules, or that 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 21, 2007. It became licensed on December 28, 2007 and commenced business on the same date.

### A. Corporate Governance

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 nor more than thirteen members. The board meets one time during each calendar year. At December 31, 2017, the board of directors was comprised of the following seven members:

| <u>Name and Residence</u>                | <u>Principal Business Affiliation</u>   |
|--|---|
| John Duane Arendt<br>Stamford, CT        | Vice President,<br>National Liability & Fire Insurance Company                            |
| Bruce John Byrnes<br>Stamford, CT        | Vice President,<br>National Indemnity Company   |
| Dale David Geistkemper<br>Omaha, NE      | Treasurer and Controller,<br>National Indemnity Company                                   |
| Ajit Jain<br>Rye, NY                     | Director,<br>Berkshire Hathaway Inc.  |
| Brian Gerard Snover<br>Stamford, CT      | Senior Vice President and General Counsel,<br>National Liability & Fire Insurance Company |
| Kevin Gerard Snover<br>North Babylon, NY | Attorney,<br>Self-employed  |
| Donald Frederick Wurster<br>Omaha, NE    | President,<br>National Indemnity Company  |

A review of the minutes of the board of directors' meetings held during the examination period indicated that one board member attended less than 50% of the meetings for which he was eligible to attend. Members of the board have a fiduciary responsibility and must evince an ongoing interest in the affairs of the insurer. It is essential that board members attend meetings consistently and set forth their views on relevant matters so that the board may reach appropriate decisions. Individuals who fail to attend

at least one-half of the regular meetings do not fulfill such criteria. It is recommended that board members who are unable or unwilling to attend meetings consistently should resign or be replaced.

As of December 31, 2017, the principal officers of the Company were as follows:

| <u>Name</u>              | <u>Title</u>          |
|--------------------------|-----------------------|
| Donald Frederick Wurster | President             |
| Bruce John Byrnes        | Secretary             |
| Dale David Geistkemper   | Treasurer             |
| Brian Gerard Snover      | Senior Vice President |
| Michael James Lawler     | Vice President        |

B. Territory and Plan of Operation

As of December 31, 2017, the Company was licensed to write business in all fifty states, the District of Columbia and Puerto Rico.

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> |
|-------------------------|-------------------------|
| 16(C)(D)(E)(F)(G)(H)(I) | Fidelity and surety     |
| 17(A)                   | Credit                  |
| 25                      | Financial guaranty      |

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 41 and 69 of the New York Insurance Law, the Company is required to maintain a minimum surplus to policyholders in the amount of \$66,400,000.

The following schedule shows the direct premiums written by the Company for the period under examination. The Company did not assume any business during the examination period.

| <u>Calendar Year</u> | <u>Total Gross Premiums</u> |
|----------------------|-----------------------------|
| 2013                 | \$12,389,792                |
| 2014                 | \$ 2,338,827                |
| 2015                 | \$12,867,729                |
| 2016                 | \$ 2,949,258                |
| 2017                 | \$ 9,016,257                |

The Company operates as a monoline bond insurer and has written insurance for tax-exempt bonds issued by states, cities and other local entities. The Company insured these securities for issuers both at the time their bonds were sold to the public and also as insurance for bonds that were already owned by investors in the secondary market. The Company ceased actively underwriting new municipal bond issuances in late 2008. The direct written premium reported by the Company during the examination period represents a small number of re-written cancelled bonds handled directly by Company officers and approved by management.

C. Reinsurance Ceded

The Company has structured its ceded reinsurance program to limit its maximum exposure to any one risk through quota share and facultative reinsurance treaties.

The following is a description of the Company's ceded reinsurance program in effect at December 31, 2017:

The Company is a party to a 49% quota share reinsurance agreement with National Indemnity Company ("NICO"), an affiliate, whereby the Company may cede to NICO 49% of the Company's acceptable risks. During the examination period, no risks were ceded under this agreement.

The Company is also a party to a facultative quota share reinsurance agreement with NICO. Under the terms of this agreement, NICO reinsures 92.5% of a surety bond the Company issues to M&T Bank Corporation.

Reinsurance agreements with affiliates were reviewed for compliance with Article 15 of the New York Insurance Law. It was noted that all affiliated reinsurance agreements were filed with the Department pursuant to the provisions of Section 1505(d)(2) of the New York Insurance Law.

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.

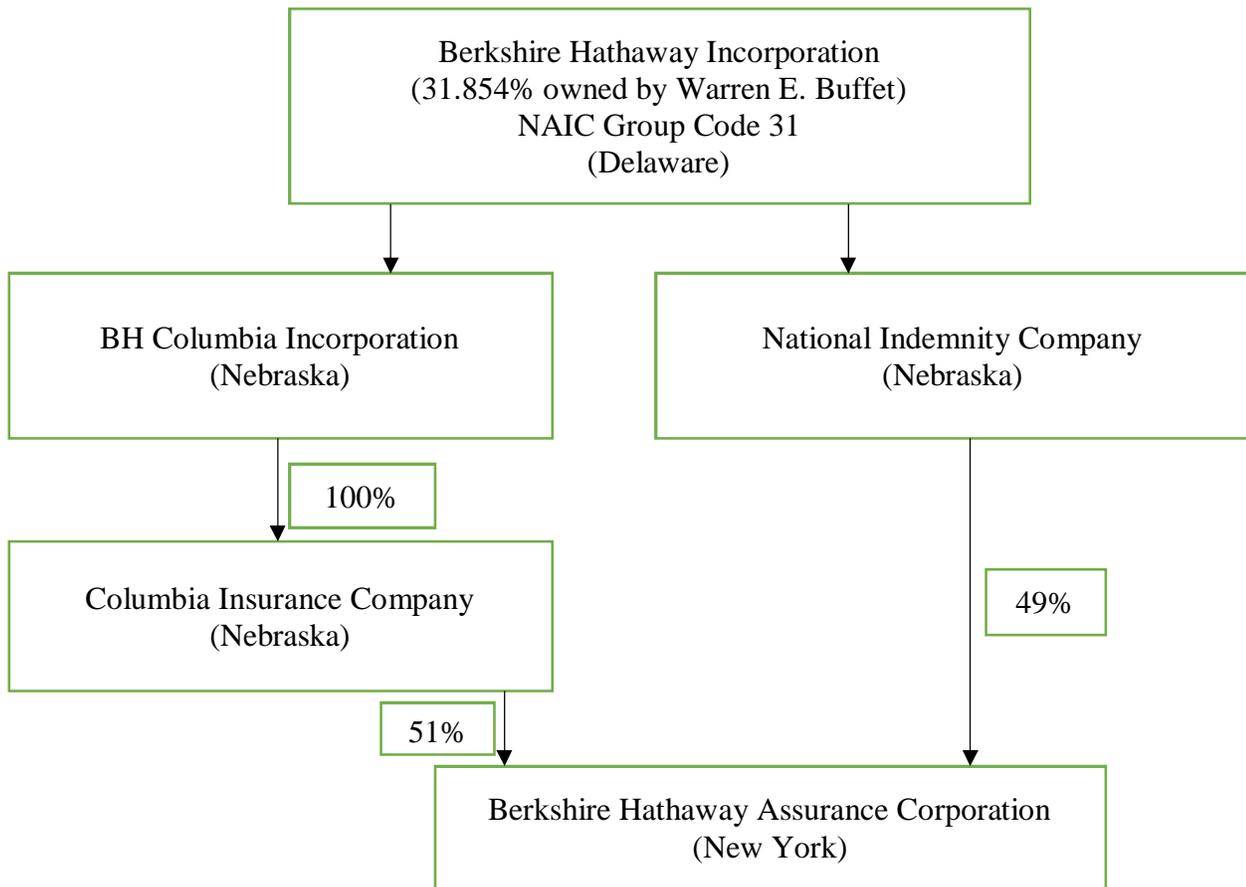
Examination review found that the Schedule F data reported by the Company in its filed annual statement accurately reflected its reinsurance transactions. Additionally, management has represented that all material ceded reinsurance agreements transfer both underwriting and timing risk as set forth in SSAP No. 62R. Representations were supported by appropriate risk transfer analyses and an attestation from the Company's President and Treasurer 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 SSAP No. 62R.

D. Holding Company System

The Company is a member of the Berkshire Hathaway Group. The Company is 51% owned by Columbia Insurance Company and 49% owned by National Indemnity Company, both Nebraska domiciled corporations, which is ultimately controlled by Berkshire Hathaway Inc. (31.854% owned by Warren E. Buffett).

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, 2017:



## Holding Company Agreements

At December 31, 2017, the Company was party to a tax allocation agreement amongst various affiliated members of its ultimate parent Berkshire Hathaway Inc. The agreement has an effective date of December 31, 2007. Pursuant to the terms of the agreement, the parties agree to file consolidated federal income tax returns, which stipulates that the Company's tax liability on a consolidated basis would not exceed the liability if the Company had filed its tax return on a stand-alone basis. The agreement was filed with the Department pursuant to Section 1505 of the New York Insurance Law.

The Company was also party to the following agreements which were not significant or not in use, as there were no expenses or very minimal expenses paid under these agreements during the examination period:

- Service agreement with National Indemnity Company;
- Service agreement with National Liability & Fire Insurance Company;
- Service agreement with FlightSafety International;
- Investment services agreement with National Indemnity Company; and
- Corporate guaranty agreement with Columbia Insurance Company ("CIC"), whereby CIC unconditionally guarantees the due and punctual payment of all future obligations and liabilities of BHAC due under financial guaranty insurance policies issued by the Company.

### E. Significant Ratios

The Company's operating ratios, computed as of December 31, 2017, fall within the benchmark ranges set forth in the Insurance Regulatory Information System of the National Association of Insurance Commissioners.

| <u>Operating Ratios</u>                        | <u>Result</u> |
|--|---------------|
| Net premiums written to policyholders' surplus | 1%            |
| Adjusted liabilities to liquid assets          | 19%           |
| Two-year overall operating                     | 0%            |

Underwriting Ratios

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 | \$ 44,066,191        | 10.42%         |
| Other underwriting expenses incurred         | 7,302,536            | 1.73           |
| Net underwriting gain (loss)                 | <u>371,672,625</u>   | <u>87.86</u>   |
| Premiums earned                              | <u>\$423,041,352</u> | <u>100.00%</u> |

The Company, as a financial guarantor, is not subject to the reporting requirements of risk based capital.

### 3. FINANCIAL STATEMENTS

#### A. Balance Sheet

The following shows the assets, liabilities and surplus as regards policyholders as of December 31, 2017 as reported by the Company:

| <u>Assets</u>   | <u>Assets</u>          | <u>Assets Not Admitted</u> | <u>Net Admitted Assets</u> |
|---|------------------------|----------------------------|----------------------------|
| Bonds   | \$ 160,018,496         | \$ 0                       | \$ 160,018,496             |
| Preferred stocks (stocks)   | 880,000                | 0                          | 880,000                    |
| Common stocks (stocks)  | 2,048,835,479          | 607,629,358                | 1,441,206,121              |
| Properties held for sale  | 3,750,000              | 3,750,000                  | 0                          |
| Cash, cash equivalents and short-term investments                       | 614,126,625            | 0                          | 614,126,625                |
| Investment income due and accrued                                       | 6,061,604              | 0                          | 6,061,604                  |
| Current federal and foreign income tax recoverable and interest thereon | <u>1,201,653</u>       | <u>0</u>                   | <u>1,201,653</u>           |
| Total assets  | <u>\$2,834,873,857</u> | <u>\$611,379,358</u>       | <u>\$2,223,494,499</u>     |

#### Liabilities, surplus and other funds

##### Liabilities

|   |                    |
|---|--------------------|
| Losses and loss adjustment expenses                                   | \$ 30,353,451      |
| Other expenses (excluding taxes, licenses and fees)                   | 100                |
| Taxes, licenses and fees (excluding federal and foreign income taxes) | (13,253)           |
| Net deferred tax liability  | 130,492,621        |
| Unearned premiums   | 150,849,825        |
| Advance premium   | 252,713            |
| Payable to parent, subsidiaries and affiliates                        | 205,894            |
| Contingency reserve   | <u>111,539,207</u> |
| Total liabilities   | \$ 423,680,558     |

##### Surplus and other funds

|  |                        |
|--|------------------------|
| Common capital stock                       | \$ 15,000,000          |
| Gross paid in and contributed surplus      | 990,000,000            |
| Unassigned funds (surplus)                 | <u>794,813,941</u>     |
| Surplus as regards policyholders           | <u>1,799,813,941</u>   |
| Total liabilities, surplus and other funds | <u>\$2,223,494,499</u> |

Note: The Internal Revenue Service has completed its audits of the Company's consolidated Federal Income Tax returns through tax year 2011. 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. Audits covering tax years 2012 and 2013 are currently under examination. The Internal Revenue Service has not yet begun to audit tax returns covering tax years 2014 through 2017. 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. Statement of Income

The net income for the examination period as reported by the Company was \$1,044,216,559 as detailed below:

### Underwriting Income

|  |                  |                   |
|--|------------------|-------------------|
| Premiums earned                              |                  | \$ 423,041,352    |
| Deductions:                                  |                  |                   |
| Losses and loss adjustment expenses incurred | \$ 44,066,191    |                   |
| Other underwriting expenses incurred         | <u>7,302,536</u> |                   |
| Total underwriting deductions                |                  | <u>51,368,727</u> |
| Net underwriting gain or (loss)              |                  | \$ 371,672,625    |

### Investment Income

|                               |                    |             |
|-------------------------------|--------------------|-------------|
| Net investment income earned  | \$271,825,584      |             |
| Net realized capital gain     | <u>540,693,899</u> |             |
| Net investment gain or (loss) |                    | 812,519,483 |

### Other Income

|  |                   |                        |
|--|-------------------|------------------------|
| Miscellaneous income (expense)                     | \$ <u>(6,780)</u> |                        |
| Total other income                                 |                   | <u>(6,780)</u>         |
| Net income before federal and foreign income taxes |                   | \$1,184,185,328        |
| Federal and foreign income taxes incurred          |                   | <u>139,968,769</u>     |
| Net income   |                   | <u>\$1,044,216,559</u> |

C. Capital and Surplus

Surplus as regards policyholders increased \$650,517,193 during the five-year examination period January 1, 2013 through December 31, 2017 as reported by the Company, detailed as follows:

|   |                             |                              |                        |
|---|-----------------------------|------------------------------|------------------------|
| Surplus as regards policyholders per Company<br>as of December 31, 2012 |                             |                              | \$1,149,296,748        |
|   | <u>Gains in<br/>Surplus</u> | <u>Losses in<br/>Surplus</u> |                        |
| Net income  | \$1,044,216,559             |                              |                        |
| Net unrealized capital gains or (losses)                                | 450,862,208                 |                              |                        |
| Change in net deferred income tax                                       |                             | \$ 15,732,161                |                        |
| Change in nonadmitted assets  |                             | 607,629,357                  |                        |
| Dividends to stockholders   |                             | 250,000,000                  |                        |
| Increase (decrease) in contingency reserve                              | <u>28,799,944</u>           | <u>0</u>                     |                        |
| Total gains / losses  | \$1,523,878,711             | \$873,361,518                |                        |
| Net increase (decrease) in surplus                                      |                             |                              | <u>650,517,193</u>     |
| Surplus as regards policyholders per Company<br>as of December 31, 2017 |                             |                              | <u>\$1,799,813,941</u> |

Capital paid in is \$15,000,000 consisting of 2,500 shares of \$6,000 par value per share common stock. Gross paid in and contributed surplus is \$990,000,000. Gross paid in and contributed surplus did not change during the examination period.

**4. LOSSES AND LOSS ADJUSTMENT EXPENSES**

The examination liability for the captioned items of \$30,353,451 is the same as reported by the Company as of December 31, 2017. The examination analysis of the loss and loss adjustment expense reserves was conducted in accordance with generally accepted actuarial principles and statutory accounting principles, including the NAIC Accounting Practices & Procedures Manual, Statement of Statutory Accounting Principle No. 60 (“SSAP No. 60”). All of the reserves relate to the financial guaranty business.

The Department reviewed the Company's modelling, modelling assumptions, and surveillance policies and procedures as of December 31, 2017 and found them to be adequate. The Company has not written new business since 2008, but has renewed existing contracts. The only area of current risk is with respect to obligations issued by Puerto Rico, which the Company insured on a second-to-pay basis; accordingly, the Company only becomes liable for such defaulted amounts if they are not paid by the primary insurer.

The Company's estimate of reserves for losses on its exposures is based on certain assumptions. Changes in these assumptions could materially adversely affect such reserve estimates; and include more adverse macroeconomic conditions, the bankruptcies of issuers of insured obligations, and the amount and timing of any claims. Under certain conditions, many of which are event-driven and outside the control of the Company, these exposures may result in significant increases in claims beyond those assumed in the Company's reserve estimate (which may or may not result in an increase in such loss reserves).

## **5. UNEARNED PREMIUM RESERVES**

Pursuant to Section 6903(c) of the New York Insurance Law, the Company maintains an unearned premium reserve. Unearned premiums represent the portion of premiums which are applicable to the unexpired risk on policies in force. As of December 31, 2017, the Company reported an unearned premium reserve of \$150,849,825.

## **6. CONTINGENCY RESERVES**

Pursuant to Section 6903(a) of the New York Insurance Law, the Company is required to establish and maintain contingency reserves for the protection of policyholders and claimants against the effect of excessive losses occurring during adverse economic cycles. As of December 31, 2017, the Company reported a contingency reserve of \$111,539,207.

7. **COMPLIANCE WITH PRIOR REPORT ON EXAMINATION**

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

| <u>ITEM</u>  | <u>PAGE<br/>NO.</u> |
|--|---------------------|
| A. It was recommended that the Company address the internal control weakness identified during the review of the Company's IT environment. | 12                  |
| The Company has complied with this recommendation.   |                     |

8. **SUMMARY OF COMMENTS AND RECOMMENDATIONS**

| <u>ITEM</u>   | <u>PAGE<br/>NO.</u> |
|---|---------------------|
| A. <u>Corporate Governance</u><br>It is recommended that board members who are unable or unwilling to attend meetings consistently should resign or be replaced | 4                   |



APPOINTMENT NO. 31770

NEW YORK STATE  
**DEPARTMENT OF FINANCIAL SERVICES**

I, Maria T. Vullo, Superintendent of Financial Services of the State of New York, pursuant to the provisions of the Financial Services Law and the Insurance Law, do hereby appoint:

**Sheik Mohamed**

as a proper person to examine the affairs of the

**Berkshire Hathaway Assurance Corporation**

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

**COMPANY**

with such other information as he shall deem requisite.

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

this 30th day of May, 2018

MARIA T. VULLO  
Superintendent of Financial Services



By:

*Joan P. Riddell*

Joan Riddell  
Deputy Bureau Chief