

REPORT ON EXAMINATION

OF

WATER QUALITY INSURANCE SYNDICATE

AS OF

NOVEMBER 30, 2015

DATE OF REPORT

FEBRUARY 22, 2017

EXAMINER

KEVIN MCNAMEE

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Department of Financial Services

ANDREW M. CUOMO
Governor

LINDA A. LACEWELL
Acting Superintendent

February 19, 2019

Honorable Linda A. Lacewell
Acting Superintendent
Department of Financial Services
New York, New York 10004

Madam:

Pursuant to the requirements of the New York Insurance Law, and in compliance with the instructions contained in Appointment Number 31534 dated September 23, 2016, attached hereto, I have made an examination into the condition and affairs of Water Quality Insurance Syndicate as of November 30, 2015, and submit the following report thereon.

Wherever the designation “the Syndicate” appears herein without qualification, it should be understood to indicate Water Quality Insurance Syndicate.

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 Syndicate’s home office located at 60 Broad Street, New York, NY 10004.

1. SCOPE OF EXAMINATION

The previous examination was conducted as of November 30, 2010. This examination covered the five-year period from December 1, 2010 through November 30, 2015, and was limited in scope to these balance sheet items considered by this Department to require analysis, verification or description including: invested assets, loss and loss adjustment expense reserves, and provision for reinsurance. The examination included a review of income, disbursements and Syndicate records deemed necessary to accomplish such analysis or verification and utilized to the extent deemed appropriate, work performed by the Syndicate's independent public accountants.

Transactions occurring subsequent to this period were reviewed where deemed appropriate by the examiner.

A review was also made to ascertain what action was taken by the Company regarding comments and recommendations contained in the prior report on examination.

This report on examination is confined to the target areas investigated pursuant to the limited scope examination instructions, 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 Syndicate is an unincorporated association of insurance companies, called subscribers, which are authorized to transact the business of marine insurance in the United States.

The Syndicate was organized in June 1971, for the specific purpose of providing the insurance protection required by owners and operators of vessels of one hundred or more tons against liability imposed under the Water Quality Improvement Act of 1970. Under the provisions of this Act, owners and operators of vessels incurred liability, with some exceptions, for the cost of removal of oil discharged into or upon the navigable waters of the United States. With the passage of the Federal Water Pollution Control Act Amendments of 1972, the Syndicate expanded its coverage to include the cost of removal of a great variety of substances designated as hazardous. Further amendments were enacted by the Clean Water Act of 1977. In 1978, Public Law 95-576 combined the Acts of 1972 and 1977. The combined legislation prohibits and imposes liability for discharges of oil or hazardous substances into or upon navigable waters of the United

States. Protection is afforded against said liability or in connection with activities under the Outer Continental Shelf Lands Act or Deepwater Port Act of 1974, or which may affect natural resources owned or managed by the United States Government, including resources under the Fishery Conservation and Management Act of 1976.

A. Corporate Governance

The business and affairs of the Syndicate are the responsibility of the board of managers. Each of the subscribing companies is entitled to have a representative on the board, each casting one vote. A review of the minutes of the board meetings indicated that such meetings were well attended. The board meets four times during each calendar year. As of November 30, 2015, the board of managers was as follows:

<u>Subscriber</u>	<u>Representative</u>	<u>Participation</u>
Atlantic Specialty Insurance Company	Robert Gallagher	8.333%
Insurance Company of North America	Karen Griswold	8.333
Liberty Insurance Underwriters, Inc.	Fatih Ozdemir	8.333
National Union Fire Ins. Company of	Paul Williamson	8.333
Navigators Insurance Company	Russell Johnson	10.000
New York Marine and General Insurance	Mark Engel	8.333
North American Specialty Insurance Company,	Lucy Mancello	10.000
RLI Insurance Company	Robert Schauer	8.333
StarNet Insurance Company,	Les Bogdan	2.000
The Continental Insurance Company	Steve Clark	7.869
U.S. Fire Insurance Company	Gordon Lewis	8.333
XL Specialty Insurance Company	Ann Marie Elder	3.467
Zurich American Insurance Company	Peter Wiswell	<u>8.333</u>
Total		<u>100.000%</u>

As of November 30, 2015, the principal officers of the Syndicate were as follows:

<u>Name</u>	<u>Title</u>
John H. Ryszetyk III	President & Chief Executive Officer
John H. Moy	Senior Vice President & Chief Underwriting Officer
Justin A. Mongello	Senior Vice President & Chief Operations Officer
Harry Diamond	Vice President & Chief Claims Officer
John J. Hassett	Vice President, Chief Financial Officer & Secretary
Ryan Puttick	Assistant Vice President, Claims

B. Water Quality Insurance Syndicate Agreement

The Syndicate conducts business for and on behalf of its subscribers pursuant to the provisions of the Water Quality Insurance Syndicate Agreement, which states that the purpose of the Syndicate is to provide, in the most convenient and efficient manner, a facility for the insurance of the following risks:

1. The costs incurred by the United States Government in the removal of oil and hazardous substances (including any costs incurred in the restoration or replacement of natural resources damaged or destroyed because of such discharge of oil or hazardous substance), and for civil penalties imposed in the case of non-removable of hazardous substances as defined in the Federal Water Pollution Control Act.
2. The costs and damages associated with the removal of oil and hazardous substances as defined in the Outer Continental Shelf Lands Act Amendments of 1978.
3. The liability for response costs and damages as defined in the Comprehensive Environmental Response Compensation and Liability Act of 1980.
4. Liabilities as defined in the Oil Pollution Act of 1990.
5. The risks of vessel owners' civil liability to third parties, including the Governments of foreign countries, for physical damage to or loss of real or personal property arising out of a discharge of oil or a hazardous substance.

The subscribers severally, but not jointly, agree to insure, and reinsure all risks pertinent to the subject of the agreement.

C. Territory and Plan of Operation

The Syndicate's subscribers are authorized to write the kinds of marine risks as specified in Section 1113(a) of the New York Insurance Law, paragraphs 20 and 21 of the New York Insurance Law.

As of November 30, 2015, the Syndicate through its licensed subscribers, wrote insurance only in the state of New York.

D. Reinsurance Ceded

The Syndicate assumes no reinsurance. Information produced by the Syndicate, equivalent to an insurance company's Schedule F, accurately reflected its reinsurance transactions for the five-year examination period.

The examiners reviewed all ceded reinsurance contracts in effect during the examination period, all of which contained the required standard clauses, including insolvency clauses as required by Section 1308 of the New York Insurance Law.

As of November 30, 2015, the Syndicate had the following reinsurance program in effect:

<u>Type of Contract</u>	<u>Cession</u>
Liability Excess of Loss-Pollution 3 layers	1 st Layer-\$3,000,000 excess of \$2,000,000, two full reinstatements of limit up to \$9,000,000 per loss or series of losses from one event. 2 nd Layer-\$15,000,000 excess of \$5,000,000, four full reinstatements of limit up to \$60,000,000 per loss or series of losses from one event. 3 rd Layer-\$120,000,000 excess of \$2,000,000, free and unlimited drop-down layer, per loss or series of losses from one event. Excludes losses covered under facultative reinsurance.
Facultative Liability Excess of Loss	\$150,000,000 excess of \$50,000,000 for any one accident/occurrence for vessel/unit/watercraft.
Marine Liability Excess of Loss-COFR Only	1 st Layer-\$598,000,000 excess of \$2,000,000 in respect of each and every loss allocated to certificates of financial responsibility accounts for vessel/unit/watercraft.

E. Affiliated Group

The Syndicate has no employees. It owns 100% of Wall Street Marine, an incorporated non-insurer, which provides payroll, benefits and other services to the Syndicate. However, no service agreement exists between the Syndicate and its subsidiary.

Section 1608(e)(4) of the New York Insurance law states in part:

“The following transactions between a domestic insurer and any subsidiary 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 the superintendent may permit, and he has not disapproved it within such period...service contracts...”

It is therefore recommended that the Syndicate establish a written agreement outlining in detail all provisions that would set forth the roles and responsibilities of each party and that such agreement be submitted to the Department pursuant to the requirements of Section 1608(e)(4) of the New York Insurance Law.

F. Significant Operating Ratios

The following ratios have been computed as of November 30, 2015, based upon the results of this examination:

	<u>Amounts</u>	<u>Ratios</u>
Losses and loss adjustment expenses incurred	\$32,756,478	36.12%
Other underwriting expenses incurred	34,787,952	38.36
Net underwriting gain	<u>23,143,248</u>	<u>25.52</u>
Premiums earned	<u>\$90,687,678</u>	<u>100.00%</u>

G. Accounts and Records

The Syndicate provided the Department with an unaudited financial statement as of November 30, 2015, which indicated a net Subscribers Accountability of \$17,192,890 and premium receivable of \$2,664,945. However, the audited financial statements as of November 30, 2015 indicated a net subscriber's accountability of \$17,714,216 and premium receivable of \$2,142,499 for a difference of \$521,326 and \$522,446 respectively. The net difference was not material; however, the unaudited financial statements included several errors.

It is recommended that the Syndicate exercise greater care in preparing and maintaining its financial statements and records. It is noted that a similar recommendation was included in the prior report on examination.

3. FINANCIAL STATEMENTS

A Balance Sheet

The following shows the assets, liabilities and the subscribers' accountability as reported in the Syndicate's audited financial statement as of November 30, 2015.

Assets

	<u>Assets</u>	<u>Assets Not Admitted</u>	<u>Admitted Assets</u>
Cash	\$5,162,293	\$ 0	\$5,162,293
Premiums receivable	3,059,451	916,952	2,142,499
Reinsurance recoverable on paid losses	74,897		74,897
Other assets	<u>1,087,689</u>	<u>597,078</u>	<u>490,611</u>
Total Assets	<u>\$9,384,330</u>	<u>\$1,514,030</u>	<u>\$7,870,300</u>

Liabilities

Losses and loss adjustment expenses	\$ 14,120,572
Other expenses	765,541
Unearned premiums	9,954,906
Provision for overdue reinsurance	<u>743,497</u>
Total liabilities	25,584,516
Net subscribers' accountability	<u>\$(17,714,216)</u>
Total liabilities and accountability	<u>\$ 7,870,300</u>

A provision for income taxes is not applicable for the Syndicate since earnings from operations are distributed to the subscriber companies and accordingly, the subscriber companies are responsible for income taxes.

B. Statement of Income

Net income for the examination period as reported by the Syndicate was \$23,143,248 as detailed below:

Underwriting Income

Premiums earned		\$90,687,678
Losses incurred and loss adjustment expenses incurred	\$32,756,478	
Other underwriting expenses incurred	<u>34,787,952</u>	
Total underwriting deductions		<u>67,544,430</u>
Total underwriting gain		\$23,143,248
Net income		<u>\$23,143,248</u>

C. Subscriber's Accountability

The subscriber's accountability decreased \$4,651,237 during the five-year examination period December 1, 2010 through November 30, 2015. It is noted that this decrease increases the deficit that the Syndicate has been carrying over from prior periods. The account activity is detailed as follows:

Subscribers' accountability per report on examination as of November 30, 2010			<u>\$(13,062,979)</u>
	<u>Gains</u>	<u>Losses</u>	
Net income	\$23,143,248		
Change in non- admitted assets		\$ 6,152	
Provision for Reinsurance	962,273	514,906	
Net remittances to and from subscribers	<u>0</u>	<u>28,235,700</u>	
Total gains and losses	<u>\$24,105,521</u>	<u>\$28,756,758</u>	
Net decrease in subscribers' accountability			<u>(4,651,237)</u>
Subscribers' accountability per report on examination as of November 30, 2015			<u>\$(17,714,216)</u>

4. LOSSES AND LOSS ADJUSTMENT EXPENSES

The examination liability for the captioned items of \$14,120,572 is the same as reported by the Syndicate as of November 30, 2015. The examination analysis was based on statistical information contained in the Syndicate's records and its financial statements. The results indicated that the reserves as established by the Syndicate as of the examination date were adequate.

5. COMPLIANCE WITH PRIOR REPORT ON EXAMINATION

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

<u>ITEM</u>	<u>PAGE NO.</u>
A <u>Accounts and Records</u>	
i. It was recommended that the Syndicate exercise greater care in maintaining its financial records.	6
The Company has not complied with this recommendation. A similar comment is made in this report.	
ii It was also recommended that the Syndicate file a copy of its audited financial statements with the Department on an annual basis.	6
The Company has complied with this recommendation.	

6. SUMMARY OF COMMENTS AND RECOMMENDATIONS

<u>ITEM</u>		<u>PAGE NO.</u>
A	<u>Affiliated Group</u>	
	The Syndicate did not have in place a service agreement with Wall Street Marine. It is recommended that the Syndicate establish a written agreement outlining in detail all provisions that would set forth the roles and responsibilities of each party and that such agreement be submitted to the Department for non-objection pursuant to the requirements of Section 1608(e)(4) of the New York Insurance Law.	5
B	<u>Accounts and Records</u>	
	It is recommended that the Syndicate exercise greater care in preparing and maintaining its financial statements and records.	6

Respectfully submitted,

_____/S/
Kevin McNamee
Associate Insurance Examiner

STATE OF NEW YORK)
)ss:
COUNTY OF NEW YORK)

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

_____/S/
Kevin McNamee

Subscribed and sworn to before me

this _____ day of _____, 2019.

APPOINTMENT NO. 31534

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:

Kevin McNamee

as a proper person to examine the affairs of the

Water Quality Insurance Syndicate

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 23rd day of September, 2016

MARIA T. VULLO
Superintendent of Financial Services



By:

Joan P. Riddell

*Joan Riddell
Deputy Bureau Chief*