

REPORT ON EXAMINATION

OF THE

KENSINGTON INSURANCE COMPANY

AS OF

DECEMBER 31, 2008

DATE OF REPORT

OCTOBER 29, 2010

EXAMINER

WEI CAO

## TABLE OF CONTENTS

<u>ITEM NO.</u>		<u>PAGE NO.</u>
1.	Scope of examination	2
2.	Description of Company	3
	A. Management	3
	B. Territory and plan of operation	5
	C. Reinsurance	6
	D. Holding company system	7
	E. Significant operating ratios	9
	F. Accounts and records	10
	G. Subsequent events	15
3.	Financial statements	17
	A. Balance sheet	17
	B. Underwriting and investment exhibit	18
4.	Losses and loss adjustment expenses	19
5.	Net deferred tax asset	19
6.	Compliance with prior report on examination	20
7.	Summary of comments and recommendations	21



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

October 29, 2010

Honorable James J Wrynn  
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 30360 dated June 24, 2009, attached hereto, I have made an examination into the condition and affairs of Kensington Insurance Company as of December 31, 2008, and submit the following report thereon.

Wherever the designation "the Company" appears herein without qualification, it should be understood to indicate Kensington 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 office located at 6 West 18<sup>th</sup> Street 11<sup>th</sup> floor, New York, NY 10011.

## 1. SCOPE OF EXAMINATION

The Department has performed a risk-focused examination of Kensington Insurance Company. This is the first financial examination of the Company after the report on organization, which was conducted as of February 1, 2005. This examination covered the period from February 2, 2005 through December 31, 2008. 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, which requires that we plan and perform the examination to evaluate the financial condition and identify 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. An 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 Statutory Accounting Principles and annual statement instructions when applicable to domestic state regulations.

All accounts and activities of the Company were considered in accordance with the risk-focused examination process. The examiners also relied upon audit work performed by the Company’s independent public accountants when appropriate.

This examination report includes a summary of significant findings for the following items as called for in the Financial Condition Examiners Handbook of the NAIC:

- Company history
- Corporate records
- Territory and plan of operation
- Reinsurance
- Holding Company System
- Accounts and records
- Subsequent events
- Financial statements
- Loss and Loss adjustment expenses
- Summary of recommendations

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**

Kensington Insurance Company was incorporated under the laws of the State of New York on December 23, 2003. It commenced business on April 8, 2005 as a commercial property and casualty insurer.

At December 31, 2008, the Company's surplus was \$3,774,236 which consisted of \$7,000,000 in gross paid in and contributed surplus, \$1,000,000 in capital stock, and (\$4,225,764) in unassigned funds. Capital paid in was \$1,000,000 consisting of 800,000 shares of \$1.25 par value per share common stock. Gross paid in and contributed surplus increased by \$4,000,000 during the examination period, as follows:

<u>Year</u>	<u>Description</u>	<u>Amount</u>
February 2, 2005	Beginning gross paid in and contributed surplus	\$3,000,000
2006	Surplus contribution	\$1,000,000
2007	Surplus contribution	1,500,000
2008	Surplus contribution	<u>1,500,000</u>
		<u>4,000,000</u>
December 31, 2008	Ending gross paid in and contributed surplus	<u>\$7,000,000</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 Company's by-laws requires the board of directors to meet a minimum of four times a year.

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.

At December 31, 2008, the board of directors was comprised of the following fourteen members:

Name and ResidencePrincipal Business Affiliation

Ching Tai Chiang  
Holmdel, NJ

Shareholder,  
KP &C Holding Company

Danny Chiang  
Marboro, NJ

Dentist and Member,  
Pediatric Dental Alliance, LLC

George Chiang  
New York, NY

Vice President,  
Pacific Concord Investment Corporation  
Vice President,  
Kensington Insurance Company

Wen Hui Chiang  
Holmdel, NJ

Chairman of the Board,  
Kensington Insurance Company  
Major Shareholder,  
KP&C Holding Company  
Entrepreneur,  
Including hotels and real estate

I-Cheng Steven Hsu  
Holmdel, NJ

Telecommunication Consultant,  
Self Employed

John Izdebski  
Jackson, NJ

Principal,  
Brouwer & Izdebski, a retail insurance  
brokerage firm in New Jersey

Richard Lai  
Bronx, NY

Associate Professor,  
St. John's University

Chuck Kuan Lin  
Brunswick, NJ

Vice President,  
C. K. Lin Inc.  
Shareholder,  
KP&C Holding Company.

Wang Chiu Shia Lin  
Holmdel, NJ

Shareholder,  
KP&C Holding Company

Ken Tu Liu  
Massapequa, NY

Executive Vice President,  
Dorcas & Kalam Co., Ltd.

Yitzhak Loria  
New York, NY

Real Estate Broker,  
Yitzhak loria Management, LLC

Brian B Smith  
Middletown, NJ

Attorney/General Counsel,  
Pacific Concord Investment Corporation

Name and ResidencePrincipal Business Affiliation

Joseph H Davis  
Merrick, NY

Officer,  
Kensington Insurance Company and New  
Horizon Agency Group Inc.

John E. Scanlan \*  
Blackwood, NJ

Self-employed consultant,  
Formerly an officer of The Proformance  
Insurance Company

\*In February 2009, John Scanlan was appointed President of Kensington Insurance Company.

As of December 31, 2008, the principal officers of the Company were as follows:

<u>Name</u>	<u>Title</u>
Wen Hui Chiang	Chairman & Chief Executive Office
Charles Shen	Executive Vice President & Chief Financial Office
Joseph Davis*	President
Brian B. Smith	Secretary

\*Joseph Davis was replaced as President by John Scanlan in February 2009.

B. Territory and Plan of Operation

As of December 31, 2008, the Company was licensed to write business in New York only.

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>
4	Fire
5	Miscellaneous property
6	Water damage
7	Burglary and theft
8	Glass
9	Boiler and machinery
12	Collision
13	Personal injury liability
14	Property damage liability
19	Motor vehicle and aircraft physical damage
20	Marine and inland marine

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 \$1,600,000.

The Company offers commercial property and casualty insurance products to small and medium-sized businesses. The Company markets its insurance products exclusively through New Horizon Agency Group ("NHAG"), an affiliated insurance agency currently licensed to operate in New York and New Jersey. NHAG provides the underwriting, marketing, policy issuance, and administrative functions for the Company. All of the Company's premium writings have been in the New York City area.

C. Reinsurance

Assumed Reinsurance

The Company has not assumed any business since inception.

Ceded Reinsurance

The Company has structured its ceded reinsurance program so that in most circumstances it maximum net exposure per property risk and per casualty occurrence is \$100,000. The Company's program is designed to limit its net catastrophe exposure to \$250,000 per occurrence. The Company's reinsurance program for 2008 is structured as follows:

<u>Type of Coverage</u>	<u>Cession</u>
Property excess of loss	\$500,000 in excess of \$100,000 per risk. \$800,000 limit per occurrence
Casualty excess of loss	\$900,000 in excess of \$100,000 each occurrence.
Catastrophe excess of loss	\$750,000 in excess of \$250,000 per loss occurrence

The casualty coverage and the basic property reinsurance coverage were secured through a multiple line excess of loss reinsurance contract. The Company had a facultative treaty in place covering property where the total insured value was over \$500,000. This facultative coverage served as the primary coverage, where the total insured value was over \$500,000, and worked in conjunction



with the multiple line excess of loss reinsurance contract. Catastrophe coverage is secured through a separate treaty. The Company had similar reinsurance coverage in effect prior to 2008.

All 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.

Management has represented that all material ceded reinsurance agreements transfer both underwriting and timing risk as set forth in NAIC Accounting Practices and Procedures Manual, Statements of Statutory Accounting Principles (“SSAP”) No. 62. Representations were supported by appropriate risk transfer analyses and an attestation from the Company's chief executive officer 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 paragraphs 18 through 25 of SSAP No. 62.

The Company did not respond to question 13.1 of the General Interrogatories Part 2 in the 2008 annual statement which asked the Company to indicate the largest net aggregate amount insured in any one risk (excluding workers’ compensation). It is noted that the largest net aggregate amount insured by the Company in any one risk is \$100,000.

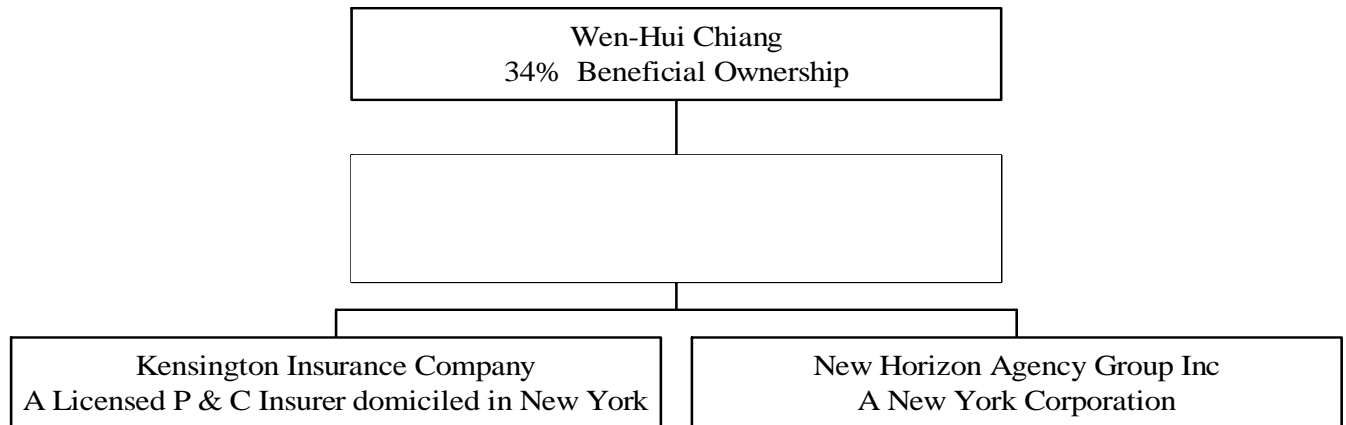
It is recommended that the Company respond to all of the questions in the annual statement’s general interrogatories.

D. Holding Company System

The Company is 100% owned by KP&C Holding Company Inc (“KP&C”). KP&C also owns New Horizon Agency Group, Inc which provides the underwriting, marketing, policy issuance and administrative functions for the Company. Prior to December 2006, the Company’s 800,000 outstanding shares were owned by various private investors. On December 27, 2006, the private investors surrendered their shares in the Company and in return were issued shares in KP&C. Mr. Wen-Hui Chiang and his family own the largest number of shares of KP&C, holding approximately 34% of the outstanding shares.

It was noted that the Company failed to update Schedule Y, of the annual statement, to reflect the transfer of the direct ownership of the Company to KP&C. Therefore, it is recommended that the Company update Schedule Y in future annual statements.

A chart depicting the Company's holding company system at December 31, 2008 appears below:



At December 31, 2008, the Company was party to the following agreements with New Horizon Agency Group:

Agency Agreement

Effective April 15, 2005, Kensington Insurance Company was a party to an agency agreement with its affiliate New Horizon Agency Group, Inc. (“NHAG”). Pursuant to the agreement, New Horizon Agency Group, Inc provides underwriting, marketing, policy issuance, administration and claim functions to Kensington Insurance Company.

This agreement was filed with the Department pursuant to Section 1505 of the New York Insurance Law.

Effective January 1, 2006, the commission rate set forth in the agency agreement was amended to 25% from the previous rate of 22.5%. However, the amendment was not submitted to the Department until March 30, 2006. Pursuant to the provisions of Section 1505(d) of the New York Insurance Law, agreements for rendering of services on a regular or systematic basis, or amendments thereto, are required to be submitted to the Department for non-disapproval at least thirty days prior

to implementation. Therefore, the Company violated Section 1505(d) of the New York Insurance Law when it failed to submit the amendment to the agency agreement to the Department for non-disapproval at least 30 days prior to implementation.

#### Space Allocation Agreement

Effective June 20, 2007, the Company was a party to a space allocation agreement with its affiliate, NHAG, pursuant to which, the Company shares space leased by NHAG from 6-8 West 18<sup>th</sup> Street, LLC (“Landlord”). The Landlord is owned by an affiliate of one of the stockholders of the Company. Pursuant to the space allocation agreement, NHAG grants the Company use of the premises, for which it is currently paying 20% of the rent due under the lease. The term shall commence on the date of the agreement and expire on May 31, 2012. The Agreement was submitted to the Department in March 2007 and was non-disapproved on June 19, 2007.

#### E. Significant Operating Ratios

The following ratios have been computed as of December 31, 2008, based upon the results of this examination:

Net premiums written to surplus as regards policyholders	133.02%
Liabilities to liquid assets (cash and invested assets less investments in affiliates)	71.09%
Premiums in course of collection to surplus as regards policyholders	12.64%

All of 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 four year period covered by this examination:

	<u>Amounts</u>	<u>Ratios</u>
Losses and loss adjustment expenses incurred	\$7,319,819	67.21%
Other underwriting expenses incurred	7,580,429	69.60
Net underwriting loss	<u>(4,009,492)</u>	<u>(36.82)</u>
Premiums earned	<u>\$10,890,756</u>	<u>100.00%</u>

F. Accounts and Records

i. Custodian Agreement

The Company has only one custodial agreement in place with HSBC Bank. The examination review of the custodial agreement indicated that it did not contain some of the protective covenants set forth in Section 3(III)(H)(2) of the 2008 NAIC Financial Condition Examiners Handbook, which states that custodial agreements should contain the following protective covenants:

2a. The custodian is obligated to indemnify the insurance company for any insurance company's loss of securities in the custodian's custody, except that, unless domiciliary state law, regulation, or administrative action otherwise require a stricter standard (Section 2.b. sets forth an example of such a stricter standard), the custodian shall not be so obligated to the extent that such loss was caused by other than the negligence or dishonesty of the custodian.

2b. If domiciliary state law, regulation, or administrative action requires a stricter standard of liability for custodians of insurance company securities than that set forth in Section 2.a., then such stricter standard shall apply. An example of a stricter standard that may be used is that the custodian is obligated to indemnify the insurance company for any loss of securities of the insurance company in the custodian's custody occasioned by the negligence or dishonesty of the custodian's officers or employees, or burglary, robbery, holdup, theft, or mysterious disappearance, including loss by damage or destruction.

2c. In the event of a loss of the securities for which the custodian is obligated to indemnify the insurance company, the securities shall be promptly replaced or the value of the securities and the value of any loss of rights or privileges resulting from said loss of securities shall be promptly replaced.

2d. The custodian shall not be liable for any failure to take any action required to be taken hereunder in the event and to the extent that the taking of such action is prevented or delayed by war (whether declared or not and including existing wars), revolution, insurrection, riot, civil commotion, act of God, accident, fire, explosions, stoppage of labor, strikes or other differences with employees, laws, regulations, orders or other acts of any governmental authority, or any other cause whatever beyond its reasonable control.

2e. In the event that the custodian gains entry in a clearing corporation through an agent, there should be a written agreement between the custodian and the agent that the agent shall be subjected to the same liability for loss of securities as the custodian. If the agent is governed by laws that differ from the regulation of the custodian, the Commissioner of Insurance of the state of domicile may accept a standard of liability applicable to the agent that is different from the standard liability.

2f. If the custodial agreement has been terminated or if 100% of the account assets in any one custody account have been withdrawn, the custodian shall provide written notification, within three business days of termination or withdrawal, to the insurer's domiciliary commissioner.

2g. During regular business hours, and upon reasonable notice, an officer or employee of the insurance company, an independent accountant selected by the insurance company and a representative of an appropriate regulatory body shall be entitled to examine, on the premises of the custodian, its records relating to securities, if the custodian is given written instructions to that effect from an authorized officer of the insurance company.

2h. The custodian and its agents, upon reasonable request, shall be required to send all reports which they receive from a clearing corporation, which the clearing corporation permits to be redistributed including reports prepared by the custodian's outside auditors, to the insurance company on their respective systems of internal control.

2i. To the extent that certain information maintained by the custodian is relied upon by the insurance company in preparation of its annual statement and supporting schedules, the custodian agrees to maintain records sufficient to determine and verify such information.

2j. The custodian shall provide, upon written request from a regulator or an authorized officer of the insurance company, the appropriate affidavits, with respect to the insurance company's securities held by the custodian.

2k. The custodian shall secure and maintain insurance protection in an adequate amount.

2l. The foreign bank acting as a custodian, or a U.S. custodian's foreign agent, or a foreign clearing corporation is only holding foreign securities or securities required by the foreign country in order for the insurer to do business in that country. A US custodian must hold all other securities.

It was noted that the custodian agreement with HSBC Bank did not include provisions 2a, 2b, 2c, 2d, 2e, 2f, 2h, 2i, 2j and 2k.

It is recommended that the Company amend the custodian agreement to incorporate all of the protective covenants included in the NAIC Financial Condition Examiners Handbook.

ii. CPA Engagement Letter

The written contracts by which the Company engaged its certified public accountants ("CPA") firm for the year 2008, did not contain the following provisions required by the Department Regulation 118, Part 89.2 which states in part:

“Every insurer subject to this Part shall retain an independent certified public accountant (CPA) who agrees by written contract with such insurer to comply with the provisions of section 307(b) of the Insurance Law, this Part and the Code of Ethics and Professional Conduct adopted by the American Institute of Certified Public Accountants (AICPA). Such contract must specify that:

(a) on or before May 31st, the CPA shall provide an audited financial statement of such insurer and of any subsidiary required by section 307(b)(1) of the Insurance Law together with an opinion on the financial statements of such insurer and any such subsidiary for the prior calendar year and an evaluation of the insurer's and any such subsidiary's accounting procedures and internal control systems as are necessary to the furnishing of the opinion;

(b) any determination by the CPA that the insurer has materially misstated its financial condition as reported to the superintendent or that the insurer does not meet minimum capital or surplus to policyholder requirements set forth in the Insurance Law shall be given by the CPA, in writing, to the superintendent within 15 calendar days following such determination;

It is recommended that the Company include in all future contracts written to engage CPA firms, the provisions required by Department Regulation 118. It is noted that Department Regulation 118 was revised effective January 1, 2010, and therefore, the Company should comply with the revised regulation going forward.

iii. U & I Exhibit – Expenses

Upon review of the Underwriting and Expense Exhibit (Part 3 – Expenses) included in the Company's 2006, 2007 and 2008 annual statements, it was noted that the Company reported 100% of its general expenses on lines 2 through 20 as “Other Underwriting Expenses.” Statement of Statutory Accounting Principles (“SSAP”) 70 requires that these expenses be allocated among Loss adjustment expenses, Other underwriting expenses, and Investment expenses.

SSAP 70, paragraph 3 states in part:

“Allocable expenses for property and casualty insurance companies shall be classified into one of three categories on the underwriting and investment exhibit as follows:

- a. Loss adjustment expenses...
- b. Investment expenses...
- c. Other underwriting expenses...

SSAP 70, paragraph 6 states in part:

“Allocation to the above categories should be based on a method that yields the most accurate results...”

SSAP 70, paragraph 7 states in part:

“Allocation may be entirely to one expense category based upon the type of expense incurred, for example, premium taxes would be 100% allocated to Other Underwriting Expenses for property and casualty companies. Other expenses may be allocated across several categories, such as salaries...”

It is recommended that the Company comply with SSAP 70 and properly allocate its general expenses to Loss adjustment expenses, Other underwriting expenses, and Investment expenses.

It is noted that the Company included a write-in item on line 2402 of the Underwriting and Investment Exhibit (Part 3 – Expenses) entitled “reclassification for ULAE” in the amount of \$(147,718). The purpose of the entry appears to be an attempt to conform with SSAP 70 and allocate a portion of the Company’s general and administrative expenses to loss adjustment expenses. There are two problems with this approach:

1. The expenses on part 3 of the underwriting and investment exhibit should be allocated to loss adjustment expenses on an individual expense basis rather than through a write-in adjustment.
2. The reclassification of \$147,718 does not clearly flow through the annual statement as the \$147,718 is not added in column 1-loss adjustment expenses of part 3 of the underwriting and investment exhibit. The Company claims that the figure is included in the loss adjustment expense reserve at December 31, 2008 despite the fact that the flow is not shown on part 3 of the underwriting and investment exhibit..

It is recommended that the Company properly allocate expenses in accordance with the annual statement instructions.

It is also noted that the Company reported the commissions it paid to NHAG, in accordance with the agency agreement described in Section 2D of this report, as commission expense in part 3 of the underwriting and investment exhibit. This classification is not in accordance with the annual statement instructions which state:

“A Company that pays any affiliated entity (including a managing general agent) for the management, administration, or service of all or part of its business operations shall allocate these costs to the appropriate expense classification items (salaries, rent, postage, etc.) as if these costs had been borne directly by the company. Management, administration or similar fees should not be reported as a one-line expense. The Company may estimate these expense allocations based on a formula or other reasonable basis.”

It is recommended that the Company allocate the fees paid to NHAG as required by the annual statement instructions.

iv. Annual Statement Preparation Issues

In addition to the issue of classification of general expenses on the underwriting and investment exhibit there were other noted annual statement preparation issues including:

- a. At December 31, 2008, the Company reported an admitted asset on line 15 (“Amounts receivable relating to uninsured plans”) of its asset page in the amount of \$10,044. This amount actually reflects a state tax overpayment and would best be reflected as either a write-in asset or a negative accrual on line 6, “Taxes licenses, and fees”, on the annual statement liability page.
- b. The Company reported a write-in liability on line 2301 of the annual statement’s liability page captioned “Loan payable” in the amount of \$11,501. The amount was actually an amount due on the Company’s directors and officers liability insurance policy. This should have been included as “Other expenses” on line 5.

It is recommended that the Company properly classify all assets and liabilities in accordance with the annual statement instructions.

- c. During the examination period, the Company reported on Schedule P, its adjusting and other payments (“Paid ULAE”) in the calendar year the payments were made rather than distributing the payments to the related accident year.

It is recommended that the Company allocate adjusting and other payments to the appropriate accident year.

v. Conflict of Interest Statements

In response to annual statement General Interrogatory number 16, which asks whether or not the Company has an established procedure for disclosure to its board of directors or trustees of any material interest or affiliation on the part of any of its officers, directors, trustees, or responsible employees that is in conflict or likely to conflict with the official duties of such person, the Company responded “yes.”



Examination review revealed that the Company did not have a formal conflict of interest policy as of December 31, 2008. Prudent business practices dictate that Company management establish formal written procedures to govern the relations between the Company and its directors, officers, and responsible employees who are charged with the conduct of its affairs. Such formal procedures should disclose to its board of directors or trustees any material interest or affiliation on the part of any of its directors, officers, trustees, or responsible employees that is in conflict or is likely to conflict with the official duties of such persons.

It is recommended that the Company distribute annual conflict of interest disclosure statements and questionnaires to all directors, officers, trustees, and designated responsible employees. It is also recommended that the Company exercise greater care in the preparation of its Annual Statement.

Subsequently, the Company submitted a draft of conflict of interest policy for approval which was approved by the board of directors on December 9, 2009.

vi. Concentration of Cash

The Company's 2008 Schedule E-part 1 indicated that the Company deposited \$2,097,130 in HSBC bank, which represents 17.3% of the Company's admitted assets of \$12,126,146.

Section 1409(a) of the New York Insurance Law states, in part:

“No domestic insurer shall have more than ten percent of its admitted assets as shown by its last statement on file with the superintendent invested in, or loaned upon, the securities (including for this purpose certificates of deposit, partnership interests and other equity interests) of any one institution.”

It is recommended that the Company limit its investments in any one institution to no more than 10% of its admitted assets pursuant to the provisions of Section 1409(a) of the New York Insurance Law.

vii. Policy Cancellation Procedures

The examination noted that the written procedures the Company has in place regarding policy cancellations do not include all the requirements included in Section 3426 of the New York Insurance Law.

It is therefore recommended that the Company include the requirements of Section 3426 of the New York Insurance law in its written cancellation procedures.

It should be noted that the above-referenced recommendation was made only to strengthen the Company's internal controls and that there were no violations of Section 3426 of the New York Insurance law noted during the examination.

#### G Subsequent Events

During 2009, the Company's surplus decreased by \$1,684,324, or 43.3%, from \$3,939,630 at December 31, 2008 to \$2,235,306 at December 31, 2009. The surplus decrease was due mainly to an underwriting loss in the amount of \$2,473,088, which represented 45.4% of the \$5,450,179 net premiums earned in 2009. Additionally, losses and loss adjustment expenses outstanding increased by 47.2% from December 31, 2008 to December 31, 2009, while premiums earned increased by only 12.3%.

The significant increase in losses and loss adjustment expenses in 2009 was not the result of adverse development for accident years 2008 and prior losses, but rather represented higher than anticipated accident year 2009 losses and loss adjustment expenses from the Company's mercantile lessors risk only business. It is noted that the Company reported a developed savings in the amount of \$389,000 for accident year 2009 losses and loss adjustment expense reserves in its quarterly statement as of September 30, 2010.

The Company's parent contributed \$1,200,000 to the Company's paid in surplus account in the first six months of 2010. This is in addition to the \$600,000 contributed in 2009.

### 3. FINANCIAL STATEMENTS

#### A Balance Sheet

The following shows the assets, liabilities and surplus as regards policyholders as of December 31, 2008 as determined by this examination and as reported by the Company:

<u>Assets</u>	<u>Examination</u> <u>Net admitted Assets</u>	<u>Company</u> <u>Net admitted Assets</u>	<u>Surplus</u> <u>Increase (Decrease)</u>
Cash, cash equivalents and short-term investments	\$11,249,542	\$11,249,542	\$ 0
Investment income due and accrued	86,162	86,162	0
Uncollected premiums and agents' balances in the course of collection	477,068	477,068	0
Deferred premiums, agents' balances and installments booked but deferred and not yet due	293,922	293,922	0
Other amounts receivable under reinsurance contracts	4,256	4,256	0
Current federal tax recoverable	1,152	1,152	0
Net deferred tax asset	0	145,395	(145,395)
Guaranty funds receivable or on deposit	4,000	4,000	0
State tax overpayment	<u>10,044</u>	<u>10,044</u>	<u>0</u>
Totals assets	<u>\$12,126,146</u>	<u>\$12,271,541</u>	\$ (145,395)
 <u>Liabilities, Surplus and Other Funds</u>			
<u>Liabilities</u>	<u>Examination</u>	<u>Company</u>	<u>Surplus Increase</u> <u>(Decrease)</u>
Losses and Loss adjustment expenses	5,345,132	\$5,345,132	0
Commissions payable, contingent commissions and other similar charges	21,164	21,164	0
Other expenses (excluding taxes, licenses and fees)	53,376	53,376	0
Taxes, licenses and fees (excluding federal and foreign income taxes)	30	30	0
Unearned premiums	2,751,563	2,751,563	0
Provision for reinsurance	<u>180,645</u>	<u>180,645</u>	<u>0</u>
Total liabilities	<u>\$8,351,910</u>	<u>8,351,910</u>	<u>0</u>
 <u>Surplus and Other Funds</u>			
Common capital stock	\$1,000,000	\$1,000,000	0
Gross paid in and contributed surplus	7,000,000	7,000,000	0
Unassigned funds (surplus)	<u>(4,225,764)</u>	<u>(4,080,369)</u>	<u>(145,395)</u>
Surplus as regards policyholders	<u>\$3,774,236</u>	<u>\$3,919,631</u>	\$(145,395)
Total liability, surplus and other funds	<u>12,126,146</u>	<u>\$12,271,541</u>	\$(145,395)

NOTE: The Internal Revenue Service has not audited tax returns covering tax years 2005 through 2008. 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 decreased \$41,281 during the examination period detailed as follows:

Underwriting Income

Premiums earned		\$10,890,756
Deductions:		
Losses and loss adjustment expenses incurred	\$7,319,819	
Other underwriting expenses incurred	<u>7,580,429</u>	
Total underwriting deductions		<u>14,900,248</u>
Net underwriting gain or (loss)		\$(4,009,492)

Investment Income

Net investment income earned	<u>\$642,022</u>	
Net investment gain or (loss)		642,022

Other Income

Net gain or (loss) from agents' or premium balances charged off	\$(2,783)	
Aggregate write-ins for miscellaneous income	<u>25,002</u>	
Total other income		<u>22,219</u>
Net income after dividends to policyholders but before federal and foreign income taxes		\$(3,345,251)
Federal and foreign income taxes incurred		<u>(87)</u>
Net income		<u>\$(3,345,164)</u>

C. Capital and Surplus Account

Surplus as regards policyholders per report on organization February 1, 2005			\$3,815,517
	<u>Gains in Surplus</u>	<u>Losses in Surplus</u>	
Net income		\$3,345,164	
Change in net deferred income tax		85,786	
Change in non-admitted assets		72,662	
Change in provision for reinsurance		180,645	
Gross paid in and contributed surplus	\$4,000,000		
Prior period adjustment	0	357,024	
Total gains and losses	\$4,000,000	\$4,041,281	
Net increase (decrease) in surplus			(41,281)
Surplus as regards policyholders per report on examination as of December 31, 2008			<u>\$3,774,236</u>

**4. LOSSES AND LOSS ADJUSTMENT EXPENSES**

The examination liability for the captioned items of \$5,345,132 is the same as reported by the Company as of December 31, 2008.

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. NET DEFERRED TAX ASSET**

The Company reported an admitted asset for the captioned item in the amount of \$145,394 as of the examination date. Pursuant to this examination, the admitted asset has been eliminated.

Pursuant to the provisions of Section 1301(a)(16) of the New York Insurance Law, deferred taxes shall be deemed admitted in an amount not to exceed the amount expected to be realized within one year of the balance sheet date. It is noted that the Company has not paid any federal income taxes in the past three years; therefore, it cannot avail itself of a loss carry-backs. Additionally, the Company has loss carry-forwards of approximately \$2.6 million; therefore, it will not be required to

pay any federal income taxes in 2009. Therefore, the Company has no federal income taxes paid or payable from which it can realize any deferred tax benefit within one year of the balance sheet date.

It is recommended that the Company non-admit any deferred tax assets that do not meet the requirements of Section 1301(a)(16) of the New York Insurance Law.

## **6. COMPLIANCE WITH PRIOR REPORT ON EXAMINATION**

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

<u>ITEM</u>	<u>PAGE NO.</u>
<p>A. It was recommended that the board of directors elect the appropriate officers, as required by the Company's by-laws.</p> <p>The Company has complied with this recommendation.</p>	3
<p>B. It is recommended that the Company comply with Section 1301(a)(18) of the New York State Insurance Law and only report electronic data processing equipment with a cost of \$50,000 or more.</p> <p>The Company has complied with this recommendation.</p>	6
<p>C. It is recommended that the Company amend the custodial agreement with the Great Eastern Bank to comply with the guidelines set forth in the NAIC Examiners' handbook.</p> <p>At December 31, 2008 the Company's invested assets were no longer held with the Great Eastern Bank. The Company's current custodian is HSBC and the agreement with HSBC also does not comply with the NAIC guidelines. A similar recommendation is included in the report.</p>	7
<p>D. Should the Company decide to renew its service agreement with New Horizon Agency upon the licensing of KIC, management is directed to file such agreement for Department review pursuant to the provisions of Article 15 of the New York Insurance Law.</p> <p>The Company has complied with this recommendation.</p>	9

## **7. SUMMARY OF COMMENTS AND RECOMMENDATIONS**

<u>ITEM</u>	<u>PAGE NO.</u>
A.	<u>General Interrogatories</u>
	It is recommended that the Company respond to all of the questions in the annual statement's general interrogatories. 7
B.	<u>Holding Company</u>
i	It is recommended that the Company update Schedule Y in future annual statements. 8
ii	The Company violated Section 1505(d) of the New York Insurance Law when it failed to submit the amendment to the agency agreement to the Department for non-disapproval at least 30 days prior to implementation. 9
C.	<u>Accounts and Records</u>
i	It is recommended that the Company amend the custodian agreement to incorporate all of the protective covenants included in the NAIC Financial Condition Examiners Handbook. 11
ii	It is recommended that the Company include in all future contracts written to engage CPA firm, the provisions required by Department Regulation 118. 12
iii	It is recommended that the Company comply with SSAP 70 and properly allocate its general expenses to Loss adjustment expenses, other underwriting expenses, and Investment expenses. 13
iv	It is recommended that the Company properly allocate expenses in accordance with the annual statement instructions. 13
v	It is recommended that the Company allocate the fees paid to NHAG as required by the annual statement instructions. 14
vi	It is recommended that the Company properly classify all assets and liabilities in accordance with the annual statement instructions. 14
vii	It is recommended that the Company allocate adjusting and other payments to the appropriate accident year. 14
viii	It is recommended that the Company distribute annual conflict of interest disclosure statements and questionnaires to all directors, officers, trustees, and designated responsible employees. 15

<u>ITEM</u>		<u>PAGE NO.</u>
ix	It is recommended that the Company exercise greater care in the preparation of its Annual Statement.	15
	Subsequently, the Company submitted a draft of conflict of interest policy for approval which was approved by the board of directors on December 9, 2009.	
x	It is recommended that the Company limit its investments in any one institution to no more than 10% of its admitted assets pursuant to the provisions of Section 1409(a) of the New York Insurance Law.	15
xi	It is recommended that the Company include the requirements of Section 3426 of the New York Insurance law in its written cancellation procedures.	16
D.	<u>Deferred Tax Asset</u>	
	It is recommended that the Company non-admit deferred tax assets that do not meet the criteria set by Section 1301(a)(16) of the New York Insurance Law.	20



Respectfully submitted,

---

Wei Cao  
Senior Insurance Examiner

STATE OF NEW YORK     )  
                                  ) SS:  
                                  )  
COUNTY OF NEW YORK )

WEI CAO being duly sworn, deposes and says that the foregoing report, subscribed by her, is true to the best her knowledge and belief.

---

Wei Cao

Subscribed and sworn to before me

this \_\_\_\_\_ day of \_\_\_\_\_, 2010.

Appointment No. 30360

STATE OF NEW YORK  
INSURANCE DEPARTMENT

I, ERIC R. DINALLO, Superintendent of Insurance of the State of New York,  
pursuant to the provisions of the Insurance Law, do hereby appoint:

**Wei Cao**

as proper person to examine into the affairs of the

**KENSINGTON 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 24th day of June, 2009



A handwritten signature in black ink, appearing to read "Eric Dinallo", written over a horizontal line.

ERIC R. DINALLO  
Superintendent of Insurance