

REPORT ON EXAMINATION
OF THE
RESPONSE INDEMNITY COMPANY
AS OF
DECEMBER 31, 2003

DATE OF REPORT

JANUARY 21, 2005

EXAMINER

ADEBOLA AWOFOESO

TABLE OF CONTENTS

<u>ITEM NO.</u>	<u>PAGE NO.</u>
1. Scope of examination	2
2. Description of Company	3
A. Management	4
B. Territory and plan of operation	5
C. Reinsurance	7
D. Holding company system	8
E. Abandoned property law	11
F. Significant operating ratios	11
G. Accounts and records	12
3. Financial statements	13
A. Balance sheet	13
B. Underwriting and investment exhibit	15
4. Losses and loss adjustment expenses	17
5. Market conduct activities	17
6. Compliance with prior report on examination	18
7. Summary of comments and recommendations	20



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

January 21, 2005.

Honorable Howard Mills
Acting 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 22235 dated June 23, 2004 attached hereto, I have made an examination into the condition and affairs of Response Indemnity Company as of December 31, 2003, and submit the following report thereon.

The examination was conducted at the Company's administrative offices located at 500 South Broad Street, Meriden, Connecticut 06450

Wherever the designations "the Company" or "RNY" appear herein without qualification, they should be understood to indicate Response Indemnity Company. In addition, wherever the designations the "parent company" or "DRC" appear herein without qualification, they should be understood to indicate Direct Response Corporation.

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

1. SCOPE OF EXAMINATION

The previous examination was conducted as of December 31, 2000. This examination covered the three-year period from January 1, 2001 through December 31, 2003. Transactions occurring subsequent to this period were reviewed where deemed appropriate by the examiner.

The examination comprised a complete verification of assets and liabilities as of December 31, 2003. It included a review of income, disbursements and company records deemed necessary to accomplish such analysis or verification and utilized, to the extent considered appropriate, work performed by the Company's independent 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
- Loss experience
- Reinsurance
- Accounts and records
- Financial statements

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, which involve departures from laws, regulations or rules, or which are deemed to require explanation or description.

2. DESCRIPTION OF COMPANY

Response Indemnity Company was originally incorporated on October 17, 1995, as Adirondack Insurance Company by the Plymouth Rock Company of Boston Massachusetts. On November 22, 1996, ownership of Adirondack Insurance Company was transferred to Direct Response Corporation (“DRC”). It was organized and granted a certificate of authority pursuant to the New York Insurance Law on May 9, 1997. On September 17, 1997, Adirondack Insurance Company changed its name to Response Indemnity Company, the present title. The Company began operations as a direct writer of private and passenger automobile insurance on October 15, 1997.

Capital paid in is \$1,000,000 consisting of 10,000 shares of \$100 par value per share common stock. Gross paid in and contributed surplus is \$12,136,328. Gross paid in and contributed surplus increased by \$2,500,000 during the examination period, as follows:

<u>Year</u>	<u>Description</u>	<u>Amount</u>
2001	Beginning gross paid in and contributed surplus	\$ 9,636,328
2001	Surplus contribution	\$1,200,000
2002	Surplus contribution	<u>1,300,000</u>
	Total Surplus Contributions	<u>2,500,000</u>
2003	Ending gross paid in and contributed surplus	<u>\$12,136,328</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 or more than twenty-one members. The board met four times during each calendar year. At December 31, 2003, the board of directors was comprised of the following fourteen members:

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
August P. Alegi Stamford, CT	Vice President, General Counsel & Secretary, Response Indemnity Company Direct Response Corporation
Danny A. Collins Avon, CT	Vice President and Director, Response Indemnity Company
Kathleen A. Gleeson Sandy Hook, CT	Vice President and Director, Response Indemnity Company
Colleen Granahan Newton, MA	Counsel to the Chairman, The Plymouth Rock Company Incorporated
John J. Javaruski Avon, CT	President and Director, Response Indemnity Company
Mory Katz Katonah, NY	Chairman and Director, Response Indemnity Company
George Kowalsky Portland, CT	Vice President and Treasurer, Director, Response Indemnity Company
Eileen A. Lehman Hamden, CT	Director, Response Indemnity Company
Jayshree Maurantonio Dobbs Ferry, NY	Director, Response Indemnity Company
Steven B. Oakley Ridgefield, CT	Vice president and Director, Response Indemnity Company
Sean P. Payne Meriden, CT	Director, Response Indemnity Company

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Francis M. Quido North Brandford, CT	Vice President and Director, Response Indemnity Company
David I. Schonbrun White Plains, NY	Assistant Secretary, Deputy General Counsel and Director, Response Indemnity Company
Clifford Wess Flanders, NJ	Vice President, Chief Actuary and Director, Response Indemnity Company

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 had an acceptable record of attendance.

As of December 31, 2003, the principal officers of the Company were as follows:

<u>Name</u>	<u>Title</u>
John J. Javaruski	President
George Kowalsky	Vice President and Treasurer
August P. Alegi	Vice President, Secretary and General Counsel
Danny A. Collins	Vice President
Kathleen A. Gleeson	Vice President
Steven B. Oakley	Vice President
Francis M. Quido	Vice President
Clifford Wess	Vice President

B. Territory and Plan of Operation

As of December 31, 2003, the Company was licensed to write business only in New York.

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>
3	Accident & health
4	Fire
5	Miscellaneous property damage
6	Water damage
7	Burglary and theft
8	Glass
12	Collision
13	Personal injury liability
14	Property damage liability
19	Motor vehicle and aircraft physical damage
20	Marine and inland marine
26	Gap

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 \$3,700,000.

The following schedule shows the direct premiums written by the Company both in total and in New York for the period under examination:

DIRECT PREMIUMS WRITTEN

<u>Calendar Year</u>	<u>New York State</u>	<u>Total United States</u>	<u>Premiums Written in New York State as a percentage of United States Premium</u>
2001	\$4,156,328	\$4,156,328	100.00%
2002	\$2,461,048	\$2,461,048	100.00%
2003	\$2,326,148	\$2,326,148	100.00%

The Company began operations as a direct writer of private passenger automobile insurance. At present, the Company continues writing only private passenger liability and physical damage insurance. Business is solicited and marketed through direct mail, radio and affinity groups, such as professional or trade associations and also the internet.

C. Reinsurance

Assumed

The Company does not assume any reinsurance business.

Ceded

The Schedule F data as contained in the Company's filed annual statements was found to accurately reflect its reinsurance transactions.

The examiner reviewed all ceded reinsurance contracts in effect at December 31, 2003. The contracts all contained the required standard clauses including insolvency clauses meeting the requirements of Section 1308 of the New York Insurance Law.

The Company had the following ceded reinsurance program in effect at December 31, 2003:

<u>Type of treaty</u>	<u>Cession</u>
First Private Passenger Excess of Loss Reinsurance Agreement 100% Authorized	100% of \$700,000 of the Company's ultimate net loss each occurrence in excess of \$300,000 not to exceed \$700,000, in any one occurrence.
Second Private Passenger Excess of Loss Reinsurance Agreement 100% Authorized	100% of \$1,000,000 of the Company's ultimate net loss each occurrence in excess of \$1,000,000 not to exceed \$1,000,000, in any one occurrence.
Third Private Passenger Excess of Loss Reinsurance Agreement 100% Authorized	50% of \$1,000,000 of the Company's ultimate net loss each occurrence in excess of \$2,000,000 not to exceed \$1,000,000, in any one occurrence.
90% Quota Share Reinsurance Agreement of Personal Umbrella Business 100% Authorized	90% of the first \$1,000,000 of the Company's net loss each occurrence and 100% of the difference, if any between the policy limit and the first \$1,000,000. The coverage shall not exceed \$3,000,000 for each occurrence.

The Company's retention increased from \$250,000 to \$300,000 and its limits remained the same compared with the prior examination period. The percentage of cessions to authorized reinsurers remained the same compared with the prior examination period.

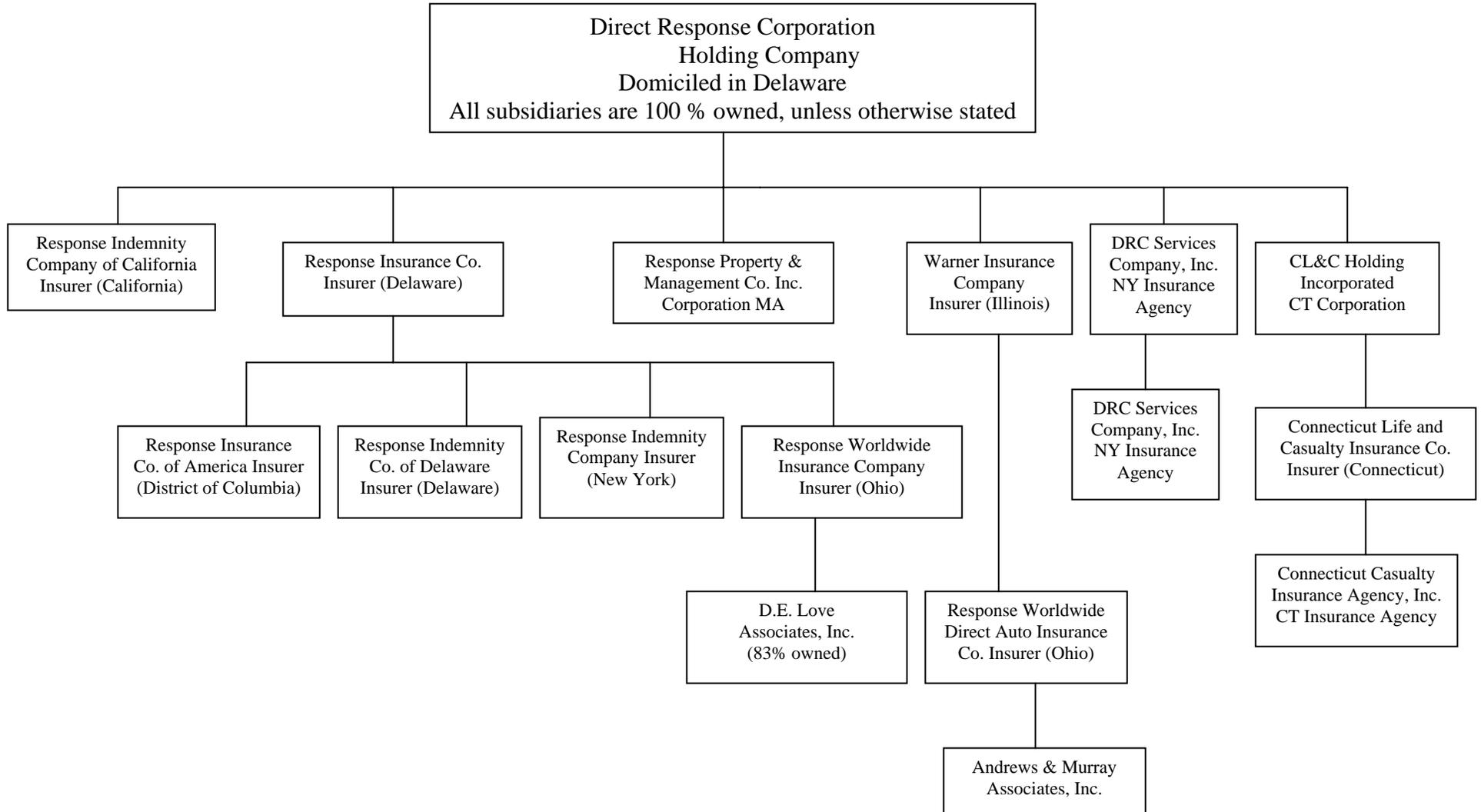
D. Holding Company System

The Company is a wholly-owned subsidiary of Response Insurance Company, a Delaware domiciled insurer; and is ultimately controlled by Direct Response Corporation.

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 a chart of the holding company system at December 31, 2003:

HOLDING COMPANY SYSTEM ORGANIZATIONAL CHART



At December 31, 2003, the Company was party to the following agreements with other members of its holding company system:

Tax Allocation Agreement

The Company is party to a tax allocation agreement with Direct Response Corporation, effective March 7, 2001. Pursuant to the term of the agreement, the parties will file consolidated federal income tax returns. The agreement stipulates that the Company's tax liability, on a consolidated basis, would be no more than what it would have been if the Company filed a separate return. The agreement was submitted to the Department on March 2, 2001 for review and non-disapproval as required by Circular Letter No. 33 (1979).

Service Agreement with Direct Response Corporation

Effective January 1, 1999, the Company entered into a service agreement with Direct Response Corporation. The agreement was established to provide RNY with all the necessary administrative, production, marketing, underwriting, investment, and accounting functions with respect to its business operations. The service agreement was amended effective January 1, 2004, to include prior examination report recommendations. The amended agreement was submitted to the Department for review and non-disapproval as required by Section 1505(d) of the New York Insurance Law.

The service agreement settlement provision stated that:

“within ten (10) days after the end of each month, DRC shall send RNY an invoice setting forth the amount due RNY for services and claim service provided by DRC during the preceding month. RNY shall pay the amount set forth in the invoice within fifteen (15) days of its receipts of the invoice.”

Examination review of compliance with aforementioned clause indicated remittances were made on an estimated basis. It is recommended that the Company adhere to its service agreement clauses as stated.

E. Abandoned Property Law

Section 1316 of the New York Abandoned Property Law provides that amounts payable to a resident of this state from a policy of insurance, if unclaimed for three years, shall be deemed to be abandoned property. Such abandoned property shall be reported to the comptroller on or before the first day of April each year. Such filing is required of all insurers regardless of whether or not they have any abandoned property to report.

The Company's abandoned property reports for calendar years 2002 and 2003 were not filed on a timely basis pursuant to the provisions of Section 1316 of the New York State Abandoned Property Law. It is recommended that the Company file its abandoned property reports on a timely basis pursuant to the provisions of Section 1316 of the New York Abandoned Property Law.

F. Significant Operating Ratios

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

Net premiums written to surplus as regards policyholders	28%
Liabilities to liquid assets (cash and invested assets less investments in affiliates)	34%
Premiums in course of collection to surplus as regards policyholders	1%

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 three-year period covered by this examination:

	<u>Amounts</u>	<u>Ratios</u>
Losses and loss		
adjustment expenses incurred	\$10,471,775	95.08%
Other underwriting expenses		
incurred	2,198,698	19.96
Net underwriting loss	<u>(1,656,499)</u>	<u>(15.04)</u>
Premiums earned	<u>\$11,013,974</u>	<u>100.00%</u>

G. Accounts and Records

Custodian Agreement

Management answered affirmatively to the following General Interrogatory:

“Excluding items in Schedule E, real estate, mortgage loans and investments held physically in the reporting entity’s offices, vaults or safety deposit boxes, were all stocks, bonds and other securities, owned throughout the current year held pursuant to a custodial agreement with a qualified bank or trust company in accordance with Part 1-General, Section IV.H-Custodial or Safekeeping Agreements of the NAIC Financial Condition Examiners Handbook?”

However, a review of this response disclosed that the Company’s custodial agreement was lacking the protective covenants set forth in Section IV.H of the NAIC Financial Condition Examiners Handbook.

It is recommended that the Company amend its custodial agreement to comply with NAIC guidelines.

3. FINANCIAL STATEMENTS

A Balance Sheet

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

<u>Assets</u>	<u>Assets</u>	<u>Assets Not Admitted</u>	<u>Net Admitted Assets</u>
Bonds	\$11,779,271	\$	\$11,779,271
Cash, cash equivalents and short-term investments	454,500		454,500
Investment income due and accrued	118,963		118,963
Uncollected premiums and agents' balances in the course of collection	112,405	50,154	62,251
Deferred premiums, agents' balances and installments booked but deferred and not yet due	179,273		179,273
Net deferred tax assets	2,294,617	2,294,617	0
Receivables from parent, subsidiaries and affiliates	<u>145,224</u>	<u> </u>	<u>145,224</u>
Totals assets	<u>\$15,084,253</u>	<u>\$2,344,771</u>	<u>\$12,739,482</u>

Liabilities

Losses	\$2,989,558
Loss adjustment expenses	847,075
Other expenses (excluding taxes, licenses and fees)	93,853
Taxes, licenses and fees (excluding federal and foreign income taxes)	(100,467)
Unearned premiums	545,530
Ceded reinsurance premiums payable (net of ceding commissions)	(6,012)
Payable to parent, subsidiaries and affiliates	2,456
Aggregate write-ins for liabilities	<u>20,575</u>
 Total liabilities	 \$4,392,568

Surplus and Other Funds

Common capital stock	\$1,000,000
Gross paid in and contributed surplus	12,136,328
Unassigned funds (surplus)	<u>(4,789,414)</u>
Surplus as regards policyholders	<u>8,346,914</u>
 Totals liabilities surplus and other funds	 <u>\$12,739,482</u>

NOTE: The Internal Revenue Service has not yet begun to audit the income tax returns covering tax years 2001 through 2003. 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 increase \$3,050,209 during the three years examination period

January 1, 2001 through December 31, 2003, detailed as follows:

<u>Underwriting Income</u>		
Premiums earned		\$11,013,974
Deductions:		
Losses incurred	\$7,895,335	
Loss adjustment expenses incurred	2,576,440	
Other underwriting expenses incurred	<u>2,198,698</u>	
Total underwriting deductions		<u>12,670,473</u>
Net underwriting loss		\$(1,656,499)
 <u>Investment Income</u>		
Net investment income earned	\$1,198,186	
Net realized capital gains	<u>779,387</u>	
Net investment gain		1,977,573
 <u>Other Income</u>		
Net gain or (loss) from agents' or premium balances charged off	\$(12,385)	
Finance and service charges not included in premiums	214,625	
Miscellaneous income	<u>2</u>	
Total other income		<u>202,242</u>
Net income before dividends to policyholders and before federal and foreign income taxes		\$523,316
Federal and foreign income taxes incurred		<u>2</u>
Net income		<u>\$523,318</u>

C. Capital and Surplus Account

Surplus as regards policyholders per report on examination as of December 31, 2000			\$5,296,705
	<u>Gains in Surplus</u>	<u>Losses in Surplus</u>	
Net income	\$523,318		
Change in net deferred income tax	2,294,617		
Change in non-admitted assets		\$2,267,726	
Surplus adjustments paid in	<u>2,500,000</u>		
Total gain to surplus	<u>\$5,317,935</u>	<u>\$2,267,726</u>	
Net increase in surplus			<u>3,050,209</u>
Surplus as regards policyholders per report on examination as of December 31, 2003			<u>\$8,346,914</u>

4. LOSSES AND LOSS ADJUSTMENT EXPENSES

The examination liability for the captioned items of \$3,836,633 is the same as reported by the Company as of December 31, 2003. The analysis of this item was conducted in accordance with generally accepted actuarial principles and practices and was based on statistical information contained in the Company's internal records and in its filed annual statements.

5. MARKET CONDUCT ACTIVITIES

In the course of this examination, a review was made of the manner in which the Company conducts its business practices and fulfills its contractual obligations to policyholders and claimants. The review was general in nature and is not to be construed to encompass the more precise scope of a market conduct investigation, which is the responsibility of the Market Conduct Unit of the Property Bureau of this Department.

The general review was directed at practices of the Company in the following areas:

- A. Underwriting
- B. Claims and complaint handling

No problem areas were encountered.

6. COMPLIANCE WITH PRIOR REPORT ON EXAMINATION

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

<u>ITEM</u>	<u>PAGE NO.</u>
A <u>Management</u>	
It is recommended that board members who are unable or unwilling to attend meetings consistently should resign or be replaced.	5
The Company complied with this recommendation	
It is recommended that the Company comply with Section 1411(a) of the New York Insurance Law, which requires that investments be approved and authorized by the Company's board of directors or any committee thereof.	6
The Company complied with this recommendation	
It is recommended that the Company exercise care when answering general interrogatories of its filed and sworn to annual statements.	6
The Company complied with this recommendation	
B <u>Reinsurance</u>	
It is recommended that the Company amend its reinsurance agreements to revise the insolvency clause so that it complies with the requirements of Section 1308 of the New York Insurance Law.	9
The Company complied with this recommendation	
It is recommended that an agreement indicating how ceded reinsurance premiums shall be allocated be established. This agreement should meet the standards of Section 1505(a) of the New York Insurance Law and be submitted to the Department pursuant to Section 1505(d)(3) of the New York Insurance Law.	10
The Company complied with this recommendation	

ITEMPAGE NO.C Holding Company SystemUnallocated Loss Adjustment Expense Payments

It is recommended that the Company comply with Department Regulation 30, Part 106.6 and Section 1505 of the New York Insurance Law. 13

The Company complied with this recommendation

It is recommended that the service agreement with DRC be amended to include claim functions as part of the services provided to the Company. If claim services are also provided to the Company's affiliates, such amendment should include provisions that formally set forth the basis upon which the allocation percentages of each company is calculated. Amendments to inter-company agreements should meet the standards of Section 1505(a), comply with Department Regulation 30, and be submitted to the Department pursuant to Section 1505(d)(2) of the New York Insurance Law. 14

The Company complied with this recommendation

D Accounts and RecordsInvestments

It is recommended that the Company monitor its investment portfolio for compliance with Section 1409(a) of the New York Insurance Law. 15

The Company complied with this recommendation

Underwriting and Investment Exhibit Part 4-Expenses

It is recommended that the Company comply with Department Regulation 30 and annual statement instructions when completing its Underwriting and Investment Exhibit Part-4 Expenses and allocate its service fee and unallocated loss adjustment expense to the appropriate expense account item. 16

The Company complied with this recommendation

Schedule P: Reporting of Loss Adjustment Expense Reserves

It is recommended that for future filings the Company properly categorize its allocated loss adjustment expense reserves. 17

The Company complied with this recommendation

ITEMPAGE NO.Disaster Recovery Plan

It is recommended that the Company ensure that its disaster recovery plan be finalized and implemented. Once this plan is established, the Company should perform periodic testing to ensure that formulated procedures will operate as intended.

17

The Company complied with this recommendation.

7. **SUMMARY OF COMMENTS AND RECOMMENDATIONS**

ITEMPAGE NO.

A Service Agreement with Direct Response Corporation

It is recommended that the Company adhere to its service agreement clauses as stated.

11

B Abandoned Property Law

It is recommended that the Company file its abandoned property reports on a timely basis pursuant to the provisions of Section 1316 of the New York Abandoned Property Law.

11

C Custodian Agreement

It is recommended that the Company amend its custodial agreement to comply with NAIC guidelines.

12

Respectfully submitted,

_____/S/_____
Adebola Awofeso,
Senior Insurance Examiner

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

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

_____/S/_____
Adebola Awofeso

Subscribed and sworn to before me
this _____ day of _____, 2005.

Appointment No 22235

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:

Adebola Awofeso

as proper person to examine into the affairs of the

RESPONSE INDEMNITY COMPANY

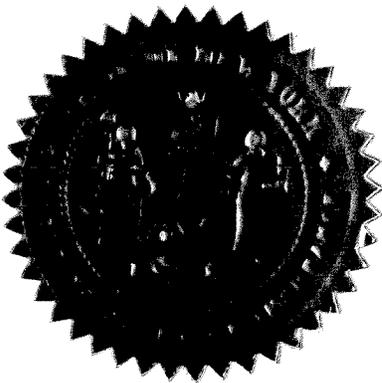
and to make a report to me in writing of the condition of the said

Company

with such other information as he shall deem requisite.

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

this 23rd day of June, 2004





GREGORY V. SERIO
Superintendent of Insurance