

REPORT ON EXAMINATION

OF THE

BERKSHIRE HATHAWAY ASSURANCE CORPORATION

AS OF

DECEMBER 31, 2012

DATE OF REPORT

MAY 23, 2014

EXAMINER

ADEBOLA AWOFESO

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NEW YORK STATE  
DEPARTMENT *of*  
FINANCIAL SERVICES

Andrew M. Cuomo  
Governor

Benjamin M. Lawsky  
Superintendent

May 23, 2014

Honorable Benjamin M. Lawsky  
Superintendent of Financial Services  
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 30965 dated February 26, 2013, attached hereto, I have made an examination into the condition and affairs of Berkshire Hathaway Assurance Corporation as of December 31, 2012, 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 main administrative office located at 3024 Harney Street, Omaha, Nebraska 68131.

## 1. SCOPE OF EXAMINATION

The Department has performed a coordinated group examination of the Berkshire Hathaway Assurance Corporation. The examination was conducted in conjunction with the state of Nebraska, which was the coordinating state of the Berkshire Hathaway Group of Insurance Companies. This is the first financial examination of the Company after the report on organization, which was conducted as of December 27, 2007. This examination covered the period from December 28, 2007 through December 31, 2012. Transactions occurring subsequent to this period were reviewed where deemed appropriate by the examiner.

The examination was performed concurrently with the examinations of the following insurers:

- American Centennial Insurance Company (DE)
- Berkshire Hathaway Assurance Corporation (NY)
- Berkshire Hathaway Homestate Insurance Company (NE)
- Berkshire Hathaway Life Insurance Company of Nebraska (NE)
- Brookwood Insurance Company (IA)
- Columbia Insurance Company (NE)
- Continental Divide Insurance Company (CO)
- Cypress Insurance Company (CA)
- Finial Reinsurance Company (CT)
- National Fire & Marine Insurance Company (NE)
- National Indemnity Company (NE)
- National Indemnity Company of Mid-America (IA)
- National Indemnity Company of the South (FL)
- National Liability & Fire Insurance Company (CT)
- Oak River Insurance Company (NE)
- Redwood Fire and Casualty Insurance Company (NE)
- Stonewall Insurance Company (NE)
- Unione Italiana Reinsurance Company of America (NY)
- Wesco-Financial Insurance Company (NE)

Other states participating in this examination were California, Colorado, Connecticut, Delaware, Florida, Iowa and Nebraska.

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 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 Statutory Accounting Principles and annual statement instructions when applicable to domestic state regulations.

All financially significant 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 Handbook:

- Significant subsequent events
- Company history
- Corporate records
- Management and control
- Fidelity bonds and other insurance
- Territory and plan of operation
- Growth of Company
- Loss experience
- Reinsurance
- Accounts and records
- Statutory deposits
- Financial statements
- 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

Berkshire Hathaway Assurance Corporation was incorporated under the laws of the State of New York on December 21, 2007. It became licensed on December 28, 2007 in the State of New York to engage in financial guaranty and surety insurance business.

The Company operates as a monoline bond insurer and provides insurance for tax-exempt bonds issued by states, cities and other local entities. The Company insures these securities for issuers both at the time their bonds are sold to the public (primary transactions) and also provides insurance for bonds that are already owned by investors in the secondary market.

The Company is 51% owned by Columbia Insurance Company (“CIC”) and 49% owned by National Indemnity Company (“NICO”), both Nebraska domiciled insurers.

Capital paid in is \$15,000,000 consisting of 2,500 shares of \$6,000 par value per share common stock. Effective January 18, 2008, the Company amended its charter to increase the par value of its common stock from \$1,000 per share to \$6,000 per share. Gross paid in and contributed surplus is \$990,000,000. The following chart shows the changes to capital stock and gross paid in and contributed surplus during the examination period:

<u>Date</u>	<u>Description</u>	<u>Common Capital Stock</u>	<u>Gross paid in and contributed surplus</u>
12/28/2007	Beginning balance	\$ 2,500,000	\$102,500,000
1/18/2008	Increase in par value of common stock	12,500,000	(12,500,000)
3/31/2008	Surplus contribution from parent	<u>0</u>	<u>900,000,000</u>
12/31/2012	Ending balance	<u>\$15,000,000</u>	<u>\$990,000,000</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 seven members. At December 31, 2012, the board of directors was comprised of the following eight members:

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
John Duane Arendt, Stamford, CT	Insurance Executive, National Liability & Fire Insurance Company

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Erika Bunner Duffy, Fairfield, CT	Attorney, National Liability & Fire Insurance Company
Lori Jill Friedman, Armonk, NY	Attorney, National Liability & Fire Insurance Company
Dale David Geistkemper Omaha, NE	Treasurer and Controller, National Indemnity Company
Ajit Jain, Rye, NY	Chairman of the Board, National Liability & Fire Insurance Company
Forrest Nathan Krutter, Milyon Mills, NH	Attorney, Insurance Executive, National Indemnity Company
Brian Gerard Snover, Stamford, CT	Attorney, Insurance Executive, National Liability & Fire Insurance Company
Donald Frederick Wurster, Omaha, NE	Insurance Executive, National Indemnity Company

As of December 31, 2012, the principal officers of the Company were as follows:

<u>Name</u>	<u>Title</u>
Donald Frederick Wurster	President
Dale David Geistkemper	Treasurer
Erika Bunner Duffy	Secretary

B. Territory and Plan of Operation

As of December 31, 2012, 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)	Surety
17 (A)	Credit
25	Financial Guaranty

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 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 both in total and in New York for the period under examination:

<u>Calendar Year</u>	<u>New York State</u>	<u>Total Premiums</u>	<u>Premiums Written in New York State as a Percentage of Total Premium</u>
2008	\$500,859,153	\$593,629,919	84.37%
2009	\$ 18,862,526	\$ 38,814,133	48.60%
2010	\$ 0	\$ 6,511,350	0.00%
2011	\$ 0	\$ 5,379,513	0.00%
2012	\$ 1,853,850	\$ 10,214,551	18.15%

The company operates as a monoline bond insurer and provides insurance for tax-exempt bonds issued by states, cities and other local entities. The Company insures these securities for issuers both at the time their bonds are sold to the public (primary transactions) and also provides insurance for bonds that are already owned by investors in the secondary market.



C. Reinsurance

The Company has structured its ceded reinsurance program to limit its maximum 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, 2012:

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

The Company entered into a facultative quota share reinsurance agreement with National Indemnity Company ("NICO"), an affiliate. Under the terms of this agreement NICO agrees to reinsure 92.5% of a surety bond the Company issued 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 of the Schedule F data reported by the Company in its filed annual statement was found to accurately reflect its reinsurance transactions.

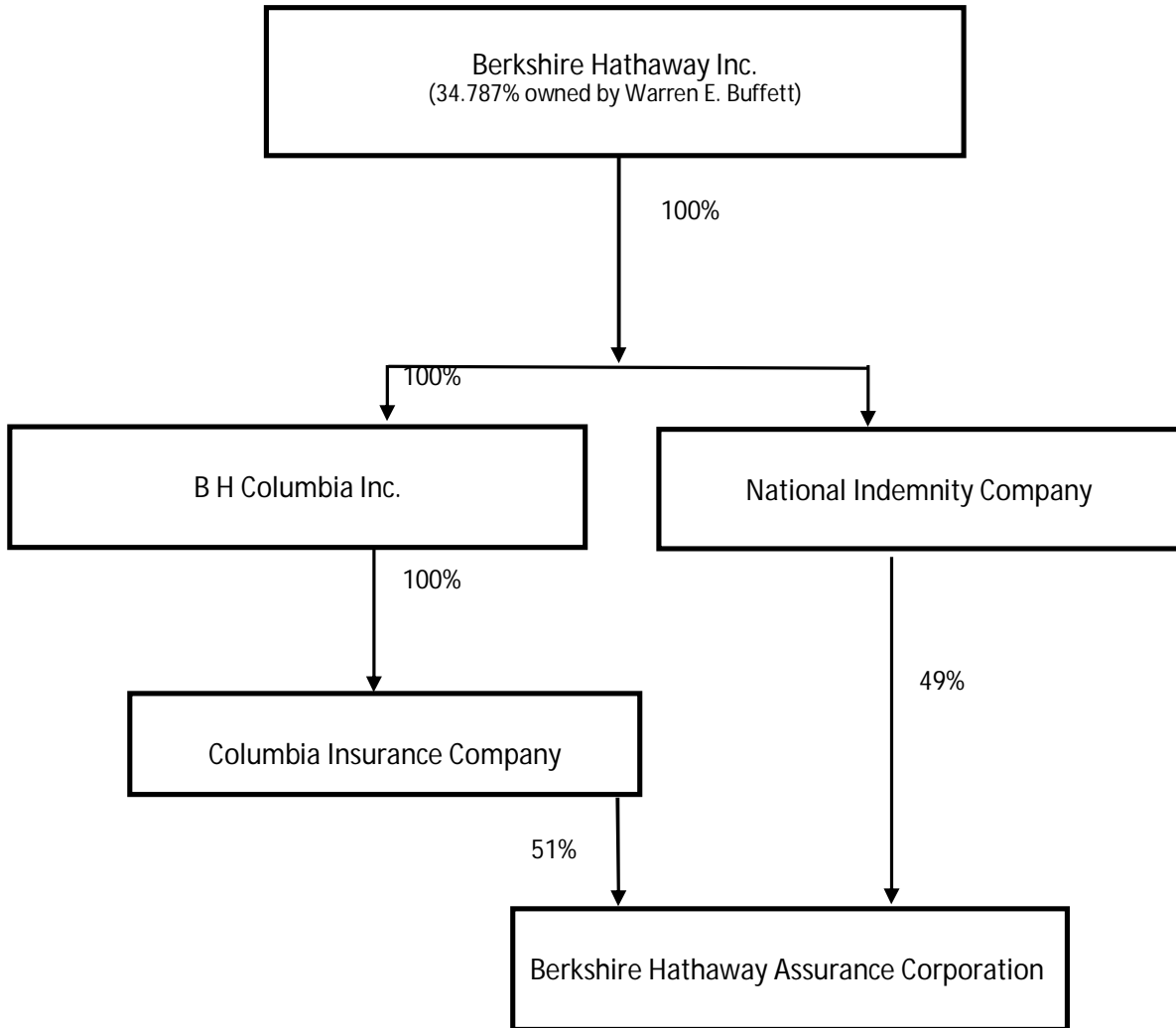
Additionally, management has represented that all material ceded reinsurance agreements transfer both underwriting and timing risk as set forth in SSAP No. 62R. Representations were supported by appropriate risk transfer analyses and an attestation from the Company's Chief Executive Officer pursuant 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 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 are ultimately controlled by Berkshire Hathaway Inc. (34.787% 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 abbreviated chart of the Company's holding company system at December 31, 2012:



At December 31, 2012, 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 among 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 will file consolidated federal income tax returns. Said agreement stipulates that the Company's tax liability on a consolidated basis would not exceed the liability had the Company 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.

Service Agreement with National Indemnity Company

Effective January 1, 2008, the Company and its affiliate, National Indemnity Company ("NICO"), entered into a service agreement. Under the terms of this agreement, NICO performs certain administrative and special services on behalf of the Company. The agreement provides that payment for services provided shall be on an actual cost basis. The agreement was filed with the Department pursuant to Section 1505 of the New York Insurance Law.

Service Agreement with National Liability & Fire Insurance Company

Effective January 1, 2008, the Company and its affiliate, National Liability & Fire Insurance Company ("NLF"), entered into a service agreement. Under the terms of this agreement, NLF performs certain administrative and special services on behalf of the Company. The agreement provides that payment for services provided shall be on an actual cost basis. The agreement was filed with the Department pursuant to Section 1505 of the New York Insurance Law.

### Investment Services Agreement

Effective December 31, 2007, the Company and NICO entered into an Investment Services Agreement. Pursuant to the agreement, NICO will act as an investment manager of the Company. The agreement was filed with the Department pursuant to Section 1505 of the New York Insurance Law.

### Inter-Company Service Agreement with FlightSafety International

Effective January 1, 2008, the Company and its affiliate, FlightSafety International (“FlightSafety”), entered into a service agreement. Under the terms of this agreement, FlightSafety performs certain administrative and special services on behalf of the Company. The agreement provides that payment for services provided shall be on an actual cost basis. The agreement was filed with the Department pursuant to Section 1505 of the New York Insurance Law.

### E. Significant Operating Ratios

The following ratios have been computed as of December 31, 2012, based upon the results of this examination:

Net premiums written to surplus as regards policyholders	1%
Liabilities to liquid assets (cash and invested assets less investments in affiliates)	38%
Premiums in course of collection to surplus as regards policyholders	0%

All of the above ratios fall within the benchmark range set forth in the Insurance Regulatory Information System (“IRIS”) of the National Association of Insurance Commissioners.

The underwriting ratios presented below are on an earned/incurred basis and encompass the December 28, 2007 to December 31, 2012 time period covered by this examination:

	<u>Amounts</u>	<u>Ratios</u>
Losses and loss adjustment expenses incurred	\$ 0	0.00%
Other underwriting expenses incurred	48,089,161	41.81
Net underwriting gain	<u>66,920,679</u>	<u>58.19</u>
Premiums earned	<u>\$115,009,840</u>	<u>100.00%</u>

F. Risk Management and Internal Control

A review was made of the Company's internal control with regard to its IT environment. The review found numerous internal control weaknesses. The Company was provided with a copy of the IT recommendations, none of which will be considered a serious control deficiency.

It is recommended that the Company address the internal control weaknesses identified during the review of the Company's IT environment.

### 3. FINANCIAL STATEMENTS

#### A. Balance Sheet

The following shows the assets, liabilities and surplus as regards policyholders as of December 31, 2012 as determined by this examination and as reported by the Company:

<u>Assets</u>	<u>Assets</u>	<u>Assets Not Admitted</u>	<u>Net Admitted Assets</u>
Bonds	\$ 544,335,858	\$ 0	\$ 544,335,858
Preferred stocks	128,000,000		128,000,000
Common stocks	423,032,584		423,032,584
Property held for sale	3,750,000	3,750,000	0
Cash, cash equivalents and short-term investments	733,699,804		733,699,804
Investment income due and accrued	12,067,273		12,067,273
Uncollected premiums and agents' balances in the course of collection	<u>101,198</u>	<u>0</u>	<u>101,198</u>
Total assets	<u>\$1,844,986,717</u>	<u>\$3,750,000</u>	<u>\$1,841,236,717</u>

#### Liabilities, Surplus and Other Funds

##### Liabilities

Losses and loss adjustment expenses		\$ 0
Taxes, licenses and fees (excluding federal and foreign income taxes)		258,892
Current federal and foreign income taxes		4,343,760
Net deferred tax liability		9,859,827
Unearned premiums		534,329,314
Advance premium		2,760,194
Payable to parent, subsidiaries and affiliates		48,831
Contingency reserves		<u>140,339,151</u>
Total liabilities		\$ <u>691,939,969</u>

##### Surplus and Other Funds

Common capital stock	\$ 15,000,000	
Gross paid in and contributed surplus	990,000,000	
Unassigned funds (surplus)	<u>144,296,748</u>	
Surplus as regards policyholders		<u>\$1,149,296,748</u>
Total liabilities, surplus and other funds		<u>\$1,841,236,717</u>

Note: The Internal Revenue Service has completed its audits of the Company's consolidated Federal Income Tax returns through tax year 2009. 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 2010 through 2011 are currently under examination. 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

Surplus as regards policyholders increased \$1,044,296,748 during the examination period December 28, 2007 through December 31, 2012, detailed as follows:

Underwriting Income

<u>Premiums earned</u>		\$ 115,009,840
Deductions:		
Losses and loss adjustment expenses incurred	\$	0
Other underwriting expenses incurred		<u>48,089,161</u>
Total underwriting deductions		<u>48,089,161</u>
Net underwriting gain		\$ 66,920,679

Investment Income

Net investment income earned	\$	250,562,739
Net realized capital gain		<u>18,864,173</u>
Net investment gain		\$ 269,426,912

Other Income

Aggregate write-ins for miscellaneous income	\$	<u>(193,567)</u>
Total other income		\$ <u>(193,567)</u>
Net income before federal and foreign income taxes		\$ 336,154,024
Federal and foreign income taxes incurred		<u>122,262,323</u>
Net income		\$ <u>213,891,701</u>



Surplus as regards policyholders per report on organization as of December 27, 2007			\$105,000,000
	<u>Gains in Surplus</u>	<u>Losses in Surplus</u>	
Net income	\$213,891,701	\$	
Net unrealized capital gains or (losses)	54,830,115		
Change in net deferred income tax	19,664,081		
Change in non-admitted assets		4,953,584	
Cumulative effect of changes in accounting	1,203,584		
Capital transferred from surplus	12,500,000		
Surplus paid in	900,000,000		
Surplus transferred to capital stock		12,500,000	
Increase in contingency reserve		<u>140,339,151</u>	
Total gains and losses	<u>\$1,202,089,483</u>	<u>\$157,792,735</u>	
Net increase (decrease) in surplus			<u>\$1,044,296,748</u>
Surplus as regards policyholders per report on examination as of December 31, 2012			<u>\$1,149,296,748</u>

#### **4. LOSSES AND CONTINGENCY RESERVES**

The examination liabilities for losses and contingency reserves are \$0 and \$140,339,151, respectively, as of December 31, 2012. These are the same as the amounts reported by the Company in its 2012 filed annual statement.

In addition to case reserves, the Company is required to establish and maintain contingency reserves for the protection of insureds and claimants against the effect of excessive losses occurring during adverse economic cycles. The amount required for those reserves depends on the types of bonds being insured and are established pursuant to the provisions of Section 6903(a) of the New York Insurance Law. New York Insurance Law requires that one-eightieth of required contingency reserves are accreted every quarter over a twenty year period, however the Company has committed to the Department it would accrete one fortieth of required contingency reserves each quarter over a ten year period.

5. **COMPLIANCE WITH REPORT ON ORGANIZATION**

The report on organization did not contain any comments or recommendations.

6. **SUMMARY OF COMMENTS AND RECOMMENDATIONS**

ITEM

PAGE NO.

A. Risk Management and Internal Control

It is recommended that the Company address the internal control weaknesses identified during the review of the Company's IT environment.

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APPOINTMENT NO. 30965

NEW YORK STATE

**DEPARTMENT OF FINANCIAL SERVICES**

I, BENJAMIN M. LAWSKY, 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:

*Adebola Awofeso*

*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 26th day of February, 2013*

**BENJAMIN M. LAWSKY**  
*Superintendent of Financial Services*



By:

*Jean Marie Cho*  
*Deputy Superintendent*