

REPORT ON EXAMINATION

OF THE

STERLING INSURANCE COMPANY

AS OF

DECEMBER 31, 2010

DATE OF REPORT

FEBRUARY 24, 2012

EXAMINER

WAYNE LONGMORE

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NEW YORK STATE
DEPARTMENT *of*
FINANCIAL SERVICES

Andrew M. Cuomo
Governor

Benjamin M. Lawsky
Superintendent

February 24, 2012

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 30740 dated June 30th, 2011, attached hereto, I have made an examination into the condition and affairs of Sterling Insurance Company as of December 31, 2010, and submit the following report thereon.

Wherever the designations “the Company” or “SIC” appear herein without qualifications, they should be understood to indicate Sterling Insurance Company.

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 home office located at 182 Barnerville Road, Cobleskill, New York 12043.

1. SCOPE OF EXAMINATION

The Department has performed a single-state examination of Sterling Insurance Company. The previous examination was conducted as of December 31, 2005. This examination covered the five-year period from January 1, 2006 through December 31, 2010. Transactions occurring subsequent to this period were reviewed where deemed appropriate by the examiner.

This examination was conducted in accordance with the National Association of Insurance Commissioners (“NAIC”) Financial Condition Examiners Handbook (“Handbook”), which requires that we plan and perform the examination to evaluate the financial condition and identify 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:

- 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
- 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

The Company was incorporated under the laws of the State of New York on October 17, 1895, as the Schoharie and Otsego Mutual Fire Insurance Company for the purpose of transacting business as a co-operative fire insurance corporation. The Company adopted its current name on May 20, 1959. The Company's charter currently permits it to transact business in all counties of this state.

On May 12, 2004, the Company issued a 30-year surplus note in the amount of \$3 million. The interest rate is set each quarter based upon the three-month LIBOR plus 3.8%. The terms of this surplus note were approved by the Department on April 22, 2004. As of December 31, 2010, the Company has received approval from the State of New York to pay down \$200,000 of principal. Payments of \$100,000 each were made in September and December of 2010. At December 31, 2010, the balance on this note was \$2.8 million with accrued interest thereon approximating \$4,786.

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 nine nor more than thirteen members. The board met five times during each calendar year for the period under examination. At December 31, 2010, the board of directors was comprised of the following nine members:

| <u>Name and Residence</u> | <u>Principal Business Affiliation</u> |
|-------------------------------------|---|
| Stephen A. Harris Cobleskill, NY | President, Sterling Insurance Company |
| Brian A. Kaiser Howes Cave, NY | Coordinator of Communiversitry Affairs, SUNY Cobleskill |
| Henry Lamont Cobleskill, NY | Owner, Lamont Engineers Vice President, Sterling Insurance Company |

| <u>Name and Residence</u> | <u>Principal Business Affiliation</u> |
|---------------------------------------|--|
| Frederick J. Lindsay Herkimer, NY | Retired, Retail Management |
| Patricia A. MacNeil Cobleskill, NY | Secretary, Sterling Insurance Company |
| Daniel B. Schulte Cobleskill, NY | Owner, Bert Schulte Construction, Inc. Contractor |
| Howard J. Stauble Cobleskill, NY | Treasurer, Sterling Insurance Company |
| Donald R. Whiting Selkirk, NY | Retired Insurance Professional |
| Paula D. Wissenbach Cobleskill, NY | Chief Financial Officer and Assistant Treasurer, Sterling Insurance 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, 2010, the principal officers of the Company were as follows:

| <u>Name</u> | <u>Title</u> |
|------------------------|-----------------------|
| Stephen A. Harris | President |
| Howard J. Stauble | Treasurer |
| Patricia A. MacNeil | Secretary |
| Howard J. Rickard, Jr. | Senior Vice President |
| Christopher F. Schline | Senior Vice President |
| Janette F. Rosscoe | Senior Vice President |
| Paula D. Wissenbach | Senior Vice President |

B. Territory and Plan of Operation

As of December 31, 2010, 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 (inland marine only) |

Based on the lines of business for which the Company is licensed and pursuant to the requirements of Articles 13, 41 and 66 of the New York Insurance Law, the Company is required to maintain a minimum surplus to policyholders in the amount of \$700,000.

In 2006, the Company began writing boiler and machinery business. However, its license did not include authority to write this kind of insurance until it was amended effective February 8, 2010. It is recommended that the Company refrain from writing kinds of insurance for which it is not licensed pursuant to Section 1113(a) of the New York Insurance Law.

The Company's predominant lines of business are homeowners multiple peril and commercial multiple peril, which accounted for 61.4% and 29.0%, respectively, of the Company's 2010 direct written business. At December 31, 2010, the Company wrote business through approximately 495 independent agents.

The Company participates as a direct writer in any combination policy issued by New York Mutual Underwriters ("NYMU"). As of November 1997, the Company shares, with one other advance premium corporation, one-half of all NYMU's premiums, losses and expenses. NYMU's predominate lines of business are commercial/special multiple peril, commercial landlord, personal dwellings and allied lines of business. Approximately 8% of the Company's total direct written premiums were attributable to New York Mutual Underwriters.

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

| <u>Calendar Year</u> | <u>Direct Premiums Written</u> |
|----------------------|--------------------------------|
| 2006 | \$48,728,320 |
| 2007 | \$48,763,072 |
| 2008 | \$48,299,146 |
| 2009 | \$47,499,243 |
| 2010 | \$47,465,939 |

C. Reinsurance

Assumed

Assumed reinsurance accounted for less than 1% of the Company's gross premium written at December 31, 2010. During the period covered by this examination, the Company's assumed reinsurance business has increased since the last examination. The assumption reflects the Company's participation in the Regional Reciprocal Catastrophe Pool ("RRCPP"). Under the RRCPP the Company reinsures its pro-rata share of a catastrophe pool.

Ceded

Since the previous examination, the Company's net retention has increased from \$200,000 to \$300,000 on property business, and from \$150,000 to \$175,000 on casualty business, excluding any quota share reinsurance agreements effective during that timeframe.

The Company has structured its ceded reinsurance program as of December 31, 2010, as follows:

Type of Treaty

Cession

Property Per Risk Excess of Loss
3 layers

Layer 1: \$200,000 excess of \$300,000 ultimate net loss any one risk, each loss occurrence; limit \$600,000 per occurrence. Terrorism aggregate limit of \$600,000 ultimate net loss arising out of multiple acts of terrorism.

Layer 2: \$750,000 excess of \$500,000 ultimate net loss any one risk, each loss occurrence; limit \$2,250,000 per occurrence. Terrorism aggregate limit of \$2,250,000 ultimate net loss arising out of multiple acts of terrorism.

Type of TreatyCession

Layer 3: \$1,000,000 excess of \$1,250,000 ultimate net loss any one risk, each loss occurrence; limit \$2,000,000 per occurrence. Terrorism aggregate limit of \$2,000,000 ultimate net loss arising out of multiple acts of terrorism.

The limitations as respects terrorism and counter-terrorism only apply if: 1) total property damages sustained by all persons and entities exceeds \$25,000,000; or 2) 50 or more persons sustain death or serious physical injury.

Property Catastrophe

6 layers

First layer 62% authorized

Second layer 63% authorized

Third layer 71% authorized

Fourth layer 58% authorized

Fifth layer 64% authorized

Sixth layer 60% authorized

\$30,500,000 in excess of \$1,500,000 each and every loss occurrence (two or more risks involved).

Casualty Excess of Loss

3 layers

50% authorized

Layer 1: \$325,000 excess of \$175,000 ultimate net loss any one occurrence. Terrorism aggregate limit of \$975,000 ultimate net loss arising out of multiple acts of terrorism.

Layer 2: \$500,000 excess of \$500,000 ultimate net loss any one occurrence. Terrorism aggregate limit of \$1,500,000 ultimate net loss arising out of multiple acts of terrorism.

Layer 3: \$1,000,000 excess of \$1,000,000 ultimate net loss any one occurrence. \$1,000,000 excess of \$1,000,000 as respects all losses arising out of microbial contamination.

The limitations in the first 2 layers as respects terrorism and counter-terrorism only apply if: 1) total property damages sustained by all persons and entities exceeds \$25,000,000; or 2) 50 or more persons sustain death or serious physical injury.

Type of TreatyCessionBasket Property and Casualty

(Relative to the first layers of the property per risk and casualty excess of loss contracts included in this section).
60% authorized

\$175,000 in excess of \$300,000 each loss occurrence involving a combination of property and casualty business.

Boiler and Machinery

100% Authorized

100% of \$10,000,000 of equipment breakdown liability.

As of December 31, 2010, the Company had facultative quota share reinsurance in place for its personal, farm and commercial umbrella liability business. The Company agrees to cede and the reinsurer agrees to accept 95% of up to \$1,000,000 of the Company's ultimate net loss each occurrence, each policy.

It is the Company's policy to obtain the appropriate collateral for its cessions to unauthorized reinsurers. Letters of credit obtained by the Company to take credit for cessions to unauthorized reinsurers were reviewed for compliance with Department Regulation 133. No exceptions were noted.

All significant ceded reinsurance agreements in effect as of the examination date were reviewed and found to contain the required clauses, including an insolvency clause meeting the requirements of Section 1308 of the New York Insurance Law.

Examination review found that the Schedule F data reported by the Company in its filed annual statement accurately reflected its reinsurance transactions. Additionally, management has represented that all material ceded reinsurance agreements transfer both underwriting and timing risk as set forth in NAIC Accounting Practices and Procedures Manual, Statements of Statutory Accounting Principles ("SSAP") No. 62. Representations were supported by an attestation from the Company's chief executive officer and chief financial officer pursuant to the NAIC Annual Statement Instructions. All ceded reinsurance agreements were accounted for utilizing reinsurance accounting as set forth in SSAP No. 62.

All significant ceded reinsurance agreements in effect as of the examination date were reviewed for the required clauses.

Insolvency Clause

The insolvency clauses in the Company's ceding agreements make reference to a novation. Department Circular Letter No. 5 (1988) states, in part, the following in reference to a novation:

“Any references to such an event in the reinsurance agreement should indicate that, prior to the implementation of a novation, the certificate of assumption on New York risks would have to be approved by the Superintendent. . .”

It is recommended that the Company include the above referenced language from Department Circular Letter No. 5 (1988) in all reinsurance contracts which make reference to a novation.

D. Affiliated Group

In February of 1993, the Department approved the organization of a wholly owned subsidiary named Sterling Marketing Services, Inc. (“SMS”). SMS was organized to act as a general insurance agency for insurers other than the Company and to solicit placement of insurance policies with such insurers' agents. Sterling Insurance Company contributed capital to the subsidiary by purchasing fifty shares of no par common stock at \$400 per share, for a total investment of \$20,000.

SMS is housed at the Company's home office and Sterling Insurance Company provides services to SMS in accordance with an “agreement and statement of policy” between the two companies.

E. Significant Operating Ratios

The following ratios have been computed as of December 31, 2010, based upon the results of this examination:

| | |
|--|-------|
| Net premiums written to surplus as regards policyholders | .69:1 |
| Liabilities to liquid assets (cash and invested assets less investments in affiliates) | 53% |
| Premiums in course of collection to surplus as regards policyholders | 4% |

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 five-year period covered by this examination:

| | <u>Amounts</u> | <u>Ratios</u> |
|--|----------------------|----------------|
| Losses and loss adjustment expenses incurred | \$116,217,264 | 52.76% |
| Other underwriting expenses incurred | 82,805,359 | 37.59 |
| Net underwriting gain | <u>21,240,691</u> | <u>9.64</u> |
| Premiums earned | <u>\$220,263,314</u> | <u>100.00%</u> |

F. Accounts and Records

i. Written Contract with independent Certified Public Accountants (“CPA”)

The contract between the Company and its independent CPA firm for the annual statement audit as of December 31, 2010 was reviewed for compliance with the requirements of Department Regulation 118. Part 89.10(a) of Department Regulation 118 prescribes four provisions that the contract must specify. The review revealed that the contract did not include the following three required provisions (item numbers below refer to the paragraph numbers in the Regulation):

- (1) that the CPA is independent with respect to the company and is acting in conformity with the standards of the CPA's profession, such as contained in the Code of Professional Ethics and pronouncements of the AICPA and the Rules of Professional Conduct of the New York Board of Public Accountancy, or similar code and meets the definition of a CPA set forth in subdivision (g) of section 89.1 of this Part;
- (2) that the CPA understands the annual audited financial report, that the CPA's opinion thereon will be filed in compliance with this Part and that the superintendent will be relying on this information in the monitoring and regulation of the financial condition of the company;
- (4) that the CPA represents that it is in compliance with the requirements of Section 89.5 of this Part.

Additionally, the executed contract provides that the CPA firm will notify the superintendent, the board of directors and the Company's audit committee within fifteen business days of any determination by the CPA that the company has materially misstated its financial condition as reported to the superintendent as of the balance sheet date currently under audit or that the company does not meet the minimum capital or surplus requirement of the insurance law as of that date. It is noted that Part 89.8(a) of Department Regulation 118 requires notification within five business days.

It is recommended that the Company ensure that future agreements with its CPA are in compliance with the requirements of Department Regulation 118. It is noted that the prior report on examination included a similar recommendation. It is further noted that the Company has taken steps to ensure that the 2011 agreement incorporates all of the above requirements of Department Regulation 118.

ii. Reporting of results of New York Mutual Underwriters (“NYMU”) by the Company

NYMU is an unincorporated association of two advance premium insurance companies domiciled in New York, one of which is the Company. Direct premiums written by NYMU in 2010 totaled \$7.6 million and consisted predominantly of fire and commercial multiple peril policies. Each of the two companies participates equally in the results of the business written by NYMU.

NYMU collects premiums and remits them to the participating insurers; however, the remittances are generally not made until several months after the premiums are collected by NYMU. The Company explained that the unremitted premiums represent a cash advance by the participating companies to provide funding for the operations of NYMU.

The Company reports the premiums that have been collected by NYMU but have not yet been remitted to the Company as an admitted asset under the caption “Uncollected premiums and agents’ balances in the course of collection.” These unremitted premiums should have been reported under the caption “Equities and deposits in pools and associations” pursuant to paragraph 10 of SSAP 63, which states, in part:

Equity interests in, or deposits receivable from, a pool represent cash advances to provide funding for operations of the pool. These are admitted assets and shall be recorded separately from receivables and payables related to a pool’s underwriting results.

It is recommended that the Company report its share premiums collected by NYMU, but not yet remitted to the Company as an admitted asset under the caption “Equities and deposits in pools and associations” pursuant to paragraph 10 of SSAP 63.

Additionally, it was noted that NYMU reported to the Company premiums that it had collected prior to the effective date of the policies. The Company did not record these advance premiums anywhere on its financial statements. These advance premiums should have been reported as an admitted asset under the caption “Equities and deposits in pools and associations”, with an offsetting liability under the caption “Advance premiums” pursuant to paragraph 8 of SSAP 63, which states, in part:

Underwriting results relating to voluntary and involuntary pools shall be accounted for on a gross basis whereby the participant's portion of premiums, losses, expenses and other operations of the pools are recorded separately in the financial statements rather than netted against each other. Premiums and losses shall be recorded as direct, assumed and/or ceded as applicable.

It is recommended that the Company report its share of advance premiums collected by NYMU pursuant to the provisions of paragraph 8 of SSAP 63.

iii. Schedule P Claim Count Reporting

It was noted during the examination of Schedule P on the filed 2010 annual statement that the totals indicated for the number of cumulative claims reported at December 31, 2010, was misstated and inconsistent with the supporting documentation provided by the Company. The specific sections of Schedule P are column 10, Section 3 of parts 5A and 5E as well as column 12 Section 1E of the 2010 filed Annual Statement.

The Company indicated that these were typographical errors in the filed annual statement and agreed to take corrective action in future filings.

It is recommended that the Company take due care when completing Schedule P in all future financial statement filings.

3. FINANCIAL STATEMENTS

A. Balance Sheet

The following shows the assets, liabilities and surplus as regards policyholders as of December 31, 2010 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 | \$ 84,057,466 | \$ 0 | \$ 84,057,466 |
| Common stocks | 12,784,445 | | 12,784,445 |
| Real estate: properties occupied by the company | 1,225,827 | | 1,225,827 |
| Cash, cash equivalents and short-term investments | 10,396,634 | | 10,396,634 |
| Other invested assets | 1,171,682 | | 1,171,682 |
| Investment income due and accrued | 839,820 | | 839,820 |
| Uncollected premiums and agents' balances in the course of collection | 2,477,759 | 13,901 | 2,463,858 |
| Deferred premiums, agents' balances and installments booked but deferred and not yet due | 3,541,021 | | 3,541,021 |
| Amounts recoverable from reinsurers | 260,902 | | 260,902 |
| Net deferred tax asset | 1,940,521 | | 1,940,521 |
| Electronic data processing equipment and software | 41,244 | | 41,244 |
| Furniture and equipment, including health care delivery assets | 201,871 | 201,871 | 0 |
| Cash value of life insurance | 4,469,810 | 0 | 4,469,810 |
| Equities in pools & associations | <u>923,212</u> | <u>846</u> | <u>922,366</u> |
| Total assets | <u>\$124,332,214</u> | <u>\$216,618</u> | <u>\$124,115,596</u> |

Liabilities, Surplus and Other FundsLiabilities

| | |
|---|---------------|
| Losses and loss adjustment expenses | \$ 27,790,900 |
| Commissions payable, contingent commissions and other similar charges | 1,730,490 |
| Other expenses (excluding taxes, licenses and fees) | 1,032,849 |
| Current federal and foreign income taxes | 1,762,995 |
| Unearned premiums | 25,534,704 |
| Advance premium | 549,796 |
| Ceded reinsurance premiums payable (net of ceding commissions) | 85,850 |
| Funds held by company under reinsurance treaties | 810,883 |
| Amounts withheld or retained by company for account of others | 14,428 |
| Reserve for supplemental pension | 1,845,100 |
| Reserve for LAD costs | <u>10,000</u> |
| Total liabilities | \$61,167,995 |

Surplus and Other Funds

| | |
|---|----------------------|
| Aggregate write-ins for special surplus funds | \$ 886,364 |
| Surplus notes | 2,800,000 |
| Unassigned funds (surplus) | <u>59,261,237</u> |
| Surplus as regards policyholders | <u>62,947,601</u> |
| Totals liabilities, surplus and other funds | <u>\$124,115,596</u> |

NOTE: The Internal Revenue Service has not yet begun to audit tax returns covering tax years 2006 through 2010. 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 \$27,656,945 during the five-year examination period January 1, 2006 through December 31, 2010, detailed as follows:

Underwriting Income

| | | |
|---|----------------|--------------------|
| Premiums earned | | \$220,263,314 |
| Deductions: | | |
| Losses and loss adjustment expenses incurred | \$116,217,264 | |
| Other underwriting expenses incurred | 82,589,475 | |
| Aggregate write-ins for underwriting deductions | <u>215,884</u> | |
| Total underwriting deductions | | <u>199,022,623</u> |
| Net underwriting gain or (loss) | | \$ 21,240,691 |

Investment Income

| | | |
|-------------------------------|------------------|------------|
| Net investment income earned | \$ 16,586,026 | |
| Net realized capital gain | <u>(429,990)</u> | |
| Net investment gain or (loss) | | 16,156,036 |

Other Income

| | | |
|---|----------------|----------------------|
| Net gain or (loss) from agents' or premium balances charged off | \$ (52,733) | |
| Finance and service charges not included in premiums | 3,203,878 | |
| Aggregate write-ins for miscellaneous income | <u>668,206</u> | |
| Total other income | | <u>3,819,351</u> |
| Net income before federal and foreign income taxes | | \$ 41,216,078 |
| Federal and foreign income taxes incurred | | <u>13,013,912</u> |
| Net income | | \$ <u>28,202,166</u> |

C. Capital and Surplus Account

| | | | |
|--|-------------------------|--------------------------|---------------------|
| Surplus as regards policyholders per report on examination as of December 31, 2005 | | | \$35,290,656 |
| | <u>Gains in Surplus</u> | <u>Losses in Surplus</u> | |
| Net income | \$28,202,166 | \$ 0 | |
| Net unrealized capital gains or (losses) | 5,169 | | |
| Change in net deferred income tax | 1,170,329 | | |
| Change in non-admitted assets | 106,753 | | |
| Change in surplus notes | | 200,000 | |
| Aggregate write-ins for gains and losses in surplus | <u>0</u> | <u>1,627,472</u> | |
| Total gains or losses in surplus | <u>\$29,484,417</u> | <u>\$1,827,472</u> | |
| Net increase (decrease) in surplus | | | <u>27,656,945</u> |
| Surplus as regards policyholders per report on examination as of December 31, 2010 | | | <u>\$62,947,601</u> |

4. LOSSES AND LOSS ADJUSTMENT EXPENSES

The examination liability for the captioned items of \$27,790,900 is the same as reported by the Company as of December 31, 2010. 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. COMPLIANCE WITH PRIOR REPORT ON EXAMINATION

The prior report on examination contained five 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 the Company comply with Section 704(a) of the New York Business Corporation Law and have the three director groups divided as nearly equal in number as possible. | 3 |
| The Company has complied with this recommendation. | |
| B. <u>Accounts and Records</u> | |
| i. It is recommended that the Company comply with Section 6611(a)(1) of the New York Insurance Law and maintain proper records and books of accounts at New York Mutual Underwriters, which will facilitate the preparation and verification of its annual statements. | 10 |
| The Company has complied with this recommendation. | |
| ii. It is recommended that the Company ensure that the contract with the CPA for all future audits contain the wording required by Department Regulation 118. | 10 |
| The Company has not complied with this recommendation and a similar recommendation is included in this report. | |
| iii. It is recommended that the Company comply with Department Regulation 110 Part 72.4 and include the required coinsurance percentage in its Directors and Officers policy. | 11 |
| The Company has complied with this recommendation. | |
| C. <u>Market Conduct</u> | |
| It is recommended that the Company comply with Section 3425(b) of the New York Insurance Law and give more detailed description of the reason for the cancellation. | 16 |
| The Company has complied with this recommendation. | |

6. **SUMMARY OF COMMENTS AND RECOMMENDATIONS**

| <u>ITEM</u> | <u>PAGE NO.</u> |
|---|-----------------|
| A. <u>Territory and Plan of Operation</u> | |
| It is recommended that the Company refrain from writing kinds of insurance for which it is not licensed pursuant to Section 1113(a) of the New York Insurance Law. | 5 |
| B. <u>Reinsurance</u> | |
| It is recommended that the Company include the above referenced language from Department Circular Letter No. 5 (1988) in all reinsurance contracts which make reference to a novation. | 9 |
| C. <u>Accounts and Records</u> | |
| i. It is recommended that the Company ensures that future agreements with its CPA are in compliance with the requirements of Department Regulation 118. | 11 |
| ii. It is recommended that the Company report its share premiums collected by NYMU, but not yet remitted to the Company as an admitted asset under the caption "Equities and deposits in pools and associations" pursuant to paragraph 10 of SSAP 63. | 11 |
| iii. It is recommended that the Company report its share of advance premiums collected by NYMU pursuant to the provisions of paragraph 8 of SSAP 63. | 12 |
| iv. It is recommended that the Company take due care when completing Schedule P in all future financial statement filings. | 12 |

Respectfully submitted,

_____/s/_____
Wayne Longmore,
Senior Insurance Examiner

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

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

_____/s/_____
Wayne Longmore

Subscribed and sworn to before me
this _____ day of _____, 2012.

STATE OF NEW YORK
INSURANCE DEPARTMENT

I, James J. Wynn Superintendent of Insurance of the State of New York,
pursuant to the provisions of the Insurance Law, do hereby appoint:

Wayne Longmore

as proper person to examine into the affairs of the

STERLING INSURANCE 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 30th day of June, 2011



James J. Wynn

JAMES J. WYNN
Superintendent of Insurance