

REPORT ON EXAMINATION

OF THE

ALLIANCE NATIONAL INSURANCE COMPANY

AS OF

DECEMBER 31, 2007

DATE OF REPORT

SEPTEMBER 24, 2008

EXAMINER

SHEIK H. MOHAMED

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

September 24, 2008

Mr. Eric R. Dinallo  
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 22733 dated January 15, 2008 attached hereto, I have made an examination into the condition and affairs of Alliance National Insurance Company as of December 31, 2007, and submit the following report thereon.

Wherever the designations "the Company" or "ANIC" appear herein without qualification, they should be understood to indicate Alliance National 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 administrative offices located at 220 W Germantown Pike Suite 240, Plymouth Meeting, PA 19462.

## 1. **SCOPE OF EXAMINATION**

The previous examination was conducted as of December 31, 2003. This examination covered the four-year period from January 1, 2004 through December 31, 2007. Transactions occurring subsequent to this period were reviewed where deemed appropriate by the examiner.

The examination comprised a verification of assets and liabilities as of December 31, 2007. The examination 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 certified public accountants ("CPA"). 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 ("NAIC"):

- 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

The Company was incorporated under the laws of the State of New York in 1914, under the name of Utilities Mutual Insurance Company. It became licensed on July 1, 1914 and commenced business on the same day.

In 2000, the Company ceased writing business and went into run-off. During 2000, the Company entered into a loss portfolio transfer agreement, whereby it transferred 100% of its outstanding loss and loss adjustment expense reserves relating to accident years 1999 and prior. Additionally, the Company entered into a 100% quota share reinsurance agreement covering business written in calendar year 2000.

Effective May 23, 2001, The Company converted from a mutual insurer to a stock property/casualty insurer pursuant to the provisions of Section 7307 of the New York Insurance Law and changed its name to UMI Insurance Company. Capital paid in at the time of conversion was \$5,000,000 consisting of 100,000 shares of common stock at \$50 par value per share. Gross paid in and contributed surplus was \$400,000, resulting from the dissolution of the special reserve fund that the Company had held pursuant to a statutory requirement for mutual insurers. In November of 2002, the Company amended its restated charter to reduce the Company's capital from \$5 million to \$1 million comprised of 20,000 shares with a par value of \$50 per share. The excess capital of \$4 million was returned to its sole shareholder, UMICO Holdings Inc.

On April 21, 2006, Alliance Risk Management, LLC (parent company of Alliance Risk Holdings, Inc., which is the parent company of UMICO Holdings, Inc.) acquired 100% control of UMI Insurance Company through a stock purchase of UMICO Holdings, Inc. The Company's name was changed to its current title at the time of its acquisition.

Capital paid in is \$1,000,000 consisting of 20,000 shares of \$50 par value per share common stock. Gross paid in and contributed surplus is \$3,182,980. Gross paid in and contributed surplus increased by \$2,782,980 during the examination period, as follows:

<u>Year</u>	<u>Description</u>	<u>Amount</u>
2003	Beginning gross paid in and contributed surplus	\$ 400,000
2005	Surplus contribution	\$ 302,980
2006	Surplus contribution	<u>2,480,000</u>
	Total Surplus Contributions	<u>2,782,980</u>
2007	Ending gross paid in and contributed surplus	<u>\$3,182,980</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 nineteen members. At December 31, 2007, the board of directors was comprised of the following fourteen members:

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Hugh James Agnew Flourtown, PA	President and Chief Executive Officer, Alliance National Insurance Company
Linda Sue Agnew Farmingdale, NY	Partner, Jaspan Schlesinger Hoffman, LLC
Charles Douglas Barber Villanova, PA	President, Green Tree Perpetual Assurance Company
Brian Bonar Escondido, CA	Chairman and Chief Executive Officer, Dalrada Financial Group
Eric Kurtis Bossard Lansdale, PA	Part Owner, Alliance Risk Management, LLC
Randall Edward Dyen Raynham, MA	Retired
Kevin Joseph Kelly Drexel Hill, PA	Owner, Kelly and Associates
Peter Grant Klein New York, NY	Real Estate Developer, Fidelco Realty Group
Mark Daniel Lunney Fort Washington, PA	President, UnionONE Insurance Group, LLC
Frederick Ike Milbert Elkins Park, PA	Board Member, Alliance National Insurance Company
Joseph Gregory Shockey Lake Forrest, IL	Chief Executive Officer, Bank Direct Capital Finance
Randall Paul Siko Drexel Hill, PA	President, Archway Insurance Services, LLC
Robert James Wilkin Jr. North Wales, PA	Retired

Name and ResidencePrincipal Business Affiliation

Michael Richard Yach  
Havertown, PA

Assistant Vice President,  
Archway Insurance Services, LLC

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.

Conflict of interest statements signed by officers and directors of the Company for years 2006 and 2007 were not available for review. It is recommended that the Company maintain signed conflict of interest statements at its home office for each year subject to examination.

As of December 31, 2007, the principal officers of the Company were as follows:

<u>Name</u>	<u>Title</u>
Hugh James Agnew	President and Chief Executive Officer
Kevin Joseph Kelly	Secretary

B. Territory and Plan of Operation

As of December 31, 2007, the Company was licensed to write business in New York, New Jersey and Pennsylvania.

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>
12	Collision
13	Personal injury liability
14	Property damage liability
15	Workers' compensation and employers' liability

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 \$1,300,000.

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 United States</u>	<u>Premiums written in New York State as a percentage of United States Premium</u>
2004	\$0	\$ (12,294)	0.00%
2005	\$0	0	0.00%
2006	\$0	\$1,536,954	0.00%
2007	\$0	\$1,763,224	0.00%

At December 31, 2007, the Company wrote insurance through an exclusive arrangement with Archway Insurance Services, LLC. The Company's predominate line of business is a workers' compensation large deductible program which accounted for 100% of the Company direct written premiums.

#### C. Reinsurance

Assumed reinsurance accounted for eighteen percent of the Company's gross premium written at December 31, 2007. The Company's assumed reinsurance program consists mainly of participation in various mandated pools. The Company utilizes reinsurance accounting as defined in NAIC Accounting Practices and Procedures Manual, Statements of Statutory Accounting Principles ("SSAP") No. 62 for all of its assumed reinsurance business.

The company has structured its ceded reinsurance program to limit its maximum exposure on any one occurrence. The Company's reinsurance program attaches at \$1,000,000 for any workers' compensation loss on a per occurrence basis subject to a \$10,000,000 maximum. The Company currently only writes workers' compensation insurance policies. A majority of the reinsurance is assumed by Lloyd's of London participants and authorized reinsurers assume 82.5% of the reinsurance program.

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 Regulations 133. No exceptions were noted.

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.

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. 62. Representations were supported by appropriate risk transfer analyses and an attestation from the Company's chief executive officer pursuant to NAIC Annual Statement instructions.

Additionally, examination review did not identify any finite reinsurance agreements. All ceded reinsurance agreements were accounted for utilizing reinsurance accounting as set forth in SSAP No. 62, except for the loss portfolio transfer which was accounted for as retroactive reinsurance.

#### Loss Portfolio Transfer

During 2000, the Company entered into a loss portfolio transfer agreement whereby the Company ceded 100% of its outstanding loss and loss adjustment expense reserves relating to accident years 1999 and prior. The claims covered by this agreement are handled by an independent third party administrator. The Company transferred \$67,334,000 in liabilities for a consideration of \$71,570,696; the agreement provides coverage up to a maximum aggregate amount of \$123 million. As of December 31, 2007, the Company had approximately \$22 million of coverage remaining under the agreement. The Company reported a contra-liability in the amount of \$45.3 million relating to this agreement as of December 31, 2007. The agreement is accounted for pursuant to the provisions of Department Regulation 108, which governs loss portfolio transfer agreements effective prior to January 1, 2001.

#### D. Holding Company System

The Company is 100% owned by UMICO Holdings, a New York corporation, which is 100% owned by Alliance Risk Holdings, Inc., a Pennsylvania corporation, which is ultimately controlled by Alliance Risk Management LLC, a Pennsylvania corporation.

A review of the holding company registration statements filed with this Department indicated that such filings were complete; however, it was noted that the registration statements for the years 2004 and 2005 were filed more than 120 days after the end of the ultimate holding company's fiscal year in violation of the provisions of Part 80-1.4 of Department Regulation 52. It is noted that filing of the 2004 and 2005 holding company registration statements was the responsibility of the Company's prior management; therefore, no recommendation is included herein.

Upon review of the business produced for the Company by Archway Insurance Services, LLC ("Archway"), it was determined that the Company met the definition of a producer-controlled insurer, pursuant to the provisions of Part 80-2.2 of Department Regulation 52-A. Upon review of the management agreement between the Company and Archway, it was noted that the agreement was missing several provisions required pursuant to Part 80-2.2(b)(4) of Department Regulation 52-A. The Company subsequently amended the agreement to comply with Department Regulation 52-A.

Additionally, it was noted that the Company was not filing the required reports pursuant to Part 80-2.2(c) of Department Regulation 52-A, which requires that the controlled insurer shall annually, on or before April 1, provide to the superintendent:

(1) In addition to the loss reserve opinion required to be filed with the annual statement pursuant to section 307 of the insurance law, an opinion by an independent casualty actuary, who shall be a member of the American Academy of Actuaries and in active practice, or by any other independent loss reserve specialist acceptable to the superintendent. The opinion shall report on the adequacy of loss and loss adjustment expense reserves established by the controlled insurer as of the preceding December 31, for each line of insurance on the annual statement for which any business was placed by a controlling producer; and

(2) A report, consisting of the following:

(i)(a) the amount of premiums on insurance business placed with the controlled insurer by the controlling producer;

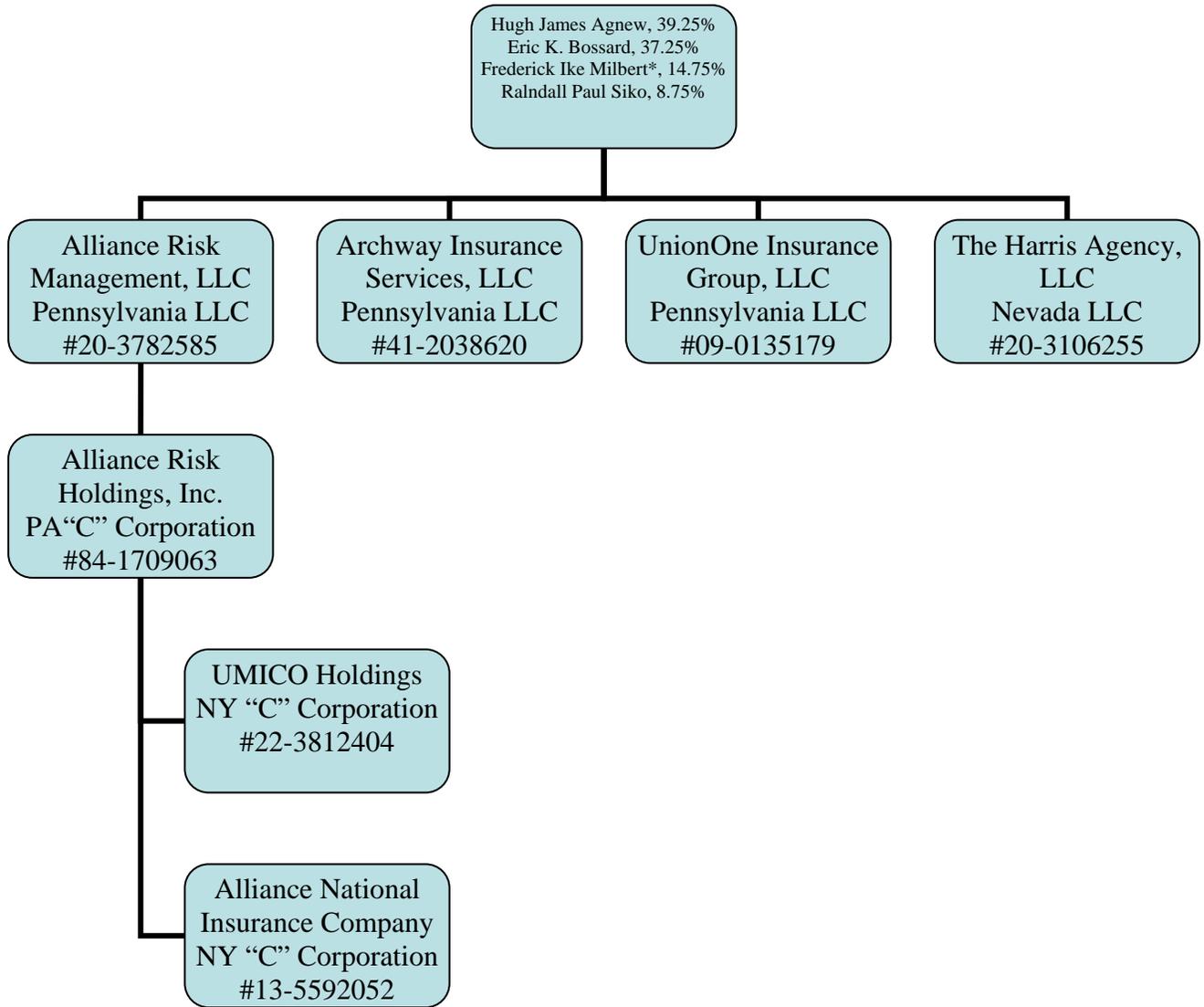
(b) the amount of commissions, charges or other fees paid by the controlled insurer to the controlling producer during the previous calendar year; and

(c) the amounts owed to the controlling producer on the business by line of insurance on the annual statement; and

(ii) the percentage that the amounts specified in subparagraph (i) of this paragraph represent of the controlled insurer's net premiums written for each such line of insurance."

It is recommended that the Company file the information required by Department Regulation 52-A. It is noted that, upon being advised of its failure to file the producer-controlled report, the Company subsequently filed the 2007 report with the Department on June 2, 2008.

The following is a chart of the holding company system at December 31, 2007:



\*Mr. Milbert owns a % of the following (exclusive of Archway Insurance Services, LLC):

- UnionOne Insurance Group, LLC
- The Harris Agency, LLC
- Alliance Risk Management, LLC

Note: The ownership percentage of Frederick Ike Milbert is being disputed in the court. If the court rules that Mr. Milbert did not pay consideration for additional shares, his ownership in the Company will be seven percent, and the ownership of the other three investors would increase proportionately. If the court rules in Mr. Milbert’s favor, his ownership in the Company will be 14.75%.

At December 31, 2007, the Company was party to the following agreements with other members of its holding company system:

#### Management Agreement

Effective May 1, 2006, the Company and Archway Insurance Services, LLC (“Archway”) entered into a management agreement in which Archway would supervise, direct and implement the production, underwriting, policy issuance, premium collection, accounting, statistical and other work necessary or incidental to the insurance business. Archway would also set up and maintain books and records and handle claims processing. The agreement was filed with this Department pursuant to Section 1505 of the New York Insurance Law. As noted previously, the Company has been deemed to be a producer-controlled insurer pursuant to the provisions of Department Regulation 52-A, based on the business produced for the Company pursuant to this agreement.

The agreement provides that the Company will pay a base commission of 12.5% of gross collected premiums to Archway for the business produced. Upon review of the premiums written, it was noted that Archway received a commission of only 11.4% for one insured and 5.9% for another. It is recommended that the commissions paid to Archway comply with the terms of the management agreement.

Section 9 of the management agreement requires that money due the Company on business produced by the Manager shall be paid not later than forty-five days after the close of the month in which the premium is written. Upon review of the premiums remitted to the Company by the Manager, it was noted that several items were not remitted in a timely manner. It is also recommended that money due the Company by Archway be remitted pursuant to the terms of the management agreement.

#### Tax Allocation Agreement

Effective April 1, 2006, the Company is a party to a tax allocation agreement with Alliance Risk Holdings, Inc. (“ARH”) and UMICO Holdings Inc. The agreement provides for the calculation of the Company’s tax liability on a separate return basis. Settlements under the agreement shall be made within thirty days of filing the applicable estimated or actual consolidated federal corporate tax return except where a refund is due ARH, in which case, it may defer payment to ANIC to within thirty days of receipt of such refund.

Upon review, it was noted that the tax allocation agreement was not submitted to this Department pursuant to Department Circular Letter No. 33 (1979), which states:

“Any domestic insurer which currently does not participate in a consolidated tax return shall file a copy of its tax allocation agreement with this Department within thirty days of electing to do so. Furthermore, notification to this Department should be given within thirty days of any amendment to or termination of a tax allocation agreement.”

The agreement was subsequently submitted to the Department and non-objected to. However, it is recommended that in the future, the Company file its intercompany agreements in a timely manner pursuant to the provisions of Department Circular Letter No. 33 (1979).

#### Intercompany Loans to Parent

In 2006, Archway paid pre-acquisition costs related to the acquisition of the Company in the amount of \$62,916 on behalf of Alliance Risk Management, LLC (the Company's parent). On June 30, 2006, the Company paid Archway for the pre-acquisition costs, thereby creating a receivable from parent and, in effect, funding its own acquisition. The reimbursement by the Company of the pre-acquisition costs represents a loan to its parent, which is in violation of the provisions of Section 1407(a)(4) of the New York Insurance Law, which prohibits investments in “obligations, shares or other securities issued by a parent corporation...” It is noted that when this was brought to the Company's attention, the parent remitted the receivable balance to the Company promptly; however, it is recommended that the Company refrain from making loans to its parent pursuant to the provisions of Section 1407(a)(4) of the New York Insurance Law.

Also in 2006, the Company paid various expenses (legal fees, tax preparation fees, and D&O insurance, etc.), a portion of which was allocated to Alliance Risk Management, LLC (“ARM”). The expenses paid by the Company totaled \$168,686 and the Company judgmentally allocated \$68,900 of the expenses to ARM. No agreement was in place that permitted this transaction. Section 1505(d)(3) of the New York Insurance Law requires that the superintendent be notified at least thirty days prior to any transaction between a domestic controlled insurer and any person in its holding company system involving rendering of services on a regular or systematic basis.

The Company subsequently submitted an expense allocation agreement to the Department on June 2, 2008; however, it is recommended that, in the future, the Company refrain from rendering services to an affiliate without notifying the Department at least thirty days prior, pursuant to the provisions of Section 1505(d)(3) of the New York Insurance Law.

E. Significant Operating Ratios

The following ratios have been computed as of December 31, 2007, based upon the results of this examination:

Net premiums written to surplus as regards policyholders	24%
Liabilities to liquid assets (cash and invested assets less investments in affiliates)	62%
Premiums in course of collection to surplus as regards policyholders	22%

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	\$15,051,446	1,027%
Other underwriting expenses incurred	2,552,641	174
Net underwriting loss	<u>(16,137,985)</u>	<u>(1,101)</u>
Premiums earned	<u>\$1,466,102</u>	<u>100%</u>

It is noted that the above ratios are distorted due to the fact that the Company was in run-off during most of the examination period; therefore the premiums earned is very low. Additionally, a large percentage of the losses and loss adjustment expenses incurred represent adverse development of prior period business, which is offset by the loss portfolio transfer gain, which was reported as "other income" in the income statement.

F. Accounts and Records

A review of the Company's accounts, records and annual statements revealed the following:

1. Approval of Investments

Section 1411(a) of the New York Insurance Law states, in pertinent part:

"No domestic insurer shall make any loan or investment ... unless authorized or approved by its board of directors or a committee thereof responsible for supervising or making such investment or loan. The committee's minutes shall be recorded and a report submitted to the board of directors at its next meeting."

During the review of the Company's investments, it was noted that none of the Company's investments made from October 1, 2005 to December 31, 2007 were approved by the Company's board of directors. Thus, the Company did not comply with the requirements of Section 1411(a) of the New York Insurance Law.

It is recommended that the Company comply with the requirements of Section 1411(a) of the New York Insurance Law by having all of its investments authorized or approved as indicated in such section.

## 2. Article 14 Investment Limitations

A review of the Company's cash investments revealed that the Company invested more than 10 percent of its assets in overnight Eurodollar time deposit accounts with Sovereign Bank's Cayman Islands branch via sweep service on a daily basis. These investments are considered foreign investments.

Section 1404(a)(6) of the New York Insurance Law states in pertinent part:

“Investments in a foreign country .... shall not exceed ten percent of the insurer's admitted assets as shown by its last statement on file with the superintendent.”

Based on the above, it appears that the Company violated Section 1404(a)(6) of the New York Insurance Law on a daily basis. Therefore, it is recommended that the Company comply with Section 1404(a)(6) of the New York Insurance Law.

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

“... 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.”

The Company did not comply with Section 1409(a) of the New York Insurance Law as it invested more than ten percent of its admitted assets in Sovereign Bank. Therefore, it is recommended that the Company comply with Section 1409 of the New York Insurance Law.

3. Directors and Officers (“D & O”) Indemnification Policy Retention Amount and Minimum Co-Insurance

The Company did not comply with Department Regulation 110, which requires an individual retention of \$4,000 and an aggregate retention of \$40,000, as well as a coinsurance percentage of 0.40% be included in any Directors and Officers policy.

According to Department Regulation 110, 72.1(c):

“Retention amounts and co-insurance are both required, in accordance with this Part, for Directors and Officers indemnification policies issued to corporations formed under the Insurance Law, Religious Corporations Law, Transportation Corporations Law, or any other law of this state, where provisions of such laws make such corporations subject to BCL section 727 or N-PCL section 727.”

It is noted that the Company subsequently amended its directors and officers policy to comply with the requisite retentions and the coinsurance percentage stipulated in Department Regulation 110.

4. General Expenses Findings

During the review of the Company's expenses it was noted that the Company did not retain receipts for credit card purchases, and as a result the examiners were unable to verify if these expenses were business related. Also, wireless telephone bills were paid for a person who was not an employee of the Company. The Company should not have paid for the expense related to the wireless bill. Additionally, the Company paid wireless telephone bills for an employee who works for several other companies in the holding company system. Therefore, the employee's cell phone costs should have been allocated among those companies in the holding company system.

The lack of adequate supporting documentation as noted during the 2007 examination is a violation of Section 1217 of the New York Insurance Law which states, in part:

"No domestic insurance company shall make any disbursement of one hundred dollars or more unless evidenced by a voucher signed by or on behalf of the payee as compensation for goods or services rendered for the company, and correctly describing the consideration for the payment. If such disbursement be for services and disbursements, such vouchers shall set forth the services rendered and itemize the disbursements;... If such voucher is unobtainable, the disbursement shall be evidenced by a statement of an officer or responsible employee affirmed by him as true under the penalties of perjury, stating the reasons therefor and setting forth the particulars above mentioned."

Such documentation must support the legitimate business purpose of the expense as it relates to the Company. It is recommended that the Company comply with Section 1217 of the New York Insurance Law, henceforth. It is also recommended that the Company strengthen its internal controls over expenses by requiring that all expenditures be adequately supported by vouchers that sufficiently identify the services rendered, the nature of the disbursement and the business purpose as it relates to the insurer(s). Furthermore, it is recommended that all approvals to disburse funds from the insurers be appropriately documented, in writing, by an officer or a responsible employee of the insurer.

The Company allocated management fees to Alliance Risk Management, LLC using a percentage that was determined judgmentally. According to Department Regulation No. 30, Part 106.2, the Company should have allocated its expenses based on special studies or overhead of salaries.

It is recommended that the Company maintain records supporting the allocation of the costs of management fees in accordance with Department Regulation 30, Part 106.

#### 5. Data to Support Claim Counts

The Company is unable to provide detail support to reconcile claim counts by accident years. Therefore, the examiners were unable to verify the number of claims closed with loss payment, the number of claims closed without loss payment, and the number of claims reported - direct and assumed.

It is recommended that the Company obtain the cumulative loss data by accident years to support Schedule P.

#### 6. Disaster Recovery Plan

A review of the Company's information systems internal controls revealed that there is no business continuity plan which provides for the recovery of such systems in the event of a disaster. Lacking such procedures could potentially prevent the Company from being able to perform its business functions for extended periods following an adverse event.

It is recommended that the Company develop a disaster recovery plan which is based on a business analysis. It should address all significant business activities, including financial functions,

telecommunication services, data processing and network services. The plan should also be tested periodically.

7. Preparation of the 2007 Annual Statement

The Company stated in item 26 of its General Interrogatories that it had a custodial agreement in compliance with Section 3 G – Custodial or Safekeeping Agreements, of the NAIC Financial Condition Examiners Handbook. However, the Company did not have a custodial agreement.

It is recommended that the Company accurately respond to General Interrogatory #26 in its filed annual statement. It is noted that the Company subsequently executed a custodial agreement with M&T Bank.

Note 10 of the Notes to the Financial Statements requires the Company to disclose all material related party transactions including the nature of the relationship with the related party. The Company did not disclose the relationship it has with Archway Insurance Services as a controlling producer.

It is recommended that the Company disclose its relationship with its affiliate, Archway Insurance Services, LLC, as a controlling producer in Note 10 of the Notes to the Financial Statements of its Annual Statement.

The instructions for Schedule Y Part 1 of the Annual Statement require the reporting entity to attach a chart or listing presenting the identities of and interrelationships between the parent company, all affiliated insurers and other affiliates. In reviewing the Company's Schedule Y Part 1 organizational chart, the Company did not list: (a) Archway Insurance Services, LLC (“Archway”), (b) Union One Insurance Services, LLC, (c) Nevada Investment Partners, LLC and (d) The Harris Agency, LLC.

It is recommended that the Company accurately reflect its organizational chart for Schedule Y Part 1 in compliance with the instructions of the Annual Statement. It is noted that the Company corrected this finding in its first quarterly statement for 2008.

The instructions for Schedule Y Part 2 of the Annual Statement require the reporting entity to disclose all inter-company transactions between insurers and non-insurers within the holding

company system. Based on a review of the Company's Schedule Y Part 2, the Company did not disclose the direct written premiums written through its affiliate, Archway.

It is recommended that the Company accurately report its Schedule Y Part 2 to reflect transactions between itself and Archway in compliance with the instructions of the Annual Statement.

While the Company did disclose the fact that it has a retroactive reinsurance agreement under Note 23 (F) of the Notes to the Financial Statements of its 2007 Annual Statement, the Company did not include the chart stipulated in the Annual Statement Instructions. This chart should specify the reserves transferred, the consideration paid, paid losses reimbursed or recovered and special surplus for retroactive reinsurance.

It is recommended that the Company include the chart specified in the instructions of the Annual Statement for Note 23 (F) of the Notes to the Financial Statements.

The Company did not file the supplemental exhibit specified in Part 112.6(k) of Department Regulation No. 108 with regards to its loss portfolio transfer with Cologne Re Dublin.

It is recommended that the Company file the supplemental exhibit specified in Part 112.6(k) of Department Regulation No. 108 with regards to its loss portfolio transfer with Cologne Re Dublin.

### 3. FINANCIAL STATEMENTS

#### A Balance Sheet

The following shows the assets, liabilities and surplus as regards policyholders as of December 31, 2007 as determined by this examination and as reported by the Company:

<u>Assets</u>	<u>Assets</u>	<u>Examination</u> Assets Not Admitted	Net Admitted <u>Assets</u>	<u>Company</u> Net Admitted <u>Assets</u>	Surplus Increase (Decrease)
Cash, cash equivalents and short-term investments	\$8,746,268	\$2,811,192	\$5,935,076	\$8,746,268	\$(2,811,192)
Investment income due and accrued	11,284	0	11,284	11,284	0
Uncollected premiums and agents' balances in the course of collection	1,070,721	0	1,070,721	1,070,721	0
Furniture and equipment, including health care delivery assets	7,660	7,660	0	0	0
Receivables from parent, subsidiaries and affiliates	147,950	147,950	0	0	0
Receivable under high deductible policies	459,396	459,396	0	459,396	(459,396)
Prepaid Expenses	26,493	26,493	0	0	0
Due from Cologne Re Dublin	<u>81,781</u>	<u>0</u>	<u>81,781</u>	<u>81,781</u>	<u>0</u>
Total assets	<u>\$10,551,553</u>	<u>\$3,452,691</u>	<u>\$7,098,862</u>	<u>\$10,369,450</u>	<u>\$(3,270,588)</u>
					Surplus Increase (Decrease)
<u>Liabilities, surplus and other funds</u>					
					<u>Examination</u>
<u>Liabilities</u>					<u>Company</u>
Losses and loss adjustment expenses			\$50,500,573	\$45,800,573	\$(4,700,000)
Other expenses (excluding taxes, licenses and fees)			73,384	73,384	0
Taxes, licenses and fees (excluding federal and foreign income taxes)			118,959	118,959	0
Current federal and foreign income taxes			28,000	28,000	0
Unearned premiums			1,072,708	1,072,708	0
Ceded reinsurance premiums payable (net of ceding commissions)			85,000	544,396	459,396
Amounts withheld or retained by company for account of others			262,335	3,073,527	2,811,192
Loss portfolio transfer			<u>(50,018,800)</u>	<u>(45,318,800)</u>	<u>4,700,000</u>
Total liabilities			<u>\$ 2,122,159</u>	<u>\$ 5,392,747</u>	<u>\$3,270,588</u>
<u>Surplus and Other Accounts</u>					
Special surplus from retroactive reinsurance account			\$22,871,008	\$18,171,008	\$4,700,000
Common capital stock			1,000,000	1,000,000	0
Gross paid in and contributed surplus			3,182,980	3,182,980	0
Unassigned funds (surplus)			<u>(22,077,285)</u>	<u>(17,377,285)</u>	<u>(4,700,000)</u>
Surplus as regards policyholders			<u>\$ 4,976,703</u>	<u>\$ 4,976,703</u>	<u>\$ 0</u>
Total liabilities, surplus and other funds			<u>\$ 7,098,862</u>	<u>\$10,369,450</u>	<u>\$(3,270,588)</u>

NOTE: The Internal Revenue Service has not yet begun to audit tax returns covering tax years 2004 through 2007. 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 increased \$1,552,125 during the four-year examination period January 1, 2004 through December 31, 2007, detailed as follows:

Underwriting Income

Premiums earned		\$1,466,102
Deductions:		
Losses incurred	\$13,622,275	
Loss adjustment expenses incurred	1,429,171	
Other underwriting expenses incurred	<u>2,552,641</u>	
Total underwriting deductions		<u>17,604,087</u>
Net underwriting gain or (loss)		\$(16,137,985)

Investment Income

Net investment income earned	665,973	
Net realized capital gain	<u>0</u>	
Net investment gain or (loss)		665,973

Other Income

Loss portfolio transfer gain	14,345,175	
Other income (expense)	(7,742)	
Class action recovery	<u>4,436</u>	
Total other income		<u>14,341,869</u>
Net income before dividends to policyholders and before federal and foreign income taxes		\$(1,130,143)
Dividends to policyholders		<u>0</u>
Net income after dividends to policyholders but before federal and foreign income taxes		\$(1,130,143)
Federal and foreign income taxes incurred		<u>28,002</u>
Net income		<u><u>\$(1,158,145)</u></u>

C. Capital and Surplus Account

Surplus as regards policyholders per report on examination as of December 31, 2003			\$3,424,578
	<u>Gains in Surplus</u>	<u>Losses in Surplus</u>	
Net income		\$1,158,145	
Change in surplus notes		72,710	
Surplus adjustments paid in	<u>\$2,782,980</u>	<u>0</u>	
Total gains and losses	<u>\$2,782,980</u>	<u>\$1,230,855</u>	
Net increase (decrease) in surplus			<u>1,552,125</u>
Surplus as regards policyholders per report on examination as of December 31, 2007			<u>\$4,976,703</u>

4. CASH, CASH EQUIVALENTS AND SHORT-TERM INVESTMENTS

The examination admitted asset of \$5,935,076 is \$2,811,192 less than the \$8,746,268 reported by the Company as of December 31, 2007.

The examination change represents amounts held in three collateral accounts that are in the name of the Company's affiliate, Archway Insurance Services LLC and therefore, do not qualify as admitted assets. It is noted that the amounts represent collateral held for the payment of claims on certain high deductible policies written by the Company, for which the Company set up an offsetting liability under the caption "Amounts withheld or retained by company for account of others." An offsetting examination change has been made to the liability and therefore, the net surplus effect is \$0.

It is recommended that the Company ensure that all collateral accounts held by the Company for its insured should be in the name of the Company.

**5. RECEIVABLE UNDER HIGH DEDUCTIBLE POLICIES**

The Company reported an admitted asset in the amount of \$459,396 as of the examination date. Pursuant to this examination, the admitted asset has been eliminated.

The examination change represents the disallowance of high deductible receivables balances which do not meet the definition of an asset as defined in Paragraph 2 of SSAP 4. An offsetting adjustment was made to the liability "Ceded reinsurance premiums payable". Therefore, the surplus effect of this change is \$0.

**6. LOSSES AND LOSS ADJUSTMENT EXPENSES**

The examination liability for the captioned items of \$50,500,573 is \$4,700,000 more than the \$45,800,573 reported by the Company as of December 31, 2007. 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.

It is noted that the entire examination change is for losses and loss adjustment expenses incurred in accident years 1999 and prior, which are covered by a loss portfolio transfer. There is an offsetting change in the same amount to the contra-liability "Loss portfolio transfer." Therefore, the surplus effect of this change is \$0.

**7. CEDED REINSURANCE PREMIUMS PAYABLE**

The examination liability of \$85,000 is \$459,396 less than the \$544,396 balance reported by the Company as of December 31, 2007.

The examination change represents an offsetting adjustment to the disallowance of the asset "Receivable under high deductible policies" as described in Item 5 of this report. Therefore, the surplus effect of this change is \$0.

**8. AMOUNTS WITHHELD OR RETAINED BY COMPANY FOR  
ACCOUNT OF OTHERS**

The examination liability of \$262,335 is \$2,811,192 less than the \$3,073,527 reported by the Company as of December 31, 2007.

The eliminated liability represents an offset to an admitted asset reported by the Company under the caption "Cash, cash equivalents and short-term investments", which has been not admitted by this examination, as more fully explained in item 4 of this report.

**9. LOSS PORTFOLIO TRANSFER**

The examination contra-liability of \$(50,018,800) is \$4,700,000 more than the \$(45,318,800) reported by the Company as of December 31, 2007.

The examination change results from an increase to the liability "Losses and loss adjustment expenses" as more fully explained in item 6 of this report.

**10. MARKET CONDUCT ACTIVITIES**

In the course of this examination, a review was made of the manner in which the Company conducts its business 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. Sales and advertising
- B. Claims and complaint handling

No problem areas were encountered.

**11. COMPLIANCE WITH PRIOR REPORT ON EXAMINATION**

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

<u>ITEM</u>		<u>PAGE NO.</u>
A.	<u>Account and Records</u>	
	It was recommended that the Company have all contracts, letterheads and documents used in the normal course of business reflect the name of UMI Insurance Company.	9
	The Company has complied with this recommendation. One reinsurance agreement with Cologne Reinsurance Company (Dublin) Ltd. still includes the Company's previous name. The Company attempted to get the reinsurer to amend the agreement to reflect the Company's current name but the reinsurer would not make the change. It is not deemed necessary to pursue this any further.	

## 12. SUMMARY OF COMMENTS AND RECOMMENDATIONS

<u>ITEM</u>	<u>PAGE NO.</u>
A. <u>Management</u>	
i. It is recommended that the Company maintain signed conflict of interest statements at its home office for each year subject to examination.	5
B. <u>Holding Company System</u>	
i. It is recommended that the Company file the information required by Department Regulation 52-A.	9
ii. It is recommended that the commissions paid to Archway comply with the terms of the management agreement. It is also recommended that money due the Company by Archway be remitted pursuant to the terms of the management agreement.	10
iii. It is recommended that in the future, the Company file its intercompany agreements in a timely manner pursuant to the provisions of Department Circular Letter No. 33 (1979).	11
iv. It is recommended that the Company refrain from making loans to its parent pursuant to the provisions of Section 1407(a)(4) of the New York Insurance Law.	11
v. It is recommended that, in the future, the Company refrain from rendering services to an affiliate without notifying the Department at least thirty days prior, pursuant to the provisions of Section 1505(d)(3) of the New York Insurance Law.	11
C. <u>Accounts and Records</u>	
i. It is recommended that the Company comply with the requirements of Section 1411(a) of the New York Insurance Law by having all of its investments authorized or approved as indicated in such section.	13
ii. It is recommended that the Company comply with Section 1404(a)(6) of the New York Insurance Law.	13
iii. It is recommended that the Company comply with Section 1409 of the New York Insurance Law.	13
iv. It is recommended that the Company comply with Section 1217 of the New York Insurance Law, henceforth. It is also recommended that the Company strengthen its internal controls over expenses by requiring that all expenditures be adequately supported by vouchers that sufficiently identify the services rendered, the nature of the disbursement and the business purpose as it relates to the insurer(s). Furthermore, it is recommended that all approvals to disburse funds from the insurers be	15

ITEMPAGE NO.

appropriately documented, in writing, by an officer or responsible employee of the insurer.

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|-------|--|----|
| v.    | It is recommended that the Company maintain records supporting the allocation of the costs of management fees in accordance with Department Regulation 30, Part 106.   | 15 |
| vi.   | It is recommended that the Company obtain the cumulative loss data by accident years to support Schedule P.  | 15 |
| vii.  | It is recommended that the Company develop a disaster recovery plan which is based on a business analysis. It should address all significant business activities, including financial functions, telecommunication services, data processing and network services. The plan must be tested periodically. | 15 |
| viii. | It is recommended that the Company accurately respond to General Interrogatory #26 in its filed annual statement. It is noted that the Company subsequently executed a custodial agreement with M&T Bank.  | 16 |
| ix.   | It is recommended that the Company disclose its relationship with its affiliate, Archway Insurance Services, LLC, as a controlling producer in Note 10 of the Notes to the Financial Statements of its Annual Statement.   | 16 |
| x.    | It is recommended that the Company accurately reflect its organizational chart for Schedule Y Part 1 in compliance with the instructions of the Annual Statement.  | 16 |
| xi.   | It is recommended that the Company accurately report its Schedule Y Part 2 to reflect transactions between itself and Archway in compliance with the instructions of the Annual Statement.   | 17 |
| xii.  | It is recommended that the Company include the chart specified in the instructions of the Annual Statement for Note 23 (F) of the Notes to the Financial Statements.   | 17 |
| xiii. | It is recommended that the Company file the supplemental exhibit specified in Part 112.6(k) of Department Regulation No. 108 with regards to its loss portfolio transfer with Cologne Re Dublin.   | 17 |
| D.    | <p><u>Cash, cash equivalents and short-term investments</u><br/>It is recommended that the Company ensure that all collateral accounts held by the Company for its insured should be in the name of the Company.</p>   | 20 |



Appointment No. 22733

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:

**Sheik Mohamed**

*as proper person to examine into the affairs of the*

**ALLIANCE NATIONAL 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 15th day of January, 2008



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ERIC R. DINALLO

Superintendent of Insurance

