

REPORT ON EXAMINATION

OF THE

ALLIANCE ASSURANCE COMPANY OF AMERICA

AS OF

DECEMBER 31, 2002

DATE OF REPORT

JANUARY 8, 2004

EXAMINER

ADEBOLA AWOFOESO

TABLE OF CONTENTS

<u>ITEM NO.</u>	<u>PAGE NO.</u>
1. Scope of examination	2
2. Description of the Company	3
A. Management	4
B. Territory and Plan of Operation	6
C. Reinsurance	8
D. Holding Company System	8
E. Abandoned Property Law	9
F. Custodial agreement	10
3. Financial statements	11
A. Balance Sheet	11
B. Underwriting and Investment Exhibit	12
C. Capital and Surplus Account	13
4. Losses and loss adjustment exapenses	14
5. Compliance with prior report on examination	14
6. Summary of comments and recommendations	14



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

January 8, 2004

Honorable Gregory V. Serio
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 22112 dated December 5, 2003 attached hereto, I have made an examination into the condition and affairs of Alliance Assurance Company of America as of December 31, 2002, and submit the following report thereon.

The examination was conducted at the Company 's administrative offices located at 325 Donald J. Lynch Boulevard, Marlborough, Massachusetts 01752.

The Company's statutory home office is located at One Chase Plaza, 38th floor, New York, New York 10005.

Wherever the designations "the Company" or "Alliance " appear herein without qualification, they should be understood to indicate Alliance Assurance Company of America.

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

1. SCOPE OF EXAMINATION

The previous examination was conducted as of December 31, 1997. This examination covered the five-year period from January 1, 1998 through December 31, 2002. Transactions occurring subsequent to this period were reviewed where deemed appropriate by the examiner.

The examination comprised a complete verification of assets and liabilities as of December 31, 2002. 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 public accountants. A review or audit was also made of the following items as called for in the Examiners Handbook of the National Association of Insurance Commissioners:

- History of Company
- Management and control
- Corporate records
- Fidelity bond and other insurance
- Territory and plan of operation
- Growth of Company
- Business in force by states
- Loss experience
- Reinsurance
- Accounts and records
- Financial statements

A review was also made to ascertain what action was taken by the Company with regard to comments and recommendations contained in the prior report on examination.

This report on examination is confined to financial statements and comments on those matters, which involve departures from laws, regulations or rules, or which are deemed to require explanation or description.

2. DESCRIPTION OF COMPANY

Alliance Assurance Company Limited, London, England was organized in 1824 under the laws of England as the Alliance British and Foreign Life and Fire Assurance Company. A United States Branch established in 1897 was terminated in 1906. The Company re-entered the United States as a branch in 1911 under the management of Chubb & Son Inc., New York. The branch was domesticated into a corporation organized on July 26, 1991, under the laws of the State of New York with the domesticated successor being Alliance Assurance Company of America. On January 1, 1992, the Company assumed all assets and liabilities of the United States Branch.

On September 13, 1992, ownership of Alliance Assurance Company of America was transferred to Sun Alliance Insurance Overseas Limited, a wholly-owned subsidiary of Sun Alliance Group plc.

Effective January 1, 1994, ownership of the Company was transferred, via a share exchange, to Sun Alliance USA Inc., a wholly-owned subsidiary of Sun Alliance Group plc.

On July 19, 1996, Sun Alliance Group plc changed its name to Royal & Sun Alliance Insurance Group plc concurrent with a merger with Royal Insurance Holdings plc (“Royal”) under which all of the shares of Royal were acquired in exchange for shares in the renamed Royal & Sun Alliance Insurance Group plc.

Effective July 1, 2000, the Company entered into a reinsurance assignment and assumption agreement. Under this agreement, all business of Alliance Assurance Company of America was transferred to Globe Indemnity Company.

In 2000, in order to prepare the Company for sale, the Company disposed of a large portion of its investment portfolio including \$57.1 million in bonds and \$181.9 million in common stocks. This amount was remitted to the former owner in the form of an extraordinary dividend in the amount of \$239,000,000. As a result of asset disposal, the Company experienced a realized capital gain of \$171,170,993 and a net unrealized capital loss arising from the release of \$162,619,030 of accumulated unrealized capital gains.

In January 23, 2001, Eastern Casualty Insurance Company “Eastern Casualty” a Commonwealth of Massachusetts domiciled company purchased Alliance Assurance Company of America as a shell.

Capital paid in is \$5,000,000 consisting of 100 common shares at \$50,000 par value per share. Gross paid in and contributed surplus is \$5,700,000.

A. Management

Pursuant to the Company’s charter and by-laws, management of the Company is vested in a board of directors consisting of not less than thirteen nor more than twenty-one members. At December 31, 2002, the board of directors was comprised of the following thirteen members:

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Kathleen A. Conway Worcester, MA	Director of Finance, Eastern Casualty Insurance Company
Pamela A. Genelli Hubbardston, MA	Vice President, Eastern Casualty Insurance Company
Frederick J. Hansberry Andover, MA	Vice President, Eastern Casualty Insurance Company

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Dennis M. Kass Rye, NY	Vice Chairman, J. P. Morgan Fleming
Henry C. Lodge, III Bedford, NY	Executive Vice President, Star Financial
Stewart A. McIntire Melrose, MA	Vice President, Eastern Casualty Insurance Company
Frank L. McNamara, Jr., Esq. Boston, MA	Owner, McNamara & Associates
Michael M. O'Connor Chelmsford, MA	Vice President, Eastern Casualty Insurance Company
Mary Jane Peoples Hopkinton, MA	Executive Vice President, Eastern Casualty Insurance Company
James A. Radley Dedham, MA	President, Chief Executive Officer and Owner, Eastern Casualty Insurance Company
Carl F. Schmitt Lancaster, MA	Associate, McNamara & Associates
John H. Spector Holliston, MA	Partner, Spector, Abbott & Co., Inc.
John F. Sweeney, Esq. New York, NY	Partner, Morgan & Finnegan, LLP

The examiner reviewed only the minutes of meetings held in 2001 and 2002. The board met four times during each calendar year reviewed.

A review of the minutes of the board of directors' meetings held during the 2001 and 2002 indicated John Spector, Frederick Hansberry, Michael O'Connor, Stewart McIntire, John Sweeney, Henry Lodge III and Dennis Kass, each of whom attended less than 50% of the meetings for which they were eligible to attend.

Members of the board have a fiduciary responsibility and must evince an ongoing interest in the affairs of the insurer. It is essential that board members attend meetings consistently and set forth their views on relevant matters so that the board may reach appropriate decisions. Individuals who fail to attend at least one-half of the regular meetings do not fulfill such criteria. It is recommended that board members who are unable or unwilling to attend meetings consistently should resign or be replaced.

As of December 31, 2002, the principal officers of the Company were as follows:

<u>Name</u>	<u>Title</u>
James A. Radley	President and Treasurer
Frank L. McNamara, Jr., Esq.	Secretary
Mary Jane Peoples	Vice President

Conflict of interest

The Company does not have an established procedure for disclosure to its board of directors or trustees of any material interest or affiliation on the part of its officers, directors, trustees or responsible employees which is likely to conflict with the official duties of such person. It is recommended that the Company establish procedures for disclosing conflict of interest and ensures that all directors and officers complete conflict of interest statements yearly.

B. Territory and Plan of Operation

As of December 31, 2002, the Company was licensed in thirty-three states and the District of Columbia. Currently, the Company is inactive and has not written any business since its acquisition by Eastern Casualty on January 23, 2001.

As of the examination date, the Company was authorized to transact the kinds of insurance as defined in the following numbered paragraphs of Section 1113(a) of the New York Insurance Law:

<u>Paragraph</u>	<u>Line of Business</u>
3	Accident & health
4	Fire
5	Miscellaneous property damage
6	Water damage
7	Burglary and theft
8	Glass
9	Boiler and machinery
10	Elevator
11	Animal
12	Collision
13	Personal injury liability
14	Property damage liability
15	Workers' compensation and employers' liability
16	Fidelity and surety
17	Credit
19	Motor vehicle and aircraft physical damage
20	Marine and inland marine
21	Marine protection and indemnity
22	Residual value
24	Credit unemployment
30	Substantially similar kind

In addition, the Company is licensed to transact such workers' compensation insurance as may be incident to coverages contemplated under paragraphs 20 and 21 of Section 1113(a), including insurances described in the Longshoremen's and Harbor Workers' Compensation Act (Public Law No. 803, 69th Congress, as amended; 33 USC Section 901 et. seq. as amended).

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 \$4,600,000.

C. Reinsurance

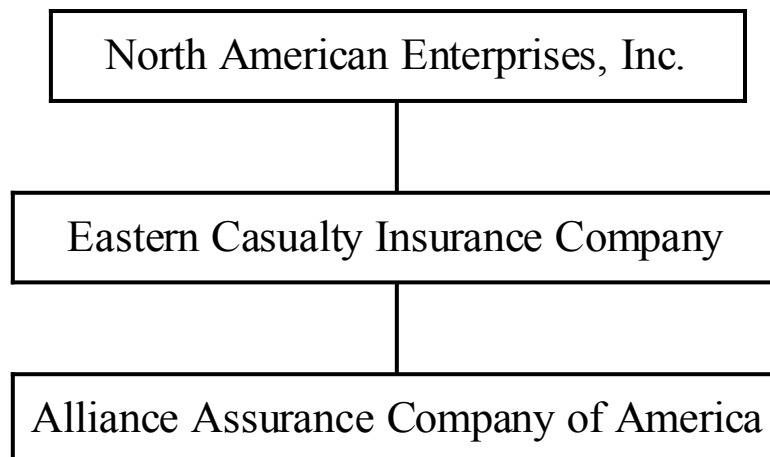
As stated in Section B- "Territory and plan of operation" the Company is currently inactive and does not assume or cede any business.

D. Holding Company System

The Company is a member of the North American Enterprises, Inc. holding company system. The Company is 100% owned by, Eastern Casualty Insurance Company, a Massachusetts corporation, which is ultimately controlled by North American Enterprises, Inc.

Pursuant to Part 80-1.4 of Department Regulation 52, all controlled insurers are required to file an annual holding company registration statement (Form HC-1) within 120 days following the end of its ultimate holding company's fiscal year. As of the date of this report, the Company has not filed a Form HC-1 for 2001 and 2002. It is recommended that the Company file its annual holding company registration statements in a timely manner pursuant to the provisions of Part 80-1.4 of Department Regulation 52.

The following is a chart of the holding company system at December 31, 2002:



Tax allocation agreement

For years 2001 and 2002, the Company filed a consolidated federal income tax return with its parent North American Enterprises, Inc. and subsidiaries. The Company does not have a written agreement to support the basis for these filings nor did the Company notify the Department in writing of its intention to enter into such arrangement.

It is recommended that the Company write a formal tax allocation agreement with North American Enterprises, Inc. and its subsidiaries. It is also recommended that the Company submit such an agreement to the Department for review pursuant to Section 1505(d) of the New York Insurance Law.

E. Abandoned Property Law

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

The Company did not file abandoned property reports for any of the years during the period of this examination. Although the Company had no abandoned property to remit, negative reports should have been filed. It is recommended that the Company file abandoned property reports annually pursuant to the provisions of Section 1316 of the New York Abandoned Property Law.

F. Custodial agreement

Management answered affirmatively to the following General Interrogatory in the Company's December 31, 2002 filed annual statement:

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

However, examination review indicated that the Company had no custodial agreement in effect for the safekeeping of its investments.

It is recommended that the Company procure a custodial agreement in compliance with NAIC guidelines.

3. FINANCIAL STATEMENTSA Balance Sheet

The following shows the assets, liabilities and surplus as regards policyholders as determined by this examination as of December 31, 2002 and as reported by the Company:

<u>Assets</u>	<u>Assets</u>	<u>Assets Not Admitted</u>	<u>Net Admitted Assets</u>
Bonds	\$ 5,939,002	\$0	\$ 5,939,002
Cash and short-term investments	6,712,285	0	6,712,285
Interest, dividends and real estate income due and accrued	<u>54,533</u>	<u>0</u>	<u>54,533</u>
Total Assets	<u>\$12,705,820</u>	<u>\$0</u>	<u>\$12,705,820</u>

Liabilities, Surplus and Other Funds

Payable to parent, subsidiaries and affiliates	\$128
Total liabilities	\$128

Surplus and Other Funds

Common capital stock	\$5,000,000
Gross paid in and contributed surplus	5,700,000
Unassigned funds (surplus)	<u>2,005,692</u>
Surplus as regards policyholders	<u>12,705,692</u>
Total liabilities, surplus and other funds	<u>\$12,705,820</u>

Note: The Internal Revenue Service has not yet begun to audit tax returns covering tax years 1998 through 2002. The examiner is unaware of any potential exposure of the Company to any tax assessment and no liability has been established herein relative to such contingency.

B. Underwriting and Investment Exhibit

Surplus as regards policyholders decreased \$232,473,084 during the five-year examination period January 1, 1998 through December 31, 2002, detailed as follows:

Underwriting Income

Premiums earned		\$ 1,610,853
Deductions:		
Losses incurred	\$ 2,728,167	
Loss adjustment expenses incurred	477,272	
Other underwriting expenses incurred	<u>654,217</u>	
Total underwriting deductions		<u>3,859,656</u>
Net underwriting loss		\$ (2,248,803)

Investment Income

Net investment income earned	\$20,829,285	
Net realized capital gain	<u>204,523,136</u>	
Net investment gain		225,352,421

Other Income

Net loss from agents' balances charged off	\$ (47)	
Total other income		<u>(47)</u>

Net income before federal and foreign income taxes		\$223,103,571
Federal and foreign income taxes incurred		<u>21,321,180</u>
Net Income		<u>\$201,782,391</u>

C. Capital and Surplus Account

Surplus as regards policyholders per report on examination as of December 31, 1997			\$245,178,776
	<u>Gains in Surplus</u>	<u>Losses in Surplus</u>	
Net income	\$201,782,391		
Net unrealized capital losses		\$188,255,475	
Dividends to stockholders		<u>246,000,000</u>	
Total gain or losses	<u>\$201,782,391</u>	<u>\$434,255,475</u>	
Net decrease in surplus			<u>(232,473,084)</u>
Surplus as regards policyholders per report on examination as of December 31, 2002			\$ <u>12,705,692</u>

4. LOSSES AND LOSS ADJUSTMENT EXPENSES

The examination liability for the captioned items of \$0 is the same as reported by the Company as of December 31, 2002. All underwriting liabilities incurred prior to the Company's acquisition by Eastern Casualty were reinsured via an assumption agreement with Globe Indemnity Company. The Company has not written any business since its acquisition by Eastern Casualty.

5. COMPLIANCE WITH PRIOR REPORT ON EXAMINATION

The recommendations cited in the prior examination report are not applicable to the current examination due to the change in control that occurred during the current examination period. Therefore, the prior examination recommendations have not been reflected in this report on examination.

6. SUMMARY OF COMMENTS AND RECOMMENDATIONS

<u>ITEM</u>		<u>PAGE NO.</u>
A	<u>Management</u>	
	It is recommended that board members who are unable or unwilling to attend meetings consistently should resign or be replaced.	6
	It is recommended that the Company establish procedures for disclosing conflict of interest and ensures that all directors and officers complete conflict of interest statements yearly.	6
B	<u>Holding Company System</u>	
	It is recommended that the Company file its annual holding company registration statements in a timely manner pursuant to the provisions of Part 80-1.4 of Department Regulation 52.	8

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	It is recommended that the Company write a formal federal tax allocation agreement with North American Enterprises, Inc. and its subsidiaries.	9
	It is recommended that the Company submit a formal federal income tax allocation agreement to the Department for review pursuant to Section 1505(d) of the New York Insurance Law.	9
C	<u>Abandoned Property Law</u>	
	It is recommended that the Company file abandoned property reports annually pursuant to the provisions of Section 1316 of the New York Abandoned Property Law.	9
D	<u>Custodial Agreement</u>	
	It is recommended that the Company procure a custodial agreement in compliance with NAIC guidelines.	10

STATE OF NEW YORK
INSURANCE DEPARTMENT

I, GREGORY V. SERIO, Superintendent of Insurance of the State of New York,
pursuant to the provisions of the Insurance Law, do hereby appoint:

Adebola Awofeso

as proper person to examine into the affairs of the

ALLIANCE ASSURANCE COMPANY OF AMERICA

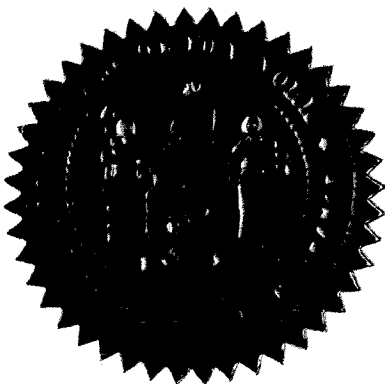
and to make a report to me in writing of the condition of the said


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 5th day of December, 2003





GREGORY V. SERIO
Superintendent of Insurance