

REPORT ON EXAMINATION

OF THE

UNITRIN ADVANTAGE INSURANCE COMPANY

AS OF

DECEMBER 31, 2002

DATE OF REPORT

JUNE 9, 2003

EXAMINER

ADEBOLA AWOFESO

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

George E. Pataki
Governor

Gregory V. Serio
Superintendent

June 9, 2003

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 22008 dated March 3, 2003 attached hereto, I have made an examination into the condition and affairs of Unitrin Advantage Insurance Company as of December 31, 2002, and submit the following report thereon.

The examination was conducted at the Company attorney's offices located at 180 Maiden Lane, New York, New York 10038.

Wherever the designation "the Company" appears herein without qualification, it should be understood to indicate Unitrin Advantage Insurance Company.

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 report on organization examination was conducted as of November 10, 1997. This examination covered the period from November 11, 1997 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

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

Unitrin Advantage Insurance Company was incorporated under the laws of the State of New York on June 20, 1997. The Company, formerly known as 1st Madison Insurance Company, MasterCare Insurance Company of New York, and Unitrin Direct Advantage Insurance Company, changed its name to Unitrin Advantage Insurance Company in 2002. It became licensed as an insurer in the State of New York on December 2, 1997.

The Company's capital stock consists of 700,000 shares of common stock at \$1.00 par value per share. Gross paid in and contributed surplus is \$835,202. Gross paid in and contributed surplus and capital paid in decreased by \$1,464,956 during the examination period, as follows:

<u>Year</u>	<u>Description</u>	<u>Amount</u>
1997	Beginning gross paid in and contributed surplus	\$2,400,000
1999	Surplus adjustment paid in	\$(1,002,320)
2000	Surplus adjustment paid in	(987,636)
2001	Surplus adjustment paid in	525,000
2001	Common capital stock	<u>(99,842)</u>
		<u>(1,564,798)</u>
2002	Ending gross paid in and contributed surplus	<u>\$835,202</u>

The reductions in surplus were approved by this Department concurrent with the Company amending its certificate of authority to write only those lines of business that its currently licensed to write as of this examination date.

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 thirteen members. The board meets four times during each calendar year. 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>
David F. Bengston Woodstock, IL	Vice President, Unitrin Services Company
James J. Collins Wildwood, MO	President, Unitrin Career Agency
Eric J. Draut Arlington Heights, IL	Executive Vice President, Unitrin Services Company
Samuel L. Fitzpatrick Burr Ridge, IL	Assistant Vice President, Unitrin Services Company
Norman Barry Greenhouse New York, NY	Retired
Dale S. Hammond Ponte Vedra Beach, FL	President, Kemper Auto and Home Group
Edward J. Konar St. Charles, IL	Vice President, Unitrin Services Company
Henry L. Lauer Glendale, NY	Retired
Vincent T. Papa Cold Spring Harbor, NY	Retired
Scott Renwick Lake Forest, IL	Senior Vice President, Secretary & General Counsel Unitrin Services Company
Richard Roeske Naperville, IL	Vice President, Unitrin Services Company

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Donald G. Southwell Wayne, IL	President & Chief Operating Officer, Unitrin Services Company
Charles L. Wood Chicago, IL	Group Executive, Unitrin Services 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 has an acceptable record of attendance.

Section 4.3 of the Company's by-laws calls for regular meeting as follows:

"In addition to the meeting of the Board of Directors following the annual meeting of shareholders, the Board of Directors shall hold at least three regularly scheduled quarterly meetings each year, none of which may take place during the quarter in which the annual meeting is held."

In 2002, the Company held two regular meetings in the same quarter as the annual meeting of the shareholders. It is recommended that the Company comply with Section 4.3 of its by-laws.

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

<u>Name</u>	<u>Title</u>
Donald G. Southwell	Chairman of the Board
Dale Stephen Hammond	President
Steven C. Andrews	Senior Vice President
Edwin Peter Schultz	Secretary and Treasurer

The Company procedure for disclosing conflict of interest by its directors, and officers was reviewed. The conflict of interest statement provides the Company's board of directors with information about the existence of relationships between persons completing the statement and parties with whom the entity may transact business. During the examination period, no conflicts of interest were disclosed to the board of directors.

B. Territory and Plan of Operation

As of December 31, 2002, the Company was licensed to write business in New York only. Currently, the Company is inactive and has not written any business during the period under examination.

As of the December 31, 2002, 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>
13	Personal injury liability
14	Property damage liability
19	Motor vehicle and aircraft physical damage

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 \$600,000.

C. Reinsurance

As stated in Section B, "Territory and plan of operation", the Company is currently inactive.

However, on December 1, 2001, the Company entered into an indemnity reinsurance agreement with the Trinity Universal Insurance Company (“ the reinsurer”), an affiliate. Pursuant to the agreement, “the Company shall cede and Trinity shall assume a 95% quota share participation in the net liability...” Although the agreement was initially approved by the New York Insurance Department, upon further review, it was noted that some areas of the agreement indicated allocation other than the 95% quota share. The Company was made aware of these discrepancies on March 22, 2003. Subsequent to the examination date, on March 26, 2003, the Company submitted a revised agreement to the Department. This agreement is currently under review.

D. Holding Company System

The Company is a member of the Unitrin, Inc. holding company system. The Company is 100% owned by Unitrin Direct Insurance Company, an Illinois corporation, which is ultimately controlled by Unitrin, Inc.

A review of the holding company registration statements filed with this Department indicated that such filings were completed and filed in a timely manner pursuant to Article 15 of the New York Insurance Law and Department Regulation 52.

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

At December 31, 2002, the Company was party to the following agreements with other members of its holding company system:

General Service Agreement

(a) The Company has a general service agreement with Unitrin Services Company (“Unitrin Services”), effective February 1, 2002. Pursuant to the terms of the agreement, Unitrin Services will provide the following services for the Company: “executive management, trade execution and investment analysis, financial accounting and reporting, purchasing and accounts payable...”. The agreement indicates payment to Unitrin Services for services provided shall be on a revenue basis. New York Insurance Department Regulation 30 (Part 109) stipulates that payment of such kind shall be based on cost. It is recommended that the Company amend this agreement to comply with Department Regulation 30.

(b) The Company has another general service agreement with Unitrin Direct Insurance Company (“UDIC”), effective December 1, 2001. Pursuant to the terms of the agreement, UDIC will provide the following services for the Company: administer the direct-marketed private passenger automobile insurance business, including all new renewal direct business, and provide the services and facilities as are described.

These contracts were submitted to and approved by the New York Insurance Department pursuant to Section 1505 of the New York Insurance Law.

Tax Allocation Agreement

The Company is party to a tax allocation agreement with Unitrin Inc, and its eligible affiliates. The agreement has an effective date of March 15, 2002. Pursuant to the terms of the agreement, the parties will file consolidated federal income tax returns. The agreement also stipulates that by filing consolidated returns the Company will be no worse off than it would have been if separate income tax returns were filed.

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 write business during the period of this examination, therefore it is exempt from filing Section 1316 of the New York State Abandoned Property Law.

F. Significant Operating Ratios

The following ratios have been computed as of December 31, 2002, based upon the results of this examination:

Net premiums written to surplus as regards policyholders	0%
Liabilities to liquid assets (cash and invested assets less investments in affiliates)	2%
Premiums in course of collection to surplus as regards policyholders	0%

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	\$	*
Other underwriting expenses incurred	680,613	*
Net underwriting loss	<u>(680,613)</u>	*
Premiums earned	<u>\$0</u>	*

* These ratios are not meaningful because the company has not yet written any business.

3. FINANCIAL STATEMENTS

A. Balance Sheet

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

<u>Assets</u>	<u>Assets</u>	Assets Not <u>Admitted</u>	Net Admitted <u>Assets</u>
Bonds	\$776,128	\$	\$776,128
Cash and short-term investments	380,263		380,263
Interest, dividends and real estate income due and accrued	<u>15,756</u>	_____	<u>15,756</u>
Total Assets	<u>\$1,172,147</u>	<u>\$0</u>	<u>\$1,172,147</u>

Liabilities

Losses and loss adjustment expenses	\$
Federal and foreign income taxes	10,496
Payable to parent, subsidiaries and affiliates	<u>16,463</u>
Total liabilities	\$26,959

Surplus and Other Funds

Common capital stock	\$700,000
Gross paid in and contributed surplus	835,202
Unassigned funds (surplus)	<u>(390,014)</u>
Surplus as regards policyholders	<u>1,145,188</u>
Total liabilities, surplus and other funds	<u>\$1,172,147</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 \$1,798,142 during the five-year examination period November 10, 1997 through December 31, 2002, detailed as follows:

Underwriting Income

Premiums earned		\$
Deductions:		
Losses incurred	\$	
Loss adjustment expenses incurred		
Other underwriting expenses incurred		<u>680,613</u>
Total underwriting deductions		<u>680,613</u>
Net underwriting gain or (loss)		\$(680,613)

Investment Income

Net investment income earned		<u>\$361,992</u>
Net investment gain or (loss)		<u>361,992</u>
Net income after dividends to policyholders but before federal and foreign income taxes		\$(318,621)
Federal and foreign income taxes incurred		<u>(122,562)</u>
Net income		<u>\$(196,059)</u>

C. Capital and Surplus Account

Surplus as regards policyholders per report on examination as of November 10, 1997				\$2,943,330
		<u>Gains in Surplus</u>	<u>Losses in Surplus</u>	
Net income			\$196,059	
Change in nonadmitted assets	\$10,000			
Capital changes paid in	158			
Surplus adjustments paid in			1,464,956	
Prior period deferred adjustments			<u>147,285</u>	
Net increase (decrease) in surplus	<u>\$10,158</u>	<u>\$1,808,300</u>	<u>(1,798,142)</u>	
Surplus as regards policyholders per report on examination as of December 31, 2002				<u>\$1,145,188</u>

4. LOSSES AND LOSS ADJUSTMENT EXPENSES

The Company has no examination liability for the captioned items because the Company has not yet begun writing business.

6. COMPLIANCE WITH PRIOR REPORT ON EXAMINATION

There was no prior report on examination.

7. SUMMARY OF COMMENTS AND RECOMMENDATIONS

<u>ITEM</u>		<u>PAGE NO.</u>
A	<u>Management</u> It is recommended that the Company comply with Section 4.3 of its by-laws.	5
B	<u>General Service Agreement</u> It is recommended that the Company amend this agreement to comply with Department Regulation 30.	9

Appointment No 22008

**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

UNITRIN ADVANTAGE 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 3rd day of March, 2003




GREGORY V. SERIO
Superintendent of Insurance