GOVERNMENT OF THE DISTRICT OF COLUMBIA

DEPARTMENT OF INSURANCE, SECURITIES AND BANKING

REPORT ON EXAMINATION

Indemnity Insurance Corporation of DC, Risk Retention Group

AS OF

DECEMBER 31, 2008

NAIC NUMBER 12018

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Washington, D.C.
March 25, 2010

Honorable Gennet Purcell
Commissioner
Department of Insurance, Securities and Banking
Government of the District of Columbia
810 First Street, NE, Suite 701
Washington, D.C. 20002

Dear Madam:

In accordance with Section 31-3931.14 of the District of Columbia Official Code, we have examined the financial condition and activities of

Indemnity Insurance Corporation of DC, Risk Retention Group

hereinafter referred to as the "Company" or "Indemnity," at the Company's offices, located at 950 Ridgebrook Road, Sparks, Maryland 21152.

SCOPE OF EXAMINATION

This full-scope examination, covering the period from June 17, 2004 through December 31, 2008, including any material transactions and/or events noted occurring subsequent to December 31, 2008, was conducted by the District of Columbia Department of Insurance, Securities and Banking ("the Department").

Our examination was conducted in accordance with examination procedures established by the Department and procedures recommended by the National Association of Insurance Commissioners ("NAIC") and, accordingly, included such tests of the accounting records and such other examination procedures as we considered necessary in the circumstances.

Our examination included a review of the Company's business policies and practices, management and corporate matters, a verification and evaluation of assets and a determination of the existence of liabilities. In addition, our examination included tests to provide reasonable assurance that the Company was in compliance with applicable laws, rules and regulations. In planning and conducting our examination, we gave consideration to the concepts of materiality and risk, and our examination efforts were directed accordingly.

The Company was audited annually by an independent public accounting firm. The firm expressed unqualified opinions on the Company's financial statements for the calendar years 2004 through 2008. We placed substantial reliance on the audited financial statements for calendar years 2004 through 2007, and consequently performed only minimal testing for those periods. We concentrated our examination efforts on the year ended December 31, 2008. We obtained and reviewed the working papers prepared by the independent public accounting firm related to the audit for the year ended December 31, 2008. We placed reliance, to the extent possible, on the work of the auditor.

STATUS OF PRIOR EXAMINATION FINDINGS

This is the first full-scope examination of the Company.

A limited-scope examination of the Company, for the period January 1, 2005 through December 31, 2005, was previously performed. The examination was conducted to address issues raised regarding the Company's operations, including transactions with its affiliated managing general agent ("MGA"); production of new business by the Company; and the Company's marketing, underwriting, and rating procedures and documentation.

In response to the findings identified during the limited-scope examination, the Department issued a cease and desist Order against the Company, effective April 14, 2006. The final limited-scope examination report, dated December 15, 2006, noted 26 findings and 24 recommendations. Certain findings in the limited-scope examination report were reviewed during this full-scope examination.

The Company responded to the findings and recommendations in the limited-scope examination report, and in October 2006, entered in to a "Consent Agreement and Order" ("Consent Agreement") with the Department. Under terms of the Consent Agreement the Company agreed to address the findings and recommendations in the limited-scope examination report. The cease and desist Order was simultaneously lifted, and the Company resumed writing business at this time.

During this full-scope examination, several areas were noted where the Company had failed to comply with the recommendations made in the prior examination. These areas are addressed within this examination report and include the following:

- Use of policies and forms that were not approved by the Department.
- Policies written in excess of the limits approved by the Department.
- Issues with the ownership structure of the Company.
- Lack of timely remittance of funds from the MGA to the Company.

SUBSEQUENT EVENTS

Letter of Credit:

During the second quarter of 2009, with the approval of the Department, the Company obtained a letter of credit ("LOC") in the amount of $47 million. Under the terms of the LOC, it expired on December 31, 2009. The purpose of the LOC was to support the financial size category assigned to the Company by AM Best. The Department's approval, which allowed the LOC to be recorded as surplus, was granted with the condition that the LOC not be used to support additional premium volume. As part of our examination, we confirmed the LOC with the issuer.

During 2009, the Company did not consistently report this LOC in its Quarterly Statements filed with the Department. See the “Comments and Recommendations” section of this Report, under the caption “Letter of Credit,” for further comments regarding this condition.

Merger of Indemnity Reinsurance Corporation of DC:

Effective October 1, 2009, the Company’s affiliate, Indemnity Reinsurance Corporation of DC (“IRCDC”), merged with and into the Company. All of the assets, liabilities and surplus of IRCDC were merged with and into the Company. This merger was approved by the Department. As of September 30, 2009, the Company’s reported surplus totaled $2,680,293, and IRCDC’s surplus as reported to the Department totaled $2,744,892.

2009 Cash Infusion:

In its 2009 Annual Statement, filed by the Company on February 26, 2010, the Company reported a cash infusion, totaling $10 million, from Jeffrey B. Cohen. The infusion was reported in the Annual Statement as “Gross paid in and contributed surplus”.

HISTORY

General:

Indemnity (formerly known as Capitol Specialty Insurance Risk Retention Group, Inc.) is an association captive insurance company domiciled in the District of Columbia. The Company received its Certificate of Authority on June 17, 2004.

The Company provides general liability, liquor liability and excess liability coverage to policyholders in the entertainment industry including nightclubs, bars, concert promoters, and special events.

Membership:

According to the Company’s approved business plan, the Company is owned 50 percent by RB Entertainment Ventures, LLC (“RB”), which is a policyholder and is owned by Jeffrey Cohen, President of the Company; and 50 percent by the International Association of Entertainment Businesses, Inc. (“IAEB”) whose President is also Jeffrey Cohen. The Company is authorized to issue class A and class B shares of common stock in accordance with the Company’s articles of incorporation. Class A and class B shares have equal voting rights. The owner of the class A shares is RB and the owner of the class B shares is the IAEB.

At inception of the Company, class B shares were non-voting. The articles of incorporation were modified in October 2006 canceling the originally issued 10 shares ($1 par value) of non-voting class B stock and replacing them with voting shares in an equal number to the number of outstanding class A ($1 par value) shares issued at that time (1,000 shares). This change was affected in response to the above-mentioned October 2006 Consent Agreement with the Department. The intent of this transaction was to create equal ownership percentages (50 percent each) between the class A shareholder, RB, and the class B shareholder, the IAEB, as well as to provide class B shareholders with voting rights, as required by the Consent Agreement.

While this change to the articles of incorporation was filed with and approved by the Department, and the Company's stock ledger reflected the cancellation of the 10 non-voting class B shares and the issuance of 1,000 class B voting shares, the funds to pay for the additional class B shares, to be contributed by the IAEB, were never collected and recorded by the Company. See the "Comments and Recommendations" section of this Report, under the caption "Common Capital Stock," for further comments regarding this condition.

As indicated above, the class B shareholder is the IAEB, and all policyholders (except for the class A shareholder, RB) are members of the IAEB. However, the Company has been collecting the membership fee ($10) from insureds, on behalf of the IAEB, but has not been remitting these fees to the IAEB. See the "Comments and Recommendations" section of this Report, under the caption "Membership," for further comments regarding this condition.

Surplus Notes:

The Company issued a surplus note on June 30, 2004 to RB. The note is for $650,000 and bears 6 percent interest. The note is due on demand and is payable in annual interest-only installments as allowed by the Department. A second surplus note in the amount of $1,000,000 was issued to Jeffrey Cohen on May 8, 2008 bearing 6 percent interest. This note is due April 15, 2058 and is payable in annual interest-only installments as allowed by the Department. Payments of principal and interest on both notes must be approved by the Department, and no payments have been requested, approved or made during the examination period. Accrued interest on the notes totaled $213,719 at December 31, 2008 and was reported as a liability of the Company. See NOTE 3 in the "Notes to Financial Statements" section of this Report for further comments regarding the accrued surplus note interest.

On September 12, 2008, via a "Unanimous Written Consent of the Board of Directors" of the Company, the amount of the second surplus note was modified from $1,000,000 to $900,000, and the issue date was changed from May 8, 2008 to April 15, 2008. The reduction in the surplus note was done in order to effectuate the transfer of $100,000 to "Common capital stock". See NOTE 4 in the "Notes to Financial Statements" section of this Report for further comments regarding this capital contribution.

Dividends and Distributions:

The Company did not declare or pay any dividends or other distributions during the period under examination.

MANAGEMENT

The following persons were serving as the Company's directors as of December 31, 2008:

Name and State of Residence	Principal Occupation
Jeffrey B. Cohen, Chairman Maryland	President IDG Companies, LLC*
Harvey Knick Maryland	Vice President IDG Companies, LLC*

*IDG Companies, LLC is the parent Company of the Company's managing general agent, The Agency.

The following persons were serving as the Company's officers as of December 31, 2008:

Name	Title
Jeffrey B. Cohen	President and Treasurer
Harvey Knick	Vice President
Evangelia Moniodis	Assistant Treasurer

Committees:

As of December 31, 2008, the Company's board of directors had not established any committees.

Conflicts of Interest:

Our review of the conflict of interest statements signed by the Company's directors and officers for the period under examination disclosed that there were no conflicts of interest reported that would adversely impact the Company. Furthermore, no additional conflicts of interest were identified during our examination.

Corporate Records:

We reviewed the minutes of the meetings of the board of directors and shareholders for the period under examination. Based on our review of minutes provided by the Company, the Company is not holding regular board meetings nor is there documentation of review and approval of the Company's significant transactions and events.

The Board voted to amend the bylaws in November 2008 through a unanimous written consent of the board of directors to reduce the number of directors from three to two. However the Company has not yet revised the bylaws as of the date of this report. See the "Comments and

Recommendations" section of this Report, under the caption, "Maintenance of Corporate Records," for further comments regarding the above conditions.

CAPTIVE MANAGER

B&D Consulting LLC ("B&D") is the Company's captive manager, and provides services including captive management and regulatory compliance services.

AFFILIATED PARTIES AND TRANSACTIONS

The Company's daily business operations are managed by The Agency, which acts as the Company's managing general agent and performs various administrative functions including underwriting, marketing, accounting, claims management, and overall program management services. The Agency's owner and President, Jeffrey Cohen, is also the owner of RB Entertainment Ventures, the Company's sole Class A shareholder, as well as 60 percent controlling owner of the Company's affiliated reinsurer, IRCDC. Jeffrey Cohen's parents, Sandra and Neal Cohen, own the remaining 40 percent of IRCDC.

Effective October 10, 2006 the Company entered into a managing general agency agreement with The Agency. The agreement is continuous until terminated. Under the terms of the agreement, The Agency acts as the Company's managing general agent, including solicitation, underwriting, and premium collection. Commissions paid by the Company to The Agency are provided for under a separate cost allocation agreement dated October 1, 2006. In the cost allocation agreement, the Company pays The Agency a percentage of the gross net premiums written on all lines (gross written premiums less refunds or cancellations).

Effective October 16, 2006, the Company also entered into a claims servicing agreement with The Agency. The agreement is continuous until terminated. The agreement calls for compensation of a claims servicing fee equal to a percentage of the amount of the Company's gross written premium.

According to the Company, the broker's commissions paid to The Agency as outlined in the cost allocation agreement were modified on January 1, 2008. However, the cost allocation agreement was not updated to reflect this change. In addition, according to the Company, the claims servicing fee as outlined in the claims servicing agreement was modified on January 1, 2008. However, the claims servicing agreement was not updated to reflect this change. See the "Comments and Recommendations" section of this Report, under the caption "Service Provider and Other Agreements," for further comments regarding these conditions.

During 2008, the Company paid brokerage commissions of $247,489 to The Agency and claim service fees of $35,651 to The Agency. Brokerage commissions and claim service fees were changed to 0 percent as of January 1, 2008, and these expenses are associated with the unearned portion (deferred acquisition costs) recorded in 2007 that was recognized in 2008.

The Company has also entered into a cost sharing agreement with its affiliated reinsurer, IRCDC, effective January 1, 2008. In this agreement, the companies agree to share and allocate certain operating costs and expenses incurred by the companies. These costs and expenses shall be mutually determined by the companies, and Indemnity will be responsible for payments of 10 percent of all operating costs and expenses, and IRCDC will be responsible for 90 percent of operating costs and expenses. The agreement is automatically renewed annually until terminated by either party.

In addition, the Company cedes business to IRCDC. See the "Reinsurance" section of this Report for further comments regarding the Company's affiliated reinsurance arrangements.

FIDELITY BOND AND OTHER INSURANCE

Indemnity maintains directors and officers liability coverage. In addition, the Company has no employees, but it is added as an insured on the Insurance Designers of Maryland, Inc. crime policy, which covers employee dishonesty, depositor's forgery and computer fraud. The Agency LLC has also been added as a named insured. These policies provide adequate coverage based on NAIC guidelines.

PENSION AND INSURANCE PLANS

The Company has no employees and therefore has no employee pension or insurance plans.

STATUTORY DEPOSITS

As of December 31, 2008, the Company did not have any statutory deposits in the District of Columbia and was not required to maintain any such deposits. In addition, the Company was not required to maintain statutory deposits with any other jurisdictions.

TERRITORY AND PLAN OF OPERATION

As of December 31, 2008, the Company was licensed in the District of Columbia, registered as a risk retention group in an additional 31 states, and was writing business in 27 states and DC. During 2008, Indemnity wrote premiums totaling $11,046,536. $3,728,976 (34 percent) of the Company's written premium in 2008 was in New York, $1,321,769 (12 percent) in Texas, $1,243,793 (11 percent) in Florida, $1,150,700 (10 percent) in DC, $1,024,505 (9 percent) in Connecticut, $457,790 (4 percent) in Nevada, $416,986 (4 percent) in California, and 2 percent or less in Alaska, Arizona, Colorado, Georgia, Hawaii, Idaho, Illinois, Kansas, Kentucky, Massachusetts, Missouri, New Hampshire, New Jersey, North Carolina, Ohio, Oklahoma, Oregon, Pennsylvania, Tennessee, Vermont, and Virginia.

The Company has no employees and its daily business operations are managed by various service providers. The Company provides comprehensive general liability coverage on an occurrence basis to members of the IAEB. Its insureds are pubs, nightclubs, and taverns, special events and concert promoters, and entertainers. The Company's policies include basic coverage for general liability with a limit of $1,000,000 each occurrence, $2,000,000 general aggregate; and liquor liability with a limit of $1,000,000 each occurrence and $2,000,000 general aggregate. Additional coverage is available for assault and battery, hired car and non-owned auto, and employee benefits liability with sub-limits up to $1,000,000 each occurrence and aggregate. Defense costs are in addition to the limits except for assault and battery coverage. Deductibles are offered on an exception basis, currently up to $10,000. The Company also offers excess liability coverage with limits up to $4,000,000 each occurrence and general aggregate. Per the Company's approved business plan, 100 percent of excess limits are required to be reinsured.

We noted several instances where the Company deviated from the approved business plan, including instances of writing policies with higher than approved limits and instances of the Company writing polices that were not covered by the Company's reinsurance. See the "Comments and Recommendations" section of this Report, under the captions "Policies Written in Excess of Limits Approved by the Department" and "Lack of Reinsurance Coverage" for further comments regarding these conditions.

We also noted that the Company made various changes in policy forms and rates that had not been filed with or approved by the Department. See the "Comments and Recommendations" section of this Report, under the caption "Changes in Business Plan" for further comments regarding these conditions.

INSURANCE PRODUCTS AND RELATED PRACTICES

This examination was a financial examination, and generally did not include market conduct procedures. An examination of the market conduct affairs of the Company has never been conducted. A market conduct examination would include detailed reviews of the Company's sales and advertising, agent licensing, timeliness of claims processing, and complaint handling practices and procedures.

The scope of our examination did not include market conduct procedures, including, but not limited to, market conduct procedures in the following areas:

- Policy Forms
- Fair Underwriting Practices
- Advertising and Sales Materials
- Treatment of Policyholders:
    - Claims Processing (Timeliness)
    - Complaints

REINSURANCE

Effective January 1, 2008 the Company entered into a "following form" Liability Quota Share Reinsurance agreement with its affiliate, IRCDC. Under this agreement, Indemnity cedes 90 percent of its gross written premium and receives a commission equal to a percentage of gross ceded premiums. Indemnity is entitled to recover 90 percent of its net liability for each policy, each occurrence on policies written or renewed between January 1, 2008 and December 31, 2008 (and each subsequent year until the agreement is cancelled).

In addition, effective February 15, 2008 the Company obtained Liability Excess of Loss Reinsurance coverage, underwritten by eight Lloyd's syndicates. Coverage is in the amount of $500,000 excess of $500,000 each occurrence for each insured on losses occurring on all in-force, new and renewal policies issued during the term of the agreement.

The Company also obtained a second Liability Excess of Loss Reinsurance contract effective August 15, 2008. Coverage, underwritten by seven Lloyd's syndicates, is in the amount of $4,000,000 excess of $1,000,000 each occurrence for each insured on losses under policies written or renewed during the term of the agreement.

Subsequent to the period of this exam, the Company cancelled the above two Excess of Loss treaties effective February 15, 2009 and rewrote them under a single contract with limits of $4,500,000 excess of $500,000 each occurrence with comparable terms and conditions.

In 2008 the ceded reinsurance premium under the above agreements totaled $10,057,354. As of December 31, 2008, the Company reported "Amounts recoverable from reinsurers" totaling $8,829 (representing amounts recoverable on paid losses), "Reinsurance receivables" totaling $4,612,144 (representing prepaid reinsurance premiums – i.e., ceded unearned premiums), and "Reinsurance loss recoverable" totaling $702,124 (representing estimated amounts recoverable on unpaid losses). If the reinsurers were not able to meet their obligations under the treaties, the Company would be liable for any defaulted amounts.

Our review of the Company's ceded reinsurance program and contracts disclosed a number of issues, including a lack of executed copies of certain treaties. See the "Comments and Recommendations" section of this Report, under the caption "Reinsurance" for further comments regarding these conditions.

ACCOUNTS AND RECORDS

The primary locations of the Company's books and records are at its offices, which are also the offices of its managing general agent, The Agency, in Sparks, Maryland.

The Company's general accounting records consist of an automated general ledger and various subsidiary ledgers. Our examination disclosed numerous issues regarding the Company's record-keeping, and numerous internal control weaknesses and issues in the Company's accounting and reporting processes, including issues regarding premium and loss data integrity, and lack of controls over intercompany and related-party transactions, premium reporting and claims processing. These conditions are addressed throughout the "Comments and Recommendations" section of this Report.

FINANCIAL STATEMENTS

The following financial statements, prepared in accordance with accounting practices generally accepted in the United States ("GAAP"), except for the condition described in NOTE 5, reflect the financial condition of the Company as of December 31, 2008, as determined by this examination:

The accompanying Notes to Financial Statements are an integral part of these Financial Statements.

BALANCE SHEET

ASSETS

		December 31, 2008
Cash ($2,286,669), cash equivalents ($0) and short-term investments ($0) **(NOTE 1)**	$	2,286,669
Subtotals, cash and invested assets	$	2,286,669
Investment income due and accrued		188
Uncollected premiums and agents' balances in the course of collection		3,864,484
Reinsurance:		
Amounts recoverable from reinsurers		8,829
Current federal and foreign income tax recoverable and interest thereon		316,890
Net deferred tax asset		521,374
Electronic data processing equipment and software		402,751
Aggregate write-ins for other than invested assets:		
Reinsurance receivables	$	4,612,144
Prepaid expenses		6,250
Deferred policy acquisition costs		131,889
Deductible receivables		23,390
Reinsurance loss recoverable		702,124
	$	5,475,797
Total	$	12,876,982

LIABILITIES, SURPLUS AND OTHER FUNDS

		December 31, 2008
Losses (**NOTE 2)**	$	143,478
Loss adjustment expenses (**NOTE 2**)		1,428,450
Other expenses (excluding taxes, licenses and fees) **(NOTE 3)**		278,957
Taxes, licenses and fees (excluding federal and foreign income taxes)		55,710
Unearned premiums		5,361,355
Ceded reinsurance premiums payable (net of ceding commissions)		3,286,643
Payable to parent, subsidiaries and affiliates		165,360
Aggregate write-ins for liabilities:		
Deferred ceding commission		1,457,032
Total Liabilities	$	12,176,985
Common capital stock (**NOTE 4**)	$	101,010
Surplus notes (**NOTE 5**)		1,550,000
Gross paid in and contributed surplus (**NOTE 4**)		0
Unassigned funds (surplus)		(951,013)
Surplus as regards policyholders	$	699,997
Total	$	12,876,982

STATEMENT OF INCOME

		2008
UNDERWRITING INCOME		
Premiums earned	$	1,061,397
DEDUCTIONS		
Losses incurred	$	119,269
Loss adjustment expenses incurred		187,815
Other underwriting expenses incurred		1,899,341
Total underwriting deductions	$	2,206,425
Net underwriting loss	$	(1,145,028)
INVESTMENT INCOME		
Net investment loss **(NOTE 3)**	$	(31,113)
Net loss, after dividends to policyholders, after capital gains tax and before all other federal and foreign income taxes	$	(1,176,141)
Federal and foreign income taxes incurred		(292,861)
Net loss	$	(883,280)

CAPITAL AND SURPLUS ACCOUNT

Net income, 2004	$	216,419
Change in surplus notes		650,000
Initial capital: Paid in		1,010
Net change in surplus as regards policyholders, 2004		867,429
Surplus as regards policyholders, December 31, 2004	$	867,429
Net income, 2005		548,233
Prior period adjustment to reconcile with audited f/s		40,918
Net change in surplus as regards policyholders, 2005		589,151
Surplus as regards policyholders, December 31, 2005	$	1,456,580
Net loss, 2006		(1,123,763)
Prior period adjustment		(3,173)
Net change in surplus as regards policyholders, 2006		(1,126,936)
Surplus as regards policyholders, December 31, 2006	$	329,644
Net income, 2007		144,586
Net change in surplus as regards policyholders, 2007		144,586
Surplus as regards policyholders, December 31, 2007	$	474,230
Net loss, 2008		(883,280)
Change in surplus notes		900,000
Capitol changes (Paid in)		100,000
Prior period audit adjustments		109,047
Net change in surplus as regards policyholders, 2008		225,767
Surplus as regards policyholders, December 31, 2008	$	699,997

ANALYSIS OF EXAMINATION CHANGES TO SURPLUS

There were no changes to the Company's surplus as a result of our examination.

COMPARATIVE FINANCIAL POSITION OF THE COMPANY

The comparative financial position of the Company for the periods since inception is as follows:

	2008	2007	2006	2005	2004
Assets*	$ 12,876,982	$ 3,695,278	$ 4,296,534	$ 3,069,167	$ 5,563,546
Liabilities*	12,176,985	3,221,048	3,966,890	1,612,587	4,696,117
Capital and surplus	699,997	474,230	329,644	1,456,580	867,429
Gross written premium*	11,046,536	1,893,095	1,447,530	449,606	4,348,865
Net earned premium	1,061,397	1,861,894	(5,728)	3,356,585	1,422,754
Net investment income (loss)	(31,113)	48,534	33,244	14,143	10,538
Net income (loss)	$ (883,280)	$ 144,586	$ (1,123,763)	$ 548,233	$ 216,419

Note:

Amounts in the preceding financial statements for the years ended December 31, 2004 through December 31, 2007 were taken from the Company's Annual Statements as filed with the Department. Amounts for the year ended December 31, 2008 are amounts per examination.

*Numerous changes to the Company's business plan have been made since inception of the Company, and the fluctuations in gross written premium, assets, and liabilities are reflective of these changes.

NOTES TO FINANCIAL STATEMENTS

NOTE 1 – Cash:

As of December 31, 2008, the Company reported "Cash" totaling $2,286,669; $2,190,336 of which was held in two institutions in amounts greater than the amount insured by the Federal Deposit Insurance Corporation ("FDIC"). During our examination, we discussed with management the potential risk to the Company from maintaining balances in excess of the FDIC insured limit in a single institution. The Company believes that the associated risk has been mitigated by maintaining deposits in high quality financial institutions.

NOTE 2 – Losses and Loss Adjustment Expense Reserves:

The Company reported "Losses and loss adjustment expenses" reserves of $1,571,928 which represents management's best estimate of the amount necessary to pay all claims and related expenses that have been incurred but are still unpaid as of December 31, 2008. The Company does not discount its loss reserves.

Reserve credits taken as of December 31, 2008 for loss reserve cessions to the Company's reinsurers totaled $702,124, which were reported as "Reinsurance recoverable" (on unpaid losses and LAE) in the Company's assets. If the reinsurers are unable to meet their obligations under the reinsurance treaty, the Company would be liable for any defaulted amounts. The Company's net loss reserves totaled $869,804 as of December 31, 2008.

The methodologies utilized by the Company to compute reserves, and the adequacy of the losses and loss adjustment expenses reserves as of December 31, 2008, were reviewed as part of our examination. As part of our review, we considered the report of the Company's independent actuary, who concluded that the Company's reserves (together with those of its affiliate, IRCDC) appeared to be deficient by $796,121. In addition, as part of our review of the Company's reserves, we engaged an independent actuary ("examination actuary") to review the methods employed, assumptions relied upon, and conclusions reached by the Company's independent actuary.

The examination actuary noted certain areas in which the methodologies and assumptions utilized by the Company's independent actuary to compute these reserves could be improved. As a result of these conditions and of the above-mentioned conclusion of the Company's independent actuary that the Company's reserves (together with those of its affiliate, IRCDC) appeared to be deficient, and as a result of other conditions outlined in this Report, the examination actuary concluded that the combined reserves of the Company and IRCDC as of December 31, 2008 were deficient by a minimum of $1,428,000. However, because the evaluation performed by the Company's independent actuary was of the combined reserves of the Company and IRCDC, and the examination actuary's review was based upon the work of the independent actuary, it was not possible for the examination actuary to make a determination of the ultimate losses separately for the Company, or of any potential reserve adjustment separately for the Company. Additional analyses to enable the examination actuary to make such determinations was beyond the scope of this examination. Due to this uncertainty, no adjustment to the Company's loss reserves has been made for the purposes of our examination. However, as indicated in the "Subsequent Events" section of this Report, effective October 1, 2009, the Company merged with IRCDC, and all of the assets, liabilities and surplus of IRCDC, including loss reserves, were merged with and into the Company. Therefore, as of December 31, 2009, the analysis of the adequacy of the Company's reserves will no longer be impacted by IRCDC and any uncertainty regarding the allocation of loss reserves between the two companies will no longer exist. Going forward, the Department will continue to closely monitor the Company's reserves, and if deemed necessary, based upon actuarial analyses, will require additional reserves to be recorded by the Company.

The Company's and IRCDC's loss reserves as of December 31, 2008, are summarized as follows:

		Company	IRCDC	Total
1.	Held net reserves per filed statements	$ 2,821,102	$ 870,000	$ 3,691,102
2.	Combined selected reserve per Company actuary			$ 4,487,223
3.	Minimum reserve per Company actuary			$ 4,183,102
4.	Deficiency from selected (2 minus 1)			$ 796,121
5.	Deficiency from minimum (3 minus 1)			$ 492,000
6.	Combined selected reserve per examination actuary			$ 5,119,102
	Deficiency from selected (6 minus 1)			$ 1,428,000

See the "Comments and Recommendations" section of this report, under the caption "Actuarial Review" for further comments regarding the above conditions.

NOTE 3 – Accruals:

Surplus Note Interest:

Included in the Company's "Other expenses" is accrued interest, totaling $213,719 at December 31, 2008, on the Company's surplus notes. In addition, the Company reported annual interest expense associated with these surplus notes ($77,219) as part of Investment Income. (Interest income on investments was offset by the interest expense on the surplus notes, resulting in a "Net investment loss" totaling $31,113.) During the examination we notified the Company that surplus note interest should not be expensed or accrued until payment of such interest is approved by the Department.

Legal Expenses:

The Company and/or its affiliate, The Agency, which provides services to the Company and allocates costs to the Company, were parties to a number of lawsuits as of December 31, 2008, some as defendant and some as plaintiff. Management of the Company has determined that as of December 31, 2008 no accruals for liabilities, including expenses, related to these lawsuits was required to be recorded by the Company.

NOTE 4 – Common Capital Stock:

As indicated above in the "Membership" section of this Report, at inception of the Company, 10 shares of non-voting class B stock ($1 par value) and 1,000 shares of voting class A stock ($1 par value) were issued by the Company. The Company therefore reported "Common capital stock" at that time totaling $1,010. In 2006, the Articles of Incorporation were modified, canceling the originally issued 10 shares of non-voting class B stock and replacing them with voting class B shares in an equal number to the number of outstanding class A shares. As a result of this transaction, the Company had outstanding stock with a par value totaling $2,000 ($1,000 class A shares and $1,000 class B shares). However, the Company continued to report "Common capital stock" totaling $1,010.

In 2008, the Department notified the Company that it needed a minimum of $100,000 in "Common capital stock" to be in compliance with DC statutes. To comply, the Company's President, Jeffrey Cohen, on behalf of RB, made a $100,000 capital contribution to the Company. This contribution was initially reported by the Company in 2008 as "Gross paid in and contributed surplus," and was later transferred in 2008 to "Common capital stock." However, upon transfer to "Common capital stock," the Company did not issue any additional stock or increase the par value of the outstanding stock to account for the $100,000. As a result, the Company's reported "Common capital stock", totaling $101,010, does not accurately reflect the amount of capital stock issued by the Company. See the "Comments and Recommendations" section of this Report, under the caption "Common Capital Stock," for further comments regarding this condition.

NOTE 5 - Surplus Notes:

At December 31, 2008, the Company's surplus as regards policyholders included $1,550,000 in surplus notes. The surplus notes and related interest may not be paid without approval of the Department. Under the Laws of the District of Columbia, surplus notes approved by the Department are allowed as admitted assets and surplus as regards policyholders. Inclusion of the surplus notes as assets and surplus as regards policyholders is not in accordance with GAAP.

COMMENTS AND RECOMMENDATIONS

Policies Written in Excess of Limits Approved by the Department:

Prior to August 2008, the Company's approved limits, for primary coverage, were $1 million per occurrence, $2 million in the aggregate for general liability and $1 million per occurrence, $2 million in the aggregate for liquor liability. In addition, under the Company's approved business plan, the Company was also approved to write excess coverage with limits up to $1 million per occurrence, $2 million in the aggregate. However, under the terms of the aforementioned October 2006 Consent Agreement, excess policies could not be issued to policyholders who had already purchased underlying general liability or liquor liability policies from the Company.

However, based upon a report provided by the Company during the examination, we noted 127 "excess" policies were written by the Company prior to August 2008, some with limits up to $4 million per occurrence. While some of these policies were excess-only policies (with no underlying primary coverage) for a limit of only $1 million per occurrence (and were therefore within the limits of the Company's approved business plan), some of the policies were written on top of primary policies issued by the Company, and/or had limits up to $4 million per occurrence which were greater than the limits approved by the Department. These policies were in violation of the Company's business plan.

In addition, we noted three policies out of fourteen primary polices tested that were written by the Company prior to August 2008 in excess of the approved limits of $1 million per occurrence, $2 million in the aggregate for general liability; and $1 million per occurrence, $2 million in the aggregate for liquor liability.

Similar conditions regarding the Company writing policies in excess of approved limits were noted in the aforementioned limited-scope examination of the Company. The Company agreed, in the aforementioned Consent Agreement, not to write limits it was not approved to write.

In July 2008, the Department approved a change to the Company's business plan whereby the Company was approved to write excess general and liquor liability coverage with maximum policy limits of $4 million per occurrence, $4 million in the aggregate. The Department's approval was subject to the excess coverage being fully reinsured. Based on this approval for excess coverage, the Company became approved to offer general liability policies with combined limits up to $5 million per occurrence, $6 million in the aggregate ($1 million primary coverage plus $4 million excess coverage per occurrence and $1 million primary coverage plus $5 million excess coverage in the aggregate) and for liquor liability up to $5 million per occurrence, $5 million in the aggregate ($1 million primary coverage plus $4 million excess coverage per occurrence and in the aggregate). Subsequent to the July 2008 approval to write the excess coverage, the Company obtained, effective August 15, 2008, 100 percent reinsurance coverage for the excess amounts.

However, we noted an excess policy written by the Company after August 15, 2008 with limits of $5 million per occurrence, $5 million in the aggregate, combined with a primary policy written for $1 million per occurrence and $2 million aggregate. This policy therefore had combined limits written by the Company of $6 million per occurrence; $7 million in the aggregate, which exceeded the Company's approved combined limits of up to $5 million per occurrence, $6 million in the aggregate.

We again recommend that the Company only write policies with limits as approved by the Department.

Reinsurance:

During our examination, we noted the following:

1. Lack of Reinsurance Coverage:

   As a result of the above conditions noted under the caption "Policies Written in Excess of Limits Approved by the Department", the Company lacked reinsurance coverage on certain policies.

   For example, the August 15, 2008 excess treaty only covered policies with maximum combined policy limits of $5 million per occurrence, $6 million in the aggregate, and the policy noted above, written for a combined primary and excess limit of $6 million per occurrence, $7 million in the aggregate, was not fully covered by reinsurance.

   We also noted numerous other policies and coverages that potentially would not be covered under the Company's reinsurance agreements. For example:

   - Liquor liability is specifically excluded in the Company's August 15, 2008 excess reinsurance treaty in effect until February 15, 2009 (although liquor liability is included in the new combined treaty effective on that date). We noted numerous excess policies written prior to February 15, 2009 that included liquor law liability coverage.
   - The Company wrote policies for policyholders with multiple locations, and although according to the Company, the per location aggregates were within the Company's reinsurance limits, the policies contained overall aggregates that exceeded the reinsurance limits. (See additional comments regarding the Company's policies with multiple-location aggregates below under the caption "Business Plan Changes.")
   - The Company wrote certain policies with two year coverage periods but it was not specified in the reinsurance treaties that these two year policies were covered.
   - The Company wrote a master policy under its Tenant Users Liability Insurance Policy (TULIP) program, and insureds were issued certificates under this master policy, but it was not clear from the reinsurance treaties whether this TULIP program was covered.

After we brought these conditions to the attention of management, the Company requested endorsements to its reinsurance treaties to address the issues and attempt to clarify in the treaties that all of the Company's policies would be covered under the reinsurance treaties. As of the date of this report, the Company had provided the Department with draft endorsements that may, except for certain policies, cover the policies in question. Specifically, the draft endorsement wording to address the policies written in excess of the Company's approved limits prior to August 15, 2008 indicates reinsurance coverage would apply to all losses occurring on new or renewed policies including those written prior to and remaining active on August 15, 2008.

We recommend that the Company finalize the endorsements to its reinsurance treaties, ensuring all identified deficiencies have been addressed, and ensuring all policies written by the Company are covered by the reinsurance program in accordance with the approved business plan. The fully executed endorsements should be forwarded to the Department by July 31, 2010.

In addition, we recommend that the Company ensure that all polices written are covered at all times by the Company's reinsurance program, in accordance with the Company's approved business plan.

2. Executed Treaties:

As indicated in the "Reinsurance" section of this Report, the company entered into excess of loss treaties effective August 15, 2008 and February 15, 2009, respectively. These treaties were approved by the Department based upon cover notes from the Company's reinsurance broker, with the understanding the executed treaties would be provided to the Department. During the examination, it was discovered that the Department did not have the executed treaties on file. Accordingly, as part of the examination, copies of the executed treaties were requested from the Company. However, as of the date of this Report, the Company had not provided copies of the executed treaties. According to management, the Company had to request complete copies of the treaties from the reinsurers. (Subsequent to the date of this report, the Company obtained executed treaties and provided copies to the Department).

We recommend that in the future, the Company obtain timely, and maintain on file, executed copies of all reinsurance treaties, and that copies of these executed treaties be submitted to the Department on a timely basis.

<u>Data Processing Controls and Integrity of Data</u>:

With regard to the Company's underwriting and claims controls and data, we noted the following:

1. <u>Underwriting:</u>

We noted a number of policies recorded in the Company's underwriting system that did not agree to hard-copies of the policies that were provided to the Department either by the Company, or by the policyholders or their agents:

Coverage Provided in Policy	Limits per Company Underwriting System (Per Occurrence / Aggregate)	Limits per Hard-Copy Policy Provided by Company	Limits per Hard-Copy Policy Obtained by Department Independently
1. General Liability (GL) Liquor Liability (LL)	\$4M / \$5M \$4M / \$4M	\$1M / \$4M \$1M / \$4M	\$4M / \$5M \$4M / \$4M
2. GL/LL Excess	\$1M / \$2M \$4M / \$4M	n/a	\$1M / \$2M \$5M / \$5M
3. Excess	\$4M / \$4M	\$4M / \$4M	\$5M / \$5M
4. Excess	\$2M / \$20M	\$2M / \$20M[1]	\$20M / \$20M[1]

[1] Subject to a maximum of $4M each location. See further discussion of this policy below under the caption "Changes to Business Plan."

The Company was unable to reasonably and satisfactorily explain why the limits in the underwriting system differed from the limits indicated on the hard-copy policies. These discrepancies, coupled with the inability of the Company to adequately explain them indicates significant potential control issues regarding the Company's underwriting system and indicates concerns regarding the reliability of the data in the Company's underwriting system.

We recommend that the Company perform a review of its underwriting and policy issuance system, including the adequacy of the controls within the system. In addition, as part of this review, all discrepancies between the data recorded in the company's system and the actual policies should be identified and corrected. Automated controls should also be established within the underwriting system to ensure that no policies are issued that are greater than the Company's approved limits. The Company shall report to the Department by September 1, 2010 regarding the results of the review and the corrective action taken or to be taken to ensure the accuracy and integrity of data in its system.

2. Claims:

A. The Company's claims are processed by The Agency (the Company's MGA) on The Agency's Insurance Management System ("IMS"). IMS is also used by The Agency to process and maintain data for carriers other than the Company. We noted one instance of a claim recorded as incurred by the Company being paid out of the loss fund of another carrier serviced by The Agency (this error was caught and corrected by the Company during 2008), and we noted two instances of claims paid from the Company's loss fund that were actually claims incurred by another carrier serviced by The Agency. The Company was not previously aware of these two errors. In all three instances the Company attributed the errors to human error in entering the carrier code in IMS. **We recommend that the Company develop, document and implement additional control procedures to ensure that only claims of the Company are paid out of the Company's loss fund.**

B. The Company records claims as paid when payment is requested, as opposed to when the payments are actually made. In addition, the Company initially records loss adjustment expenses (LAE) incurred through its general accounts payable account, as opposed to an LAE account (as of December 31, 2008, LAE payable totaling $44,994 was recorded in the accounts payable account.) (Upon payment, the Company ultimately records the LAE in a separate LAE account, and reverses the payable out of the accounts payable account.) As a result, the Company's loss data does not always accurately reflect claims paid or LAE incurred. **We recommend the Company properly record claims paid and loss adjustment expenses incurred in its claims system.**

C. In the Statement of Actuarial Opinion as of December 31, 2008, the Company's independent actuary indicated the Company's reserves on which the opinion was being expressed have been reduced due to the anticipation of receiving salvage and subrogation. However, we noted the following:

- The Company could not provide documentation that could be verified, of its salvage and subrogation amounts receivable as of December 31, 2008, or of any salvage and subrogation amounts collected subsequent to December 31, 2008.
- The Company's actuarial opinion or supporting report did not disclose the amount of estimated recoveries for salvage and subrogation and when asked to clarify the amount of the reduction, the Company's independent actuary was unable to do so.
- The Company recorded salvage and subrogation received to its general ledger as a reduction to the paid loss adjustment expenses.
- Neither salvage and subrogation receivable, or paid, was reported in the Company's Annual Statement (Schedule P).

We recommend that the Company maintain clear and verifiable records and supporting documentation of its salvage and subrogation amounts receivable

and collected. These amounts should be recorded in separate general ledger accounts, and should be reported in the Company's Annual Statements as filed with the Department. The Company should ensure reserves are only reduced for anticipated salvage and subrogation amounts that are supported. In addition, the Company should ensure its actuary discloses, in the actuarial opinion and/or supporting report, the specific dollar amount of any reduction to the Company's loss reserves for estimated recoveries for salvage and subrogation.

D. The Company reported "Deductible receivables" totaling $23,390 in its December 31, 2008 Annual Statement. However, the Company could not provide a deductible receivable listing as of December 31, 2008. In addition, deductible receivables were not uniformly or consistently recorded in the IMS claims system, which is where narrative descriptions of the status and details of the Company's claims are maintained. **We recommend that the Company develop, document and implement procedures and controls to account for deductible receivables.**

Underwriting:

We noted the following:

1. Use of Rates Outside of Underwriting Guidelines:

   In our testing and review of the Company's underwriting files and of the coverages written by the Company, we noted numerous instances of rating classifications, rating factors, and rates for these classifications that were not included in the underwriting manual. The underwriting manual permits deviations if approved by the Company President or Vice President of Underwriting, but no documentation of approval of deviations was evident in the company's files. **The Company should ensure that all rating classifications, factors and limitations are included in the underwriting manual and all premiums should be calculated using such rates. All rating classifications, factors and limitations should be clearly documented in the underwriting files and of approval of any deviations should be clearly documented in the underwriting files.**

2. Eligibility Requirements for Deductibles:

   The underwriting manual states deductibles will only be offered to insureds with a full time risk manager; require the approval of the Vice President of Underwriting; and require collateral equal to 200 percent of any expected losses. However, we noted no evidence in the Company's files that these requirements are being met for policies with deductibles. **The Company should ensure that proper approval and documentation for all policies with deductibles is included in the underwriting files.**

<u>Changes in Business Plan</u>:

Changes to information filed with the Company's application are required to be submitted to the Department. In addition, substantive changes to information in the application and to the Company's business plan require prior approval of the Department. During the period under examination, the Company has made a number of changes to the rating plan (including changes to the base rates, rating classifications, application of various schedule and merit credits and debits), policy forms (including the addition of claims made coverage and special purpose endorsements), and limits offered from those originally filed with the Department, without notification to the Department:

1. <u>Rate and Classification Changes</u>:

   The Company amended rates (e.g., Assault & Battery) and added classifications since inception without notifying the Department.

2. <u>Rate and Classification Changes</u>:

   In 2008 the Company eliminated the mandatory use of deductibles and began permitting deductibles only on an exception basis. The Department was not formally notified of this change.

3. <u>Form and Coverage Changes:</u>

   The Company has added forms and amended coverages without notifying the Department. For example:

   - Per location (per event) aggregate endorsements. Such endorsements can significantly increase the amount of coverage afforded under a policy and it is unclear whether there is full excess reinsurance coverage.
   - The Company began offering multiple location aggregate limits to certain policyholders with multiple locations. We noted one policy written with total limits of $10 million each occurrence/$10 million general aggregate. The Company explained each location has a maximum policy limit cap of $4 million each occurrence/$4 million general aggregate. Another policy indicated a limit of $2 million each occurrence/$20 million general aggregate.
   - Since May 2008 the Company has issued two master Tenant User Liability Insurance Policies (TULIP) insuring members of the International Association of Entertainment Businesses on a shared limits basis without prior notification to the Department of its intent to offer such program or of the forms used.

   The Company agreed, in the aforementioned Consent Agreement, to use only policy forms contained in the existing approved business plan.

   We recommend that all future substantive or material changes to the Company's business plan be submitted to the Department for review and approval prior to

implementation. Such changes include future material changes to rates or additions to rate classifications. Any questions regarding what may or may not constitute a material change in business plan should be clarified with the Department prior to implementation. In addition, we recommend that the Company ensure that all revisions to documents previously filed with the department be submitted to the Department.

<u>Actuarial Review</u>:

The Company reported "Losses" and "Loss adjustment expenses" reserves totaling $143,478 and $1,428,450, respectively. The methodologies utilized by the Company to compute reserves, and the adequacy of the loss and loss adjustment expenses reserves as of December 31, 2008, were reviewed as part of our examination. As part of our review, we relied on the Company's independent actuary. In addition, as part of our review, we engaged an independent actuary ("examination actuary"), to review the methods employed, assumptions relied upon, and conclusions reached by the Company's actuary. As indicated in NOTE 2 in the "Notes to Financial Statements" section of this Report, the examination actuary could not conclude, based on the work done by the independent actuary, with respect to the reasonableness of the Company's loss and loss expense reserves due to a number of factors, including:

a. The analysis performed by the Company's actuary was combined for the Company and for the Company's affiliate, IRCDC, and the reserve deficiency noted by the Company's actuary, $796,121, was not broken out by company. The examination actuary concluded that the combined reserves of the Company and IRCDC as of December 31, 2008 were deficient by a minimum of $1,428,000, but the examination actuary could not determine the amount of the deficiency related to each company.

b. In addition, the analysis of the data included losses and loss adjustment expenses combined. However, the Company uses different reserving approaches for establishing case reserves versus loss adjustment expenses and losses would have different reserving, development and payment patterns than loss adjustment expenses. For example, the Company does not set up indemnity reserves on a claim until there is some certainty that payments will be made. Therefore, the data would exhibit slow reporting of losses, however, for expenses, reserves are established on a much timelier basis.

c. The Company's actuarial opinion stated that the reserves shown in the Annual Statement on which the opinion was being expressed have been reduced for anticipated salvage and subrogation. However, as indicated above under the caption "Data Processing Controls and Integrity of Data: Claims," salvage and subrogation receivable was not indicated in the Company's Annual Statement (Schedule P) and we noted numerous issues regarding the Company's support for its salvage and subrogation. In addition, the Company's actuarial opinion or supporting report did not disclose the amount of estimated recoveries for salvage and subrogation.

d. The Company's actuarial opinion stated that earned premium, paid loss and allocated loss adjustment expenses and case reserve amounts in the supporting data provided to the actuary by the Company for use in forming an actuarial opinion were reconciled to the

Company's "Schedule P" in the Company's Annual Statement filed with the Department. However, there was no such reconciliation in the actuarial opinion or supporting report.

e. The Company's actuary indicated in the actuarial report that the Company has prepaid adjusting and other expenses (unallocated loss adjustment expenses or "ULAE") on a contractual basis and therefore no reserves are needed for ULAE. However, a liability for ULAE should be established without consideration of prepayments made to third party administrators, management companies or other entities.

f. Loss development factors were determined based on a larger data set which included data from the Company and IRCDC, as well as other entities. It was indicated that the business written from these other companies was the same type of business underwritten by the Company and IRCDC, however the names of the other companies were not provided nor a reconciliation of the data underlying the loss development triangles shown. While we do not disagree with this approach of using a larger data set, a data triangle from the Company and IRCDC should have been provided in addition to data from the combined companies for comparison and reconciliation purposes and to support the use of the large data set.

g. Separate loss development factors were chosen for assault and battery losses in New York. However, there are no underlying loss development triangles or historical experience supplied that support these selected factors, which are based upon a previous actuary's analysis. The workpapers of the previous actuary were not available for review and without these work papers that support these selections, we are unable to determine the reasonableness of the underlying assumptions.

We recommend the following:

a. The Company's actuary shall provide a high and low range of estimated reserves, and/or a selected amount of reserves for the Company. If a range is provided, the Company shall book at least to the mid-point of the range. If a selected amount is provided, the Company shall book at least that amount. If a range and a selected amount are both provided, the Company shall book to the higher of the mid-point of the range or the selected amount.

b. Any reserve deficiency identified by the Company's actuary shall be recognized in the Annual and Quarterly Statements via an increase to loss reserves for the amount of the deficiency.

c. If applicable in the future, a separate analysis (as opposed to combined with any other companies) of the Company's reserves should be performed by the Company's actuary.

d. The analysis of the data should be performed separately for losses and loss adjustment expenses.

e. The Company's actuarial analysis should disclose the amount of estimated recoveries for salvage and subrogation. Any reduction in the Company's loss reserves for salvage and subrogation shall be supported and documented.

f. **The Company's actuarial analysis should include a reconciliation of the data used by the actuary to the "Schedule P" in the Company's Annual Statement filed with the Department.**

g. **The Company should record a ULAE reserve.**

h. **The Company should ensure that sufficient information, documentation and support regarding the data and methodologies used to estimate its loss reserves is appropriately disclosed in the analysis of the reserves.**

Inter-company Transactions:

1. We noted that intercompany accounts and transactions are not settled timely in accordance with the terms of the intercompany agreements which govern the transactions. A similar condition regarding the timeliness of settlement of intercompany premium transactions was noted in the aforementioned limited-scope examination of the Company. **We again recommend that the Company settle balances between related parties on a timely basis based on the terms of the agreements between parties. Appropriate supporting documentation shall accompany the settlement of all intercompany transactions and shall be maintained for future verification.**

2. The Company reported "Uncollected premiums and agents' balances in the course of collection" totaling $3,864,484. This amount represents amounts due to the Company from its affiliate MGA, The Agency. However, the Company was unable to provide a detailed premium receivable report by insured indicating the details of this balance. **We recommend that the Company maintain detailed records of its premiums due.**

Common Capital Stock:

1. Class B Common Stock:

   As indicated above in the "Membership" section of this report, according to the Company's approved business plan, the Company is owned 50 percent by RB and 50 percent by the IAEB whose President is also Jeffrey Cohen. The Company is authorized to issue class A and class B shares of common stock in accordance with the Company's articles of incorporation. Class A and class B shares have equal voting rights, which are one vote per policyholder. The owner of the class A shares is RB and the owner of the class B shares is the IAEB.

   At inception of the Company, there was not equal ownership among RB and IAEB, and class B stock was non-voting. Initially, 10 shares of non-voting class B stock ($1 par value) and 1000 shares of voting class A stock ($1 par value) were issued by the Company. The Company therefore reported "Common capital stock" at that time totaling $1,010. In 2006, in response to the aforementioned limited-scope examination and to the Company's October 13, 2006 Consent Agreement with the Department, the articles of incorporation were modified, canceling the originally issued 10 shares of non-voting class B stock and replacing them with voting class B shares in an equal number to the number of outstanding class A shares. The intent of this transaction was to create equal ownership percentages (50 percent each) between the class A shareholder, RB, and the class B shareholder, the IAEB, as well as provide voting rights to the IAEB, as required by the Consent Agreement.

While this change to the articles of incorporation was filed with and approved by the Department, and the Company's stock ledger reflected the cancellation of the 10 non-voting class B shares and the issuance of 1,000 class B voting shares, the funds to pay for the additional class B shares, to be contributed by the IAEB, were never collected and recorded by the Company. As a result of this transaction, the Company's stock ledger reflected outstanding stock with a par value totaling $2,000 ($1,000 class A shares and $1,000 class B shares). However, the Company continued to report "Common capital stock" totaling $1,010, and as a result of the Company not collecting the additional contributions from the IAEB, and not recording in its financial records the additional amount from the IAEB, the equal ownership between RB and the IAEB, as required by the Consent Agreement, was never achieved.

We again recommend that the Company properly complete, and document the completion of this transaction, whereby RB and the IAEB will be equal owners of the Company.

2. <u>2008 Increase in Capital</u>:

   In 2008, the Department notified the Company that it needed a minimum of $100,000 in "Common capital stock" to be in compliance with DC statutes. To comply, the Company's President, Jeffrey Cohen, on behalf of the class A shareholder, RB, made a $100,000 capital contribution to the Company. This contribution was initially reported by the Company in 2008 as "Gross paid in and contributed surplus," and was later transferred in 2008 to "Common capital stock." However, upon transfer to "Common capital stock," the Company did not issue any additional stock or increase the par value of the outstanding stock to account for the $100,000 contribution. As a result, the Company's reported "Common capital stock," totaling $101,010, does not accurately reflect the amount of capital stock issued by the Company. **We recommend that in the future, the Company maintain at least the required statutory minimum capital stock of $100,000. We also recommend that the Company properly record all capital stock transactions in its stock ledger. In addition, the Company shall ensure that equal ownership of the Company is maintained between RB and the IAEB, as required by the aforementioned Consent Agreement.**

<u>Letter of Credit</u>:

As indicated in the "Subsequent Events" section of this Report, during the second quarter of 2009, with the approval of the Department, the Company obtained a letter of credit ("LOC") in the amount of $47 million. However, the Company did not report the LOC in its June 30, 2009 Quarterly Statement filed with the Department. After the Department brought this omission to the Company's attention, the Company revised and re-filed its June 30, 2009 Quarterly Statement to include the LOC. However, subsequent to this re-filing, the Company again amended and re-filed its June 30, 2009 Quarterly Statement, once again removing the LOC from the Statement. The Company explained the LOC was removed from the Statement because the Company did not plan to renew it after the December 31, 2009 expiration date. In addition, the Company informed the Department that the LOC would not be included in the September 30, 2009 Quarterly Statement to be filed with the Department for the same reason it was removed from the June 30, 2009 Statement. However, because the LOC did not expire until December 31, 2009, the Company should have reported it in its financial statements up to that date. **We recommend the Company properly reflect all assets, liabilities and other amounts in its future financial statements.**

Membership:

According to the Company's business plan, Indemnity complies with the ownership requirements of the Federal Liability Risk Retention Act ("LRRA") by requiring all policyholders to be members of the IAEB (the "Association"), the class B shareholder of the Company. According to the Company, each policyholder pays a $10 membership fee each year for an ownership interest in the Association. However, although the Company is collecting the $10 membership fee from all policyholders on behalf of the Association, the Company is not remitting these fees to the Association, but is instead recording the fees as part of premiums written. In addition, during our examination, we were informed by the Company there is no membership agreement for the Association, nor any documentation maintained by the Association of its members.

Although the membership fees are immaterial to the financial position of the Company, to ensure valid membership of all policyholders of the Company in the IAEB, we recommend that the Company remit membership fees to the Association and ensure the membership of the Association is documented.

Maintenance of Corporate Records:

1. Section 31-3931.11(d) of the D.C. Official Code requires the board of directors of a captive insurer to meet at least one time each year in the District. However, based on documentation provided by the Company during the examination, the Company does not hold regular board meetings, and during the examination period the Company has met only one time in the District of Columbia (an organizational meeting in 2004). We noted certain board actions were documented during the examination period via unanimous written consents in lieu of board meetings, but these consents generally do not discuss or approve the Company's significant transactions and events. For example, there is no mention in board meeting minutes or unanimous written consents of hiring a new captive manager, B&D Consulting LLC, as of January 1, 2008; no mention of the Department's full-scope financial examination as of December 31, 2008; no discussion of pending law suits; and no discussion of underwriting or claims reports. **We recommend that the Company comply with the aforementioned provision of the DC Official Code and physically meet, with at least a quorum of directors present, at least one time each year in the District. In addition, the minutes for these meetings should reflect review and approval of the Company's significant transactions and events.**

2. The board voted to amend the bylaws in November 2008 through a Unanimous Written Consent of the board of directors to reduce the number of directors from three to two. However the Company has not yet revised the bylaws as of the date of this report. **We recommend that corporate documents such as bylaws be maintained up to date, and submitted to the Department promptly when changes are made.**

Service Providers and Other Agreements:

The Cost Allocation Agreement with The Agency effective October 1, 2006 has not been updated to reflect the change in commission as of January 1, 2008. In addition, the Claims Servicing Agreement dated October 16, 2006 with The Agency was not updated to reflect the change in compensation as of January 1, 2008. **We recommend that the Company review all contracts and make any necessary amendments. In addition, we recommend that all revised agreements be submitted promptly to the Department.**

CONCLUSION

Our examination disclosed that as of December 31, 2008 the Company had:

Admitted Assets	$	12,876,982
Liabilities and Reserves		12,176,985
Common Capital Stock		101,010
Unassigned Funds (Surplus)		(951,013)
Total Surplus		699,997
Total Liabilities, Capital and Surplus	$	12,876,982

Based on our examination, except for the potential effects of the conditions noted in NOTES 2 through 4 in the "Notes to Financial Statements" section of this Report, and except for the potential effects of various conditions noted in the "Comments and Recommendations" section of this Report, the accompanying balance sheet properly presents the financial position of the Company at December 31, 2008, and the accompanying statement of income properly presents the results of operations for the period then ended.

Chapter 39 ("CAPTIVE INSURANCE COMPANIES") of Title 31 ("Insurance and Securities") of the D.C. Official Code specifies the level of capital and surplus required for the Company. Except for the potential effects of the conditions noted in NOTES 2 through 4 in the "Notes to Financial Statements" section of this Report, we concluded that the Company's capital and surplus funds exceeded the minimum requirements during the period under examination.

SIGNATURES

In addition to the undersigned, the following examiners representing the District of Columbia Department of Insurance, Securities and Banking participated in certain phases of this examination:

Christina M. Bonney, Collins Consulting, Inc.
John G. Gantz, Collins Consulting, Inc.

The actuarial portion of this examination was completed by N. Terry Godbold, ACAS, MAAA, FCA, President & Senior Actuary, Godbold, Malpere & Co.

Respectfully submitted,

Pamela C Woodroffe

Pamela C. Woodroffe
Examiner-In-Charge
Collins Consulting, Inc.

Under the Supervision of,

Xiangchun Li

Xiangchun (Jessie) Li, CFE
Supervising Examiner
District of Columbia Department of Insurance, Securities and Banking

BEFORE THE
DISTRICT OF COLUMBIA
COMMISSIONER OF INSURANCE, SECURITIES AND BANKING

Re: Report on Examination **- Indemnity Insurance Corporation of DC, Risk Retention Group**, as of December 31, 2008

FINAL FINDINGS OF FACT

1. The financial examination of Indemnity Insurance Corporation of DC, Risk Retention Group ("the Company") produced evidence to support a finding that the Company wrote policies in excess of limits approved by the Department of Insurance, Securities and Banking ("Department"). Prior to August 2008, the Company was authorized to issue policies with the following limits: $1 million per occurrence and $2 million in the aggregate for general liability, and $1 million per occurrence and $2 million in the aggregate for liquor liability. Pursuant to the Company's approved business plan, the Company also was approved to write excess coverage with limits up to $1 million per occurrence, $2 million in the aggregate. The Company was not authorized to issue excess policies to policyholders who had already purchased underlying general liability or liquor liability policies from the Company.

During the Department's review of the Company's policies issued prior to August 2008, it was noted that some of the policies written by the Company were in addition to primary policies issued by the Company, and had total limits up to $4 million per occurrence, which exceeded the limits approved by the Department.

Similar findings regarding the Company's practice of writing policies in excess of approved limits were noted in the limited-scope examination of the Company in 2005. The Company agreed, in a 2006 Consent Agreement, not to write limits it was not approved to write.

In July 2008, the Department approved a change to the Company's business plan whereby the Company was approved to write excess general and liquor liability coverage with maximum policy limits of $4 million per occurrence, and $4 million in the aggregate. The Department's approval was subject to the excess coverage being fully reinsured. Based on this approval for excess coverage, the Company was approved to offer general liability policies with combined limits up to $5 million per occurrence and $6 million in the aggregate ($1 million primary coverage plus $4 million excess coverage per occurrence, and $1 million primary coverage plus $5 million excess coverage in the aggregate), and for liquor liability up to $5 million per occurrence and $5 million in the aggregate ($1 million primary coverage plus $4 million excess coverage per occurrence and in the aggregate).

During a review of the Company's policies issued after August 15, 2008, the Department discovered that the Company wrote an excess policy with limits of $5 million per occurrence and $5 million in the aggregate, in addition to a primary policy written for $1 million per occurrence and $2 million aggregate. This policy, for a single insured, had combined limits of $6 million per occurrence and $7 million in the aggregate, which exceeded the Company's approved combined limits of up to $5 million per occurrence, $6 million in the aggregate.

On June 29, 2010, the Company filed a written response to the draft financial examination report. In the Company's reply to this finding, the Company asserts that the Department's Examiner in Charge, Pamela R. Collins, President of Collins Consulting, Inc., is not qualified to determine whether coverage exists under any form of insurance contract. The Company also states Ms. Collins lacks relevant U.S. judicial experience necessary to opine on coverage related matters. The Company also states that its reinsurer has conducted an extensive underwriting and claims audit, and has concluded that the Company is not engaged in any business that would fall outside of the scope of the reinsurance coverage.

The Company's assertion that Collins Consulting does not possess the qualifications required to determine the Company's compliance with its reinsurance treaty is unfounded. Pamela Collins is a certified public accountant with over 20 years of experience in insurance company financial operations and reporting, including reinsurance matters. Collins Consulting also employs other experts with significant insurance and reinsurance experience. John Gantz, who has over 30 years of insurance industry experience, including reinsurance matters, assisted Ms. Collins in her examination of the Company. Moreover, one hardly needs to be an expert in reinsurance matters to compare the policy limits the Company was authorized to write with the policy limits issued to its insureds. The Department's review of the pertinent reinsurance treaty and the sampling of policies issued by the Company show that policies were sold by the Company that provided limits that in excess of those covered in the treaty. The Department's review also shows that Company sold coverage for liquor liability in 2008, but the reinsurance treaty covering that period excluded coverage for liquor liability. The Company's response that its reinsurer has not engaged in business that falls outside of the scope of the Company's reinsurance coverage is not supported by the facts.

2. The financial examination of the Company produced evidence that supports the finding that the Company failed to maintain reinsurance coverage on certain policies**.** The Company's excess of loss treaty only covered policies with maximum combined limits of $5 million per occurrence and $6 million in the aggregate. Therefore, the policy noted in the first Finding of Fact, written for a combined primary and excess limit of $6 million per occurrence, $7 million in the aggregate, was not fully covered by reinsurance.

Liquor liability is specifically excluded in the Company's August 15, 2008 excess reinsurance treaty in effect until February 15, 2009. The Company, however, wrote excess policies prior to February 15, 2009 that included liquor law liability coverage.

The Company wrote a policy for one policyholder with multiple locations with limits of $10 million each occurrence, and $10 million general aggregate. The Company also wrote a policy with limits of $2 million each occurrence, and $20 million general aggregate. These policies contained overall aggregates that exceeded the reinsurance limits.

In response to the Department's finding, the Company again asserts that Collins Consulting is unqualified to make this determination. The Company also relies on the assertion that its reinsurers believes the Company to be in compliance with the terms of its reinsurance treaty. The Department hereby incorporates its response to the first finding of fact in support of its response to this second finding of fact.

3. The financial examination of the Company produced evidence to support the finding that the Company failed to establish and maintain adequate underwriting and claims systems. On some of the policies reviewed, the Company's computerized underwriting system produced policy limits that were different from the policy limits stated on the hard-copy policies issued by the Company. The Company also used rating classifications, rating factors, and rate limitations that were different than those set forth in the Company's underwriting manual. The Company's underwriting files failed to properly document deviations from the ratings and classifications, as required in the Company's underwriting manual.

The Department also determined that claims were paid from the Company's loss fund when in fact those claims should have been paid from the loss fund of another insurer. Also, it was noted on at least one occasion, a claim incurred by the Company was paid from the loss fund of another insurer. The Company records claims as paid when payment is requested, as opposed to when the payments are actually made. In addition, the Company's practice of initially recording loss adjustment expenses (LAE) incurred in its general accounts payable account, as opposed to an LAE account, results in the Company's inability to report claims paid or LAE incurred accurately.

The Company's response to the examination report indicates that all deviations from its underwriting manual are approved by its President or Vice President of Underwriting. However, the Company's response fails to rebut the examiner's finding that the policy limits reviewed in the Company's computerized system did not agree with policy limits found in hard copies of the same policies that were provided by the Company, its policyholders or their agents. The Company also fails to rebut the examiners finding that the Company's failed to document deviations from ratings and classifications in the Company's underwriting files. Finally, the Company does not rebut the evidence related to the payment of claims from the incorrect loss funds.

4. The financial examination of the Company produced evidence to support the finding that the Company made changes to its Business Plan without the prior written approval of, or notification to, the Department. The Company made a number of changes to base rates, rating classifications, its application of various schedule and merit credits and debits, policy forms, and limits. Specifically, the Company made the following changes to its Business Plan without the prior written approval of, or notification to, the Department:

- Amended its rates for Assault & Battery;
- Eliminated the mandatory use of deductibles and began permitting deductibles only on an exception basis;
- Added forms and amended coverages, including, per location (per event) aggregate endorsement;
- Began offering multiple location aggregate limits to certain policyholders with multiple locations; and

- Since May 2008, issued two master Tenant User Liability Insurance Policies insuring members of the International Association of Entertainment Businesses on a shared limits basis.

The Company took these actions without notification to, or approval from, the Department although the Company agreed in the 2006 Consent Agreement to use only policy forms contained in the existing approved business plan. The Company does not rebut the evidence supporting the finding that the Company changed its approved business plan without the prior written consent of, or notification to, the Department.

5. The Company's independent actuary performed an evaluation of the Company's loss and loss adjustment expense reserves on a combined basis—with the Company and its affiliate Indemnity Reinsurance Corporation of DC (IRCDC). The Company's actuary noted a reserve deficiency in the amount of $796,121, but the deficiency was not allocated between the Company and its affiliate, IRCDC. The Department's examination actuary concluded that the combined reserves of the Company and IRCDC, as of December 31, 2008, were deficient by a minimum of $1,428,000, but the examination actuary could not determine the amount of the deficiency related to each company. As a result of the Company's combined analysis, it was impossible for the examination actuary to make a determination of the Company's ultimate losses.

Also, it was determined that the Company failed to establish indemnity reserves in a timely manner. The Company's practice of not establishing indemnity reserves on a claim until it believes it is certain that indemnity payments will be made results in the slower reporting (i.e., underreporting) of losses. The examination of the Company, also disclosed that the Company's practice of reducing its loss reserves based on anticipated recoveries for salvage and subrogation without being able to provide adequate support for how it determined the value of the salvage and subrogation results in an under reporting of the Company's liabilities and an over reporting of the Company's assets.

The Company's response to the examination report indicates it hired an independent actuary to perform the actuarial analysis in accordance with National Association of Insurance Commissioners and Department standards. The Company also states that it has engaged five different actuaries through the Company's history (five years as of December 31, 2008) and all have used similar assumptions and arrived at the same methodologies. The response also states that the Company's independent auditors have not taken issue with the independent actuaries' methods. The Company not address the specific examination findings (i.e., the combined reserve analysis with IRCDC, the failure to establish reserves in a timely manner, and the lack of adequate documentation to support its salvage and subrogation values).

6 The financial examination of the Company produced evidence to support a finding that it failed to record certain transactions and failed to maintain adequate records of some transactions, including: (1) inter-company transactions; (2) stock and letter of credit transactions; (3) transactions with members of the Company; and (4) corporate matters. The examination determined that the Company failed to settle inter-company transactions in a timely manner and in accordance with inter-company agreements, and failed to maintain adequate records to support inter-company transaction balances. The examiners further determined that the Company failed to collect and record funds due it for the issuance of certain Class B shares, and failed to comply with the terms of the 2006 Consent Agreement, wherein the Company agreed to change the ownership structure of the Company. Additionally, the Company was found to have failed to properly record and report the amount of capital stock issued by the Company. During the second quarter of 2009, the Company obtained a letter of credit in the amount of $47 million, which expired on December 31, 2009. The Company, however, did not record the letter of credit on its June 30, 2009 quarterly financial statement. The Department informed the Company of this oversight and the Company re-filed the second quarterly financial statement to include the letter of credit, but subsequently re-filed its second quarterly statement a second time removing of the letter of credit from that financial statement. The Company also failed to record the letter of credit on its September 30, 2009 quarterly financial statement. The Company collects membership fees from its insureds, which are required to be remitted to IAEB Association. However, the Company retained the membership fees and recorded them as part of premiums collected from the insureds. The examiners also found that the Company's board of directors failed to meet annually in the District of Columbia, and the board failed to discuss, approve, and record significant Company transactions and events.

The Company, in its response to the examination report, does not rebut the evidence supporting the finding that the Company failed to maintain records, record, and settle transactions pursuant its inter-company agreements, or properly record transactions related to its letter of credit, Class B Shares, and members. The Company, however, asserts that its board of directors has always met at least annually in the District with a quorum of directors present, but the Company was unable to provide documentation or other evidence of the annual meetings when asked for the information during the examination. The Company's response indicates that it will keep minutes detailing who attended the meetings and the matters discussed.

CONCLUSIONS OF LAW

1. The Company violated D.C. Official Code § 31-3931.15(a) (1) and (7) by writing policies in excess of limits approved by the Department.

2. The Company violated D.C. Official Code § 31-3931.15(a)(1) and (7) by failing to maintain reinsurance coverage on certain policies.

3. The Company violated D.C. Official Code § 31-3931.15(a) (7) by failing to establish and maintain adequate underwriting and claims systems.

4. The Company violated D.C. Official Code § 31-3931.15(a)(1) and (7) by making changes to its business plan without the prior written approval of the Commissioner.

5. The Company violated D.C. Official Code § 31-3931.15(a)(7) by engaging in reserving policies and practices that are inadequate and unreliable.

6. The Company violated D.C. Official Code § 31-3931.15(a)(7) by failing to maintain adequate records and to record transactions including: (1) inter-company transactions; (2) stock and letter of credit transactions; (3) transactions with members of the Company; and (4) corporate matters.

ORDER

An Examination of **Indemnity Insurance Corporation of DC, Risk Retention Group,** as of December 31, 2008, has been conducted by the District of Columbia Department of Insurance, Securities and Banking.

It is hereby **ORDERED** on this 20th day of August, 2010, that the attached financial condition examination report be adopted and filed as an official record of this Department.

In addition, it is hereby **ORDERED** that the Company comply with the recommendations contained in the attached financial condition examination report.

Pursuant to Section 31-1404(d)(1) of the D.C. Official Code, this Order is considered a final administrative decision and may be appealed pursuant to Section 31-4332 of the D.C. Official Code.

Pursuant to Section 31-1404(d)(1) of the D.C. Official Code, within 30 days of the issuance of the adopted report, the company shall file affidavits executed by each of its directors stating under oath that they have received a copy of the adopted report and related order.

Pursuant to Section 31-1404(e)(1) of the D.C. Official Code, the Department will continue to hold the content of the report as private and confidential information for a period of 10 days from the date of this Order.

Gennet Purcell
Commissioner

Government of the District of Columbia
Department of Insurance, Securities and Banking

Gennet Purcell
Commissioner

May 28, 2010

Jeffrey B. Cohen
President
Indemnity Insurance Corporation of DC, Risk Retention Group
C/o Lawrence Stern, Director, Baker & Daniels Group
1050 K Street, N.W., Suite 400
Washington, DC 20001

Dear Mr. Cohen:

Pursuant to the provisions of Section 31-1404 of the D.C. Official Code, enclosed is a draft copy of the Report on Examination ("Report") of the affairs and financial condition of **Indemnity Insurance Corporation of DC, Risk Retention Group**, as of December 31, 2008.

Please submit, to my attention, a written response calling attention to any errors or omissions in the draft Report. In addition, the Company's response shall include responses to each of the recommendations included in the "Comments and Recommendations" section of this Report. These responses should indicate the Company's agreement or disagreement with each recommendation, as well as a summary of the corrective measures which will be taken by the Company for each recommendation. If the Company disagrees with any of these recommendations, the response shall indicate the reason(s) for the disagreement, as well as an explanation of alternative measures to be taken by the Company to address the conditions which lead to the recommendations.

The response must be in writing and shall be furnished to this Department by June 25, 2010**.** In addition to a hard-copy response, please also furnish the response electronically via e-mail to me, in a Microsoft "Word" format, to sean.odonnell@dc.gov.

Sincerely,

Sean O'Donnell

Sean O'Donnell
Director of Financial Examination,
Risk Finance Bureau

Enclosure

Indemnity

Corporation Of DC

A.M. BEST

RECEIVED

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INSURANCE
URITIES AND BANKING

Monday, June 28, 2010

BY EMAIL AND OVERNIGHT DELIVERY

Honorable Gennet Purcell
Commissioner
Department of Insurance, Securities and Banking
Government of the District of Columbia
810 First Street, NE, Suite 701
Washington, D.C. 20002

Dear Madam Commissioner:

Pursuant to D.C. Code section 31-1404(b) and 31-3931.14, Indemnity Insurance Corporation of DC, Risk Retention Group, Inc. (referred to as "IICDC"), hereby submit their response to the report of financial condition and activities for the period of June 17, 2004 through December 31, 2008 (referred to as "Exam"), which was provided to IICDC on June 25, 2010.

The General Soundness of the Financial Position of IICDC

As previously documented within the prior examination conducted on October 24, 2005 and again documented within this Exam, the Examiners failed to discover any material misstatements, changes to surplus or any other material financial adjustments.

Examiner Unprofessional Conduct

Collins Consulting, Inc. (referred to as "Examiner") was the examining firm engaged to conduct this Exam; the Examiner-In-Charge (referred to as "EIC") and principal of the firm is Pamela C. Woodroffe.

[redacted]

The EIC further provided a biased, dishonest and subjectively opinioned based report that contradicts the established NAIC examination guidelines. A formal grievance to be filed with the exam standards group of the NAIC is being considered.

950 Ridgebrook Road, Suite 1500 • Sparks, MD 21152 • Ph 410.472.6000 • Fax 410.472.6020
www.IICDC.com

Responses to Specific Findings

The following comments are identified based on the summarized topic contained within the "Comments and Recommendations" section of the Exam Report.

1. Policies Written in Excess of Limits Approved by the Department

Per the NAIC Financial Condition Examiner Handbook (referred to as "FCEH"), the examiner is to use professional judgement to assess the inherent risk of the identified activity by determining the likelihood of occurrence and magnitude of the impact or impairment to surplus. The examiner utilized a self review of the reinsurance treaties of IICDC to determine if, in their sole opinion, that policies written by IICDC were not covered by the reinsurance.

The EIC is not a qualified expert to ascertain whether coverage exists under any form of insurance contract and does not have relevant U.S. judicial experience to provide evidence of the technical expertise needed to opine on coverage related matters. The EIC was informed by the Company's reinsurer that the specific risks identified within the exam were covered by IICDC reinsurance treaties. IICDC reinsurer has an intimate knowledge of the operations as conducted by IICDC, including all classes of business and policy forms. In addition, IICDC reinsurer has conducted an exhaustive underwriting and claims audit of IICDC; in which the reinsurer concluded that IICDC is not engaged in any business that would fall outside of the scope of the reinsurance coverage.

A copy of the finalized applicable reinsurance endorsement was provided to the Department in May 2010. The finalized reinsurance endorsement addressed all deficiencies; all policies written by IICDC will be covered under its reinsurance program and will contain limits as approved by the Department.

2. Executed Treaties

IICDC will work with its vendors to ensure prompt delivery to the Department of all reinsurance documents.

3. Data Processing Controls and Integrity of Data

Underwriting: IICDC will perform a review of its underwriting and policy issuance controls, identify and correct any discrepancies found and provide a report summarizing the findings to the Department by September 1, 2010.

Claims: A process to ensure appropriate claim payments and the proper recordation of claim expenses is already in place.

Actuarial Opinion: IICDC refutes the finding depicted within the Exam. IICDC has and continues to maintain clear and verifiable records to support the salvage and subrogation amounts receivable and collected. The amounts are recorded in separate general ledger accounts, are updated quarterly, and are reported within the Annual Statements as filed with the Department. IICDC is not able to dictate to an independent actuary how to perform their independent duty; IICDC will request that the independent actuary provide better documentation.

Deductible Receivables: IICDC refutes the finding depicted within the Exam. If there were any outstanding requests the examiner would have alerted IICDC regarding same; no communication exists to evidence a repeated request for an item. Outstanding deductible(s) were sent to the EIC via email on 11/5. There was only 1 deductible in the amount of $390. The remaining amount resulted from an improper journal entry that IICDC's outsourced CFO (SMART Consulting) had done back in 2006/2007 (amount of this was $23k—this amount was written off in 2009) The Examiner (John) requested the same information on 11/19 for which IICDC forwarded the same email that had been sent previously. An additional request by the Examiner (John) requested a listing of deductibles that had been written off during 2008. IICDC provided him this list (only 2 deductibles) on 11/19 via email. The amount in question does not meet the materiality standard developed within this exam

4. **Underwriting**

IICDC refutes the finding depicted within the Exam. All deviations from the underwriting manual have been approved by either the President or the Vice President of Underwriting. The Examiner fails to disclose that ALL underwriting is performed by either the President or Vice President. IICDC will submit a comprehensive update to its business plan on file with the Department before September 1, 2010.

5. **Eligibility Requirements for Deductibles**

IICDC has and continues to maintain accurate records of all deductible compliance issues.

6. **Changes in Business Plan**

All changes to the IICDC business plan that require notice and/or approval of the Department will be submitted for appropriate consideration prior to implementation. IICDC will submit a comprehensive update to its business plan on file with the Department before September 1, 2010.

7. **Actuarial Review**

All actuarial analyses require the actuary to make educated assumptions of unknown items. In turn, actuaries go through extensive training and must pass many levels of exams before becoming certified. IICDC hired an INDEPENDENT actuary according to NAIC and DISB standards; based on her training and expertise, the actuary made determinations of the indicated reserve. The determination made differs from the examiner that was hired for the exam. A sole determination of methodology cannot be established as the claims have not all been closed; however, the actuary that IICDC hired does have more experience with IICDC's data and operations, as she has been involved in interim analysis as well as met with management of IICDC numerous times to discuss and learn about the claims and reserving processes. For the Examiner to include comments and make assertions that IICDC's independent actuary is not performing properly and not working within the Department's mandated scope of services is simply inappropriate and unfounded.

It is worth noting that IICDC has engaged 5 different independent actuaries throughout IICDC's history and ALL of the independent actuaries have used similar assumptions and ALL have arrived at the same methodologies. In addition, per the regulations of NAIC and the Department, an independent auditor reviews all workpapers and methodologies of the independent actuaries and to date, none of the independent auditors have disagreed or differed in the opinions and methods used by the independent actuaries

a) IICDC currently utilizes the higher of the range as specified
b) IICDC currently recognizes any reserve deficiency in the period in which it is identified
c) IICDC is not able to dictate to an independent actuary how to perform their independent duty; IICDC will recommend this to its independent actuary
d) IICDC is not able to dictate to an independent actuary how to perform their independent duty; IICDC will recommend this to its independent actuary
e) IICDC is not able to dictate to an independent actuary how to perform their independent duty; IICDC will recommend this to its independent actuary
f) IICDC is not able to dictate to an independent actuary how to perform their independent duty; IICDC will recommend this to its independent actuary

g) IICDC has and continues to record a ULAE reserve
h) IICDC is not able to dictate to an independent actuary how to perform their independent duty; IICDC will recommend this to its independent actuary

8. **Intercompany Transactions**

IICDC will settle balances between related parties on a timely basis and retain appropriate supporting documentation for future verification. IICDC has and will continue to maintain detailed records of its premiums due.

9. **Common Capital Stock**

IICDC will complete and properly document the transaction to effect the ownership split between IAEB & RB. IICDC will maintain the required amount of capital stock and record all of the stock transactions within its stock ledger.

10. **Letter of Credit**

IICDC has and continues to reflect all assets, liabilities, and other amounts in its financial statements.

11. **Membership**

IICDC is no longer receiving membership dues. IICDC's MGA is collecting all membership dues and remitting to IAEB.

12. **Maintenance of Corporate Records**

IICDC has and continues to physically meet with a quorum of directors present, at least one time each year in the District. In the future, the minutes of the meetings will be specifically detailed to represent who attended and what was discussed.

13. **Service Providers and Other Agreements**

All current service provider agreements will be updated with the revised business plan submission scheduled for September 1, 2010.

Sincerely,

Jeffrey Cohen
President

Cc: Lawrence Stern
Sean O'Donnell

Government of the District of Columbia
Department of Insurance, Securities and Banking

Gennet Purcell
Commissioner

August 24, 2010

Jeffrey B. Cohen
President
Indemnity Insurance Corporation of DC, Risk Retention Group
C/o Lawrence Stern, Director, Baker & Daniels Group
1050 K Street, N.W., Suite 400
Washington, DC 20001

Dear Mr. Cohen:

We are in receipt of your response, dated June 28, 2010, regarding the Report on Examination of **Indemnity Insurance Corporation of DC, Risk Retention Group** ("Company"), as of December 31, 2008. Except for the following, the response is deemed adequate.

Excerpt from June 28, 2010 Company Response:

Examiner Unprofessional Conduct

Collins Consulting, Inc. (referred to as "Examiner") was the examining firm engaged to conduct this Exam; the Examiner-In-Charge (referred to as "EIC") and principal of the firm is Pamela C. Woodroffe.

The EIC further provided a biased, dishonest and subjectively opinioned based report that contradicts the established NAIC examination guidelines. A formal grievance to be filed with the exam standards group of the NAIC is being considered.

Department Response to the Company's Response:

A portion of the response is inappropriate and has been redacted.

The EIC submitted a draft examination report to the Department based upon the examination procedures performed under the direction and supervision of the Department. This draft report was then edited by Department personnel. The report is based upon and is supported by the examination procedures performed and the examination work papers, including documents provided by the Company.

As previously communicated to the Company, the Department conducts its exams in accordance with the guidelines in the 2006 NAIC Financial Condition Examiners Handbook.

Examination Recommendation: Policies Written in Excess of Limits Approved by the Department:

We again recommended that the Company only write policies with limits as approved by the Department.

Examination Recommendation: Reinsurance:

We recommended that the Company finalize the endorsements to its reinsurance treaties, ensuring all identified deficiencies have been addressed, and ensuring all policies written by the Company are covered by the reinsurance program in accordance with the approved business plan. The fully executed endorsements should be forwarded to the Department by July 31, 2010.

In addition, we recommend that the Company ensure that all polices written are covered at all times by the Company's reinsurance program, in accordance with the Company's approved business plan.

Company Response to the Above Recommendations:

Per the NAIC Financial Condition Examiner Handbook (referred to as "FCEH"), the examiner is to use professional judgement (sic) to assess the inherent risk of the identified activity by determining the likelihood of occurrence and magnitude of the impact or impairment to surplus. The examiner utilized a self review of the reinsurance treaties of IICDC to determine if, in their sole opinion, that policies written by IICDC were not covered by the reinsurance.

The EIC is not a qualified expert to ascertain whether coverage exists under any form of insurance contract and does not have relevant U.S. judicial experience to provide evidence of the technical expertise needed to opine on coverage related matters. The EIC was informed by the Company's reinsurer that the specific risks identified within the exam were covered by IICDC reinsurance treaties. IICDC reinsurer has an intimate knowledge of the operations as conducted by IICDC, including all classes of business and policy forms. In addition, IICDC reinsurer has conducted an exhaustive underwriting and claims audit of IICDC; in which the reinsurer concluded that IICDC is not engaged in any business that would fall outside of the scope of the reinsurance coverage.

A copy of the finalized applicable reinsurance endorsement was provided to the Department in May 2010. The finalized reinsurance endorsement addressed all deficiencies; all policies written by IICDC will be covered under its reinsurance program and will contain limits as approved by the Department.

Department Response to the Company's Response:

Policies Written in Excess of Limits Approved by the Department:

As previously noted, the Department conducts its exams in accordance with the guidelines in the 2006 NAIC Financial Condition Examiners Handbook. In addition, the Department conducts its examinations using personnel with appropriate background, qualifications, skills and experience.

As indicated in our report, the Company wrote policies at limits in excess of the maximum limits approved by the Department. The Company's response did not address this point. As recommended in the report, the Company shall only write policies with limits as approved by the Department.

Reinsurance:

The Department has not received copies of the final, fully executed endorsements to its reinsurance treaties. The fully executed endorsements shall be forwarded to the Department by September 1, 2010.

Examination Recommendation: Data Processing Controls and Integrity of Data:

2. **Claims:**

C. We recommended that the Company maintain clear and verifiable records and supporting documentation of its salvage and subrogation amounts receivable and collected. These amounts should be recorded in separate general ledger accounts, and should be reported in the Company's Annual Statements as filed with the Department. The Company should ensure reserves are only reduced for anticipated salvage and subrogation amounts that are supported. In addition, the Company should ensure its actuary discloses, in the actuarial opinion and/or supporting report, the specific dollar amount of any reduction to the Company's loss reserves for estimated recoveries for salvage and subrogation.

Company Response to the Above Recommendation:

IICDC refutes the finding depicted within the Exam. IICDC has and continues to maintain clear and verifiable records to support the salvage and subrogation amounts receivable and collected. The amounts are recorded in separate general ledger accounts, are updated quarterly, and are reported within the Annual Statements as filed with the Department. IICDC is not able to dictate to an independent actuary how to perform their independent duty; IICDC will request that the independent actuary provide better documentation.

Department Response to the Company's Response:

As indicated in the report, sufficient documentation of salvage and subrogation was not available during the examination. In addition, neither salvage and subrogation receivable, or paid, was reported in the Company's 2008 Annual Statement (Schedule P).

Examination Recommendation: Underwriting:

1. **Use of Rates Outside of Underwriting Guidelines:**

We recommended the Company ensure that all rating classifications, factors and limitations are included in the underwriting manual and all premiums should be calculated using such

rates. All rating classifications, factors and limitations should be clearly documented in the underwriting files and of approval of any deviations should be clearly documented in the underwriting files.

Company Response to the Above Recommendation:

IICDC refutes the finding depicted within the Exam. All deviations from the underwriting manual have been approved by either the President or the Vice President of Underwriting. The Examiner fails to disclose that ALL underwriting is performed by either the President or Vice President. IICDC will submit a comprehensive update to its business plan on file with the Department before September 1, 2010.

Department Response to the Company's Response:

As indicated in the examination report, approval of any deviations should be clearly documented in the underwriting files.

Examination Recommendation: Maintenance of Corporate Records:

2. **We recommended that corporate documents such as bylaws be maintained up to date, and submitted to the Department promptly when changes are made.**

Company Response to the Above Recommendation:

The Company's response did not address this recommendation.

Department Response to the Company's Response:

As recommended in the examination report, all corporate documents such as bylaws shall be maintained up to date, and submitted to the Department promptly when changes are made. The Company shall submit updated bylaws to the Department by September 1, 2010.

The adopted Report (which includes a copy of this letter), and the Order evidencing such adoption are enclosed. Pursuant to Section 31-1404(e)(1) of the D.C. Official Code, the adopted Report will be held private and confidential for a period of 10 days from the date of the Order evidencing such adoption. After this 10 day period has passed, the Report will be publicly available. The Department of Insurance, Securities and Banking will forward the adopted Report electronically to each Commissioner whose name is set forth on Page 1 of the Report, as well as to the National Association of Insurance Commissioners.

Pursuant to Section 31-1404(d)(1) of the D.C. Official Code, within 30 days of the date of the above-mentioned Order, affidavits executed by each Company director stating under oath that he or she has received a copy of the adopted examination Report and related Order shall be filed with this Department. Please send these affidavits to my attention at the Department.

Please contact me at 202-535-1169 if you have any questions.

Sincerely,

Sean O'Donell

Sean O'Donnell
Director of Financial Examination
Risk Finance Bureau

Enclosures