



110

October 6, 2014

James R. Potts, Esq.  
Cozen O'Connor  
1900 Market Street  
Philadelphia, PA 19103

Re: Application of Armour Group Holdings Limited for Approval of Acquisition of Control of OneBeacon Insurance Company, Potomac Insurance Company, One Beacon America Insurance Company, and The Employers' Fire Insurance Company

Dear Mr. Potts:

The Pennsylvania Insurance Department ("the Department") is continuing its review of documents filed in connection with the above-referenced Form A. As part of this ongoing review, the Department has compiled below a list of areas with respect to which it seeks clarification and/or additional information. These are prompted in part by the Department's ongoing review of the Stock Purchase Agreement ("SPA"), related documents, and amendments to those documents, and in part by the Department's preliminary review of the transcript of the July 23, 2014 public informational hearing, comments submitted by the public before and during the hearing and the post-hearing responses submitted by Armour Group Holdings Limited ("Armour") and OneBeacon Insurance Group, Ltd. ("OBIG") and by Towers Watson on August 12, 2014.

When preparing your response, please reference the number of the Department's request to which you are responding. Your responses and any documents that you attach will become part of the public files, unless you expressly assert the confidentiality of specifically identified information and the Department agrees such information is confidential.

1. The Department understands that Towers Watson will use paid and case incurred data through June 30, 2014 to roll forward the nominal reserve ranges and the payment forecast from the Analysis of Unpaid Loss and LAE as of September 30, 2012, December 31, 2012, and March 31, 2013, which is dated September 9, 2013. As part of this roll forward, Towers Watson also will provide qualitative analyses of the potential impact of recent data on the stochastic model and the impact of any significant claim developments. Please also provide a comparison analysis and demonstrate how Towers Watson's A & E models have been updated during this time. The Department further understands that re-estimation and update will be completed and delivered to the Department no later than mid-October. If this timing changes, or if the Department's understanding of the roll forward is not correct, please provide prompt notice to the Department.

19

2. In June, Armour representatives informed the Department that Armour would submit to the Department a copy of the proposed Purchaser Intercompany Agreement (as defined in the SPA), along with a detailed explanation as to why the agreement, including the fees set forth therein, is fair and reasonable. Please provide a copy of this agreement and explanation without further delay.

3. During the public informational hearing, Armour was asked specific questions regarding its expected cost savings. In the August 12, 2014 submission, Armour provided some general examples of expected cost savings. The Department seeks more detail as to these examples, and inquires whether other cost savings are anticipated. Please provide the analysis underlying the statement that Armour expects its cost savings to be 50% or more when compared to the legacy systems, initially up to \$1.5 million annually, with more savings potentially realizable in the future. In this regard, please also provide, if possible, specific examples from Armour's experience with Excalibur.

4. During the public informational hearing, Armour was asked to provide support for the statement that Armour has access to different kinds of capital. Please provide a response, with supporting documentation.

5. The Department observes that under Section 6 of SPA Amendment 3, subject to required regulatory approvals, Armour may elect to have One Beacon America Insurance Company prepay all or some of the surplus notes "in connection with OneBeacon Insurance entering into one or more reinsurance agreements to provide surplus relief to replace some or all of surplus represented by the Surplus Notes." Please explain what, if anything, the parties are contemplating under this provision and what impact such a transaction might have on each of the target domestic insurers.

6. The Department also observes that the Amended Retained Business Reinsurance Agreement (Amended SPA Exhibit 3) and the Amended Run-off Business Reinsurance Agreement (Amended SPA Exhibit 6) each changed the definition of "Policy" (i.e., the Policies being reinsured under the reinsurance agreement). Under the amended definition, it appears that the term Policy now include policies issued by the cedent and all reinsurance contracts under which the subject type of business is assumed by the cedent through the closing date of the transactions contemplated by the SPA. Please consider amending the language to clarify that there will be no business covered by either reinsurance agreement that has not been accounted for in the Towers Watson modeling.

7. Please explain why net loss reserves are projected to decrease by 61% by December 2017, but cash and investment assets are projected to decrease by 39% by that same time.

8. Towers Watson's August 12, 2014 response referenced an analysis of uncollectible reinsurance it had conducted in connection with its work. Please provide this analysis to RRC for RRC's review. In addition, to the extent an analysis of ceded reinsurance was conducted, please provide that analysis.

9. The Department understands that Towers Watson made several adjustments to its proprietary Economic Scenario Generator in the area of asset yield assumptions based on a consultation with Towers Watson's investment consulting group. Please provide additional information about this investment consulting group, including the group's analysis, what recommendations it made, what recommendations were accepted, and what recommendations, if any, were rejected.

10. Towers Watson made the following statement on page 12 of its August 12, 2014 response: "We also note that severity inflation by disease has been benign in recent years." Please provide statistical support for that statement.

11. Please explain why OBIG's reserves shown on its proposed consolidated closing date balance sheet are lower than the central estimate used by Towers Watson in its stochastic model.

12. Please confirm that Towers Watson did not use deferred tax assets in its stochastic model and that any deferred tax assets will not have any impact on the model.

13. Some commenters were concerned that the definition of "failure" is too narrow. Although the Department believes the definition of failure is appropriate, it would be valuable to see an analysis using alternative definitions. For example, if projected loss reserves for the current runoff business were substituted for paid claims in the stochastic model, in what percentage of the cases – measured at various points in time – does the model project that assets will be inadequate to cover those reserves? Additional alternative definitions of failure could also be considered (e.g., a specific level of surplus).

The Department reserves the right to request additional clarification or information and documentation on anything relevant to the Form A application, including your responses to this letter. These requests are continuing requests, and the Applicant should promptly update its responses as soon as new information becomes available. In addition, please be aware that the Department's review of the existing record is ongoing, and there may be additional comments or questions. Feel free to contact the Department for clarification of any of the requests made above.

Sincerely,



Stephen J. Johnson, CPA  
Deputy Insurance Commissioner  
Office of Corporate and Financial Regulation