Examination Warrant Number 14-00313-33898-R1

Report of Examination of

Aegis Security Insurance Company
Harrisburg, Pennsylvania

As of December 31, 2014

Aegis Security Insurance Company

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Harrisburg, Pennsylvania
January 22, 2016

Honorable Joseph DiMemmo, CPA
Deputy Insurance Commissioner
Commonwealth of Pennsylvania
Insurance Department
Harrisburg, Pennsylvania

Dear Sir:

In accordance with instructions contained in Examination Warrant Number 14-00313-33898-R1, dated, March 25, 2014, an examination was made of

Aegis Security Insurance Company, NAIC Code: 33898

a Pennsylvania domiciled multi-state property and casualty insurance company, hereinafter referred to as "Company" or "ASIC." The examination was conducted at the Company's home office, located at 2407 Park Drive, Suite 200, Harrisburg, Pennsylvania 17110.

A report of this examination is hereby respectfully submitted.

SCOPE OF EXAMINATION

The Pennsylvania Insurance Department ("Department") has performed our examination of the Company, which was last examined as of December 31, 2009.

This examination covered the five-year period from January 1, 2010 through December 31, 2014.

Work programs employed in the performance of this examination were designed to comply with the standards promulgated by the Pennsylvania Insurance Department and the National Association of Insurance Commissioners ("NAIC") *Financial Condition Examiners Handbook* ("Handbook").

The Handbook requires that the Department plan and perform the examination to evaluate the financial condition, assess corporate governance, identify current and prospective risks of the Company, evaluate system controls and procedures used to mitigate those risks, and review subsequent events. An examination also includes identifying and evaluating significant risks that could cause an insurer's surplus to be materially misstated both currently and prospectively.

All accounts and activities of the Company were considered in accordance with the risk-focused examination process. This may include assessing significant estimates made by management and evaluating management's compliance with statutory accounting principles.

The examination does not attest to the fair presentation of the financial statements included herein. If, during the course of the examination an adjustment is identified, the impact of such adjustment will be documented separately following the Company's financial statements.

This examination report includes significant findings of fact, in accordance with

40 P.S. § 323.5(a), and general information about the Company and its financial condition. There may be other items identified during the examination that, due to their nature (e.g., subjective conclusions, proprietary information, etc.), are not included within the examination report but separately communicated to other regulators and/or the Company.

For 2010 through 2012, the certified public accounting ("CPA") firm of Brown Schultz Sheridan & Fritz provided an unqualified audit opinion on the Company's year-end financial statements based on statutory accounting principles. For 2013 and 2014, the CPA firm of Johnson Lambert LLP ("JL") provided an unqualified audit opinion on the Company's year-end financial statements based on statutory accounting principles. Relevant work performed by JL, during its annual audit of the Company, was reviewed during the examination and incorporated into the examination workpapers.

The following company was examined at the same time during the above examination:

Company	NAIC Code
American Sentinel Insurance Company (Pennsylvania)	17965

HISTORY

The Company was incorporated on May 25, 1977, licensed by the Department on August 4, 1977, and commenced business on the same date.

On February 16, 2010, the Department approved an amendment to the Company's Articles of Incorporation increasing the number of authorized shares of common stock from 3.0 million to 5.0 million and increasing the par value from $1.00 to $1.40.

There were no changes to the Company's By-laws during the examination period. The Company's By-laws were amended and restated subsequent to the examination period.

The Company is currently authorized to transact those classes of insurance described in 40 P.S. § 382, (b)(1) Fire and Allied Lines, (b)(2) Inland Marine and Auto Physical Damage, (b)(3) Ocean Marine, (c)(1) Fidelity and Surety, (c)(2) Accident and Health, (c)(3) Glass, (c)(4) Other Liability, (c)(5) Boiler and Machinery, (c)(6) Burglary and Theft, (c)(8) Water Damage, (c)(9) Elevator, (c)(11) Auto Liability, and (c)(13) Personal Property Floater.

MANAGEMENT AND CONTROL

CAPITALIZATION

As of the examination date, December 31, 2014, the Company's total capital was $52,596,272, consisting of 3,000,000 capital shares of issued and outstanding common stock with a par value of $1.40 per share amounting to $4,200,000; $5,266,827 in paid in and contributed surplus; and $43,129,445 in unassigned funds (surplus).

The Company reported $1,218,929 for electronic data processing and software on the December 31, 2014 annual statement as an admitted asset. This was attributed to development costs associated with the new policy and claims platform being developed for Aegis Security

Insurance Company, American Sentinel Insurance Company, and Aegis General Insurance Agency. Subsequent to filing the annual statement, the Company determined this type of software was not operating software and did not meet the admissibility requirements of SSAP 16R. It was decided to have Aegis General Insurance Agency reimburse the Company 100.0% of the costs, which was done in the first quarter of 2015. This change was reported on the March 31, 2015 filed quarterly statement in Note 2 – Accounting Changes and Corrections of Errors.

The Company's total capital at December 31, 2014, following the correction of the admitted asset error, was $53,400,765, consisting of 3,000,000 capital shares of issued and outstanding common stock with a par value of $1.40 per share amounting to $4,200,000; $5,266,827 in paid in and contributed surplus; and $43,933,938 in unassigned funds (surplus).

The Company's minimum capital and minimum surplus requirements for the types of business for which it is licensed, pursuant to 40 P.S. § 386, is $1,500,000 in capital and $750,000 in surplus. The Company has met all governing requirements throughout the examination period.

The Company's shares of issued and outstanding common stock are pledged to M&T Bank for lines of credit totaling $17.5 million on behalf of Aegis Security, Inc. and K2 Insurance Services, LLC.

SHAREHOLDER

All shares of ASIC common stock are owned by its parent, Aegis Security, Inc. ("ASI"), a holding company organized in 1977. ASI was acquired by K2 Insurance Services, LLC ("K2") effective April 15, 2013.

The Company paid $11,700,000 of ordinary dividends to its sole shareholder, ASI, for the period under examination. Dividends were paid as shown below:

2014	2013	2012	2011	2010
$1,000,000	$2,000,000	$3,500,000	$2,800,000	$2,400,000

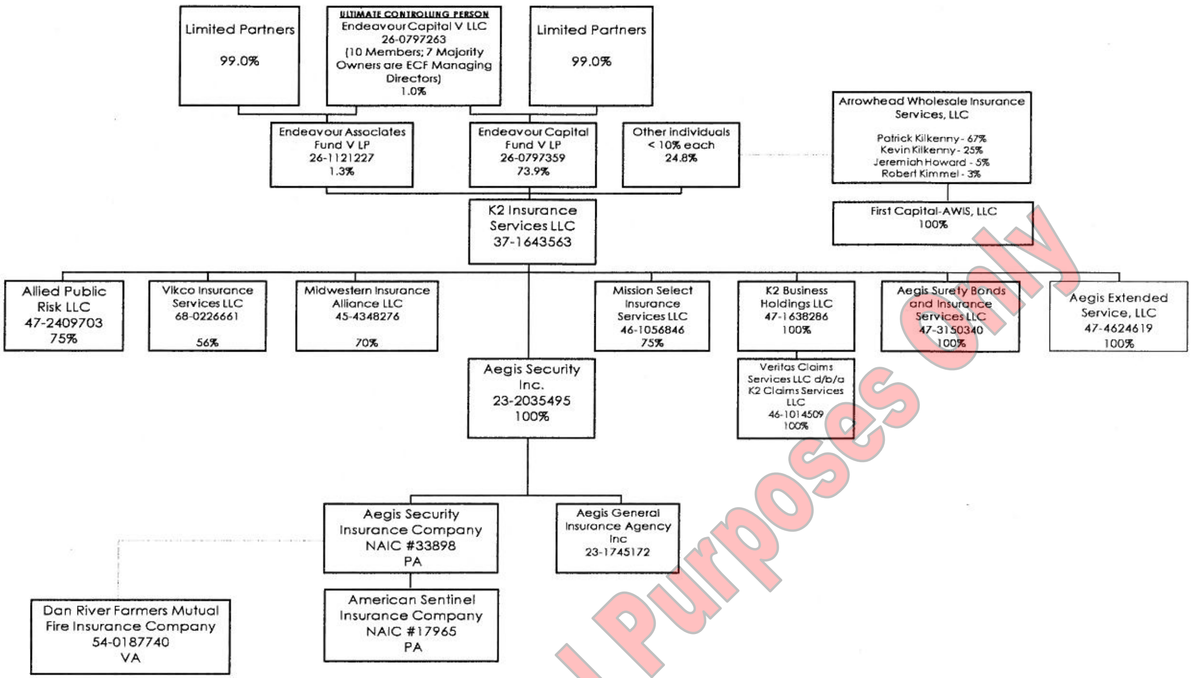
The Company provided notice to the Department for all dividends in accordance with 40 P.S. § 991.1404. No extraordinary dividends requiring authorization were paid during the examination period.

INSURANCE HOLDING COMPANY SYSTEM

The Company meets the requirements for filing an Insurance Holding Company System Registration Statement, in compliance with the 40 P.S. §§ 991.1401 - 991.1413. The Company has filed the required insurance holding company system registration statements for all years under examination.

Endeavour Capital Fund V, LLC is named as the Ultimate Controlling Person ("UCP") in the system as of April 15, 2013. Martin G. Lane, Jr. had been the UCP prior to the K2 acquisition date.

An organizational chart of the insurance holding company System at December 31, 2015, is as follows:



FOOTNOTES:

(1) Dan River Farmers Mutual Fire Insurance Company is managed by Aegis Security Insurance Company. Aegis has no ownership interest.

(2) One individual that owns less than 10% of K2 also has a controlling interest in Arrowhead Wholesale Insurance Services LLC

Members of the insurance holding company system include the following entities briefly described below:

K2 Insurance Services, LLC

K2, founded by Patrick Kilkenny and Robert Kimmel in 2011 with the goal of creating a leading specialty insurance services company through acquisitions that generate diverse earning streams and improve distribution economics, is located in Solana Beach, California. K2 owns 100.0% of ASI stock and is the ultimate parent of the affiliated entities. Endeavour Capital Fund V, LP and Endeavor Associates Fund V, LP hold approximately 73.9% and 1.3%, respectively, of the K2 stock. Endeavour Capital Fund V, LP and Endeavor Associates Fund V, LP are ultimately controlled by Endeavour Capital Fund V, LLC. Endeavour Capital Fund V, LLC is comprised of 10 members with 7 majority owners being the Endeavour Capital Fund managing directors.

At December 31, 2014, Endeavour Capital Fund V, LP and Endeavour Associates Fund V held 75.2% of the K2 stock. The remaining stock was held by Patrick J. Kilkenny (9.6%), Martin G. Lane, Jr. (9.6%), and other individuals and entities (5.6%).

Endeavour Capital Fund V, LLC is required to file as UCP annually.

K2 provides overall leadership and strategic guidance for the affiliates. K2 executive management includes:

Patrick J. Kilkenny, CEO

Robert J. Kimmel, President

Matthew T. LuBien, COO

Nathan D. Hunter, CFO

Aegis Security, Inc.

ASI is an insurance holding company organized in 1977 pursuant to the laws of the Commonwealth of Pennsylvania, with its principal place of business in Harrisburg, Pennsylvania. ASI is the sole shareholder of the Company. Effective April 15, 2013, ASI was acquired by K2.

ASI provides a financial guarantee, through the pledge of ASIC and Aegis General Insurance Agency stock, on the combined debt facility structured as two lines of credit with M&T Bank, one in the amount of $7.5 million for K2 and one in the amount of $10.0 million for ASI.

Lakeside Insurance Company became a wholly owned subsidiary of ASI through the exchange of stock involving minority ownership of Cabrillo Pacific Insurance Agency and Tidewater Pacific Insurance Adjusters. Lakeside Insurance Company was liquidated in 2014.

Aegis Insurance Group ("Group")

The Group is comprised of ASIC, American Sentinel Insurance Company ("AMS"), and Aegis General Insurance Agency ("AGIA") (formerly Mobile-Rec, Inc. ("Mobile-Rec")). The Group specializes in insurance for manufactured homes, other low-value dwellings and motorcycles. The insurance companies underwrite surety bonds, accident and health products and other niche business. The main office is located in Harrisburg, Pennsylvania with remote offices located in Syracuse, New York and Wayne, Pennsylvania as of December 31, 2014.

The Group and K2 operate under a written management services agreement effective May 1, 2013. K2 provides oversight of business operations, including investment advice, property and casualty rate and form development, business development, and overall operational guidance and management in exchange for a monthly fee from the Company and AMS.

For the year ended December 31, 2014, the amount paid by the Company and AMS to K2 under the management agreement was $1,800,000 and $600,000, respectively.

Aegis Security Insurance Company

The Company is a domestic stock property and casualty insurance company wholly-owned by ASI. The Company specializes in manufactured home and low value dwelling products. Additionally, the Company underwrites contract and commercial surety bonds, accident and health products, difference in conditions products, and power sports and recreational vehicle products. The Company is licensed and authorized to write business in 50 states and the District of Columbia. As of December 31, 2014, the Company was writing business in all licensed states except Alaska and Hawaii.

American Sentinel Insurance Company

AMS is a domestic stock casualty insurance company wholly-owned by the Company. AMS writes accident and health products and disability products for individuals and groups.

ASIC's investment in AMS was properly reported in its December 31, 2014, Annual Statement at its statutory equity value of $15,656,804. A separate Report of Examination, as of December 31, 2014, is being issued for AMS.

AMS pays rent to the Company for space utilized in the common home office pursuant to a written rent sharing agreement.

The Company and AMS operate under an intercompany pooling reinsurance agreement ("pooling agreement") whereby the Company assumes 100.0% of AMS's net business then cedes 25.0% of the combined business back to AMS.

Aegis General Insurance Agency

AGIA, formerly known as Mobile-Rec prior to January 1, 2014, is a Pennsylvania licensed insurance agency that specializes in mobile home and recreational vehicle coverages.

AGIA is party to an agency agreement with the Company whereby the Company pays commission based on premium volume, and AGIA is eligible for contingent commissions based on specific criteria. AGIA pays rent to the Company for space utilized in the common home office pursuant to a written rent sharing agreement.

AGIA started two new divisions during 2014, **Aegis Specialty** and **Aegis Powersports**. Aegis Specialty underwrites and produces homeowners' and dwelling products in California, Oregon, Washington, Arizona and Nevada. Aegis Powersports writes extended service contracts and service maintenance agreements, primarily in the state of California. Aegis Powersports was spun off into a separate limited liability company in July 2015 known as **Aegis Extended Service, LLC.**

Effective January 1, 2016, the officers of AGIA are Patrick J. Kilkenny, Chief Executive Officer; Robert J. Kimmel, President; Matthew T. LuBien, Chief Operating Officer and Secretary; Nathan D. Hunter, Chief Financial Officer and Rebecka Kilkenny, Chief Information Officer.

Midwestern Insurance Alliance LLC ("MIA")

MIA, an agency based in Louisville, Kentucky, is 70.0% owned by K2. MIA writes workers compensation insurance on behalf of QBE Insurance Corporation ("QBE"), Praetorian Insurance Company ("Praetorian"), and North Pointe Insurance Company ("North Pointe"). Its primary insureds are commercial truckers in Kentucky, Tennessee, Louisiana, South Carolina, and Indiana. MIA also writes workers' compensation in California for a variety of businesses and writes coverage for the forestry industry through Stonewood National Insurance Company.

ASI provides a financial guarantee on behalf of MIA to M&T Bank for an Irrevocable Standby Letter of Credit, established to collateralize premium escrow funds collected on behalf of Praetorian. K2 provides a financial guarantee on behalf of MIA to M&T Bank for an Irrevocable Standby Letter of Credit, established to collateralize premium escrow funds collected on behalf of QBE, Praetorian and North Pointe. MIA is the program administrator on behalf of the workers' compensation coverage it writes through the above named carriers.

Mission Select Insurance Services LLC ("MSIS")

MIS is a start-up agency operation formed in October 2012 by K2, Dave Lacefield and Ashley Hunter. K2 owns 75.0% of the agency. This agency writes low value homeowners' coverage in Texas through National Unity Insurance Company. Effective March 2015, the agency began writing homeowners' coverage through ASIC.

Vikco Insurance Services LLC ("Vikco")

Vikco is a California based agency, acquired by K2 on July 31, 2014, that specializes in the sales and service of difference in conditions ("DIC") policies on commercial risks of approximately $20.0 million total insured value, primarily multi-family and small office or retail complexes, located in California. Perils covered include earthquake shock, flood, and earthquake sprinkler leakage with policy limits of $5.0 million on a primary, excess of loss, or quota share basis. Policy limits of up to $10.0 million are available with facultative reinsurance. The program has two predominant restrictions; no unreinforced masonry buildings and no flood coverage in specific zones. Vikco writes on behalf of two carriers, ASIC and Allied World Insurance Company ("AWIC"). K2 owns 43.75% of Vicko as of December 31, 2014.

As of March 31, 2015, K2 owns 56.0% of Vikco. The remaining ownership of Vikco is First Capital –AWIS, LLC (31.5%) and Brian Cindric (12.5%). First Capital-AWIS, LLC is discussed further below.

K2 Business Holdings, LLC

This entity was formed August 1, 2014, with its sole member being K2. The entity's sole asset is its investment in a claims adjusting company, Veritas Claims Services, LLC d/b/a K2 Claims Services, LLC.

Veritas Claims Services, LLC d/b/a K2 Claims Services, LLC

This entity, wholly owned by K2 Business Holdings, LLC and formed subsequent to the formation of K2 Business Holdings, LLC, will provide claims adjusting services on behalf of affiliated and non-affiliated carriers as a third party administrator. The target date for this entity to begin providing claims adjusting services for affiliated and non-affiliated entities is the first quarter of 2016.

Affiliates under common ownership or control

The Dan River Farmers Fire Mutual Insurance Company ("Dan River")

Dan River is a Virginia domiciled mutual assessment property and casualty insurance company. The Company provides management and administrative oversight of Dan River. The Board of Directors of Dan River is comprised of ASIC and K2 management.

First Capital-AWIS, LLC

This entity is a program administrator contracted with AGIA to administer a commercial trucking program. Arrowhead Wholesale Insurance Services ("AWIS"), owns 100.0% of First Capital-AWIS, LLC. AWIS is owned by Pat Kilkenny (67.0%), Kevin Kilkenny (25.0%), Jeremiah Howard (5.0%) and Bob Kimmel (3.0%). Jeremiah Howard is an employee of MIA.

Affiliates sold or dissolved during the examination period

JMT Property Corporation ("JMT")

JMT was a provider of transportation services. The Company had contracted with JMT for various transportation services from January 1, 2010 through the date of the acquisition by K2 on April 15, 2013. This entity was disposed of on the date of the K2 acquisition. The assets were transferred to JGS Partnership ("JGS") owned by Martin G. Lane, Jr., the prior UCP of the Company.

Mobile-Rec entered into a three-year Master Lease and Aircraft Availability Agreement with JGS for the right to use specific real estate and assets in exchange for quarterly payments totaling $6.4 million over the life of the lease. This lease terminated December 31, 2015.

Picnic Lane Holdings

This entity, an inactive yellow page directory advertising business, was dissolved December 31, 2012.

Capital Advantage Group

This entity, a real-estate development and leasing company, was dissolved December 31, 2012.

Global HR Research PA, LLC
Global HR Research NE, LLC

ASI owned the majority of the stock and voting rights of Global HR Research PA, LLC, which in turn owned the majority of the stock and voting rights of Global HR Research NE, LLC as of the prior examination. The Global HR companies provide human resource technology services, talent assessment and employee screening services. The prior UCP acquired these assets on April 15, 2013.

New entities formed subsequent to December 31, 2014

Allied Public Risk, LLC ("APR")

APR was initially formed as a division of AGIA in April 2014. January 1, 2015, APR became a limited liability company and the entire APR division was transferred to the entity. Its membership consists of K2 (75.0%) and AWIC (25.0%). Allied World Assurance Company ("AWAC"), a division of AWIC, is APR's carrier partner. The entity specializes in underwriting and distribution of public entity risks for townships, boroughs, etc., and is the program manager for AWIC's municipal package product serving populations under 100,000. Policy coverage includes property, crime, inland marine, auto liability and physical damage, general liability, cyber liability, educators' legal liability, public officials' liability, law enforcement liability, employment practices liability, umbrella liability, and following form/excess liability.

Aegis Surety Bonds and Insurance Services, LLC

This entity was formed March 1, 2015, originally as Aegis Surety, LLC with a subsequent name change. K2 owns 100.0% of its membership. The entity was formed for the purpose of underwriting and distributing contract and commercial surety products offered by ASIC and will serve as program administrator for the surety program business on behalf of ASIC. The target date for this entity to start operations is early 2016.

Aegis Extended Service, LLC

This entity, formed in July 2015, is a spin-off from AGIA and formerly known as Aegis Powersports. Aegis Extended Service, LLC provides extended service contracts to the motorcycle and all-terrain vehicle industry. Aegis Extended Service, LLC filed with the California Secretary of State as a domestic company on July 20, 2015 and with the Texas Secretary of State as a foreign limited liability company on October 13, 2015.

BOARD OF DIRECTORS

Management of the Company is vested in its Board of Directors ("Board"), which was comprised of the following members as of the examination date, December 31, 2014:

Name and Address	Principal Occupation
Patrick J. Kilkenny Del Mar, CA	Chairman of the Board K2 Insurance Services, LLC Managing Member Seaview Surety LLC
Leland M. Jones West Pasadena, CA	Managing Director DVSM LLC
William R. de Jonge New York, NY	President/Managing Director de Jonge LLC
Russell R. Kilkenny Portland, OR	Attorney Scarboro, McNeese, O'Brien & Kilkenny, P.C.
Martin G. Lane, Jr. Tavernier, FL	Former Majority Shareholder Aegis Security, Inc.
Francis E. Lauricella, Jr. San Francisco, CA	CFO/Seaview Insurance Company Managing Director/FL Advisors LLC
John E. Von Schlegell Portland, OR	Managing Director Endeavour Capital

Directors are elected to serve one year terms at the Annual meeting. Directors serve until their successors have been elected and qualified.

The Company has a conflict of interest policy with statements signed annually by each Director and Officer of the Company.

The Board appointed Audit, Investment, and Recommendation and Review Committees for all years under examination except 2014.

COMMITTEES

During all years, except 2014, of the period under examination, the Board appointed directors to serve on various committees. The committees were determined to be acting in accordance with the Company's By-laws. At December 31, 2014 the standing committees and the members serving were as follows:

Investment	Audit	Recommendation and Review
Leland M. Jones	Leland M. Jones	Leland M. Jones
Francis E. Lauricella, Jr.	Francis E. Lauricella, Jr.	Francis E. Lauricella, Jr.
William R. de Jonge	William R. de Jonge	William R. de Jonge

As of December 31, 2014, the Company did not have a committee performing the functions of compensation and/or nominating committees in accordance with 40 P.S. § § 991.1405(c)(4) and (4.1). The Recommendation and Review Committee was appointed, but held no meetings subsequent to April 15, 2013.

The Company did not have board and committee membership that met the necessary independence requirements and had not established independent committees to comply with 40 P.S. § § 991.1405(c) (3), (4), and (4.1) as of December 31, 2014.

Upon communication of the Board independence and committee independence issues to the Company, and subsequent to the examination date, an additional independent director was added to the Company's Board of Directors. The independent director was also appointed to the Audit, Investment and Recommendation and Review Committees by the Board of Directors bringing the Company into compliance with 40 P.S.§ § 991.1405(c)(3), (4), and part of (4.1).

It is recommended the Company appoint a committee in accordance with 40 P.S. § 991.1405(c)(4) and ensure the committee is active and performing the required responsibilities outlined with regards to nominations, principal officer performance evaluations and compensation recommendations.

The Company was compensating a director for maintaining meeting minutes and other administrative functions, previously performed by the Company, without a written agreement. This practice is not in compliance with Statement of Statutory Accounting Principles ("SSAP") No. 25 - *Accounting for and Disclosures about Transactions with Affiliates and Other Related Parties,* specifically section 7 which states "Transactions between related parties must be in the form of a written agreement." Director is included in the definition of related party at section 3(d).

Upon communication of this issue to the Company, the compensation to the director was terminated.

OFFICERS

As of the examination date, December 31, 2014, the following officers were appointed and serving in accordance with the Company's By-laws:

Name	Title
Robert J. Kimmel	Chief Executive Officer
William J. Wollyung, III	Chief Financial Officer
Darleen J. Fritz	President
Deborah A. Good	Secretary
Jeremy J. Gluck	Senior Vice President
Matthew T. LuBien	Senior Vice President

Effective January 1, 2016, the officers of ASIC and AMS, are William J. Wollyung, III, Chief Executive Officer/President; Brett G. Crise, Chief Financial Officer; Deborah A. Good, Secretary; and Darleen J. Fritz, Chief Risk Officer.

CORPORATE RECORDS

MINUTES

A compliance review of corporate minutes revealed the following:

- The Annual Meetings of the Company's stockholder were held in compliance with its By-laws for all years except 2014.
- The stockholder elected directors at such meetings in compliance with the By-laws for all years except 2014.
- The stockholder ratified the prior year's actions of the officers and directors for all years except 2014.
- Quorums were not present at all directors' meetings subsequent to April 15, 2013.
- The Company's investment transactions were approved quarterly by the Board.
- All directors attended Board meetings regularly prior to April 15, 2013. Subsequent to April 15, 2013, some directors did not attend Board meetings regularly.
- The Investment Committee and Audit Committee meetings were held in conjunction with the Board meetings.
- The Company's Board meeting minutes do not document review and approval of the reinsurance program.

Upon communication of the lack of compliance with the Company's By-laws, the Company amended and restated its By-laws to change the date of the Annual Meeting, to redefine the definition of a quorum, and to change the number of directors subsequent to the examination period.

ARTICLES OF INCORPORATION

On February 16, 2010, the Department approved an amendment to the Company's Articles of Incorporation increasing the number of authorized shares of common stock from 3,000,000 to 5,000,000 and increasing the par value from $1.00 to $1.40.

BY-LAWS

There were no changes to the Company's By-laws during the examination period. The Company's By-laws were amended and restated subsequent to the examination period.

SERVICE AND OPERATING AGREEMENTS

Federal Tax Allocation Agreement

ASI, ASIC, AMS, Mobile-Rec, JMT and Management Solution Associates, Inc. ("Management Solutions") executed a tax allocation agreement on December 31, 1998. The agreement was amended on December 31, 2002, removing Management Solutions from the agreement as a result of its dissolution, and again on April 15, 2013, removing JMT as party to the allocation agreement following the sale of ASI to K2 and the sale of JMT to Martin G. Lane, Jr. The agreement was not amended subsequent to Mobile-Rec's name being changed to AGIA, effective January 1, 2014. The agreement and subsequent amendments to the agreement have been approved by the Company's Board of Directors as required by 40 P.S. § 991.1405(a)(1)(iii).

The consolidated tax liability is allocated based upon the percentage that each member's individual tax liability bears to the sum of the individual tax liabilities for all members. Settlement between parties is defined as being within 60 days of tax payment date.

The Company was not settling the tax liability in accordance with the terms of the agreement during the examination period as required by 40 P.S. § 991.1405(a)(2) - *Standards for Transactions between Insurer and Affiliate.* Settlement was occurring within 60 days of the filing of the consolidated tax return when tax liabilities were determined and not when estimated tax payments were being made.

It is recommended the tax allocation agreement, as well as other intercompany agreements naming Mobile-Rec, Inc., be amended to reflect the current name of Aegis General Insurance Agency from Mobile-Rec, Inc.

It is further recommended the tax allocation agreement settlement terms be amended to reflect the Company's operational strategy of tax settlement after the consolidated tax return has been filed.

The amended tax allocation agreement, and any other agreement requiring the name change, is to be filed with the Department in accordance with 40 P.S. § 991.1405(a)(2) - Standards for Transactions between Insurer and Affiliate.

Cost Sharing Agreement

ASIC and Mobile-Rec executed a cost sharing agreement January 2, 1997, for the allocation of costs incurred by Mobile-Rec on behalf of the two companies. The expenses may be advanced by ASIC.

Mobile-Rec is reimbursed by ASIC for certain shared operating expenses incurred based upon the allocated percentage of direct earned premium. Additionally, ASIC pays Mobile-Rec market rate commissions.

The agreement terms do not meet the requirements noted in SSAP No. 25 as settlement terms are not included in the agreement. Upon communication of this to the Company, management responded that this agreement would not be effective in the future as the companies will be paying expenses individually. ASIC has executed an agency agreement with AGIA, formerly Mobile-Rec, to address the commissions paid.

This agreement was terminated and reported to the Department October 28, 2015, in a Form B filing.

Rent Sharing Agreement

ASIC, AMS and Mobile-Rec executed a rent sharing agreement October 1, 1999. This agreement was amended August 1, 2001, following ASIC purchasing the home office building. ASIC has leases for office space with AMS ($4,500 per month) and Mobile-Rec ($1,875 per month) based upon estimated square footage utilized by each entity.

Claims Management Agreement – AMS

ASIC and AMS executed a claims management agreement November 1, 2001, which was amended on January 1, 2013. AMS acts as claims administrator for business produced by the Wilson Gregory Agency ("WGA") in exchange for a percentage of total written premium of WGA. Settlement is defined as 45 days following month-end which may be offset against intercompany balances.

Management Services Agreement – Dan River

ASIC provides administrative, accounting and underwriting services for Dan River, an affiliated entity by virtue of common management. ASIC does not provide investment services for Dan River. The agreement was executed January 30, 2012, and provides for a monthly management fee for actual costs as can be determined, but shall not exceed 15.0% of Dan River's monthly earned premium.

Fees are charged monthly with amounts due by the fifteenth business day following quarter-end.

Management Services Agreement – K2

K2 provides investment advice, property and casualty product rate and form development, business development, overall operational guidance and management to ASIC, AMS, and Mobile-Rec under a management services agreement executed May 1, 2013. Fees to be paid by Mobile-Rec are not discussed in the agreement and are not currently being assessed.

ASIC and AMS pay a monthly fee of $150,000 and $50,000, respectively. Reconciliations are performed at least quarterly and settlement terms are included in the agreement.

The agreement was submitted to the Department for approval, and approved, pursuant to 40 P.S. § 991.1405(a)(2) - *Standards for Transactions between Insurer and Affiliate.*

Martin Lane Consulting and Director Agreement

ASIC and Martin G. Lane, Jr. executed a three-year Consulting and Director Agreement, effective April 15, 2013, whereby Mr. Lane provides management and strategic consulting services to ASIC and affiliates as requested by the Board of Directors. Mr. Lane also serves on the ASIC and AMS Boards of Directors. The agreement includes confidentiality and non-compete clauses.

Mr. Lane receives an annual compensation, paid quarterly, reimbursement for healthcare insurance, and reimbursement for a specified threshold for business expenses per year.

ASIC provides accounting services to Mr. Lane for his personal financial affairs, including the JGS Partnership.

Advisory Agreement

K2 and DVSM, LLC ("DVSM"), an affiliate of Endeavor Capital Fund V, LP and Endeavour Associates Fund V, LP, executed an advisory agreement effective April 15, 2013, which is effective so long as the Endeavour entities, directly or indirectly, hold any of the outstanding voting equity of K2 or any successor entity resulting from reorganization or restructuring of K2.

DVSM provides financial, operational, organizational and other advisory services to K2, affiliates, and the K2 Board of Managers in exchange for a quarterly fee based on a percentage of aggregate capital contributions.

The agreements with affiliates meet the fair and reasonable standards in 40 P.S. § 991.1405(a)(1) as of the examination date.

REINSURANCE

As of December 31, 2014, the Company had six quota share agreements, five excess of loss agreements, and an intercompany reinsurance pooling agreement that were active. There were also seven quota share agreements in runoff, with four having immaterial case reserves remaining as of the examination date. The Company utilizes facultative reinsurance when necessary.

The Company reported an immaterial amount of reinsurance recoverable as of the examination date, none of which were overdue or in dispute. An immaterial amount of letters of credit for two unauthorized reinsurers was held as of the examination date.

Subsequent to the examination date, the Company made changes to its reinsurance program and entered into reinsurance intermediary agreements with Guy Carpenter & Company, LLC ("Guy Carpenter"), Vista Reinsurance Intermediaries, Inc. ("Vista Re"), and Willis Re, Inc. ("Willis Re").

CEDED

The Company executed reinsurance agreements through Guy Carpenter and Vista Re, acting as intermediaries with the subscribing reinsurers, and with six direct companies for the 2014 reinsurance program. The Company's reinsurance agreements name ASIC, AMS, Dan River and the Texas Republic Group ("Republic Group") of Companies (4 named) as insureds. The Texas companies are included on the reinsurance treaties, as part of an agreement made in the mid 1980's when ASIC began writing business in Texas. The Company pays all reinsurance premiums. The agreements include settlement provisions, proper insolvency and arbitration clauses, extra contractual obligation ("ECO") and losses in excess of policy limits ("XPL") coverage. The Company retains the right to cancel subscribing reinsurers in the event of specified triggers.

The Company's reinsurance intermediaries, Guy Carpenter and Vista Re, are licensed by the Department as required by 40 P.S. § 321.2 (a) *Reinsurance intermediaries; licensing.* The Company did not have the programs operating pursuant to properly executed written authorizations between the Company and the intermediaries in accordance with 40 P.S. § 321.3 as of the examination date.

Prior to the end of examination fieldwork, the Company executed reinsurance intermediary authorization agreements with Guy Carpenter and Vista Re in accordance with 40 P.S. § 321.3.

Excess of Loss Agreements

Property Catastrophe Excess of Loss Reinsurance – one-year and two year agreements

Agreement, effective July 1, 2014, covering property business written by ASIC, AMS, and Dan River or business written by the Republic Group that is underwritten and assumed by the previously named insurers. The Republic Group includes, but is not limited to, Southern County Mutual Insurance Company, Republic Lloyds, Republic Vanguard Insurance Company and Southern Insurance Company all of Dallas, TX. The agreement covers losses under policies classified as property business in force at the inception of the contract or written or renewed during the contract term.

There are three layers to the agreement with the Company retention for each loss occurrence being $2.0 million, $6.0 million and $12.0 million, respectively, ultimate net losses. The reinsurers' ultimate net loss each occurrence per layer is $4.0 million, $6.0 million and $18.0 million. The reinsurer also has an ultimate net loss for all loss occurrences commencing during the contract term per layer of $8.0 million, $12.0 million and $36.0 million. The agreement includes a provision whereby the Company may elect to purchase optional coverage once the initial $4.0 million limit is exhausted. If elected, the optional coverage would apply to this agreement and the first year of the Company's property catastrophe excess of loss agreement.

Reinstatement Premium Protection Agreement

Agreement, effective July 1, 2014, covering property business written by ASIC, AMS, and Dan River or business written by the Republic Group that is underwritten and assumed by the previously named insurers. The agreement covers the Company's liability under reinstatement provisions of the original agreement. The reinsurer is liable to pay the reinstatement premium subject to $480,000 limit and is tied to the property catastrophe agreement discussed above.

Difference in Conditions Excess of Loss

Agreement, effective November 15, 2013, covering property business, specifically DIC for earthquake shock, flood, and earthquake sprinkler leakage perils, written by ASIC, AMS, and all affiliated or subsidiary insurance companies under common control or management.

The four layers of this agreement became effective at staggered dates between November 15, 2013 and August 15, 2014, each applying to loss occurrences commencing on or after the respective dates.

Quota Share Agreements

Multi-Line Quota Share

Agreement, effective October 1, 2014 through October 1, 2015, covering new, renewal and extension business produced by sub-producing agents of AGIA. ASIC has entered into an agency agreement with AGIA. This is a loss occurrence agreement for property and casualty business written by the Republic Group.

Lines of business include, but are not limited to, Fire, Allied Lines, Extended Coverage, Dwelling Fire, Mobile Home, Homeowners' Multi-Peril, and Personal Liability when written in conjunction with dwelling coverage.

The reinsurer assumes 50.0% gross liability on new business and 20.0% on renewal business, with a maximum ceded gross written premium of $15.0 million, excluding any run-off coverage. AGIA is responsible for the issuance, maintenance and servicing of the policies, claims and other business transactions under this reinsurance agreement.

ASIC is required to maintain the property catastrophe excess of loss reinsurance agreements (both one-year and two-year) and the reinstatement premium protection agreement discussed above.

This agreement was terminated in cut-off status at expiration.

Accident & Health Quota Share with Catlin Underwriting, Inc. for and on behalf of Lloyd's Syndicate 2003 ("SJC") Summit, NJ

This is a 50.0% quota share agreement, effective July 1, 2014, covering liability arising out of claims under policies issued by ASIC, AMS and all affiliated companies.

The agreement excludes reinsurance assumed by the Company, except for intercompany reinsurance agreements.

Storage Business Owners Alliance Tenant Storage ("SBOA")

This 50.0% quota share agreement, effective March 1, 2011, was amended to 100.0% quota share effective July 1, 2012, and continues until terminated. The agreement covers the insurance provided to tenants of storage units. The 100.0% quota share agreement contains provisions for the Company to purchase and maintain inuring catastrophe excess of loss reinsurance coverage with a Company retention of $500,000 each occurrence. The agreement had four amendments during the examination period. The subscribing reinsurer is SBOA TI Reinsurance Ltd. ("SBOA TI"), an unauthorized reinsurer. The Company ceded $9,907,000 in premiums to SBOA TI, approximately 94% of total premiums ceded to an unauthorized reinsurer, as of the examination date.

Surety Reinsurance Agreements

Delaware Surety Insurance Company

This agreement, effective January 1, 2010, was executed January 28, 2010, and is continuous until cancelled by either party with 60 days written notice. The agreement will terminate in run-off status upon cancellation. As of the examination date, this agreement was not terminated.

This is a 50.0% quota share agreement covering new and renewal surety bonds written through Delmarva Underwriters, LTD, becoming effective on or after January 1, 2010, with individual bond limits of $1.0 million each Principal and 25.0% quota share for individual bond limits over $1.0 million but not exceeding $2.0 million. Surety bonds classified as surety in the Company's rate manual and issued in Delaware, Maryland, New Jersey, Pennsylvania and Virginia are covered under this agreement.

ECO coverage is included as a direct proportion to the reinsurance coverage with an aggregate limit of ECO being $2.0 million.

Everest Reinsurance Company ("Everest")

This quota share agreement, effective January 1, 2010, was executed February 19, 2010, and replaced the prior agreement, effective January 1, 2009, that terminated in run-off status. The agreement was amended twice during the examination period.

Surety bonds with renewal dates on or after January 1, 2013, are covered at 20.0% quota share for bonds up to and including $1.0 million and at 50.0% for bonds greater than $1.0 million. The agreement was terminated in run-off status and replaced with a new agreement, effective July 1, 2015, as discussed below in the subsequent events.

Sub-suretyship, Power of Attorney and Indemnification Agreement

This agreement, executed and effective January 1, 2014, covers principal surety-issued bond business effective on or after the effective date on which the reinsurer provides support under the January 1, 2010, surety quota share reinsurance agreement, as subsequently amended and discussed above. Everest acts as a cut-through reinsurer in cases where a carrier with a rating of A+ from A.M. Best is required, a Treasury listing exceeding the Company's Treasury listing of approved sureties is required, or when requested as an additional surety on bonds in exchange for annual administrative fee.

The reinsurer must approve each applicable bond and the bond must fall within the scope of the quota share agreement. Everest is held harmless from and against any and all liability and/or expense arising from its subsurety support on bonds issued by the Company. The reinsurer's total cost on all outstanding bonds at any one time shall not exceed $15.0 million. The reinsurer is included on the Company's Errors and Omissions insurance policy.

This agreement was terminated and replaced with an agreement, effective July 1, 2015, as discussed below in the subsequent events.

First Indemnity Company of America

This is a 50.0% quota share agreement covering surety bonds written or renewed on behalf of Aegis by the Whitewood Agency, Ltd., on or after September 1, 2011. The reinsurer's liability continues until the expiration or cancellation of the surety bond. The reinsurer's liability is limited to $250,000 per surety bond.

Terminated Reinsurance Agreements

American Safety Casualty Insurance Company

This 100.0% quota share agreement, covering contract and commercial surety bonds produced and underwritten by Bluestone Agency, Inc., was in effect from July 2, 2012 through June 30, 2014. The agreement terminated in cut-off status.

Bluestone Surety, LTD. /General Reinsurance Corporation

This 75.0% quota share agreement, covering contract and commercial surety bonds produced and underwritten by Bluestone Agency, Inc., terminated in run-off status effective July 1, 2012.

Overall

All reinsurance contracts contain appropriate insolvency and arbitration clauses. Additionally included were offset, errors & omissions, and entire agreement clauses.

All reinsurance contracts noted above meet the required transfer of risk as noted in SSAP No. 62R.

Management has represented that all material ceded reinsurance agreements transfer both underwriting and timing risk as set forth in SSAP No. 62R. Representations were supported by appropriate risk transfer analyses and an attestation from the Company's Chief Executive Officer and Chief Financial Officer pursuant to the NAIC *Property and Casualty Annual Statement Instructions*. Additionally, examination review indicated that the Company was not a party to any finite reinsurance agreements. All ceded reinsurance agreements were accounted for utilizing reinsurance accounting as set forth in SSAP No. 62R.

ASSUMED

As of December 31, 2014, ASIC assumed business from AMS and other various insurers affiliated with the Company.

Pooling Agreement with American Sentinel Insurance Company

The Company and AMS are parties to an intercompany reinsurance pooling agreement whereby the Company assumes 100.0% of the net business from AMS and cedes 25.0% of the net business back to AMS.

Other Assumed Reinsurance Agreements

The Company assumes an immaterial amount of business from Dan River (VA), Hudson Insurance Company (DE), Ranchers and Farmers Mutual Insurance Company (TX), and Republic Vanguard Insurance Company (AZ).

The Company assumes 100.0% of the business written on Southern County Mutual, Republic Lloyds, Republic Vanguard, and Southern Insurance Company (all of Dallas, TX) paper. The Texas business is covered under the catastrophe treaties.

TERRITORY AND PLAN OF OPERATION

The Company is licensed to write business in 50 states and the District of Columbia. As of December 31, 2014, Aegis was writing business in all states except Alaska and Hawaii. As of December 31, 2014, approximately 42.0% of the Company's written premium is attributable to California and Pennsylvania. No other state attributed to greater than 5.0% of the written premium.

The Company's major lines of business are homeowners' multiple peril, group accident & health, private passenger auto and surety. Its major product line is mobile homeowners' and manufactured homeowners' coverage with most policies underwritten on an actual cash basis rather than a replacement cost basis.

The Company markets its products through an agency system of approximately 72 general agents and 104 independent agents as of December 31, 2014. The Company distribution network changed, effective January 1, 2015, when AGIA entered into agency agreements with former ASIC agents for the sale and servicing of policies underwritten for homeowners', manufactured homes, fire and accident and health. AGIA is now responsible for paying the commissions to the agents.

The Company reported the following net written premiums, by line of business, for the year ended December 31, 2014:

Line of Business	Direct and Assumed Premium	Ceded Premium	Net Written Premium	Percentage of Total
December 31, 2014				
Fire	$ 3,213,916	$ 1,149,551	$ 2,064,365	3.3%
Homeowners multiple peril	27,832,110	9,158,173	18,673,937	30.0%
Inland marine	10,507,946	10,533,705	(25,759)	0.0%
Earthquake	8,059,223	3,038,074	5,021,149	8.1%
Group accident and health	13,692,699	4,620,555	9,072,144	14.6%
Other accident and health	322,770	80,700	242,070	0.4%
Other liability - occurrence	1,108,581	304,990	803,591	1.3%
Private passenger auto liability	12,532,965	3,133,200	9,399,765	15.1%
Commercial auto liability	2,967,520	741,900	2,225,620	3.6%
Auto physical damage	4,688,920	1,172,200	3,516,720	5.6%
Surety	21,678,445	10,377,743	11,300,702	18.1%
Totals	$ 106,605,095	$ 44,310,791	$ 62,294,304	100.0%

SIGNIFICANT OPERATING RATIOS AND TRENDS

The underwriting ratios summarized below are on an earned/incurred basis, and encompass the five-year period covered by this examination.

	Amount	Percentage
Premiums earned	$ 299,884,833	100.0 %
Losses incurred	$ 128,758,097	42.9 %
Loss expenses incurred	22,397,528	7.5 %
Other underwriting expenses incurred	131,358,275	43.8 %
Net underwriting gain or (loss)	17,370,933	5.8 %
Totals	$ 299,884,833	100.0 %

The Company reported the following net underwriting, investment and other gains during the period under examination:

	2014	2013	2012	2011	2010
Admitted assets	$ 101,270,992	$ 97,859,200	$ 89,125,777	$ 85,453,841	$ 77,392,008
Liabilities	$ 47,870,227	$ 46,374,165	$ 44,607,725	$ 41,922,712	$ 35,244,808
Surplus as regards policyholders	$ 53,400,765	$ 51,485,035	$ 44,518,052	$ 43,531,129	$ 42,147,200
Gross premium written	$ 106,605,095	$ 108,685,711	$ 103,456,383	$ 94,034,004	$ 81,599,548
Net premium written	$ 62,294,304	$ 69,360,396	$ 62,678,105	$ 58,246,942	$ 52,921,978
Underwriting gain/(loss)	$ 940,336	$ 6,922,969	$ 3,949,666	$ 3,521,147	$ 2,036,815
Investment gain/(loss)	$ 2,865,385	$ 1,003,223	$ 406,162	$ 1,583,757	$ 1,509,181
Other gain/(loss)	$ 461,370	$ 509,819	$ 459,578	$ 472,089	$ 478,991
Net income	$ 3,459,070	$ 5,734,330	$ 3,191,172	$ 4,112,932	$ 3,201,850

ACCOUNTS AND RECORDS

The Company maintains accounting, investment and claims records at its home office in Harrisburg, Pennsylvania and the K2 office in Solana Beach, California.

PENDING LITIGATION

As of December 31, 2014, the Company is subject to litigation and arbitration arising in the normal course of business. As of the date of this examination report, January 22, 2016, the Company is not a party to any material litigation or arbitration, other than as routinely encountered in claims activity, which will, in the opinion of management, have a material adverse effect on the Company's capital and surplus.

FINANCIAL STATEMENTS

The financial condition of the Company, as of December 31, 2014, and the results of its operations for the five-year period under examination, are reflected in the following statements:

Comparative Statement of Assets, Liabilities, Surplus and Other Funds;
Comparative Statement of Income;
Comparative Statement of Capital and Surplus; and
Comparative Statement of Cash Flow

Comparative Statement of Assets, Liabilities, Surplus and Other Funds As of December 31,

	2014	2013	2012	2011	2010
Bonds	$ 42,472,807	$ 16,702,092	$ 18,250,907	$ 20,280,492	$ 13,660,286
Preferred stocks	600,815	665,128	1,723,101	1,688,168	1,922,328
Common stocks	24,160,474	28,329,378	29,164,779	26,669,431	28,883,551
Mortgage loans on real estate	0	366,447	1,418,571	2,734,706	3,315,106
Real estate	2,218,922	2,493,797	4,312,572	5,408,946	5,152,903
Cash, cash equivalents, and short term investments	13,968,422	33,187,670	18,931,867	12,372,430	12,414,035
Other invested assets	1,198,467	2,072,454	1,880,980	1,428,630	1,180,550
Aggregate write-ins for invested assets	1	0	0	0	0
Subtotals, cash and invested assets	84,619,908	83,816,966	75,682,777	70,582,803	66,528,759
Investment income due and accrued	454,351	233,990	261,911	253,828	183,809
Premiums and agents' balances due	10,015,497	9,458,584	7,920,954	7,533,192	7,796,829
Amounts recoverable from reinsurers	2,585,756	1,485,991	1,875,741	1,167,380	1,201,506
Funds held by or deposited with reinsured companies	278,808	0	0	0	0
Current federal and foreign income tax recoverable and interest thereon	0	0	600,663	0	0
Net deferred tax asset	1,641,510	1,679,200	1,687,958	1,866,622	1,681,105
Electronic data processing equipment and software	1,218,929	0	0	0	0
Receivable from parent, subsidiaries and affiliates	306,700	0	0	0	0
Aggregate write-ins for other than invested assets	149,533	1,184,469	1,095,773	4,050,016	0
Total	$ 101,270,992	$ 97,859,200	$ 89,125,777	$ 85,453,841	$ 77,392,008
Losses	$ 13,422,255	$ 13,870,615	$ 14,868,146	$ 12,687,722	$ 10,436,166
Reinsurance payable on paid loss and loss adjustment expenses	837,825	935,564	599,438	550,697	577,125
Loss adjustment expenses	3,677,363	2,932,293	1,561,765	1,565,408	1,625,742
Commissions payable, contingent commissions and other similar charges	1,782,604	408,592	382,180	1,287,237	1,012,859
Other expenses	645,466	540,676	459,916	739,755	859,002
Taxes, licenses and fees	520,901	394,999	427,955	488,275	465,842
Current federal and foreign income taxes	28,329	262,694	0	526,760	414,159
Unearned premiums	21,100,270	20,036,359	17,592,319	15,897,781	15,773,786
Advance premium	7,900	240,207	207,091	247,137	249,275
Ceded reinsurance premiums payable (net of ceding commissions)	1,823,329	2,811,785	2,270,185	2,614,163	1,854,299
Amounts withheld or retained by company for account of others	3,882,418	3,790,081	4,995,330	4,198,477	835,253
Payable to parent, subsidiaries and affiliates	0	150,300	1,243,400	1,119,300	1,141,300
Payable for securities	141,567	0	0	0	0
Total liabilities	47,870,227	46,374,165	44,607,725	41,922,712	35,244,808
Aggregate write-ins for special surplus funds	0	0	0	263,220	243,440
Common capital stock	4,200,000	4,200,000	4,200,000	4,200,000	4,200,000
Gross paid in and contributed surplus	5,266,827	5,266,827	5,266,827	5,266,827	5,266,827
Unassigned funds (surplus)	43,933,938	42,018,208	35,051,225	33,801,082	32,436,933
Surplus as regards policyholders	53,400,765	51,485,035	44,518,052	43,531,129	42,147,200
Totals	$ 101,270,992	$ 97,859,200	$ 89,125,777	$ 85,453,841	$ 77,392,008

Comparative Statement of Income
For the Year Ended December 31,

Underwriting Income	2014	2013	2012	2011	2010
Premiums earned	$ 61,230,393	$ 66,916,356	$ 60,983,567	$ 58,122,947	$ 52,631,570
Deductions:					
Losses incurred	25,097,784	26,636,913	27,495,284	25,609,717	23,918,399
Loss expenses incurred	5,620,704	5,847,028	3,930,533	3,526,972	3,472,291
Other underwriting expenses incurred	29,571,569	27,509,446	25,608,084	25,465,111	23,204,065
Total underwriting deductions	60,290,057	59,993,387	57,033,901	54,601,800	50,594,755
Net underwriting gain or (loss)	940,336	6,922,969	3,949,666	3,521,147	2,036,815
Investment Income					
Net investment income earned	1,517,908	1,612,485	1,438,906	1,580,822	1,493,371
Net realized capital gains or (losses)	1,347,477	(609,262)	(1,032,744)	2,935	15,810
Net investment gain or (loss)	2,865,385	1,003,223	406,162	1,583,757	1,509,181
Other Income					
Net gain or (loss) from agents' or premium balances charged off	(4,698)	(2,122)	(2,596)	(3,409)	(1,479)
Finance and service charges not included in premiums	398,993	399,563	417,853	458,655	465,332
Aggregate write-ins for miscellaneous income	67,075	112,378	44,321	16,843	15,138
Total other income	461,370	509,819	459,578	472,089	478,991
Net income before dividends to policyholders and before federal and foreign income taxes	4,267,091	8,436,011	4,815,406	5,576,993	4,024,987
Federal and foreign income taxes incurred	808,021	2,701,681	1,624,234	1,464,061	823,137
Net income	$ 3,459,070	$ 5,734,330	$ 3,191,172	$ 4,112,932	$ 3,201,850

Comparative Statement of Capital and Surplus
For the Year Ended December 31,

	2014	2013	2012	2011	2010
Surplus as regards policyholders,					
December 31, previous year	$ 51,485,035	$ 44,518,052	$ 43,531,129	$ 42,147,200	$ 39,495,627
Net income	3,459,070	5,734,330	3,191,172	4,112,932	3,201,850
Net unrealized capital gains or (losses)	18,822	2,315,270	978,148	40,903	1,590,049
Change in net deferred income tax	(405,375)	257,087	210,313	(114,416)	(104,693)
Change in nonadmitted assets	(156,787)	660,296	107,290	124,730	407,648
Cumulative effect of changes in accounting principles	0	0	0	0	286,721
Capital changes:					
Transferred from surplus (Stock Dividend)	0	0	0	0	1,200,000
Surplus adjustments:					
Transferred to capital (Stock Dividend)	0	0	0	0	(1,200,000)
Dividends to stockholders	(1,000,000)	(2,000,000)	(3,500,000)	(2,800,000)	(2,400,000)
Aggregate write-ins for gains and losses in surplus	0	0	0	19,780	(330,002)
Change in surplus as regards policyholder for the year	1,915,730	6,966,983	986,923	1,383,929	2,651,573
Surplus as regards policyholders,					
December 31, current year	$ 53,400,765	$ 51,485,035	$ 44,518,052	$ 43,531,129	$ 42,147,200

Comparative Statement of Cash Flow
For the Year Ended December 31,

	2014	2013	2012	2011	2010
Cash from Operations					
Premiums collected net of reinsurance	$ 60,280,991	$ 68,397,482	$ 61,906,319	$ 59,268,305	$ 51,780,149
Net investment income	1,768,093	1,874,534	1,677,070	1,700,408	1,654,420
Miscellaneous income	461,370	509,819	459,578	472,089	478,991
Total income	62,510,454	70,781,835	64,042,967	61,440,802	53,913,560
Benefit and loss related payments	27,022,457	26,946,478	25,998,664	23,356,575	22,048,017
Commissions, expenses paid and aggregate write-ins for deductions	32,842,499	31,873,820	30,763,292	28,868,562	26,937,550
Federal and foreign income taxes paid (recovered)	1,065,026	1,838,324	2,751,657	1,420,500	(19,357)
Total deductions	60,929,982	60,658,622	59,513,613	53,645,637	48,966,210
Net cash from operations	1,580,472	10,123,213	4,529,354	7,795,165	4,947,350
Cash from Investments					
Proceeds from investments sold, matured or repaid:					
Bonds	9,075,171	3,630,417	8,814,177	4,102,917	15,473,180
Stocks	81,912,587	7,956,370	8,143,018	9,991,587	4,395,039
Mortgage loans	143,723	1,052,123	1,156,134	1,150,198	2,626,739
Real estate	170,000	1,691,155	0	0	0
Other invested assets	870,246	1,137,701	376,254	334,352	42,376
Net gain or (loss) on cash and short-term investments	31	0	0	0	0
Miscellaneous proceeds	141,567	0	0	0	0
Total investment proceeds	92,313,325	15,467,766	18,489,583	15,579,054	22,537,334
Cost of investments acquired (long-term only):					
Bonds	35,229,495	2,268,844	6,986,634	10,822,618	10,078,401
Stocks	76,408,743	3,559,870	8,938,600	7,523,651	9,354,445
Mortgage loans	0	0	348,198	1,029,798	1,802,400
Real estate	0	0	0	322,147	1,206
Other invested assets	5,000	1,297,168	859,771	444,245	135,150
Total investments acquired	111,643,238	7,125,882	17,133,203	20,142,459	21,371,602
Net cash from investments	(19,329,913)	8,341,884	1,356,380	(4,563,405)	1,165,732
Cash from Financing and Miscellaneous Services					
Other cash provided (applied):					
Dividends to stockholders (paid)	1,000,000	2,000,000	3,500,000	2,800,000	2,400,000
Other cash provided or (applied)	(469,807)	(2,209,294)	4,173,703	(473,365)	(390,507)
Net cash from financing and miscellaneous sources	(1,469,807)	(4,209,294)	673,703	(3,273,365)	(2,790,507)
Reconciliation of cash and short-term investments:					
Net change in cash and short-term investments	(19,219,248)	14,255,803	6,559,437	(41,605)	3,322,575
Cash and short-term investments:					
Beginning of the year	33,187,670	18,931,867	12,372,430	12,414,035	9,091,460
End of the year	$ 13,968,422	$ 33,187,670	$ 18,931,867	$ 12,372,430	$ 12,414,035

SUMMARY OF EXAMINATION CHANGES

There were no examination changes, except as discussed above in the Capitalization section on page 2 of this report, to the preceding financial statements as filed with regulatory authorities over the review period.

NOTES TO FINANCIAL STATEMENTS

ASSETS

INVESTMENTS

As of December 31, 2014, the Company's invested assets were distributed as follows:

	Amount	Percentage
Bonds	$ 42,472,807	50.2 %
Preferred stocks	600,815	0.7 %
Common stocks	24,160,474	28.6 %
Real estate	2,218,922	2.6 %
Cash	12,161,539	14.4 %
Short-term investments	1,806,883	2.1 %
Other invested assets	1,198,467	1.4 %
Totals	$ 84,619,908	100.0 %

The Company's bond and short-term investment portfolio had the following quality and maturity profiles:

NAIC Designation	Amount	Percentage
1 - highest quality	$ 34,582,527	78.1 %
2 - high quality	9,697,163	21.9 %
Totals	$ 44,279,690	100.0 %

Years to Maturity	Amount	Percentage
1 year or less	$ 5,252,419	11.9 %
2 to 5 years	21,192,446	47.8 %
6 to 10 years	16,485,195	37.2 %
11 to 20 years	1,192,347	2.7 %
over 20 years	157,283	0.4 %
Totals	$ 44,279,690	100.0 %

As of December 31, 2014, the Company had approximately 66.7% of its invested assets in cash, short-term investments and bonds. The Company invests in high quality securities and has its bond portfolio laddered to support reasonable asset-liability matching. Approximately 96.9% of the bonds and short-term investments have maturity dates of ten years or less.

The Company has approximately 29.3% of its invested assets in preferred and common stocks. The Company invests in highly rated preferred and common stocks and does not invest in hedge funds or derivatives.

The real estate owned by the Company is the home office in Harrisburg, Pennsylvania with office space leased to affiliates.

The Company's invested assets are covered by a custodial agreement with Bank of America that was not in compliance with 31 Pa. Code § 148a.3 as of the examination date. The Company did execute a custodial agreement with Bank of America that was in compliance with 31 Pa. Code § 148a.3 prior to this examination report date.

The Company has a written investment policy as required by 40 P.S. § 653 b(b). The investment policy was not being reviewed and approved on an annual basis by the Board of Directors as of December 31, 2014, in accordance with 40 P.S. § 653 b(b) that states "Any domestic company subject to the provisions of this act is required to have a formal investment plan which shall be updated on an annual basis as authorized by the board of directors. The investment plan shall include, at a minimum, a description of the investment strategy of the company designed to provide for liquidity and diversity of the investment portfolio." The Company, at December 31, 2014, was following its investment policy.

It is recommended the Company review and approve its written investment policy on an annual basis as required by 40 P.S. § 653 b(b).

Additionally, the Company did not include Other Than Temporary Impairment ("OTTI") review as part of its investment policy as of the examination date. The Company did have the OTTI review incorporated in its investment policy as of the examination report date and was performing quarterly OTTI reviews.

LIABILITIES

LOSS AND LOSS ADJUSTMENT EXPENSE RESERVES

The Company reported reserves in the amount of $13,422,255 for losses and $3,677,363 for loss adjustment expenses ("LAE") on its December 31, 2014 Annual Statement. These amounts represent the Company's share of the intercompany pooling reinsurance arrangement.

David L. Miller, FCAS, MAAA, an independent actuarial consultant associated with the firm of David L. Miller, Ltd, has been the Company's appointed actuary for the entire exam period. At December 31, 2014, the appointed actuary issued a Statement of Actuarial Opinion concluding that the Company's reserves "make a reasonable provision for all unpaid loss and loss expense obligations of the Company under the terms of its policies and agreements".

In order for the examination team to gain an adequate comfort level with the Company's loss and LAE reserve estimates, the Department's internal property and casualty actuarial staff assisted the examination team in performing a risk-focused review of the Company's reserving and pricing processes. The Department also retained the actuarial expertise of The Actuarial Advantage, Inc. to evaluate certain risks that required Phase 5 substantive test work.

Based upon the procedures performed and results obtained, the actuarial and examination staff obtained sufficient documentation to support the conclusion that the Company's net loss and LAE reserves are reasonably stated as of December 31, 2014.

SUBSEQUENT EVENTS

The examiner performed a high level review of the Company's 2015 third quarter statement filings, meeting minutes for K2 and the Company, the 2014 Audited Financial Statement for K2 which was issued December 17, 2015, and Board meeting packets as part of the examination wrap-up procedures. Information relevant to subsequent events was followed up on and, in many cases, is included in the information below.

The holding company structure changed subsequent to December 31, 2014, with the formation of Allied Public Risk on January 1, 2015, and Aegis Surety Bonds and Insurance Services, LLC on March 1, 2015. Aegis Powersports, formerly a division of AGIA, was spun-off as a limited liability company in July 2015. See additional information on these entities in the Insurance Holding Company section on page 3 of this examination report.

The Company did not file the Form B for the change in the holding company in accordance with 40 P.S. § 991.1404 (a)(1) that states "Every insurer which is authorized to do business in this Commonwealth and which is a member of an insurance holding company system shall register with the department, except a foreign insurer subject to registration requirements and standards adopted by statute or regulation in the jurisdiction of its domicile which are substantially similar to those contained in this section and 1405(a)(1) and (2), (b) and (d). Each registered insurer shall keep current the information required to be disclosed in its registration statement by reporting all material changes or additions within fifteen (15) days after the end of the month in which it learns of each such change or addition," and in accordance with 31 Pa. Code § 25.17 <u>*Annual registration of insurers—statement filing*</u> that states " (c) An amendment to Form B shall be filed within 15 days after the end of a month in which there is a material change to the information provided in the annual registration statement, including changes in officers or directors listed in Item 4 of Form B," and "(d) Amendments shall be filed in the Form B format with only items which are being amended reported. Each amendment shall include at the top of the first page ''Amendment No. (insert number) to Form B for (insert year of most recent filing)'' and shall indicate the date of the amendment and not the date of the original filing."

It is recommended the Company review its Holding Company structure and file a Form B amendment to report changes in accordance with 31 Pa. Code § 25.17 <u>Annual registration of insurers – statement filing</u>, paragraphs (c) and (d).

It is further recommended the Company file Form B for any future changes to the Holding Company structure in accordance with 40 P.S. § 991.1404 (a)(1).

The Company executed an agency agreement with Wilson Gregory Agency effective January 1, 2015, executed September 17, 2015, and subsequently amended September 21, 2015. This agreement includes provisions for the contingent commissions previously paid by the Company without an agreement and a provision for profit sharing.

K2 assigned the ownership of the GameChanger Platform, previously being reported on the Company's balance sheet as an admitted asset with a $1,218,929 balance at December 31, 2014, to AGIA in the first quarter 2015.

The Company terminated the Storage Building Owners Association program effective July 1, 2015, but extended the deadline to December 31, 2015, to allow the new carrier time to obtain licensing in the necessary states. The Company executed two one-year excess of loss reinsurance agreements, written through Vista Re, to cover the transition period. The agreements name the Company and the two new companies writing the business. As of January 1, 2016, the Company is no longer writing this line of business.

The Company terminated numerous agency agreements effective January 1, 2015. AGIA entered into new agency agreements with many of the terminated agents and agencies effective January 1, 2015.

The Company filed a Form D with the Department requesting permission to grant a loan in the amount of $3.0 million to K2 and to report this loan as an admitted asset. This was approved by the Department on November 2, 2015, as the loan will be collateralized and will be repaid over a three-year period with interest. This loan was completed January 14, 2016.

The Company provided a notice of ordinary dividend to the Department on December 14, 2015, with an effective date of December 31, 2015, for the payment of $1.0 million to ASI. Concurrently, AMS filed a similar notice for payment of $1.0 million to the Company.

The Company's reinsurance agreements were being executed by Robert Kimmel, CEO of the Company and CEO of K2. Beginning January 1, 2016, the reinsurance agreements will be executed by William Wollyung, III, CEO or Brett Crise, CFO of the Company, bringing more control of the reinsurance program back to the insurer.

The Company entered into an excess of loss reinsurance agreement with Guy Carpenter, effective July 1, 2015, covering surety lines of business. This agreement includes a co-surety clause, an alternate payee clause, and an insolvency clause that states the alternate payee clause takes precedence. Agreements related to this excess of loss surety agreement include a letter of credit agreement, provided by the Company, and a power of attorney indemnity agreement. The alternate payee clause and insolvency clause are in violation of SSAP No. 62, paragraph 8.a and 40 P.S. § 442.1(c).

The Company is aware of the violation and is working with Guy Carpenter to have the alternate payee clause removed from the reinsurance agreement. The Company will provide the amended agreement to the Department for review. No examination recommendation is being included in the current examination report.

The Company entered into a reinsurance agreement, effective July 1, 2015, with State National Insurance Company and TST Insurance Services, LLC as a 30.0% subscribing reinsurer covering business classified as commercial automobile liability, physical damage, general liability and inland marine written in 16 states. The Company is required to secure 110.0% of its obligations under the agreement with collateral. This agreement is written through Guy Carpenter and includes an insolvency clause and an alternate payee clause. The alternate payee clause is in violation 40 P.S. § 442.1(c). The Company executed an amendment dated January

22, 2016, directly with State National Insurance Company and TST Insurance Services, LLC, deleting the alternate payee clause from the reinsurance agreement.

The Company has obtained licensure for writing commercial trucking, inland marine, commercial auto liability and physical damage business in Idaho, Oklahoma, Texas, Arkansas, Nebraska, Wisconsin, Utah, Montana, Illinois, North Dakota and South Dakota. The Company will begin writing this business directly, formerly written through State National Insurance Company, in 2016 and ceding 70.0% to subscribing reinsurers.

The Company entered into a 50.0% quota share reinsurance agreement, as the ceding company, with Allied World Insurance Company covering the difference in conditions business written by Vikco Insurance Services, LLC in the state of California. The Company also entered into an agreement, as the reinsurer, with Allied World Insurance Company and affiliates, to assume 50.0% of the business written by Vikco in the state of California.

The Company entered into a reinsurance intermediary authorization agreement with Willis Re on July 1, 2015. Willis Re was appointed as Broker of Record, effective July 20, 2015, for the Texas only property catastrophe reinsurance placement. A one-year agreement, effective July 20, 2015, was executed for the Texas property catastrophe excess of loss coverage for $20.0 million aggregate reinsurer liability. The sole subscriber on the agreement is Everest.

RECOMMENDATIONS

PRIOR EXAMINATION

The prior examination report contained no recommendations.

CURRENT EXAMINATION

As a result of the current examination, the following recommendations are being made:

1. The Company did not have board and committee membership that met the necessary to meet the requirements of 40 P.S. § 991.1405 (c)(4.1) *Standards and management of an insurer within a holding company system*, that states: "the board of directors of a domestic insurer shall establish one or more committees comprised solely of directors who are not officers or employees of the insurer or of any entity controlling, controlled by or under common control with the insurer. The committee or committees shall have responsibility for recommending candidates to be nominated by the board of directors, in addition to any other nominations by voting shareholders or policyholders, for election as directors by voting shareholders or policyholders, evaluating the performance of officers deemed to be principal officers of the insurer and recommending to the board of directors the selection and compensation of the principal officers." (See "Committees," page 10)

    It is recommended the Company appoint a committee in accordance with 40 P.S. § 991.1405(c)(4.1) and ensure the committee is active and performing the required responsibilities outlined with regards to nominations, principal officer performance evaluations and compensation recommendations.

2. The Company and affiliates are parties to a Tax Allocation Agreement executed December 31, 1998, amended December 31, 2002, and again April 15, 2013. The

agreement has not been amended to reflect the name change from Mobile-Rec, Inc. to Aegis General Insurance Agency. Furthermore, the tax balances are not being settled in accordance with the tax allocation agreement. (See "Service and Operating Agreements," page 12)

> ***It is recommended the tax allocation agreement, as well as other intercompany agreements naming Mobile-Rec, Inc., be amended to reflect the current name of Aegis General Insurance Agency from Mobile-Rec, Inc.***
>
> ***It is further recommended the tax allocation agreement settlement terms be amended to reflect the Company's operational strategy of tax settlement after the consolidated tax return has been filed.***
>
> ***The amended tax allocation agreement, and any other agreement requiring the name change, is to be filed with the Department in accordance with 40 P.S. § 991.1405(a)(2) - Standards for Transactions between Insurer and Affiliate.***

3. The Company has a written investment policy as required by 40 P.S. § 653 b(b). The investment policy was not being reviewed and approved on an annual basis by the Board of Directors as of December 31, 2014, as required by 40 P.S. § 653 b(b). (See "Investments," page 27)

> ***It is recommended the Company review and approve its written investment policy on an annual basis as required by 40 P.S. § 653 b(b).***

4. The Company did not file the required Form B and Form B Amendment to report changes to the holding company structure when Aegis Powersports was spun off and renamed Aegis Extended Service, LLC in 2015. These filings are to be filed within 15 days after the end of a month that there is a material change. (See "Subsequent Events," page 28)

> ***It is recommended the Company review its Holding Company structure and file a Form B amendment to report changes in accordance with 31 Pa. Code § 25.17 Annual registration of insurers – statement filing, paragraphs (c) and (d).***
>
> ***It is further recommended the Company file Form B for any future changes to the Holding Company structure in accordance with 40 P.S. § 991.1404 (a)(1).***

CONCLUSION

As a result of this examination, the financial condition of Aegis Security Insurance Company, as of December 31, 2014, was determined to be as follows:

		Amount	Percentage
Admitted assets	$	101,270,992	100.0 %
Liabilities	$	47,870,227	47.3 %
Surplus as regards policyholders		53,400,765	52.7 %
Total liabilities and surplus	$	101,270,992	100.0 %

Since the previous examination, made as of December 31, 2009, the Company's assets increased by $28,768,537, its liabilities increased by $14,863,399, and its surplus increased by $13,905,138.

This examination was conducted by Jenny Jeffers, CISA and Joe Detrick, CPA, CISA, CFE, AES of Jennan Enterprises; Laura Martin, FCAS, MAAA, Dennis Henry, FCAS, MAAA, and Kyle Mrotek, FCAS, MAAA, of The Actuarial Advantage, Inc.; Kevin Prescott, CFE, AES, CISA, David Hughes, and Robin Roberts, CFE, of the Department with the latter in charge.

Respectfully,

Melissa Greiner

Melissa Greiner
Acting Director, Bureau of Financial Examinations

David R. Evans -cdd

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Robin Roberts, CFE
Examiner-in-Charge

The CFE designation has been conferred by an organization not affiliated with the federal or any state government. However the CFE designation is the only designation recognized by the NAIC for the purposes of directing statutory Association examinations of insurance companies