Examination Warrant Number 11-04705-13285-R1

Report of Examination of

Allegheny Casualty Company
Norristown, Pennsylvania

As of December 31, 2011

Allegheny Casualty Company

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Harrisburg, Pennsylvania
May 28, 2013

Honorable Stephen J. Johnson, CPA
Deputy Insurance Commissioner
Commonwealth of Pennsylvania
Insurance Department
Harrisburg, Pennsylvania

Dear Sir:

In accordance with instructions contained in Examination Warrant Number 11-04705-13285-R1, dated, February 25, 2011, an examination was made of

Allegheny Casualty Company, NAIC Code 13285

a Pennsylvania domiciled property and casualty company, hereinafter referred to as "Company" or "ACC." The examination was conducted at the Company's main administrative office, located at One Newark Center, 20th Floor, Newark, New Jersey 07102.

A report of this examination is hereby respectfully submitted.

SCOPE OF EXAMINATION

The Company was last examined as of December 31, 2006.

This examination covered the five-year period from January 1, 2007 through December 31, 2011, and consisted of a general survey of the Company's business practices, management, and operations, and an evaluation of the Company's financial condition as of the latter date. Material subsequent events were also reviewed.

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

The format of this report is consistent with the current practices of the Department and the examination format prescribed by the NAIC. It is limited to a description of the Company, a discussion of financial items that are of specific regulatory concern, and a disclosure of other significant regulatory information.

For the years 2007 and 2008, the Certified Public Accounting ("CPA") firm of Brown Schultz Sheridan & Fritz ("BSSF") has provided an unqualified opinion on the Company's year-end financial statements based on statutory accounting principles. For the years 2009, 2010 and 2011, the Certified Public Accounting ("CPA") firm of Ernst and Young, LLP ("E&Y"), has provided an unqualified opinion on the Company's year-end financial statements based on statutory accounting principles. Relevant work performed by the CPA firm, during its annual audit of the Company, was reviewed during the examination and incorporated into the examination workpapers.

HISTORY

The Company was incorporated on April 15, 1936 and commenced business as Allegheny Mutual Casualty Company on April 21, 1936.

The policyholders unanimously voted to become a stock insurance company effective January 1, 1998. On December 31, 1997, the Company filed Amended and Restated Articles of Incorporation which converted it from a mutual to a stock insurance company in accordance with the requirements of the Insurance Company Mutual-to-Stock Conversion Act of 1995, 15 PA C.S.§1965, effective January 1, 1998.

Effective January 1, 1998, Allegheny Mutual Casualty Company converted from a mutual insurer to a stock insurer, and changed its name to Allegheny Casualty Company ("ACC"). As part of the conversion, each policyholder received shares of voting, no par common stock of the company representing 20,000 shares of the 50,000 authorized.

All eligible stockholders exchanged the ACC stock for an equivalent percentage of stock in The Chestnut Group ("TCG"), which resulted in TCG's ownership of 100% of the voting common stock of ACC.

Effective October 1, 2006, ACC amended its Articles of Incorporation to allow the Company to issue 35,000 shares of Series B Preferred Stock, $100 par value. The Company issued 20,000 shares to AIA Holdings, Inc. ("AIA") on December 28, 2006.

On April 2, 2007, AIA, ACC and TCG Shareholders entered into a Stock Purchase Agreement ("Agreement") whereby AIA would acquire 79.67369% of the issued and outstanding voting stock of TCG.

On May 14, 2007, the Insurance Department of the Commonwealth of Pennsylvania ("Department") received an initial application ("Application") from AIA for approval to acquire control of ACC. This application was subsequently approved by the Department on June 28, 2007.

On July 31, 2009, the Department received an initial application ("Application") from International Fidelity Insurance Company ("IFIC") for approval to acquire control of ACC. This application was subsequently approved by the Department on October 22, 2009.

On August 17, 2009, IFIC and the current shareholders of TCG entered into a Stock Purchase/Sale Agreement ("Agreement") whereby IFIC would acquire 100% of the issued and outstanding capital stock of TCG.

October 26, 2009, IFIC, Newark, New Jersey, closed the transaction with the purchase of 100% of the issued and outstanding common stock of TCG, the parent company of ACC, with an effective date of October 1, 2009.

The Company is currently authorized to transact those classes of insurance described in the Pennsylvania Insurance Company Law 40 P.S. § 382, Subsection (c), Paragraph (1) Fidelity and Surety.

MANAGEMENT AND CONTROL

CAPITALIZATION

As of the examination date, December 31, 2011, the Company's total capitalization was $18,505,753, consisting of 1,500,000 Series B, common capital shares, issued and outstanding with a par value of $1 per share amounting to $1,500,000; 12,000 Series A, non-voting, callable, cumulative, 10% preferred capital shares authorized and issued with a par value of $100 per share amounting to $1,200,000; 20,000 Series B, non-voting, callable, cumulative, 8% preferred capital shares authorized and issued with a par value of $100 per share amounting to $2,000,000; $1,000,000 in paid in and contributed surplus; and $14,065,753 in unassigned funds (surplus). During the prior examination periods, the Company had acquired 12,000 Series A, preferred capital shares at a cost of $1,260,000, to be retained as treasury stock. The total capitalization was offset by the $1,260,000 Series A, preferred capital shares of treasury stock.

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 (c), is $750,000 in capital and $375,000 in surplus. The Company has met all governing requirements throughout the examination period.

STOCKHOLDERS

The voting stock of the Company consists of 1,500,000 shares of common stock, the sole owner of which is TCG, a mid-stream holding company. IFIC owns 100% of the issued and outstanding common stock of TCG, the parent company of ACC.

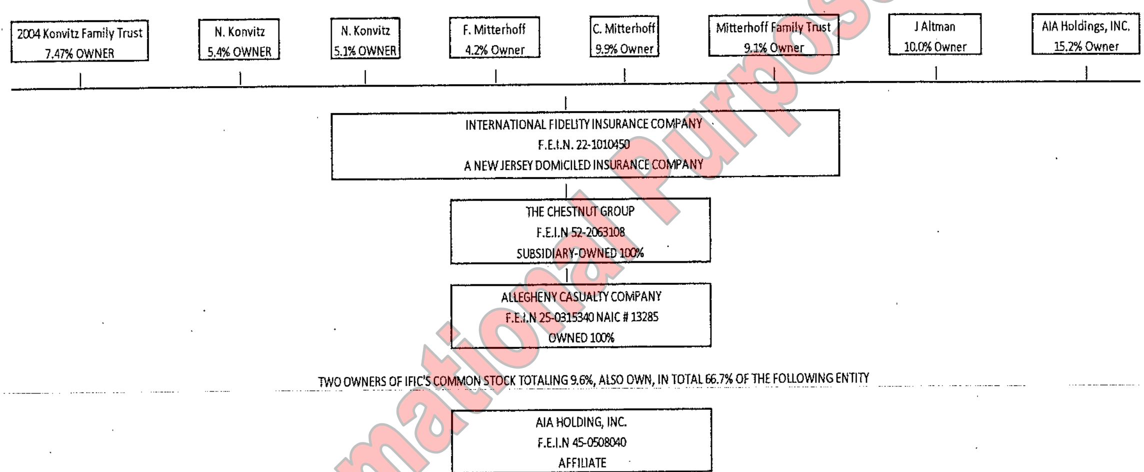
The non-voting stock of the Company consists of 12,000 Series A, non-voting, callable, cumulative, 10% preferred capital shares maintained as treasury stock and 20,000 Series B, non-voting, callable, cumulative, 8% preferred capital shares owned by an affiliated entity, AIA Holdings, Inc.

During the period under examination, the Company paid ordinary dividends to the former stockholders of $40,000 in 2008 and $445,000 in 2007. No ordinary or extraordinary dividends were paid in 2009, 2010 and 2011. The Board of Directors approved all ordinary dividend distributions. Insurance Department review of the ordinary dividends was noted.

INSURANCE HOLDING COMPANY SYSTEM

The Company meets the requirements for filing an insurance holding company system registration statement, in compliance with the Pennsylvania Insurance Company Law 40 P.S. §§ 991.1401-991.1413. An Annual Insurance Holding Company System Registration Statement and various amendments have been filed with the Department for the period under examination.

The following organizational chart depicts the Company's relationship within the holding company system at December 31, 2011:



At December 31, 2011, members of the holding company system include the following entities and individuals briefly described:

Francis L. Mitterhoff ("Mitterhoff") is an individual with his principal place of business located in Newark, New Jersey. Mitterhoff is considered an Ultimate Controlling Person of the Company. Mitterhoff owns 4.2% of IFIC common stock and 33.33% of AIA Holdings, Inc. which owns 15.2% of IFIC common stock.

Norman R. Konvitz and Nina Konvitz, husband & wife (together "Konvitz") are individuals with their principal place of business located in Newark, New Jersey. Konvitz is considered an Ultimate Controlling Person of the Company. Konvitz owns 10.48% of IFIC common stock and 33.33% of AIA Holdings, Inc. which owns 15.2% of IFIC common stock.

Brian N. Nairin ("Nairin") is an individual with his principal place of business located in Calabasas, California. Nairin is considered an Ultimate Controlling Person of the Company. Nairin owns 33.33% of AIA Holdings, Inc. which owns 15.2% of IFIC common stock.

International Fidelity Insurance Company is a New Jersey domiciled property and casualty insurance company, and the owner of 100% of the stock of TCG. International Fidelity Insurance Company is the ultimate parent of ACC.

TCG is a Delaware corporation organized for the purpose of purchasing and holding all of the stock of the converted stock insurance company and is the direct parent and 100% stockholder of ACC.

AIA Holdings, Inc. is a Delaware corporation, incorporated in 2003 for the purpose of acting as an agent, operating and managing the bail business of licensed insurers. AIA Holdings, Inc. owns 15.2% of the capital stock of International Fidelity Insurance Company, which owns 100% of TCG.

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, 2011:

Name and Address	Principal Occupation
Robert William Minster Princeton, NJ	President Allegheny Casualty Company
Francis Louis Mitterhoff Bernardsville, NJ	Vice-President Allegheny Casualty Company
Brian Nathan Nairin Hidden Hills, CA	Vice-President Allegheny Casualty Company
Vincent Mark Riccordella Long Valley, NJ	Secretary Allegheny Casualty Company
Norman Roger Konvitz Newark, NJ	Executive Vice President International Fidelity Insurance Company
Michael Myer Abergel Hidden Hills, CA	President/Owner Abergel & Associates, Inc.
Jerry Wayne Watson Calabasas, CA	Chief Legal Officer AIA Holdings, Inc.
Mark Paul Francis Morganville, NJ	Chief Financial Officer AIA Holdings, Inc.

The Board of Directors shall be comprised of at least seven (7) members. The Directors are to be elected annually at the Company's Annual Shareholders' Meeting. A review of the minutes of the meetings of the Company's Board of Directors, Shareholders and Committees indicated that the Company's Shareholders had performed the appointment of the Board of Directors, as required in the Company By-Laws, through September 29, 2010. Limited documentation memorializing the Board of Director and Committee meetings is available after September 29, 2010 so the Department examiners were not able to verify that the Directors were elected annually at the Annual Shareholders' Meeting as required in the Company's By-Laws or that appropriate Board and committee meetings were held in accordance with the By-Laws subsequent to September 29, 2010.

It is recommended that the Company's Shareholders, Board of Directors and its committees meet in accordance with the Company's By-Laws and that a complete and accurate record of all meetings be kept in accordance with 15 Pa. C.S. § 1508(a).

Prior to becoming qualified, all Directors must file a written acceptance of trust and conflict of interest statement with the Secretary. The Board's Secretary administers the Company's conflict of interest certification. All members of the Board of Directors sign a Conflict of Interest that certifies he or she has no material interest or affiliation which is in or likely to conflict with the official duties of such person as an officer, director, or employee of Allegheny Casualty Company.

The Board has the responsibility of appointing several committees in accordance with the Company's By-Laws. Limited documentation memorializing the Board of Director or Committee meetings is available after September 29, 2010 so the Department examiners were not able to verify that the Company has nominated and appointed the appropriate committees as required by the Company's By-Laws after September 29, 2010.

It is recommended that the Company's Board of Directors appoint the appropriate committees in accordance with the Company's By-Laws.

COMMITTEES

According to the By-Laws of the Company, the Board of Directors may designate one or more committees, each of which is to consist of one or more directors as may be designated by the Board.

At the Board of Directors meeting held on December 29, 2009, the following individuals were appointed to serve on committees for the calendar year 2010.

Actuarial & Audit Committee

Vincent Mark Riccordella
Mark P. Francis

Investment Committee

Vincent Mark Riccordella
John C. Soff
Robert W. Minster

Nominating Committee

Jerry W. Watson
Michel M. Abergel

Pension Committee

Vincent Mark Riccordella
Mark P. Francis
Jerry W. Watson

A review of the Board minutes indicated that the Company has not appointed committees in accordance with the By-Laws since December 29, 2009. Please refer to recommendation under previous section of this report.

Pennsylvania Holding Company Law, namely, 40 P.S. § 991.1405 (c) (3) Standards of transactions between insurer and affiliate (within the holding company system) states, in part, that "not less than one-third of the directors of any domestic insurer and not less than one-third of the members of each committee of the board of directors of any domestic insurer shall be persons who are not officers or employees of such insurer or of any entity controlling, controlled by or under common control with such insurer and who are not beneficial owners of a controlling interest in the voting stock of such insurer of any such entity. At least one such person must be included in any quorum for the transaction of business at any meeting of the board of directors or any committee thereof".

Likewise, Pennsylvania Holding Company Law, 40 P.S. § 991.1405 (c) (4) Standards of transactions between affiliates (within the holding company system), further states that "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 and who are not beneficial owners of a controlling interest in the voting stock of the insurer or any such entity. The committee or committees shall have the responsibility for recommending the selection of independent certified public accountants, reviewing the insurer's financial condition, the scope and results of the independent audit and any internal audit, nominating candidates for director for election by 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."

Pennsylvania Holding Company Law, 40 P.S. § 991.1405 (c) (5) proclaims that the cited laws above shall not apply to a domestic insurer if the person controlling such insurer is an insurer or a publicly held corporation having a board of directors and committees thereof which already meet the requirements of paragraphs (3) and (4).

The Company communicated that it has designated its ultimate parent's (IFIC) Audit, Nominating and Compensation Committee with the responsibility to perform the required committee functions for the Company. A review of IFIC's corporate minutes indicates that the IFIC's Audit, Nominating and Compensation Committee has not performed the required committee functions for ACC, in accordance with Pennsylvania Insurance Company Law, 40 P.S. § 991.1405(c) (3), (4), (4.1) and (5).

It is recommended that the Company comply with the provisions of Pennsylvania Insurance Company Law 40 P.S. § 991.1405(c) (3), (4), (4.1) and (5). The Company's By-Laws should accurately reflect specific designated authorities and responsibilities of the committee or committees that are established by the Board in compliance with this recommendation.

Also, in accordance with the Company's written Investment Policy, the Company's Board shall appoint an Investment Committee, comprised of three (3) directors, one of which shall be a non-employee director. A review of the minutes indicates that the Company has not appointed committees in accordance with the By-Laws since December 29, 2009.

It is recommended that the Company's Board appoint an Investment Committee in accordance with the Company's written Investment Policy in order to perform the functions as set forth therein or properly change the Company's Investment Policy to be consistent with its practices.

OFFICERS

As of the examination date, December 31, 2011, the following officers were serving:

Name	Title
Robert William Minster	President
Maria Dulce Costa	Treasurer
Vincent Mark Riccordella	Secretary
Francis Louis Mitterhoff	Vice President
Brian Nathan Nairin	Vice President

A review of the Board of Directors', Annual Shareholders' and Committee minutes does not provide evidence that the Company's Board has performed the annual appointment of the Company Officers as required in the Company By-Laws.

It is recommended that the Company's Board annually appoint the Company's officers in accordance with the Company's By-Laws.

CORPORATE RECORDS

MINUTES

A compliance review of corporate minutes through September 29, 2010, revealed that the annual meeting of the Company's stockholders was held in compliance with its By-Laws. The directors were elected at the Annual Stockholders' Meeting in compliance with the Company's By-Laws. The actions of the Company's directors, officers and committees were reviewed and approved at the annual meetings. Quorums were present at all meetings of stockholders, directors and officers. The Company's officers were duly appointed at the Annual Board of Directors' meetings. Actions taken by the Investment Committee were reviewed and approved, as required.

Limited documentation memorializing the Board of Director or Committee meetings is available after September 29, 2010. Shortly after the sale of the Company in October 2009 to IFIC, the Company no longer prepared and maintained written Board and Committee minutes and records in accordance with Corporation Business Law Title 15 P.S.§ 1508(a). This non-compliance results in significant overarching effects on the Company's compliance with statutorily required actions, as well as, actions required and outlined in corporate documents, including evidential matter to ensure the nomination and appointment of the Board of Directors, Officers, Committees, Actuary and CPA.

ARTICLES OF INCORPORATION

During the period under examination and as a result of the sale of the Company to IFIC, the Company amended their Articles of Incorporation to reflect a change of address for the Company's Statutory and Main Administrative Offices.

BY-LAWS

During the period under examination the Company amended Section 3.1 of its By-Laws to read: The Board of Directors shall elect a President, who shall also be one of the Directors; a Secretary/Treasurer; a First Vice President; a Regional Vice President; one or more Assistant Secretaries and such other officers as it deems advisable. All such officers shall serve until their successors are duly elected. The President and Secretary/Treasurer shall be different persons.

SERVICE AND OPERATING AGREEMENTS

TAX ALLOCATION AGREEMENT

The Company became party to a Tax Allocation Agreement between International Fidelity Insurance Company and ACC in respect to U.S. Federal Income Taxes. The Agreement was made on October 1, 2009 and effective each taxable year ending on or after September 30, 2009.

The intent of the tax allocation agreement is to designate IFIC as its agent and to provide a fair and equitable allocation of responsibilities, liabilities and benefits between the entities. According to the agreement, the tax charge (refund) shall be the amount that the insurer would have paid (or received) as if it had filed a separate return with the Internal Revenue Service.

The tax allocation agreement requires quarterly settlement to be made within thirty days of the filing or upon completion of calculation of estimated taxes. The Company appears to be complying with the terms of the Agreement. The Agreement appears to satisfy fair and reasonable provisions of Pennsylvania Insurance Company Law, 40 P.S. § 991.1405(a)(1).

EXPENSE SHARING AGREEMENT

The Company is party to an Expense Sharing Agreement between IFIC and ACC. This Agreement is effective January 1, 2010.

The intent of the Expense Sharing Agreement is for IFIC to provide administrative support, office space and necessary equipment to conduct and support the Company's business activities. The Expense Sharing Agreement requires quarterly reporting and invoicing. During 2011, the Company paid IFIC expenses specific to this agreement in the amount of $1,493,523.

Upon review of the Agreement, no settlement provisions are evident.

It is recommended that the Company perform a review and amend the Expense Sharing Agreement to include the settlement requirements as set forth in Statement of Statutory Accounting Principles ("SSAP") #25 Accounting for and Disclosures about Transactions with Affiliates and Other Related Parties.

MANAGEMENT AGREEMENT

The Company is party to an exclusive Management Agreement with AIA Holdings, Inc. ("AIA"), a closely held non-insurance affiliate and stockholder in IFIC. This Agreement was entered into on October 1, 2007 and details the responsibilities of the parties related to the production and management of bail bond business by AIA.

According to the Agreement, the Company shall pay AIA a fee equal to the total out-of-pocket expenses directly related to the Company's business incurred by AIA plus 6.0% of the amount of such costs and expenses. The fee is payable within five (5) days following the end of each calendar month. During 2011, AIA processed $20,762,566 in bail bond premiums for the Company and received a related management fee of $17,240,528, or 83.0%, of Gross Bail Bond Premium as a management fee for the Bail Bond program.

A review indicates that AIA maintains all records for the bail bond program and provides a report and payment of $1.80 per $1,000 of penal liability, plus applicable premium taxes, to the Company within ten (10) business days from the end of the month. The payment terms and process vary from the original Agreement and, therefore, the Company is not performing pursuant to the terms of the agreement.

It is recommended that the Company perform a review of the Management Agreement and Bail Bond Program and all other applicable agreements and update them as necessary to

comply with the provisions of Pennsylvania Insurance Company Law, 40 P.S.§ 991.1405(a)(1).

During our review of the Bail Bond Program and the Management Agreement it was also noted that the Management Agreement permits AIA to manage "part" of the Company's business, therefore, it appears that AIA meets the definition of a "manager", as AIA manages all or part of the insurance business of an insurer and does not act as an agent for such insurer, which requires a separate license.

It is recommended that the Company perform a review of the Management Agreement and Bail Bond Program including an assessment of the need for AIA to be licensed as a Manager pursuant to Pennsylvania Insurance Company Law 40 P.S. § 310.1, et. seq., and provide the Department with a written assessment of the Company's findings.

INDEMNITY AGREEMENT

The Company is party to an Indemnity Agreement with AIA Holdings, Inc. This Agreement provides for indemnification of the Company against losses related to bail bonds produced by AIA Holdings, Inc. The Company appears to be complying with the terms of the Agreement. The Agreement appears to satisfy fair and reasonable provisions of Pennsylvania Insurance Company Law, 40 P.S. § 991.1405(a)(1).

CONSULTING AGREEMENT

The Company is party to a consulting agreement with Brian N. Nairin, President of AIA Holdings, Inc. This Agreement provides for certain surety insurance consulting expertise for the Company. The Company appears to be complying with the terms of the Agreement. The Agreement appears to satisfy fair and reasonable provisions of Pennsylvania Insurance Company Law, 40 P.S. § 991.1405(a)(1).

RECIPROCAL HOLD HARMLESS AGREEMENT

The Company is party to a Reciprocal Hold Harmless Agreement with IFIC. This Agreement details the terms and responsibilities of each party related to Co-Surety or any other bonds issued by the request of the other. This Agreement does not apply to bail bonds. The Company appears to be complying with the terms of the Agreement. The Agreement appears to satisfy fair and reasonable provisions of Pennsylvania Insurance Company Law, 40 P.S. § 991.1405(a)(1).

REINSURANCE

CEDED

The Company maintained reinsurance coverage for contract surety business only. No bail bonds underwritten are subject to reinsurance. The reinsurance policy in-force at December 31, 2011 was as follows:

Reinsurer:	International Fidelity Insurance Company
Type of contract:	100% quota-share participation
Intermediary:	None
Effective date:	January 1, 2010
Term:	Continuous until either party provides thirty (30) days prior written notice and approval is granted by the Pennsylvania Insurance Department and New Jersey Department of Banking and Insurance.
Business covered:	Only business written and classified as Surety.
Company's retention:	N/A
Reinsurance limits:	Any and all bonds on or after January 1, 2010 issued by the Company as surety and utilizing the Company's Powers of Attorney.
Ceding Commission:	3.0%

The agreement contains an appropriate insolvency and arbitration clauses.

ASSUMED

The Company assumed no reinsurance coverage during the examination period.

TERRITORY AND PLAN OF OPERATIONS

The Company has acquired licenses in Maine, Massachusetts, Nebraska, New Hampshire, North Dakota, Oregon, Rhode Island, Vermont, and Puerto Rico since the last examination. The Company is now licensed in 52 states or territories, as follows:

Alabama	Alaska	Arizona
Arkansas	California	Colorado
Connecticut	Delaware	District of Columbia
Florida	Georgia	Hawaii
Idaho	Illinois	Indiana

Iowa	Kansas	Kentucky
Louisiana	Maine	Maryland
Massachusetts	Michigan	Minnesota
Mississippi	Missouri	Montana
Nebraska	Nevada	New Hampshire
New Jersey	New Mexico	New York
North Carolina	North Dakota	Ohio
Oklahoma	Oregon	Pennsylvania
Rhode Island	South Carolina	South Dakota
Tennessee	Texas	Utah
Vermont	Virginia	Washington
West Virginia	Wisconsin	Wyoming
Puerto Rico		

The Company's business has primarily revolved around the bail bonds. Bail operations are managed through an extensive agency system, managed by affiliate, AIA, through a non-exclusive Management Agreement with the Company. AIA and its agency system execute indemnification agreements and a collateral system to protect the Company against all potential losses.

Since the last examination, the Company has added a Non-Standard (Specialty) Surety product to supplement its stable Bail operations. This Non-Standard (Specialty) Surety business is marketed and managed through a network of regional offices and agents in localized regions of the country. The branch offices are located as follows: Chicago, Illinois; Dallas, Texas; Denver, Colorado; Newark, New Jersey; Philadelphia, Pennsylvania; San Diego, California; and Tallahassee, Florida.

In order to minimize the risk and promote growth within the Non-Standard (Specialty) Surety line of business, the Company has entered into a 100% reinsurance agreement with its parent, IFIC, who in turn has a Quota Share treaty with three (3) A-rated reinsurance carriers.

The following is the distribution of the Company's lines of business by percentage of total net written premium for the last year under examination:

Line of Business	Direct and Assumed Premium	Ceded Premium	Net Written Premium	Percentage of Total
December 31, 2011				
Surety	$ 31,045,031	$ 9,860,612	$ 21,184,419	100.0%
Totals	$ 31,045,031	$ 9,860,612	$ 21,184,419	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	$ 134,362,297	100.0 %
Losses incurred	$ 1,250,974	0.9 %
Loss expenses incurred	401,625	0.3 %
Other underwriting expenses incurred	128,575,677	95.7 %
Net underwriting gain or (loss)	4,134,021	3.1 %
Totals	$ 134,362,297	100.0 %

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

	2011	2010	2009	2008	2007
Admitted assets	$ 33,462,944	$ 29,830,099	$ 24,505,769	$ 22,763,706	$ 22,171,287
Liabilities	$ 14,957,191	$ 11,312,793	$ 7,075,279	$ 5,383,662	$ 5,910,977
Surplus as regards policyholders	$ 18,505,753	$ 18,517,306	$ 17,430,490	$ 17,380,044	$ 16,260,310
Gross premium written	$ 31,045,031	$ 23,264,829	$ 29,106,339	$ 33,423,456	$ 31,600,185
Net premium written	$ 21,184,419	$ 20,745,799	$ 27,559,465	$ 33,219,767	$ 29,860,061
Underwriting gain/(loss)	$ 80,858	$ 868,216	$ 130,819	$ 1,395,288	$ 1,658,840
Investment gain/(loss)	$ 551,052	$ 472,698	$ 587,620	$ 532,869	$ 742,139
Other gain/(loss)	$ 1	$ 4	$ 36,802	$ 22,750	$ 22,000
Net income	$ 521,650	$ 1,607,698	$ 256,926	$ 1,308,633	$ 1,648,175

ACCOUNTS AND RECORDS

The Company maintains its accounts and records at their main administrative offices at One Newark Center, 20th Floor, Newark, New Jersey 07102. The Company, as a purchaser of the services, has its accounting, premium, and claim processing records kept on an automated and partially integrated accounting system with respect to the general ledger, trial balance, receivables, and payables. All relevant files and records were made available during the examination.

PENDING LITIGATION

The Company is involved in various legal and compliance actions and proceedings that arise in the ordinary course of business. A review of the legal representation letter from both internal and external legal counsel indicated that counsel has not given substantive attention to, nor represented the Company in connection with material litigation or other loss contingencies which would be required to be disclosed in the statutory financial statements of the Company.

FINANCIAL STATEMENTS

The financial condition of the Company, as of December 31, 2011, 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,

	2011	2010	2009	2008	2007
Bonds	$ 9,476,857	$ 11,457,745	$ 14,620,165	$ 14,030,608	$ 13,408,574
Preferred stocks	1,500,000	0	0	0	0
Real estate	0	40,334	43,346	39,479	35,734
Cash, cash equivalents, and short term investments	19,156,983	16,040,113	7,117,963	7,435,851	7,954,346
Subtotals, cash and invested assets	30,133,840	27,538,192	21,781,474	21,505,938	21,398,654
Investment income due and accrued	205,679	183,328	195,614	189,248	183,341
Premiums and agents' balances due	1,523,431	880,059	536,591	488,087	226,904
Amounts recoverable from reinsurers	534,514	0	294,900	0	3,873
Net deferred tax asset	892,309	1,092,978	1,445,940	241,850	267,837
Electronic data processing equipment and software	0	58,283	174,850	291,417	76
Receivable from parent, subsidiaries and affiliates	173,171	77,259	4,016	2,004	5,328
Aggregate write-ins for other than invested assets	0	0	72,384	45,162	85,274
Total	$ 33,462,944	$ 29,830,099	$ 24,505,769	$ 22,763,706	$ 22,171,287
Losses	$ 288,872	$ 201,581	$ 915,663	$ 99,946	$ 16,408
Loss adjustment expenses	57,776	40,316	237,673	23,270	2,296
Commissions payable, contingent commissions and other similar charges	240,558	122,408	0	0	0
Other expenses	115,200	728	448,809	561,273	442,676
Taxes, licenses and fees	412,815	259,250	276,675	223,840	150,932
Current federal and foreign income taxes	443,878	332,009	678,246	72,515	202,679
Unearned premiums	2,859,897	3,033,217	3,096,864	3,537,026	3,930,651
Advance premium	0	0	35,333	38,555	0
Ceded reinsurance premiums payable (net of ceding commissions)	2,158,920	571,918	158,608	105,348	1,822
Amounts withheld or retained by company for account of others	8,374,781	5,837,893	1,227,408	502,432	604,913
Provision for reinsurance	3,782	211	0	0	0
Payable to parent, subsidiaries and affiliates	0	912,570	0	0	0
Aggregate write-ins for liabilities	712	692	0	219,457	558,600
Total liabilities	14,957,191	11,312,793	7,075,279	5,383,662	5,910,977
Common capital stock	1,500,000	1,500,000	1,500,000	1,500,000	1,500,000
Preferred capital stock	3,200,000	3,200,000	3,200,000	3,200,000	3,200,000
Gross paid in and contributed surplus	1,000,000	1,000,000	1,000,000	1,000,000	1,000,000
Unassigned funds (surplus)	14,065,753	14,077,306	12,990,490	12,940,044	11,820,310
Less treasury stock at cost - preferred	1,260,000	1,260,000	1,260,000	1,260,000	1,260,000
Surplus as regards policyholders	18,505,753	18,517,306	17,430,490	17,380,044	16,260,310
Totals	$ 33,462,944	$ 29,830,099	$ 24,505,769	$ 22,763,706	$ 22,171,287

Comparative Statement of Income
For the Year Ended December 31,

Underwriting Income	2011	2010	2009	2008	2007
Premiums earned	$ 21,357,738	$ 20,809,446	$ 27,999,627	$ 33,613,392	$ 30,582,094
Deductions:					
Losses incurred	259,490	(204,357)	1,112,303	83,538	0
Loss expenses incurred	160,133	(21,560)	234,088	25,577	3,387
Other underwriting expenses incurred	20,857,257	20,167,147	26,522,417	32,108,989	28,919,867
Total underwriting deductions	21,276,880	19,941,230	27,868,808	32,218,104	28,923,254
Net underwriting gain or (loss)	80,858	868,216	130,819	1,395,288	1,658,840
Investment Income					
Net investment income earned	365,331	470,918	596,861	528,917	728,333
Net realized capital gains or (losses)	185,721	1,780	(9,241)	3,952	13,806
Net investment gain or (loss)	551,052	472,698	587,620	532,869	742,139
Other Income					
Aggregate write-ins for miscellaneous income	1	4	36,802	22,750	22,000
Total other income	1	4	36,802	22,750	22,000
Net income before dividends to policyholders and before federal and foreign income taxes	631,911	1,340,919	755,241	1,950,907	2,422,979
Federal and foreign income taxes incurred	110,261	(266,779)	498,315	642,274	774,804
Net income	$ 521,650	$ 1,607,698	$ 256,926	$ 1,308,633	$ 1,648,175

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

	2011	2010	2009	2008	2007
Surplus as regards policyholders,					
December 31, previous year	$ 18,517,306	$ 17,430,490	$ 17,380,044	$ 16,260,310	$ 15,032,680
Net income	521,650	1,607,698	256,926	1,308,633	1,648,175
Change in net deferred income tax	204,085	(477,428)	(151,483)	(28,933)	(43,825)
Change in nonadmitted assets	(733,717)	(43,243)	(54,997)	(119,966)	68,280
Change in provision for reinsurance	(3,571)	(211)	0	0	0
Dividends to stockholders	0	0	0	(40,000)	(445,000)
Change in surplus as regards policyholder for the year	(11,553)	1,086,816	50,446	1,119,734	1,227,630
Surplus as regards policyholders,					
December 31, current year	$ 18,505,753	$ 18,517,306	$ 17,430,490	$ 17,380,044	$ 16,260,310

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

	2011	2010	2009	2008	2007
Cash from Operations					
Premiums collected net of reinsurance	$ 21,797,914	$ 20,576,308	$ 27,269,321	$ 33,065,983	$ 29,959,494
Net investment income	428,868	574,178	670,178	582,125	772,886
Miscellaneous income	(2,639)	351,076	36,802	22,750	22,000
Total income	22,224,143	21,501,562	27,976,301	33,670,858	30,754,380
Benefit and loss related payments	849,390	351,352	296,586	0	0
Commissions, expenses paid and aggregate write-ins for deductions	20,471,071	20,229,071	26,514,988	32,006,587	29,122,794
Federal and foreign income taxes paid (recovered)	94,068	260,703	1,251,113	774,474	790,464
Total deductions	21,414,529	20,841,126	28,062,687	32,781,061	29,913,258
Net cash from operations	809,614	660,436	(86,386)	889,797	841,122
Cash from Investments					
Proceeds from investments sold, matured or repaid:					
Bonds	1,895,000	3,343,099	4,263,230	5,695,000	2,150,000
Real estate	321,730	0	0	0	0
Miscellaneous proceeds	0	(1)	0	0	0
Total investment proceeds	2,216,730	3,343,098	4,263,230	5,695,000	2,150,000
Cost of investments acquired (long-term only):					
Bonds	0	267,656	4,928,212	6,368,387	2,876,754
Stocks	1,500,000	0	0	0	0
Total investments acquired	1,500,000	267,656	4,928,212	6,368,387	2,876,754
Net cash from investments	716,730	3,075,442	(664,982)	(673,387)	(726,754)
Cash from Financing and Miscellaneous Services					
Other cash provided (applied):					
Borrowed funds received or (repaid)	0	0	0	0	(3,536)
Dividends to stockholders (paid)	0	0	0	40,000	445,000
Other cash provided or (applied)	1,590,526	5,186,272	433,480	(694,905)	104,922
Net cash from financing and miscellaneous sources	1,590,526	5,186,272	433,480	(734,905)	(343,614)
Reconciliation of cash and short-term investments:					
Net change in cash and short-term investments	3,116,870	8,922,150	(317,888)	(518,495)	(229,246)
Cash and short-term investments:					
Beginning of the year	16,040,113	7,117,963	7,435,851	7,954,346	8,183,592
End of the year	$ 19,156,983	$ 16,040,113	$ 7,117,963	$ 7,435,851	$ 7,954,346

SUMMARY OF EXAMINATION CHANGES

There were no examination changes to the preceding financial statements as a result of this examination.

NOTES TO FINANCIAL STATEMENTS

ASSETS

INVESTMENTS

As of December 31, 2011, the Company's invested assets were distributed as follows:

	Amount	Percentage
Bonds	$ 9,476,857	31.4 %
Preferred stocks	1,500,000	5.0 %
Cash	18,596,982	61.7 %
Short-term investments	560,001	1.9 %
Totals	$ 30,133,840	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	$ 10,036,858	100.0 %
Totals	$ 10,036,858	100.0 %

Years to Maturity	**Amount**	**Percentage**
1 year or less	$ 2,915,411	29.0 %
2 to 5 years	6,051,614	60.3 %
6 to 10 years	1,069,833	10.7 %
Totals	$ 10,036,858	100.0 %

The cash, cash equivalents and short-term investments consisted of checking accounts, money market accounts and short-term U.S. issued government bonds. At December 31, 2011, all short-term investments owned by the Company, were held under a Custodial Agreement with The Bank of New York Mellon. The agreement was reviewed and found to be non-compliant with 31 Pa. Code §148a.3. Specifically, the agreement lacks the necessary provisions of 31 Pa. Code § 148a.3(b).

It is recommended that the Company amend its custodial agreement to comply with 31 Pa. Code § 148a.3(b).

Pennsylvania Insurance Company Law 40 P.S. § 653b (b) requires insurers to have a formal investment plan which shall be updated on an annual basis as authorized by the Board of Directors. A review of the Board of Directors minutes indicates that the Company's investment policy was reviewed and approved on an annual basis by the Board through September 29, 2010. The last documented board or committee minutes for the Company were dated September 29, 2010. Subsequent to September 29, 2010 the Company did not maintain appropriate documentation to provide evidence that the investment policy was reviewed and approved on an annual basis by the Board.

It is recommended that the Company comply with the provisions of Pennsylvania Insurance Company Law 40 P.S. § 653b (b).

The Company, at December 31, 2011, appears to still be following the investment policy that was reviewed and ratified by the Board on December 29, 2009.

LIABILITIES

LOSS AND LOSS ADJUSTMENT EXPENSE RESERVES

The Company reported Losses of $288,872 and Loss Adjustment Expenses ("LAE") of $57,776 on the December 31, 2011 Annual Statement.

For 2007, the Company requested an exemption from filing the Statement of Actuarial Opinion ("Opinion"), which was approved by the Department. For the remainder of the years under examination, the Board appointed three different independent qualified actuaries to provide the Opinion on the Company's loss and LAE reserve amounts carried on the balance sheet at each respective year-end date, as follows:

December 31,	Actuary	Firm
2008	Steven J. Regnier, ACAS, MAAA	Regnier Consulting Group, Inc.
2009	Christopher Diamantoukos, FCAS, MAAA	Ernst & Young, LLP
2010-2011	Dennis R. Henry, FCAS, MAAA	The Actuarial Advantage, Inc.

On December 30, 2010, the Board appointed Dennis R. Henry, FCAS, MAAA of The Actuarial Advantage, Inc. as the Company's appointed actuary replacing Christopher Diamantoukos, FCAS, MAAA of Ernst & Young, LLP. There were no disagreements, either resolved or unresolved to Mr. Diamantoukos's satisfaction, related to the content of the Opinion on matters of the risk of material adverse deviation, required disclosures, scope, procedures or data quality. We have affirmed that each of the actuaries listed above are credentialed casualty actuaries, who maintain membership in the American Academy of Actuaries.

For each year-end reflected above, each respective actuary rendered an Opinion concluding that the Company's reserves made a reasonable provision for unpaid loss and LAE obligations of the Company under the terms of its policies and agreements.

The Department examination team performed a risk focused review of the Company's reserve process underlying the carried reserves in conjunction with this exam. As a result of this review, the Department examination team obtained sufficient evidence to support that the Company's loss and LAE reserves, as of December 31, 2011, appear to be reasonable.

SUBSEQUENT EVENTS

There were no events subsequent to the balance sheet date that require disclosure in this examination report.

RECOMMENDATIONS

PRIOR EXAMINATION

The prior examination report did not contain any recommendations.

CURRENT EXAMINATION

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

1. It is recommended that the Company's Shareholders, Board of Directors and its committees meet in accordance with the Company's By-Laws and that a complete and accurate record of all meetings be kept in accordance with 15 Pa. C.S. § 1508(a). (See Board of Directors, page 5)

2. It is recommended that the Company's Board of Directors appoint the appropriate committees in accordance with the Company's By-Laws. (See Board of Directors, page 5)

3. It is recommended that the Company comply with the provisions of Pennsylvania Insurance Company Law 40 P.S. § 991.1405(c) (3), (4), (4.1) and (5). The Company's By-Laws should accurately reflect specific designated authorities and responsibilities of the committee or committees that are established by the Board in compliance with this recommendation. (See Committees, page 6)

4. It is recommended that the Company's Board appoint an Investment Committee in accordance with the Company's written Investment Policy in order to perform the functions as set forth therein or properly change the Company's Investment Policy to be consistent with its practices. (See Committees, page 6)

5. It is recommended that the Company's Board annually appoint the Company's officers in accordance with the Company's By-Laws. (See Officers, page 8)

6. It is recommended that the Company perform a review and amend the Expense Sharing Agreement to include the settlement requirements as set forth in Statement of Statutory Accounting Principles ("SSAP") #25 Accounting for and Disclosures about Transactions with Affiliates and Other Related Parties. (See Service and Operating Agreements, page 9)

7. It is recommended that the Company perform a review of the Management Agreement and Bail Bond Program and all other applicable agreements and update them as necessary to comply with the provisions of Pennsylvania Insurance Company Law, 40 P.S.§ 991.1405(a)(1). (See Service and Operating Agreements, page 9)

8. It is recommended that the Company perform a review of the Management Agreement and Bail Bond Program including an assessment of the need for AIA to be licensed as a Manager pursuant to Pennsylvania Insurance Company Law 40 P.S. § 310.1, et. seq., and provide the Department with a written assessment of the Company's findings. (See Service and Operating Agreements, page 9)

9. It is recommended that the Company amend its custodial agreement to comply with 31 Pa. Code § 148a.3 (b). (See Investments, page 20)

10. It is recommended that the Company comply with the provisions of Pennsylvania Insurance Company Law 40 P.S. § 653b (b). (See Investments, page 20)

CONCLUSION

As a result of this examination, the financial condition of the Company, as of December 31, 2011, was determined to be as follows:

	Amount	Percentage
Admitted assets	$ 33,462,944	100.0 %
Liabilities	$ 14,957,191	44.7 %
Surplus as regards policyholders	18,505,753	55.3 %
Total liabilities and surplus	$ 33,462,944	100.0 %

Since the previous examination, made as of December 31, 2011, the Company's assets increased by $11,668,675, its liabilities increased by $8,195,602, and its surplus increased by $3,473,073.

This examination was conducted by Barbara Kowalski, William Umbaugh, CFE, CISA, AES and Joseph Evans, CFE, with the latter in charge.

Respectfully

Annette B. Szady

Annette B. Szady, CPA
Director, Bureau of Financial Examinations

Joseph Evans -cdd

Joseph Evans, 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.