

BEFORE THE DEPUTY INSURANCE COMMISSIONER
OF THE
COMMONWEALTH OF PENNSYLVANIA

In Re: : Pursuant to Sections 1401 and 1402 of
: the Insurance Holding Companies Act,
Application of PMA Capital Corporation : Article XIV of the Insurance Company
Requesting Exemption from the : Law of 1921, Act of May 17, 1921, P.L.
Requirements of 40 P.S. §991.1402 for the : 682, as amended, 40 P.S. §§991.1401 and
Modification of the Insurance Holding : 991.1402
Company System, which includes :
Manufacturers Alliance Insurance :
Company, Pennsylvania Manufacturers :
Indemnity Company and Pennsylvania :
Manufacturers' Association Insurance :
Company : Order No. ID-RC-04-10

DECISION AND ORDER

AND NOW, on this 25th day of June, 2004, Stephen J. Johnson, Deputy Insurance Commissioner of the Commonwealth of Pennsylvania ("Deputy Commissioner"), hereby makes the following Decision and Order:

Pursuant to the Insurance Holding Companies Act and in consideration of the documents, presentations and reports received, as well as other inquiries and studies as permitted by law, the Deputy Commissioner hereby makes the following findings of fact:

FINDINGS OF FACT

Identity of Involved Persons

1. Manufacturers Alliance Insurance Company ("MAIC") is a domestic stock casualty insurance company organized under the laws of the Commonwealth of Pennsylvania with its principal place of business in Blue Bell, Pennsylvania.
2. Pennsylvania Manufacturers Indemnity Company ("PMIC") is a domestic stock casualty insurance company organized under the laws of the Commonwealth of Pennsylvania with its principal place of business in Blue Bell, Pennsylvania.

3. Pennsylvania Manufacturers' Association Insurance Company ("PMAIC") is a domestic stock casualty insurance company organized under the laws of the Commonwealth of Pennsylvania with its principal place of business in Blue Bell, Pennsylvania.
4. MAIC, PMIC and PMAIC share results through an intercompany pooling agreement ("Pool Companies").
5. PMA Capital Insurance Company ("PMA Re") is a domestic stock casualty reinsurance company organized under the laws of the Commonwealth of Pennsylvania with its principal place of business in Philadelphia, Pennsylvania.
6. PMA Re directly holds 100% of the outstanding capital stock of the Pool Companies.
7. PMA Capital Corporation ("PMA") is an insurance holding company organized under the laws of the Commonwealth of Pennsylvania with its principal place of business in Philadelphia, Pennsylvania.
8. PMA directly holds 100% of the outstanding capital stock of PMA Re.
9. The stock of PMA is publicly traded on the NASDAQ National Market.
10. No person, directly or indirectly, controls 10% or more of the voting securities of PMA.
11. PMA is the sole ultimate controlling person of the Pool Companies.

Filing of the Application

12. On March 30, 2004, the Insurance Department of the Commonwealth of Pennsylvania ("Department") received an initial request (which together with all material subsequently received in connection therewith is collectively referenced as "Application") from PMA for approval to modify the structure of its holding company system to transfer direct control of 100% of the outstanding capital stock of the Pool Companies from PMA Re to PMA ("Proposed Transfer").
13. The Insurance Holding Companies Act, Article XIV of the Insurance Company Law of 1921, Act of May 17, 1921, P.L. 682, as amended, 40 P.S. §§991.1401 et seq. ("Insurance Holding Companies Act"), provides that all changes in control of domestic insurers must be filed with the Department for approval or disapproval.
14. The Application was filed pursuant to Section 1402 of the Insurance Holding Companies Act.

15. Section 1402(g) of the Insurance Holding Companies Act provides that a transaction is exempt from the requirements of Section 1402 if it does not have the effect of changing or influencing the control of a domestic insurer.

Department Procedures

16. On April 10, 2004, the Department published notice in the *Pennsylvania Bulletin* that the Application was received, and such notice invited interested persons to submit comments to the Department regarding the Application for 45 days following the date of the publication (“Comment Period”).
17. As of June 16, 2004, comments were received from 68 interested persons.
18. Fourteen comments were limited to requests for copies of the application or other materials filed with the Department.
19. Fifteen comments expressed support for the Application. The comments expressing support for the Application were submitted primarily by entities with a business relationship with the Pool Companies, including commercial insureds, brokerage entities, and insurance entities.
20. Thirty-two comments expressed opposition to the Application. The comments expressing opposition for the Application were submitted primarily by entities with a business relationship with PMA Re, including insurance entities, risk management entities, brokerage entities and other insurance-related businesses.
21. Of the commenters opposed to the Application, many expressed concern regarding the reserve and surplus adequacy of PMA Re after the Proposed Transfer.
22. All comments were forwarded to PMA for response.
23. The Department reviewed and considered, in its analysis of the Application, all of the comments as well as PMA’s responses to those comments and the issues raised in those comments.

The Transaction

24. As described in the Application, at September 30, 2003, PMA Re recorded a reserve charge of \$150 million.
25. As described in the Application, as a result of the reserve charge, A.M. Best and Moody’s Investors Service lowered the insurer financial strength rating of PMA Re and the Pool Companies during the fourth quarter of 2003 and first quarter of 2004.

26. As described in the Application, as a result of the reserve charge and ratings actions, PMA Re withdrew from the reinsurance business during the fourth quarter of 2003 and PMA Re is currently in run-off.
27. As described in the Application, PMA Re proposes to transfer its direct ownership in the Pool Companies to PMA via a transfer of stock.
28. As described in the Application, the modification to the holding company system is being pursued to allow the Pool Companies and PMA Re to be evaluated separately by the nationally recognized rating agencies that rate the financial strength and claims paying ability of the Pool Companies and PMA Re.
29. The Application included a Statement of Actuarial Opinion from an officer of PMA Re opining that the loss and loss adjustment expense reserves carried as of December 31, 2003:
 - (a) meet the requirements of the insurance laws of Pennsylvania;
 - (b) are computed in accordance with accepted loss reserving standards and principles; and
 - (c) make a reasonable provision for all unpaid loss and loss expense obligations of PMA Re under the terms of its contracts and agreements.
30. The Application included an opinion of Bickerstaff, Whatley, Ryan and Berkhalter, an independent actuarial firm, concluding that PMA Re's carried loss reserves and loss adjustment expenses as of December 31, 2003, are reasonable.
31. The Application included an opinion of Keefe, Bruyette & Woods, Inc., an independent investment banking firm, opining that after the Proposed Transfer, the admitted assets of PMA Re will exceed its liabilities plus the greater of (i) any capital and surplus required by law for its organization and (ii) its authorized and issued capital stock.
32. The Application included 3-year projected statutory financial highlights for PMA Re reflecting a risk-based capital at year-end 2004 of 259%, year-end 2005 of 371% and year-end 2006 of 496%.
33. As described in the Application, on June 18, 2004, PMA Re entered into an adverse development reinsurance agreement to cover potential adverse development of the loss reserves of its run-off operations.
34. As described in the Application, this reinsurance was placed with third party reinsurers and provides for transferring to the reinsurers \$100 million of PMA Re's assets in exchange for coverage for adverse development of up to \$120 million over the loss reserves. If development on the loss reserves exceeds \$120

million, PMA Re will be required to pay up to \$35 million in additional premiums, at certain contractually determined levels, for an additional \$85 million of coverage.

35. The Deputy Commissioner finds that the Proposed Transfer described in the Application does not have the effect of changing or influencing the control of a domestic insurer and finds that the transaction is exempt from the requirements of Section 1402 of the Insurance Holding Companies Act.
36. The ultimate controlling person before and after consummation of the Proposed Transfer is PMA.
37. If any of the above Findings of Fact are determined to be Conclusions of Law, they shall be incorporated in the Conclusions of Law as if fully set forth therein.

CONCLUSIONS OF LAW

1. Under Section 1402 of the Insurance Holding Companies Act, the Department has jurisdiction to review and approve the acquisition of controlling securities of a domestic insurer if, after consummation thereof, the acquiring person would be in control of the domestic insurer.
2. The Deputy Commissioner has jurisdiction over the parties and subject matter of this proceeding.
3. The Application was properly filed pursuant to and in accordance with Section 1402(g) of the Insurance Holding Companies Act.
4. The instant transaction is not being contemplated to change or influence the ultimate control of the Pool Companies, and, therefore, is exempt from the requirements of Section 1402 of the Insurance Holding Companies Act.
5. The ultimate controlling person before and after consummation of the Proposed Transfer is PMA.
6. If any of the above Conclusions of Law are determined to be Findings of Fact, they shall be incorporated in the Findings of Fact as if fully set forth therein.

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In Re:	:	Pursuant to Sections 1401 and 1402 of the
	:	Insurance Holding Companies Act,
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Modification of the Insurance Holding	:	991.1402
Company System, which includes	:	
Manufacturers Alliance Insurance	:	
Company, Pennsylvania Manufacturers	:	
Indemnity Company and Pennsylvania	:	
Manufacturers' Association Insurance	:	
Company	:	Order No. ID-RC-04-10

ORDER

Upon consideration of the foregoing, the Deputy Insurance Commissioner of the Commonwealth of Pennsylvania, hereby makes the following Order:

An approving determination for the modification of the insurance holding company system, which includes Manufacturers Alliance Insurance Company ("MAIC"), Pennsylvania Manufacturers Indemnity Company and Pennsylvania Manufacturers' Association Insurance Company, as set forth in the Application, is hereby granted, subject to this Order and the following conditions:

1. PMA Capital Insurance Company ("PMA Re") shall be prohibited from declaring or paying any dividends, returns of capital or any other types of distributions to PMA Capital Corporation ("PMA") or any affiliates of PMA during the 2004 and 2005 calendar years.
2. PMA Re shall be prohibited, without the prior approval of the Department, from declaring or paying any dividends, returns of capital or any other types of distributions to PMA or any affiliates of PMA during the 2006 calendar year should the risk based capital of PMA Re be below 225% immediately following the distribution.
3. PMA Re shall be prohibited from declaring or paying any extraordinary dividends, returns of capital or any other types of distributions during the 2007

3. PMA Re shall be prohibited from declaring or paying any extraordinary dividends, returns of capital or any other types of distributions during the 2007 calendar year and thereafter unless said distribution has been approved by the Department as a transaction between affiliates filed under the Insurance Holding Companies act, Article XIV of the Insurance Company Law of 1921, Act of May 17, 1921, P.L. 682, as amended, 40 P.S. §§991.1401 et seq.

The conditions of this Order shall supersede any previous agreements PMA Re or its parent or affiliates may have with the Department.

This Order is effective immediately.




STEPHEN J. JOHNSON
Deputy Insurance Commissioner