

IN THE COMMONWEALTH COURT OF PENNSYLVANIA

IN RE: Commonwealth Insurance Company, :
In Liquidation : No. 1 CIC 2014

ANNUAL REPORT OF THE LIQUIDATOR
ON THE STATUS OF THE LIQUIDATION
OF COMMONWEALTH INSURANCE COMPANY
AS OF DECEMBER 31, 2014

I. INTRODUCTION

Teresa D. Miller, Acting Insurance Commissioner of the Commonwealth of Pennsylvania, in her official capacity as Statutory Liquidator (“Liquidator”) of Commonwealth Insurance Company (“CIC” or “Estate”), through her undersigned counsel, hereby submits this Annual Report on the status of the liquidation of CIC for the period from March 20, 2014¹ through December 31, 2014 (“Report”).

II. REPORT

A. Financial Statements.

CIC has prepared Special Purpose Statements of Assets, Cash Flows and Operations for the period from March 20, 2014 through December 31, 2014 (“Statements”). The Statements

¹CIC was placed into liquidation by order of this Court dated March 20, 2014.

include estimates as noted below and may not fully reflect the effects of the liquidation upon some assets and liabilities. Consequently, the ultimate distribution to creditors is unknown at this time. For this reason, third parties should not rely on the financial information contained herein as providing any certainty as to the ultimate distribution that will be made from CIC. These notes to the Special Purpose Statements describe the nature of the line items on the Statements and should be included in any review of CIC's financial information.

The Statements are addressed in more detail in sections 1 through 3 below.

1. Special Purpose Statement of Assets – EXHIBIT A.

As of December 31, 2014, the attached Special Purpose Statement of Assets shows estimated total assets were \$368,330.

a. Cash.

CIC had cash amounting to \$348,904 as of December 31, 2014.

b. Premium Receivable.

As of December 31, 2014, approximately \$10,240 remains outstanding from agents on bonds issued by the company prior to liquidation. The Liquidator has collected \$533,000 while approximately \$72,000 has been returned due to the flat cancellation of renewals on bonds effective after the date of liquidation. An additional \$15,300 was written off reflecting uncollectability of balances due. The Liquidator continues to pursue the collection of these funds through internal efforts.

c. Inter-company Receivables.

CIC was a wholly owned subsidiary of Pennsylvania Group, LTD. The parent company owed \$181,892 to CIC as of December 31, 2013. Moreover, Commonwealth Surety Agency, an

affiliate of CIC, owed CIC \$130,499 as of December 31, 2013. These receivables have been written off at December 31, 2014, as uncollectible.

d. Reinsurance Recoverable.

The company had no reinsurance.

e. Collateral Held for Principals.

Under certain construction projects, CIC required that principals provide collateral in the form of cash, Certificates of Deposit, an Irrevocable Letter of Credit (ILOC), or a real estate mortgage to secure CIC's interests in the bond in the event the principal failed to perform as required and to help offset the bond exposure to the company. Under the collateral arrangement certificates of deposit were obtained, or cash funds were set aside in separate bank accounts identified by project while the ILOCs were secured in a local bank safe deposit box for safekeeping. Mortgages were duly recorded. The Liquidator has released some of the cash collateral to the principals, where there were funds remaining in the accounts, as well as the ILOCs for projects with no claims, or where all claims have been settled. Mortgages are satisfied when all claims have been resolved, or upon transfer of real estate, with the collateral proceeds held in escrow until the time of release by CIC.

f. Salvage and Subrogation Recoveries.

We currently have no recoverables on approved Notices of Determination ("NODs") as the responsible party is either out of business or bankrupt. Personal indemnitors are not being pursued either as they are bankrupt or deceased.

2. Special Purpose Statements of Liabilities – EXHIBIT B.

Total estimated liabilities at December 31, 2014, were \$1,128,231. CIC liquidation expenses are class (a) first priority payments under the Insurance Department Act of 1921, 40

P.S. §221.1 et seq. (“Act”), as are certain GA expenses, to the extent permitted by the Act. Both Liquidator and GA expenses will be paid before distributions for claims under the lower priority classes. As of December 31, 2014, there was \$169,862 in reserves for unpaid Liquidator expenses.

However, the most significant liability is the \$846,243 assigned to priority class (e) POCs. This category includes all claims under bonds issued by CIC.

a. Priority Class A.

The Operating Statement Analysis attached as Exhibit D lists \$194,048 of Liquidator administrative operating expenses incurred by CIC for March 20, 2014 through December 31, 2014. Actual paid Liquidator expenses represented \$31,158 of this total as of the end of the year.

b. Priority Class E.

Claims of surety fall under priority class (e) of the Act, along with general creditor claims. As a result, the vast majority of claims in the CIC estate fall under class (e), including bondholders making a claim under bonds. The total claims under class (e) as of December 31, 2014, is 33 issued NODs, and 18 accepted, with a total accepted allowed amount of \$846,243.

c. Priority Classes Below Class E.

Also included in total liabilities are estimated liabilities for POCs assigned to priority classifications below class (e), which total zero.

3. Special Purpose Statement of Operations – EXHIBIT D.

Attached is the Statement of Operations (“Operations Report”) for the year 2014, which reports CIC experienced a net operating loss of \$1,173,879, due mainly to the valuation of claims and the establishment of claim reserves.

4. **Operating Expense Analysis.**

The operating expenses of CIC relate to efforts by the Liquidator to marshal and maximize the assets of the Estate for the benefit of all CIC's bondholders and claimants, as well as to review and determine the ultimate liabilities of the Estate, to fulfill the public policies and purposes of the Act and the liquidation process, and to investigate those third parties alleged to have contributed to the insolvency of CIC. Additional significant time was allocated to the disposition of collateral held in the form of cash, certificates of deposit, real estate mortgages, and Irrevocable Letters of Credit held as additional security.

The attached Operating Expense Analysis indicates the total dollar amount for each major expense category for the period from March 20 to December 31, 2014. As detailed in the Operating Expense Analysis and supporting schedules, the administrative expenses of CIC for the period totaled \$ 194,048.

a. **Legal Fees.**

Attached as Exhibit F is a schedule containing the legal expense detail by entity.

b. **Professional Services Expenses.**

Attached as Exhibit G is a schedule containing the professional service expense detail by vendor name for the year. The individual entities listed in the schedule provided services including collateral review, and claims analysis.

c. **Real Estate Expenses.**

Until March 31, 2014, CIC did business at its location in Bala Cynwyd, Pennsylvania. Thereafter, operations were moved to the Pennsylvania Insurance Department.

5. **Claims Process.**

The deadline for filing POCs was November 21, 2014.

a. **Proofs of Claim Statistics – (Inception-to-Date).**

As of December 31, 2014, CIC had issued NODs for 33 of the 57 POCs received for a total allowed amount of \$958,369. Of the 33 issued, 18 have been accepted with a total allowed amount of \$846,243.

Issued NODs accounted for 58% of the POCs filed with the Estate.

b. **Notice of Claim Determination Objection Statistics.**

As of December 31, 2014, the Liquidator had received a total of zero objections to the 33 NODs issued.

c. **Claims Bar Date.**

A claims bar date has not yet been set for this estate.

6. **CIC Operations Moved to Pennsylvania Insurance Department.**

Effective April 1, 2014, CIC's operations and reporting were transferred "in house" to the Pennsylvania Insurance Department's Office of Liquidations, Rehabilitations and Special Funds. CIC's staff worked with the Liquidator's staff to transition files and records, and provided information about the company's operations, prior to the transfer.

7. **Federal Income Taxes**

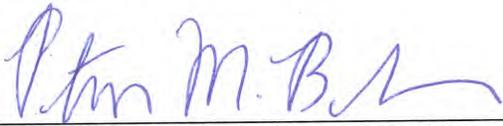
CIC's federal income taxes were filed as part of a consolidated group of affiliated companies with its parent company Pennsylvania Group, LTD. The company paid no federal taxes in 2013 or 2012 and there is no provision for federal income taxes in 2014. Penalties and interest are currently being sought by the IRS for amounts that were paid late in 2013 related to employee and employer payroll taxes. The penalties and interest assessment, amounting to \$2,400, is under a second appeal at a regional IRS branch, on the basis that CIC's former

owner's poor health prevented CIC from paying in a timely manner. Our initial appeal with the IRS was denied.

8. Recovery from Raymond W. Hovsepian Estate

Payment was made to CIC by the former owner's testamentary estate in the amount of \$30,000 in settlement of a disputed claim for repayment of certain life insurance premiums paid by CIC.

Respectfully submitted:

By: 
PRESTON M. BUCKMAN (I.D. #57570)
Insurance Department Counsel
Governor's Office of General Counsel
Pennsylvania Insurance Department
Capitol Associates Building
901 North 7th Street
Harrisburg, PA 17102
(717) 787-6009

Attorney for Teresa D. Miller, Acting Insurance Commissioner of the Commonwealth of Pennsylvania, in her official capacity as Statutory Liquidator of Commonwealth Insurance Company

Dated: 3/25/15

EXHIBIT A

Commonwealth Insurance Company (In Liquidation)

SPECIAL PURPOSE STATEMENT OF ASSETS, LIABILITIES and EQUITY - Unaudited
AS OF MARCH 20, 2014

| | | | |
|----------------------------------|--|----|-----------|
| <u>Assets</u> | | | |
| Cash | | \$ | 83,475 |
| State Deposits | | | 233,020 |
| Premiums Receivable | | | 98,141 |
| Claims Receivable | | | 170,343 |
| Other Assets | | | 314 |
| Total Assets | | \$ | 585,293 |
| <u>Liabilities</u> | | | |
| Accounts Payable | | \$ | (8,098) |
| Unearned Premiums | | | (331,075) |
| Claim and Claim Expense Reserves | | | (230,000) |
| Total Liabilities | | \$ | (569,173) |
| <u>Equity</u> | | | |
| Common Stock | | \$ | (250,000) |
| Additional Paid In Capital | | | (687,999) |
| Retained Earnings Deficit | | | 921,879 |
| Total Equity | | \$ | (16,120) |
| Total Liabilities and Equity | | \$ | (585,293) |

Assets and Liabilities in the amount of \$457,806 categorized by CIC as collateral have been removed from the balance sheet of the company on the date of liquidation. These funds represented security on specific bonded projects and are not considered as general assets of the estate available to all creditors. Such funds were previously recorded as an admitted asset with a corresponding liability in an equal amount on the company's annual statements.

EXHIBIT B

Commonwealth Insurance Company (In Liquidation)

SPECIAL PURPOSE STATEMENT OF ASSETS, LIABILITIES and EQUITY - Unaudited
As of December 31, 2014

| | <u>12/31/2014</u> |
|---|-----------------------|
| <u>Assets</u> | |
| Cash | \$ 348,904 |
| Premiums Receivable | 10,240 |
| Other Assets | 9,186 |
| Total Assets | \$ 368,330 |
| <u>Liabilities</u> | |
| Class A Liquidator Administrative Expenses Unpaid | (169,862) |
| Class E Claims - Liquidator | (846,243) |
| Class E Claims Reserve - Liquidator | (112,126) |
| Total Liabilities | \$ (1,128,231) |
| <u>Equity</u> | |
| Deficit at December 31, 2014 | \$ 759,901 |
| Total Equity | \$ 759,901 |
| Total Liabilities and Equity | \$ (368,330) |

Assets and Liabilities in the amount of \$522,001 categorized by CIC as collateral have been removed from the balance sheet of the company as of December 31, 2014. These funds represented security on specific bonded projects and are not considered as general assets of the estate available to all creditors. Such funds were previously recorded as an admitted asset with a corresponding liability in an equal amount on the company's annual statements.

See accompanying report.

EXHIBIT C

Commonwealth Insurance Company (In Liquidation)

SPECIAL PURPOSE STATEMENT RECONCILIATION OF EQUITY - Unaudited
FOR THE PERIOD MARCH 20, 2014 to DECEMBER 31, 2014 and

| | <u>2014</u> |
|--|-------------|
| Beginning Equity - March 20, 2014 | \$ (16,120) |
| Adjustment to release Pre-liquidation liabilities | (572,574) |
| Adjustment to writedown assets at date of liquidation considered uncollectable | 174,716 |
| Loss from Operations | 1,173,879 |
| Ending Deficit - December 31, 2014 | \$ 759,901 |
| | |

See accompanying report.

EXHIBIT D

Commonwealth Insurance Company (In Liquidation)

SPECIAL PURPOSE STATEMENT OF OPERATIONS - Unaudited
FOR THE PERIOD MARCH 20, 2014 to DECEMBER 31, 2014

| | <u>2014</u> |
|-------------------------------------|-----------------------|
| Income | |
| Premiums cancellations | \$ (73,141) |
| Commission Rights earned | 18,598 |
| Other Income | 33,081 |
| Total Income | \$ (21,462) |
| Claims | |
| Class E NOD's Accepted - Liquidator | \$ 846,243 |
| Class E Reserves - Liquidator | 112,126 |
| Total Claims | \$ 958,369 |
| Expenses | |
| Payroll, Taxes and Benefits | \$ 136,020 |
| Professional and Consulting Fees | 17,477 |
| Legal Fees | 10,911 |
| Real Estate related | 13,351 |
| Furniture and Equipment | 519 |
| Postage, Telephone and Supplies | 1,808 |
| Data Processing and Software | 2,341 |
| Other Operating Expenses | 11,621 |
| Total Expenses | \$ 194,048 |
| Net (Loss) Gain | \$ (1,173,879) |

See accompanying report.

EXHIBIT E

Commonwealth Insurance Company (In Liquidation)

SPECIAL PURPOSE STATEMENT OF CASH FLOWS AND CHANGES IN CASH - Unaudited
FOR THE PERIOD MARCH 20, 2014 to DECEMBER 31, 2014

| | <u>2014</u> | |
|-----------------------------------|-------------|---------|
| Beginning Cash March 20, 2014 | \$ | 83,475 |
| Sources of Cash: | | |
| Premium payments | \$ | 533 |
| State Deposits | | 233,024 |
| Salvage & Subrogation Collections | | 9,000 |
| State Taxes Recovered | | 3,097 |
| Commission Rights | | 17,953 |
| Other | | 32,980 |
| Total Sources | \$ | 296,587 |
| Uses of Cash: | | |
| Liquidator Expenses | \$ | 21 |
| Payroll, Taxes and Benefits | | 5,514 |
| Professional and Consulting Fees | | 15,861 |
| Legal Expenses | | 9,149 |
| Postage, Telephone and Supplies | | 512 |
| Other Operating | | 101 |
| Total Uses | \$ | 31,158 |
| Net Increase in Funds | \$ | 265,429 |
| Ending Cash December 31, 2014 | \$ | 348,904 |

See accompanying report.

EXHIBIT F

COMMONWEALTH INSURANCE COMPANY (IN LIQUIDATION)

LEGAL FEE EXPENSES - Unaudited
FOR THE PERIOD MARCH 20 TO DECEMBER 31, 2014

| <u>VENDOR NAME</u> | <u>2014</u> |
|------------------------------------|-----------------|
| Royal Bank America fees | \$ 200 |
| William Balaban & Associates | 3,770 |
| Stradley Ronon Stevens & Young LLP | 6,869 |
| Liquidator Allocation | 72 |
| TOTAL | <u>\$10,911</u> |

See accompanying report.

EXHIBIT G

COMMONWEALTH INSURANCE COMPANY (IN LIQUIDATION)

PROFESSIONAL SERVICE EXPENSES - Unaudited
FOR THE PERIOD MARCH 20 TO DECEMBER 31, 2014

| <u>VENDOR NAME</u> | <u>2014</u> |
|---------------------------------|------------------|
| Baker Tilly Virchow Krause, LLP | \$ 1,688 |
| ParenteBeard | 8,065 |
| Rainer & Company | 6,109 |
| Liquidator Allocation | 1,615 |
| TOTAL | <u>\$ 17,477</u> |

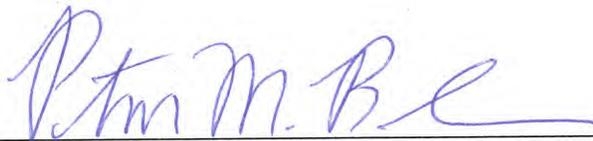
See accompanying report.

CERTIFICATE OF SERVICE

I hereby certify that I am this day serving the foregoing document upon all parties of record in this proceeding in accordance with the requirements of 1 Pa. Code Chapter 33 in the following manner:

Service via eservice through PACFile, addressed as follows:

William R. Balaban, Esquire
WBalaban@BalabanAndAssociates.com
27 North Front Street
Harrisburg, PA 17101-1606
(717) 695-2901
(717) 695-7914 (fax)



PRESTON M. BUCKMAN (I.D. #57570)
Insurance Department Counsel
Office of Liquidations, Rehabilitations
& Special Funds
Governor's Office of General Counsel
Capital Associates Building
901 North 7th Street
Harrisburg, PA 17102
(717) 787-6009

Counsel for the Statutory Liquidator of
Commonwealth Insurance Company

DATED: 3/25/15



COMMONWEALTH OF PENNSYLVANIA
GOVERNOR'S OFFICE OF GENERAL COUNSEL

March 25, 2015

Michael F. Krimmel, Chief Clerk
Commonwealth Court of Pennsylvania
601 Commonwealth Avenue, Suite 2100
P.O. Box 69185
Harrisburg, PA 17120-9185

***Re: In Re: Commonwealth Insurance Company (In Liquidation)
No. 1 CIC 2014***

Dear Mr. Krimmel:

Attached please find the Annual Report of the Liquidator on the Status of the Liquidation of Commonwealth Insurance Company as of December 31, 2014, with regard to the above-referenced matter.

Thank you for your assistance in this matter.

Very truly yours,

A handwritten signature in blue ink, appearing to read "Preston M. Buckman".

Preston M. Buckman
Insurance Department Counsel

PMB:drh

Enclosures