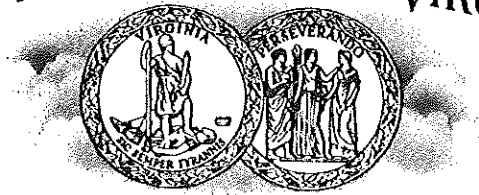


EXAMINATION REPORT
on the
VIRGINIA PROPERTY AND CASUALTY INSURANCE
GUARANTY ASSOCIATION
Boston, Massachusetts
as of
December 31, 2009

COMMONWEALTH OF VIRGINIA

ALFRED W. GROSS
COMMISSIONER OF INSURANCE
STATE CORPORATION COMMISSION
BUREAU OF INSURANCE



P.O. BOX 1157
RICHMOND, VIRGINIA 23218
TELEPHONE: (804) 371-9741
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<http://www.state.va.us/scc>

I, Alfred W. Gross, Commissioner of Insurance of the Commonwealth of Virginia, do hereby certify that the annexed copy of the Examination Report of the Virginia Property and Casualty Insurance Guaranty Association as of December 31, 2009, is a true copy of the original report on file with this Bureau.

IN WITNESS WHEREOF, I have hereunto set my hand
and affixed to the original the seal of the Bureau at the City
of Richmond, Virginia this 29th day of October, 2010

A handwritten signature in cursive script that reads "Alfred W. Gross".

Alfred W. Gross
Commissioner of Insurance

(SEAL)

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Richmond, Virginia
July 29, 2010

Honorable Alfred W. Gross
Commissioner of Insurance
Commonwealth of Virginia
Richmond, Virginia

Dear Sir:

In accordance with your instructions and by authority of § 38.2-1612 of the Code of Virginia, an examination of the affairs and the income and expenses of the

**VIRGINIA PROPERTY AND CASUALTY INSURANCE
GUARANTY ASSOCIATION,
Boston, Massachusetts**

hereinafter referred to as the Association, has been completed. The report thereon is submitted for your consideration. The Association was last examined by representatives of the State Corporation Commission's Bureau of Insurance (Bureau) as of December 31, 2005. This examination covers the four-year period from that date through December 31, 2009.

DESCRIPTION

The Association is a nonprofit, unincorporated legal entity created by Chapter 16 (§ 38.2-1600 et seq.) of Title 38.2 of the Code of Virginia. Its purpose is to provide payment of covered claims, under certain insurance policies, to reduce financial loss to claimants or policyholders because of the insolvency of an insurer, to assist in the detection and prevention of insurer insolvencies and to provide a mechanism for assessing the cost of such protection among insurers.

HISTORY

The Association's initial board of directors was appointed by the Commissioner of Insurance pursuant to § 38.1-762 of the Code of Virginia and held its first meeting on November 15, 1972. Subsequently, the plan of operation, as required by § 38.1-764, was submitted to the State Corporation Commission (Commission) which gave its approval on October 23, 1973. Amendments to the plan of operation were approved by the Commission on September 28, 1981, July 1, 1986, September 2, 1992, and June 25, 1997.

Since its organization, the Association has been involved in the insolvencies of the following companies:

<u>Company</u>	<u>Declared Insolvent</u>	<u>State of Domicile</u>
Professional Insurance Company	1974	New York
Summit Mutual Insurance Company	1975	New York
Consolidated Mutual Insurance Company	1978	New York
Reserve Insurance Company	1979	Illinois
Fauquier Home Mutual Fire Insurance Company	1981	Virginia
Proprietors Insurance Company	1981	Ohio
Security Casualty Insurance Company	1981	Illinois
Excalibur Insurance Company	1984	Texas
Aspen Indemnity Corporation	1984	Colorado
Ideal Mutual Insurance Company	1984	New York
Early American Insurance Company	1985	Alabama
Columbus Insurance Company	1985	Ohio
Eastern Indemnity Company	1985	Maryland
Union Indemnity Insurance Company	1985	New York
S & H Insurance Company	1985	California
Transit Casualty Company	1985	Missouri
American Fidelity Fire Insurance Company	1985	New York
Commercial Standard Insurance Company	1985	Texas
Iowa National Mutual Insurance Company	1985	Iowa
Carriers Insurance Company	1986	Iowa
Midland Insurance Company	1986	New York
Great Global Assurance Company	1986	Arizona
American Druggists' Insurance Company	1986	Ohio
Allied Fidelity Insurance Company	1986	Indiana
Mission Insurance Company	1987	California
Mission National Insurance Company	1987	California
Mission Reinsurance Corporation	1987	Missouri
Enterprise Insurance Company	1987	California
Integrity Insurance Company	1987	New Jersey
American Interinsurance Exchange	1988	Indiana
American Mutual Liability Insurance	1989	Massachusetts
American Mutual Insurance of Boston	1989	Massachusetts
Stone Mountain Insurance Company	1989	Georgia
Paxton National Insurance Company	1989	Pennsylvania
American Universal Insurance Company	1991	Rhode Island
Edison Insurance Company	1991	Illinois
Western Employers Insurance Company	1991	California
Rockwood Insurance Company	1991	Pennsylvania

MCA Insurance Company	1992	Oklahoma
Insurance Company of Florida	1992	Florida
Employers Casualty Company	1994	Texas
Premier Alliance Insurance Company	1994	California
Presidio Insurance Company of Indiana*	1986	Indiana
Heritage Insurance Company*	1986	Illinois
Homeland Insurance Company*	1987	California
United Fire Insurance Company*	1989	Illinois
Coronet Insurance Company	1996	Illinois
United Community Insurance Company	1994	New York
Insurance Corporation of America	1997	Texas
Granger's Mutual Insurance Company	1997	Maryland
United Southern Assurance Company	1997	Florida
Quaker City Insurance Company	1997	Pennsylvania
U.S. Capital Insurance Company*	1997	New York
American Eagle Insurance Company	1997	Texas
LMI Insurance Company	2000	Ohio
Hamilton Insurance Company	2000	California
Superior National Insurance Company	2000	California
California Compensation Insurance Company	2000	California
Commercial Compensation Casualty Company*	2000	California
Credit General Insurance Company	2001	Ohio
Acceleration National Insurance	2001	Ohio
Reliance Insurance Company	2001	Pennsylvania
International Indemnity Company*	2001	Georgia
PHICO Insurance Company	2002	Pennsylvania
Home Insurance Company	2003	New Hampshire
Reciprocal of America	2003	Virginia
Fremont Indemnity Company	2003	California
Legion Insurance Company	2003	Pennsylvania
Villanova Insurance Company	2003	Pennsylvania
Protective National Insurance Company of Omaha	2004	New Jersey
State Capital Insurance Company	2004	North Carolina
Casualty Reciprocal Exchange	2004	Missouri
IGF Insurance Company	2004	Indiana
South Carolina Insurance Company	2005	South Carolina
Vesta Fire Insurance Company	2006	Texas
Shelby Insurance Company	2006	Texas
Shelby Casualty Insurance Company	2006	Texas
Park Avenue Property & Casualty Insurance Company of Oklahoma	2009	Oklahoma

* Never Any Activity – Inactive

MANAGEMENT AND CONTROL

Management of the Association, according to the plan of operation, is vested in a board of nine directors to be elected for three-year terms by the member insurers to fairly represent all types of such insurers. A majority of the board constitutes a quorum for the transaction of business and a majority of members present at any meeting in which there is a quorum present may act as the board except that an affirmative vote of five members is required to (1) approve a contract with a servicing facility, (2) levy an assessment or provide for a refund, or (3) borrow money.

OFFICERS AND DIRECTORS

At December 31, 2009, the designated representatives of the member insurers serving on the board, and the respective officers elected by the board, were as follows:

<u>Director</u>	<u>Representing</u>
Matthew Lupino Regional Underwriting Manager	Utica Mutual Insurance Company
Douglas Joyce President	Alfa Alliance Insurance Corporation
Peggy Echols Vice President Operations	State Farm Mutual Automobile Insurance Company
Richard Mattox Director of Claims	Virginia Farm Bureau Mutual Insurance Company
L. Gerald Roach President	Mutual Assurance Society of Virginia
Donna Leaman Assistant Vice President and Senior Legislative Counsel	United Services Automobile Association
Jeff Williams Regional Counsel	Allstate Insurance Company
Elizabeth Wilson-Thomas Vice President and Associate General Counsel	CNA Insurance Company

Scott Holbrook
Assistant Regional Vice President

Hartford Accident & Indemnity Company

Officers

L. Gerald Roach
Paul M. Gulko
Kathleen M. Lavin
James S. Winskowicz

Chairman
Executive Secretary
Treasurer
Claims Manager

PLAN OF OPERATION

The Association's members include all insurers who write all classes of direct insurance except life, annuity, health or disability insurance, mortgage guaranty, financial guaranty (or other forms of insurance offering protection against investment risk), fidelity or surety bonds (or any other bonding obligations), credit insurance, insurance of warranties or service contracts, title insurance or insurance of vessels or craft used primarily in a trade or business, their cargoes and marine builders' risk and marine protection and indemnity. Any class of insurance written by cooperative nonprofit life benefit companies, mutual assessment life, accident and sickness insurers, burial societies, fraternal benefit societies, captive insurers, risk retention groups and home protection companies is also excluded from membership. Subject insurers are required to remain members of the Association as a condition of their authority to transact the business of insurance in this Commonwealth.

The Association is obligated to pay covered claims that existed prior to the determination of insolvency and which arose before the earliest of ninety-one days after the determination of insolvency, the policy expiration date or the date the insured replaces or cancels the policy. Such obligations include unearned premiums in excess of \$50 but less than \$300,000. All other claims are included up to \$300,000 per claim, except workers' compensation, which is covered for the full amount provided in the policy. In no event shall the Association be obligated to pay a claimant for an amount in excess of the insolvent insurer's obligation for a covered claim. A covered claim, which also includes unearned premiums, is one involving a claimant or insured who was a resident of this Commonwealth at the time of the insured event or for which property relating to the claim is permanently located in this Commonwealth. By law, the Association is deemed the insurer to the extent of its obligations for covered claims.

For purposes of administration and assessment, the Association is required to have three separate accounts: a worker's compensation insurance account, an automobile insurance account and an account for all other applicable insurance. Claims and expenses paid are to be allocated among these accounts separately. Assessments also are to be made against members separately for each account in an amount necessary to pay the

obligations. Assessments of each member shall be based on the ratio of the net direct written premiums of the member insurer to the net direct written premiums of all member insurers. This ratio is determined using premiums for the preceding calendar year for the specific account.

During the four-year period under review, the Association levied the following assessments and authorized the following refunds:

	<u>2006</u>	<u>2007</u>	<u>2008</u>
Automobile	\$0	\$500,000	\$0
Workers Compensation	18,727,489	19,386,958	11,000,000
All Other	<u>0</u>	<u>0</u>	<u>0</u>
Total Assessments	<u>\$18,727,489</u>	<u>\$19,886,958</u>	<u>\$11,000,000</u>

	<u>2007</u>	<u>2009</u>
Automobile	\$5,195,457	\$146,658
Workers Compensation	628,899	158,546
All Other	<u>7,301,900</u>	<u>16,339,206</u>
Total Refunds	<u>\$13,126,256</u>	<u>\$16,644,410</u>

Effective January 1, 1985, the Association entered into an agreement with Guaranty Fund Management Services (GFMS) to provide management and claim supervisory services. GFMS is a voluntary non-profit unincorporated association whose principal office is in Boston, Massachusetts. GFMS also provides services to several other state guaranty associations.

The agreement provides that certain operating costs of GFMS shall be distributed among the member guaranty funds based on the ratio of the net premiums written on covered lines of insurance for each state association to the total of net premiums written for all associations under the agreement. In addition, the agreement provides that each guaranty fund shall be responsible for the payment of its own direct obligations. Expenses, other than direct expenses, are allocated to insolvencies based on time maintained by certain employees, transaction activity and/or premium ratios.

On March 8, 1989, GFMS entered into a contract with Helmsman Management Services, Inc. (Helmsman), a subsidiary of Liberty Mutual Insurance Company, to provide claims and administrative services for workers' compensation claims arising under workers' compensation policies issued by an insolvent insurer and payable by the guaranty associations. Under the agreement, GFMS was required to maintain a deposit

with Helmsman and reimburse all amounts paid by Helmsman. Beginning with the Rockwood Insurance Company insolvency, GFMS began servicing claims arising under workers' compensation policies.

SCOPE

This is a financial examination of cash receipts and disbursements for the four-year period ending December 31, 2009. The Association maintains its records and prepares its annual report to the Commission on the basis of cash receipts and disbursements. Assessments and other revenue are recognized when received and claims and other expenses are recognized when paid. A test of income and expenses was made based on a sampling of the items.

In addition, the following items were reviewed, several of which are discussed separately under their respective captions in this report.

History
Management and Control
Plan of Operation
Accounts and Records
Claim Reserves

FINANCIAL STATEMENTS

There follows, on a modified cash basis, a statement reflecting the financial condition of the Association at December 31, 2009, a statement of revenues and expenses for the year ended December 31, 2009, a statement of cash flows, and a statement of changes in fund balance for the period under review. The statements made in this part of the report and the amounts included therein are generally in the form of the financial report filed with the Commission.

STATEMENT OF FINANCIAL POSITION**Assets**

Cash and cash equivalents	\$63,245,068
Assessments receivable	41,893
Investments at market value	90,568,773
Accrued interest	1,019,706
Other	888,409
Total assets	<u>\$155,763,849</u>

Liabilities and Fund Balance

Accounts payable	\$182,858
Refunds payable	<u>25,403,922</u>
Total liabilities	\$25,586,780
Fund balance	<u>130,177,069</u>
Total liabilities and fund balance	<u>\$155,763,849</u>

STATEMENT OF REVENUES AND EXPENSES

Revenues

Investment income	\$4,088,202
Insolvency recovery	7,317,935
Total revenue	<u>\$11,406,137</u>

Expenses

Claim and claim adjustment expense	\$6,781,662
Member refunds	16,646,064
Administrative expenses	1,920,194
Total expenses	<u>\$25,347,920</u>

Excess of expenses over revenues	(\$13,941,783)
Change in unrealized gains on investments	<u>2,498,982</u>
Surplus	<u><u>(\$11,442,801)</u></u>

STATEMENT OF CHANGES IN FUND BALANCE

	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>
Fund balance, December 31, prior year	<u>\$68,710,110</u>	<u>\$86,006,283</u>	<u>\$121,491,849</u>	<u>\$141,619,870</u>
Excess of revenues over expenses	17,092,318	34,538,558	19,799,458	(13,941,783)
Unrealized gain on investments	<u>203,855</u>	<u>947,008</u>	<u>328,563</u>	<u>2,498,982</u>
Change in fund balance	<u>\$17,296,173</u>	<u>\$35,485,566</u>	<u>\$20,128,021</u>	<u>(\$11,442,801)</u>
Fund balance, December 31, current year	<u><u>\$86,006,283</u></u>	<u><u>\$121,491,849</u></u>	<u><u>\$141,619,870</u></u>	<u><u>\$130,177,069</u></u>

STATEMENT OF CASH FLOWS

Cash flows from operating activities	
Excess of revenues over expenses	(\$13,941,783)
Adjustments to reconcile excess of revenues over expenses to net cash provided by operating activities	
Amortization of premium/discount on investments	(14,351)
(Increase) decrease in assessments receivable	10,585,525
(Increase) decrease in accrued interest	22,259
(Increase) decrease in other assets	(334,905)
Increase (decrease) in accounts payable	(1,477)
Increase (decrease) in refunds payable	16,460,459
Net cash provided by operating activities	<u>\$12,775,727</u>
 Cash flows from investing activities	
Proceeds from maturities of investments	\$73,660,000
Purchase of investments	<u>(85,674,368)</u>
Net cash used in investing activities	<u>(\$12,014,368)</u>
 Net increase in cash and cash equivalents	\$761,359
Cash and cash equivalents, beginning of year	<u>62,483,709</u>
 Cash and cash equivalents, end of year	<u><u>\$63,245,068</u></u>

SUBSEQUENT EVENT

In previous years, refunds of past assessments were treated as credits against future assessments. At the request of the Virginia Bureau of Insurance, beginning in 2010, the Association altered the way it handles refunds of past assessments. Instead of treating the refunds as credits against future assessments, the Association will issue refund checks to member insurers. Refunds that had previously been authorized and were being held as credits against future assessments, as well as authorized refunds of assessments for the 2009 calendar year, resulted in over \$25 million being sent to the members in early 2010.

A majority of the aforementioned refunds involved assessments in which a certificate of contribution was issued pursuant to Code of Virginia §38.2-1606. Members can amortize the certificates of contribution over a ten-year period and can utilize the amount of the annual amortization as a deduction from premium tax liabilities incurred on business transacted in Virginia. Since the issuance of the certificates of contribution may have resulted or will result in a reduction in the members' premium tax liabilities, the majority of the \$25 million in refunds was subsequently paid to the State Corporation Commission and deposited with the State Treasurer.

CONCLUSION

The courteous cooperation of the Association's administrator, Guaranty Fund Management Services, is gratefully acknowledged.

In addition to the undersigned, Jennifer K. Blizzard, CFE participated in the work of the examination.

Respectfully submitted,

A handwritten signature in black ink, appearing to read 'Theresa C. Lewis', with a long horizontal flourish extending to the right.

Theresa C. Lewis, CFE
Senior Insurance Examiner

VIRGINIA PROPERTY AND CASUALTY INSURANCE GUARANTY ASSOCIATION

One Bowdoin Square
Boston, MA 02114-2916
(617) 227-7020 (800) 852-2003
Claim Department Fax: (617) 305-0001

October 6, 2010

Mr. David H. Smith
Chief Examiner
Commonwealth of Virginia
State Corporation Commission
Bureau of Insurance
P.O. Box 1157
Richmond, VA 23218

STATE CORP COMMISSION
BUREAU OF INSURANCE
10 OCT 12 AM 10:11

Dear Mr. Smith:

Please accept this letter as acknowledgement of the receipt of the Virginia Property and Casualty Insurance Guaranty Association Examination Report as of December 31, 2009.

Please provide us with fifteen copies of the report.

If you have any questions, please contact me at (617) 603-4736 or klavin@gfms.org.

Sincerely,



Kathleen M. Lavin
Treasurer