

**REPORT ON EXAMINATION**  
**OF**  
**AMERICAN CAPITAL ASSURANCE**  
**CORP.**

**ST. PETERSBURG, FLORIDA**

**AS OF**  
**DECEMBER 31, 2008**

**BY THE**  
**OFFICE OF INSURANCE REGULATION**

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Tallahassee, Florida

February 26, 2010

Kevin M. McCarty  
Commissioner  
Office of Insurance Regulation  
State of Florida  
Tallahassee, Florida 32399-0326

Dear Sir:

Pursuant to your instructions, in compliance with Section 624.316, Florida Statutes, and in accordance with the practices and procedures promulgated by the National Association of Insurance Commissioners (NAIC), we have conducted an examination as of December 31, 2008, of the financial condition and corporate affairs of:

**AMERICAN CAPITAL ASSURANCE CORP.  
805 EXECUTIVE CENTER DRIVE WEST  
ST. PETERSBURG, FLORIDA 33702**

Hereinafter referred to as, the "Company". Such report of examination is herewith respectfully submitted.

## **SCOPE OF EXAMINATION**

This examination covered the period of January 1, 2008, through December 31, 2008. The Company was last examined by representatives of the Florida Office of Insurance Regulation (Office) as of December 31, 2007. This examination commenced with planning at the Office on August 19, 2009. The fieldwork commenced on August 31, 2009, and concluded as of February 26, 2010.

This financial examination was a statutory financial examination conducted in accordance with the Financial Condition Examiners Handbook, Accounting Practices and Procedures Manual and annual statement instructions promulgated by the NAIC as adopted by Rules 69O-137.001(4) and 69O-138.001, Florida Administrative Code, with due regard to the statutory requirements of the insurance laws and rules of the State of Florida.

The Financial Condition Examiners Handbook requires that the examination be planned and performed to evaluate the financial condition and identify prospective risks of the Company by obtaining information about the Company including corporate governance, identifying and assessing inherent risks within the Company, and evaluating system controls and procedures used to mitigate those risks. An examination also includes assessing the principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation and management's compliance with Statutory Accounting Principles and annual statement instructions when applicable to domestic state regulations.

Risk-focused examinations consist of a seven-phase process that can be used to identify and assess risk, assess the adequacy and effectiveness of strategies/controls used to mitigate risk and assist in determining the extent and nature of procedures and testing to be utilized in order to

complete the review of that activity. The process should generally include a determination of the quality and reliability of the corporate governance structure and risk management programs. In addition, it can be used for verification of specific portions of the financial statements or other limited-scope reviews, increased focus on, and can result in increased substantive testing of, accounts identified as being at high risk of misstatement. Conversely, the risk assessment process should result in decreased focus on, and fewer substantive tests on the accounts identified as being at low risk of misstatement. The risk-focused surveillance process can be used to assist examiners in targeting areas of high-risk.

In this examination, emphasis was directed to the quality, value and integrity of the statement of assets and the determination of liabilities, as those balances affect the financial solvency of the Company as of December 31, 2008. Transactions subsequent to year-end 2008 were reviewed where relevant and deemed significant to the Company's financial condition.

All accounts and activities of the Company were considered in accordance with the risk-focused examination process.

The examination included a review of the corporate records and other selected records deemed pertinent to the Company's operations and practices. In addition, the NAIC IRIS ratio reports, the A.M. Best Report, the Company's independent audit reports and certain work papers prepared by the Company's independent certified public accountant (CPA) and other reports as considered necessary were reviewed and utilized where applicable within the scope of this examination.

This report of examination was confined to financial statements and comments on matters that involved departures from laws, regulations or rules, or which were deemed to require special explanation or description.

### **Status of Adverse Findings from Prior Examination**

There were no exceptions or findings in the examination as of December 31, 2007.

## **HISTORY**

### **General**

The Company was incorporated in Florida on June 1, 2006, and commenced business on June 30, 2006 as American Capital Assurance Corp.

The Company was party to Consent Order No. 86390-06-CO, filed June 1, 2006, with the Office regarding the application for the issuance of a Certificate of Authority. The Company was in compliance with the provisions of this consent order.

The Company was authorized to transact the following insurance coverage in Florida on December 31, 2008:

- Fire
- Homeowners' multi peril
- Commercial multi peril
- Inland marine
- Other liability

The Articles of Incorporation and the Bylaws were not amended during the period covered by this examination.

## Capital Stock

As of December 31, 2008, the Company's capitalization was as follows:

Number of authorized common capital shares	1,000
Number of shares issued and outstanding	1,000
Total common capital stock	\$1,000
Par value per share	\$1.00

The Company was a wholly owned subsidiary of Safe Harbour Holdings, LLC (Parent), a limited liability company formed in Delaware. The ultimate parents were Flexpoint Fund, LP (52%), New Capital Partners Private Equity, LP (8%), and ARX Holding Corp (40%).

## Profitability of Company

The following table shows the profitability trend (in dollars) of the Company for the period of operations, as reported in the filed annual statements.

	<b>2008</b>	<b>2007</b>	<b>2006</b>
Premiums Earned	43,011,010	20,758,172	133,718
Net Underwriting Gain/(Loss)	13,257,469	2,913,631	(1,180,391)
Net Income	9,609,510	2,013,383	(830,912)
Total Assets	103,337,454	82,457,830	55,092,679
Total Liabilities	40,528,487	29,690,389	5,647,226
Surplus As Regards Policyholders	62,808,972	52,767,440	49,445,453

## Dividends to Stockholders

There were no declared or paid dividends to its stockholder in 2008.

## Management

The annual shareholder meeting for the election of directors was held in accordance with Sections 607.1601 and 628.231, Florida Statutes. Directors serving as of December 31, 2008, were:

### Directors

<b>Name and Location</b>	<b>Principal Occupation</b>
John Franklin Auer St. Petersburg, Florida	American Strategic Insurance Corp. President, Director and CEO
Marc Fasteau New York, New York	Fulcrum Partners, LLC Managing Director
Gregory Scott Hendrick Hamilton, Bermuda	XL Re, Ltd Senior Vice President
Kevin Robert Milkey St. Petersburg, Florida	American Strategic Insurance Corp. Executive Vice President
James Brawner Little, III Birmingham, Alabama	New Capital Partners, Inc. Managing Partner

The Board of Directors in accordance with the Company's bylaws appointed the following senior officers:

### Senior Officers

<b>Name</b>	<b>Title</b>
John Franklin Auer	President and Treasurer
Marc Fasteau	Secretary
Kevin Robert Milkey	Assistant Secretary
Bobby Chastain Dollar	Vice President
Gregory Edward Stewart	Vice President

The Company's board appointed several internal committees in accordance with Section 607.0825, Florida Statutes. Following were the principal internal board committees and their members as of December 31, 2008:

**Audit Committee**

Marc Fasteau<sup>1</sup>  
Gregory Scott Hendrick  
James Brawner Little, III

**Investment Committee**

John Franklin Auer  
James Brawner Little, III  
Marc Fasteau<sup>1</sup>

<sup>1</sup>**Chairman**

**Conflict of Interest Procedure**

The Company adopted a policy statement requiring annual disclosure of conflicts of interest in accordance with the NAIC Financial Condition Examiners Handbook.

**Corporate Records**

The recorded minutes of the shareholder, Board of Directors, and certain internal committees were reviewed for the period under examination. The recorded minutes of the Board adequately documented its meetings and approval of Company transactions and events in accordance with Section 607.1601, Florida Statutes.

## **Acquisitions, Mergers, Disposals, Dissolutions, and Purchase or Sales Through Reinsurance**

On January 23, 2008, the Company acquired 100% of the outstanding capital stock of ACA Home Insurance Company (ACA Home), formerly known as Home Pointe Insurance Company a Florida domestic property and casualty insurer.

## **Surplus Debentures**

On November 21, 2006, the Company issued a surplus note to the State Board of Administration of Florida in return for \$25.0 Million. Interest on the unpaid principal balance was calculated at the rate equivalent to the 10-year U.S. Treasury Bond rate. Any payments of interest or principal were subject to approval by the Office. In 2008, 2007 and 2006, the Company paid \$1,552,416, \$1,206,694 and \$131,826 in interest, respectively, with the approval of the Office.

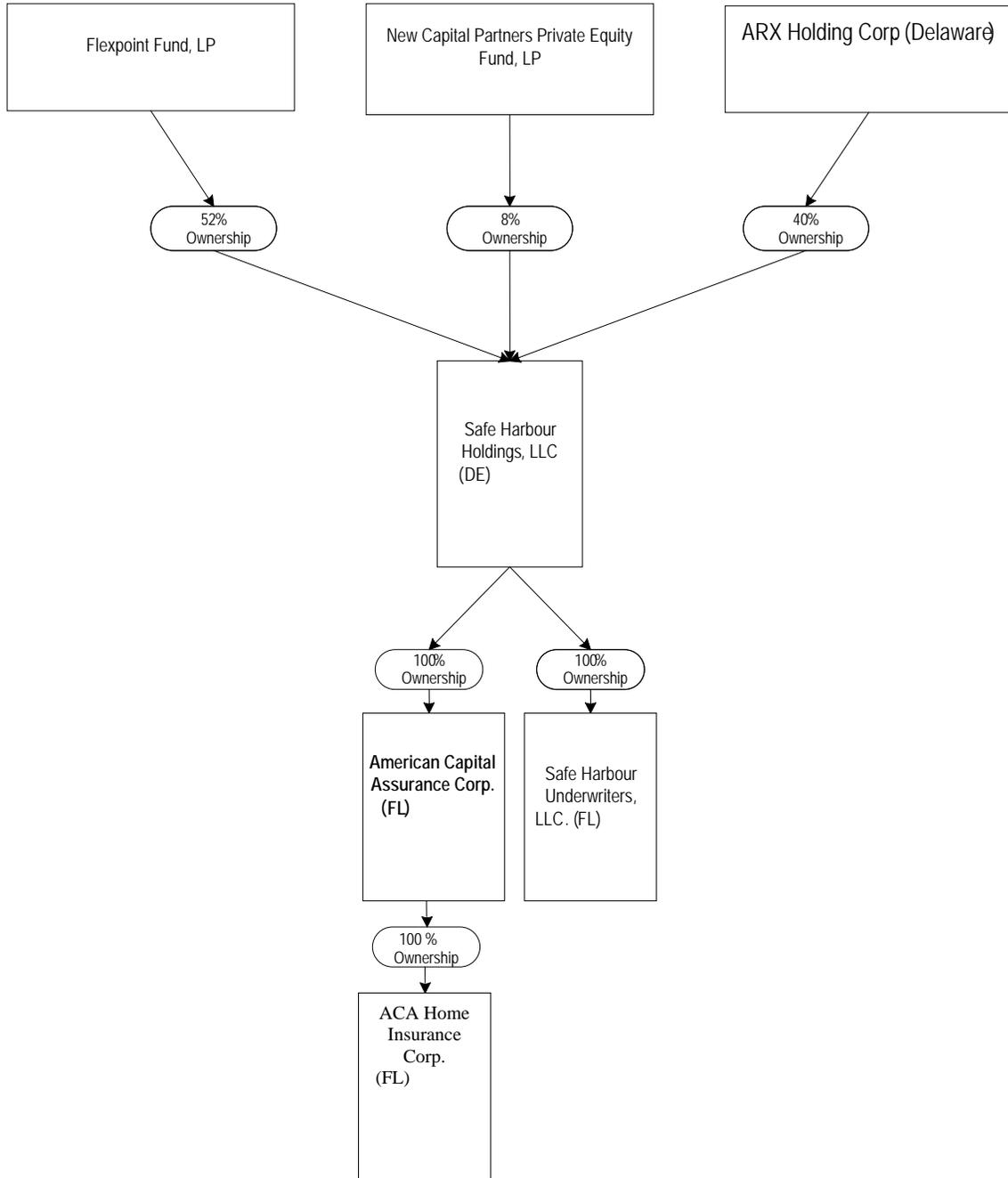
## **AFFILIATED COMPANIES**

The Company was a member of an insurance holding company system as defined by Rule 69O-143.045(3), Florida Administrative Code. The latest holding company registration statement was filed with the State of Florida on October 12, 2009 as required by Section 628.801, Florida Statutes, and Rule 69O-143.046 (4), Florida Administrative Code.

An organizational chart as of December 31, 2008, reflecting the holding company system, is shown below. Schedule Y of the Company's 2008 annual statement provided a list of all related companies of the holding company group.

**American Capital Assurance Corp.  
ORGANIZATIONAL CHART**

**DECEMBER 31, 2008**



The following agreements were in effect between the Company and its affiliates:

### **Tax Allocation Agreement**

The Company, along with its subsidiary, ACA Home, filed a consolidated federal income tax return. The method of allocation for the liability for the federal income tax was in an amount not to exceed that which would have been due had they filed a separate income tax return.

### **Intercompany Settlement Agreement**

The Company entered into an agreement with related parties through common ownership with ARX Holding Corp. and Safe Harbour Holding, LLC, effective December 1, 2007, whereby the Companies mutually acknowledge that in the ordinary course of business, it may become feasible for one company to pay expenses on behalf of another company. In such cases, the companies shall submit a bill monthly, for any expenses incurred on behalf of another and shall remit payment in full no later than 90 days after receipt.

### **Managing General Agent Agreement**

The Company entered into a managing general agent (MGA) agreement with ASI Underwriters Corp (ASIU) effective June 1, 2006. The agreement was to automatically renew for consecutive 1-year terms upon the same term provisions. ASIU provided policy management services, including underwriting and claims administration for personal lines, and claims administration for all lines. ASIU received a \$25 per policy fee, plus the commission calculated as a percentage of written premium.

The Company also entered into a one year MGA agreement with Safe Harbour Underwriters, LLC (Safe Harbour) effective March 1, 2007, whereby Safe Harbour provided policy management services including underwriting and premium processing for commercial lines. Safe Harbour received a \$25 per policy fee plus commissions calculated as 10% of the written premium and 5% of incurred non catastrophe losses and 1% of incurred catastrophe losses.

### **Administration Agreement**

The Company entered into an agreement with ARX Holding Corp (ARX), of St. Petersburg, Florida (the "Administrator") effective November 1, 2006. ARX provided services including but not limited to the completion of monthly financial statements under both Statutory Accounting Principles and Generally Accepted Accounting Principles for remuneration.

### **FIDELITY BOND**

The Company maintained fidelity bond coverage up to \$1,000,000 with a deductible of \$25,000, an amount considered adequate by the NAIC.

### **PENSION, STOCK OWNERSHIP AND INSURANCE PLANS**

The Company had a defined contribution plan. All employees of the Company were covered by a qualified contribution plan sponsored by the Company. The assets were commingled under one plan with its affiliates, Safe Harbour Underwriters LLC, American Strategic Insurance Corp, ASI Underwriters Corp, ASI Lloyds and Sunshine Security Insurance Agency, Inc. Contributions of up

to six percent of each employee's compensation were made each pay period. The Company's contribution for 2008 was \$15,465.

## STATUTORY DEPOSITS

The following securities were deposited with the State of Florida as required by Section 624.411, Florida Statutes:

STATE	Description	Par Value	Market Value
FL	Ohio St Dev Auth Rev	<u>\$300,000</u>	<u>\$322,656</u>
TOTAL SPECIAL DEPOSITS		<u>\$300,000</u>	<u>\$322,656</u>

## INSURANCE PRODUCTS AND RELATED PRACTICES

### Territory

The Company was authorized to transact insurance only in the state of Florida.

### Treatment of Policyholders

The Company established procedures for handling written complaints in accordance with Section 626.9541(1) (j), Florida Statutes.

The Company maintained a claims procedure manual that included detailed instructions for handling each type of claim in accordance with Section 626.9541(1) (i) 3a, Florida Statutes.

## REINSURANCE

The reinsurance agreements reviewed complied with NAIC standards with respect to the standard insolvency clause, arbitration clause, transfer of risk, reporting and settlement information deadlines.

### **Assumed**

The Company entered into a 100% quota share agreement with ACA Home covering all policies issued subsequent to the purchase of the subsidiary.

### **Ceded**

Under agreement covering the period from June 1, 2008 through June 1, 2009, the Company ceded risk on an excess of loss basis to various reinsurers.

#### Multi-line Excess Per Risk

The Company's retention was \$650,000 and the reinsurer's limits for each risk each loss was up to \$9.35 million.

#### Excess Catastrophe

The Company's retention was \$8.5 million and the reinsurer's limits for all loss occurrences were up to \$186 million.

The Company also was a participant in the Florida Hurricane Catastrophe Fund which provided hurricane-only excess catastrophe coverage.

The reinsurance contracts were reviewed by the Company's appointed actuary and were utilized in determining the ultimate loss opinion.

## **ACCOUNTS AND RECORDS**

The Company maintained its principal operational offices in St. Petersburg, Florida, where this examination was conducted.

An independent CPA audited the Company's statutory basis financial statements annually for the years 2008, in accordance with Section 624.424(8), Florida Statutes. Supporting work papers were prepared by the CPA as required by Rule 69O-137.002, Florida Administrative Code.

The Company's accounting records were maintained on a computerized system. The Company's balance sheet accounts were verified with the line items of the annual statement submitted to the Office.

The Company and non-affiliates had the following agreements:

### **Custodial Agreement**

The Company had a custodial agreement with JP Morgan World Wide Securities Services dated November 2, 2007. This agreement contained certain provisions and safeguards as required by Rule 69O-142.042, Florida Administrative Code.

## **Independent Auditor Agreement**

Effective January 13, 2009, the Company's Board of Directors, entered into an agreement with Gregory, Sharer & Stuart, P.A. CPA's to audit the Company's financial statements for the period of this examination.

## **Information Technology Report**

Tracy Gates, CISA, of Highland Clark, LLC performed an evaluation of the information technology and computer systems of the Company. Results of the evaluation were noted in the Information Technology Report provided to the Company.

## **FINANCIAL STATEMENTS PER EXAMINATION**

The following pages contain financial statements showing the Company's financial position as of December 31, 2008, and the results of its operations for the year then ended as determined by this examination. Adjustments made as a result of the examination are noted in the section of this report captioned, "Comparative Analysis of Changes in Surplus."

**American Capital Assurance Corp.**  
**Assets**  
**DECEMBER 31, 2008**

	Per Company	Examination Adjustments	Per Examination
Bonds	\$71,200,226	\$0	\$71,200,226
Stocks:			
Common	14,985,375		14,985,375
Real Estate:			
Properties			
occupied by Company	0		0
Other properties	0		0
Cash:	8,468,801		8,468,801
Other investments	0		0
Aggregate write-in for invested assets	0		0
Agents' Balances:			
Uncollected premium	2,055,568	0	2,055,568
Deferred premium	2,593,700		2,593,700
Reinsurance recoverable	22,497		22,497
Net deferred tax assets	2,869,965	0	2,869,965
Interest and dividend income due & accrued	755,344		755,344
Receivable from parents, subsidiaries and affiliates	232,793		232,793
Equities and deposits in pools and associations	0		0
Current federal and foreign income tax recoverable and interest thereon	153,185	0	153,185
Totals	<u>\$103,337,454</u>	<u>\$0</u>	<u>\$103,337,454</u>

**American Capital Assurance Corp.  
Liabilities, Surplus and Other Funds**

**DECEMBER 31, 2008**

	Per Company	Examination Adjustments	Per Examination
Losses	\$6,934,866		\$6,934,866
Reinsurance payable on paid loss and lae	136,492		136,492
Loss adjustment expenses	907,956		907,956
Commission payable	687,387	0	687,387
Other expenses	369,098		369,098
Taxes, licenses and fees	1,024,120		1,024,120
Unearned premium	25,351,069		25,351,069
Advanced premium	2,737,454		2,737,454
Ceded reinsurance premium payable	2,110,378		2,110,378
Payable to parent, subsidiaries and affiliates	269,667		269,667
Aggregate write-ins for liabilities	0		0
<b>Total Liabilities</b>	<b>\$40,528,487</b>	<b>\$0</b>	<b>\$40,528,487</b>
Common capital stock	\$1,000		\$1,000
Surplus notes	25,000,000		25,000,000
Gross paid in and contributed surplus	24,999,000		24,999,000
Unassigned funds	12,808,972		12,808,972
<b>Surplus as regards policyholders</b>	<b>\$62,808,972</b>		<b>\$62,808,972</b>
<b>Total liabilities, surplus and other funds</b>	<b>\$103,337,459</b>	<b>\$0</b>	<b>\$103,337,459</b>

**American Capital Assurance Corp.  
Statement of Income**

**DECEMBER 31, 2008**

<b>Underwriting Income</b>		
Premiums earned		\$43,011,010
	<b>Deductions:</b>	
Losses incurred		8,550,144
Loss expenses incurred		983,015
Other underwriting expenses incurred		20,220,382
Aggregate write-ins for underwriting deductions		0
Total underwriting deductions		<u>\$29,753,541</u>
Net underwriting gain or (loss)		\$13,257,469
<b>Investment Income</b>		
Net investment income earned		\$3,065,788
Net realized capital gains or (losses)		(493,058)
Net investment gain or (loss)		<u>\$2,572,730</u>
<b>Other Income</b>		
Net gain or (loss) from agents' or premium balances charged off		\$0
Finance and service charges not included in premiums		99,850
Aggregate write-ins for miscellaneous income		0
Total other income		<u>\$99,850</u>
Net income before dividends to policyholders and before federal & foreign income taxes		\$15,930,049
Dividends to policyholders		<u>0</u>
Net Income, after dividends to policyholders, but before federal & foreign income taxes		\$15,930,049
Federal & foreign income taxes		<u>6,320,539</u>
Net Income		\$9,609,510
<b>Capital and Surplus Account</b>		
Surplus as regards policyholders, December 31 prior year		\$52,767,440
Net Income		\$9,609,510
Net unrealized capital gains or losses		(815,501)
Change in non-admitted assets		0
Change in net deferred income tax		1,463,714
Change in non-admitted assets		(216,193)
Surplus adjustments: Paid in		0
Aggregate write-ins for gains and losses in surplus		0
Examination Adjustment		0
Change in surplus as regards policyholders for the year		<u>\$10,041,530</u>
Surplus as regards policyholders, December 31, 2008		<u><u>\$62,808,970</u></u>

## COMMENTS ON FINANCIAL STATEMENTS

### Liabilities

Loss and Loss adjustment expense \$7,842,822

An outside actuarial firm appointed by the Board of Directors, rendered an opinion that the amounts carried in the balance sheet as of December 31, 2008, made a reasonable provision for all unpaid loss and loss expense obligations of the Company under the terms of its policies and agreements.

Kay Kufera, FCAS of Kufera Consultants, Inc. was retained by the Office to conduct a review of the Company's loss and loss adjustment expense reserves as of December 31, 2008, and was in concurrence with this opinion.

### Capital and Surplus

The amount reported by the Company of \$62,808,972 exceeded the minimum of \$4,000,000 required by Section 624.408, Florida Statutes.

A comparative analysis of changes in surplus is shown below.

**American Capital Assurance Corp**  
**COMPARATIVE ANALYSIS OF CHANGES IN SURPLUS**  
**DECEMBER 31, 2008**

The following is a reconciliation of Surplus as regards policyholders between that reported by the Company and as determined by the examination.

Surplus as Regards Policyholders December 31, 2008, per Annual Statement	\$62,808,972
-----------------------------------------------------------------------------	--------------

	<u>PER COMPANY</u>	<u>PER EXAM</u>	<u>INCREASE (DECREASE) IN SURPLUS</u>
<b>ASSETS:</b>			
No adjustments			\$0
<b>LIABILITIES:</b>			
No adjustments			\$0
Net Change in Surplus:			0
Surplus as Regards Policyholders December 31, 2008, Per Examination			\$62,808,972

## **SUMMARY OF FINDINGS**

### **Compliance with previous directives**

The Company took the necessary actions to comply with the recommendations made in the 2007 examination report issued by the Office.

### **Current examination comments and corrective action**

There were no findings in this examination.

## CONCLUSION

The insurance examination practices and procedures as promulgated by the NAIC have been followed in ascertaining the financial condition of **American Capital Assurance Corp.** as of December 31, 2008, consistent with the insurance laws of the State of Florida.

Per examination findings, the Company's Surplus as regards policyholders was \$62,808,972 in compliance with Section 624.408, Florida Statutes.

In addition to the undersigned, Kethessa Carpenter, CPA, Financial Examiner/Analyst Supervisor, Kay Kufera, FCAS of Kufera Consultants, Inc., and Tracy Gates, CISA of Highland Clark, LLC participated in the examination.

Respectfully submitted,

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Mark A. Brown  
Reinsurance/Financial Specialist  
Florida Office of Insurance Regulation