

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

**ST. PETERSBURG, FLORIDA**

**AS OF**  
**DECEMBER 31, 2007**

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

## TABLE OF CONTENTS

<b>LETTER OF TRANSMITTAL .....</b>	<b>-</b>
<b>SCOPE OF EXAMINATION.....</b>	<b>1</b>
STATUS OF ADVERSE FINDINGS FROM PRIOR EXAMINATION .....	2
<b>HISTORY .....</b>	<b>2</b>
GENERAL .....	2
CAPITAL STOCK .....	3
PROFITABILITY OF COMPANY .....	3
DIVIDENDS TO STOCKHOLDERS .....	4
MANAGEMENT .....	4
CONFLICT OF INTEREST PROCEDURE.....	5
CORPORATE RECORDS .....	5
ACQUISITIONS, MERGERS, DISPOSALS, DISSOLUTIONS, AND PURCHASE OR SALES THROUGH REINSURANCE.....	6
SURPLUS DEBENTURES .....	6
<b>AFFILIATED COMPANIES .....</b>	<b>6</b>
<b>ORGANIZATIONAL CHART .....</b>	<b>8</b>
MANAGING GENERAL AGENCY AGREEMENT.....	9
ADMINISTRATION AGREEMENT.....	10
<b>FIDELITY BOND.....</b>	<b>10</b>
<b>PENSION, STOCK OWNERSHIP AND INSURANCE PLANS .....</b>	<b>10</b>
<b>STATUTORY DEPOSITS.....</b>	<b>11</b>
<b>INSURANCE PRODUCTS AND RELATED PRACTICES.....</b>	<b>11</b>
TERRITORY .....	11
TREATMENT OF POLICYHOLDERS.....	12
<b>REINSURANCE .....</b>	<b>12</b>
ASSUMED.....	12
CEDED .....	12
<b>ACCOUNTS AND RECORDS.....</b>	<b>13</b>
CUSTODIAL AGREEMENT .....	14
INVESTMENT ADVISORY AGREEMENT .....	14
INFORMATION TECHNOLOGY REPORT.....	14
<b>FINANCIAL STATEMENTS PER EXAMINATION.....</b>	<b>14</b>
ASSETS .....	15
LIABILITIES, SURPLUS AND OTHER FUNDS .....	16
STATEMENT OF INCOME.....	17

<b>COMMENTS ON FINANCIAL STATEMENTS.....</b>	<b>18</b>
LIABILITIES .....	18
CAPITAL AND SURPLUS.....	18
<b>AMERICAN CAPITAL ASSURANCE CORP .....</b>	<b>19</b>
<b>COMPARATIVE ANALYSIS OF CHANGES IN SURPLUS.....</b>	<b>19</b>
<b>SUMMARY OF FINDINGS .....</b>	<b>20</b>
<b>SUBSEQUENT EVENTS.....</b>	<b>20</b>
<b>CONCLUSION .....</b>	<b>21</b>

Tallahassee, Florida

June 12, 2008

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, 2007, of the financial condition and corporate affairs of:

**American Capital Assurance Corp.  
805 Executive Center Drive West  
Suite 300  
St. Petersburg, FL 33702**

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

## **SCOPE OF EXAMINATION**

This examination covered the period from inception through December 31, 2007. This examination commenced, with planning at the Florida Office of Insurance Regulation (Office), on March 17, 2008, to March 21, 2008. The fieldwork commenced on March 24, 2008, and was concluded as of June 12, 2008.

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 NAIC 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 NAIC annual statement instructions when applicable to domestic state regulations.

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 is confined to financial statements and comments on matters that involve departures from laws, regulations or rules, or which are deemed to require special explanation or description.

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

This is the first examination of the Company.

## **HISTORY**

### **General**

The Company was incorporated in Florida on June 1, 2006 and commenced business on June 30, 2006. The Company wrote through independent insurance agents within the State of Florida.

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 that order.

At December 31, 2007, the Company was authorized to write the following lines of business: Fire, Allied lines, Homeowners' multi peril, Commercial multi peril, Inland marine, and Other liability.

The articles of incorporation and bylaws were not amended during the period under examination.

## **Capital Stock**

As of December 31, 2007, 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 is a wholly owned subsidiary of Safe Harbour Holdings, LLC (Parent), a privately owned company formed in Delaware. The ultimate parents are Flexpoint Fund, LP (52%), New Capital Partners Private Equity, LP (8%), and ARX Holding Corp. (40%). ARX Holding Corp., a Delaware company, was owned 46% by XL Re Ltd., a Bermuda corporation, 25% by ARX Executive Holdings, LLP, a Florida company, 11% by Marc Fasteau, a New York resident, 10% by Fasteau Insurance Holdings, LLC, a Delaware company and the remaining 8% was owned by other individuals and entities. XL Re Ltd. was owned 100% by Mid Ocean Holdings Ltd., a Bermuda corporation, which was owned 100% by Mid Ocean Limited, which was owned 100% by XL Capital Limited, a Cayman corporation. ARX Executive Holdings, LLP was owned 80% by John F. Auer and 20% by Kevin R. Milkey.

## **Profitability of Company**

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

	<b>2007</b>	<b>2006</b>
Premiums Earned	20,758,172	133,718
Net Underwriting Gain/(Loss)	2,913,631	(1,180,391)
Net Income	2,013,383	(830,912)
Total Assets	82,457,831	55,092,679
Total Liabilities	29,690,389	5,647,226
Surplus As Regards Policyholders	52,767,440	49,445,453

### **Dividends to Stockholders**

There were no declared or paid dividends to its stockholder in either 2006 or 2007.

### **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, 2007, were:

#### **Directors**

##### **Name and Location**

##### **Principal Occupation**

John Franklin Auer  
St. Petersburg, Florida

American Strategic Insurance Corp.  
President, Director and CEO

Marc Fasteau, Chair  
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
Kevin Robert Milkey	Executive Vice President
Marc Fasteau	Secretary

The Company's board appointed several internal committees in accordance with Section 607.0825, Florida Statutes. Following are the principal internal board committees and their members as of December 31, 2007:

#### **Audit Committee**

Marc Fasteau, Chair  
Gregory Scott Hendrick  
James Brawner Little, III

#### **Investment Committee**

John Franklin Auer  
James Brawner Little, III  
Marc Fasteau, Chair

### **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, including the authorization of investments as required by Section 625.304, Florida Statutes.

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

During this examination period, there were no acquisitions, mergers, disposals, dissolutions or purchases or sales through reinsurance.

#### **Subsequent Event:**

On January 23, 2008, the Company purchased Home Pointe Insurance Company.

### **Surplus Debentures**

On November 21, 2006, the Company received funds from the State Board of Administration of Florida in the form of a surplus note in the amount of \$25. million. For the first three years of the note, the Company was only required to make interest payments on a quarterly basis. Any payments of interest or principal were subject to approval by the Office. In 2007 and 2006, the Company accrued and paid \$1,206,694 and \$131,826 in interest, respectively.

## **AFFILIATED COMPANIES**

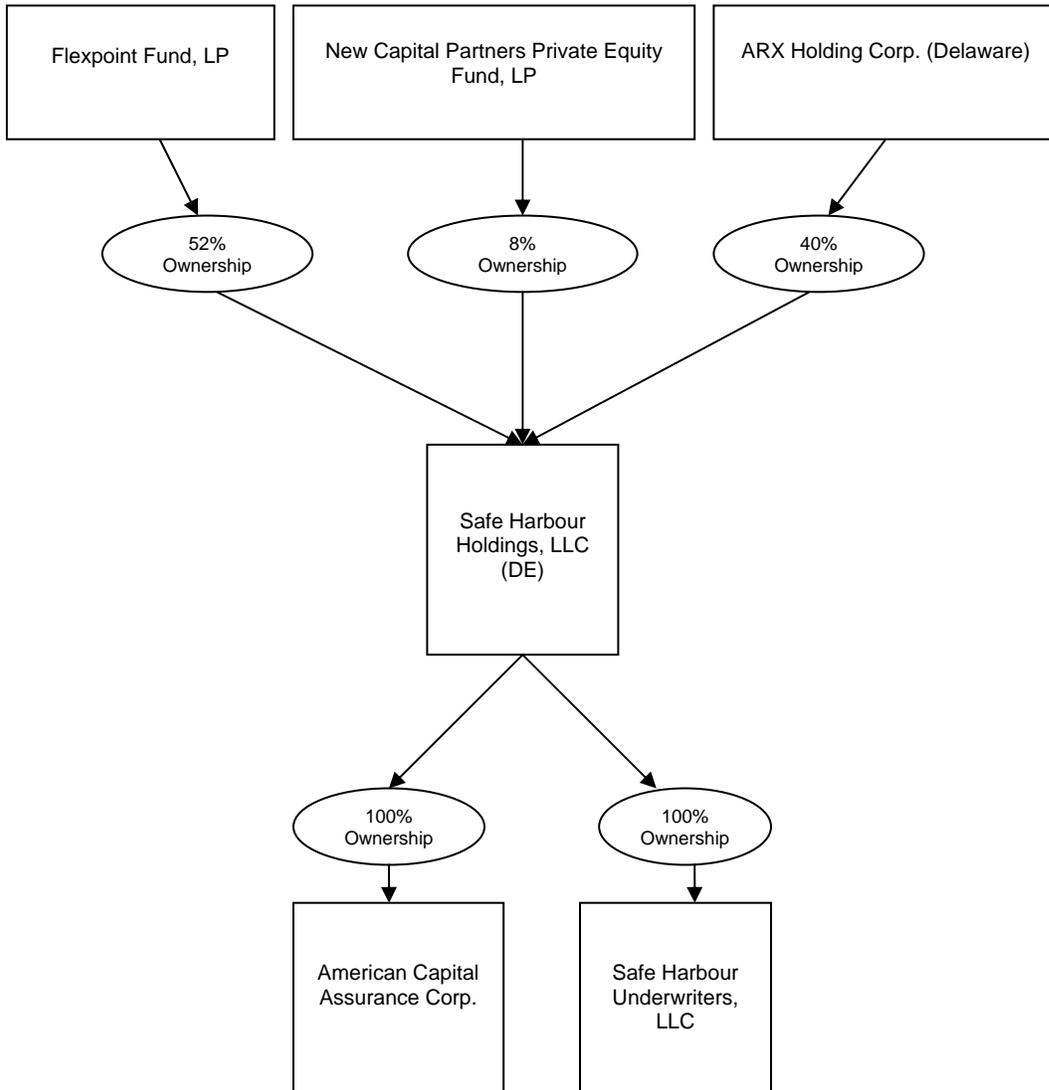
The Company was a member of an insurance holding company system as defined by Rule 69O-143.045(3), Florida Administrative Code. The latest holding company registration statement was filed with the State of Florida on November 26, 2007, as required by Section 628.801, Florida Statutes, and Rule 69O-143.046 (4), Florida Administrative Code.

**Subsequent event:** The Company filed updated holding company registration statements on February 29, 2008, and May 15, 2008, to reflect the purchase of Home Pointe Insurance Company and the related party agreements.

An organizational chart as of December 31, 2007, reflecting the holding company system, is shown below. Schedule Y of the Company's 2007 annual statement provided a list of all related companies of the holding company group.

**American Capital Assurance Corp.  
ORGANIZATIONAL CHART**

**DECEMBER 31, 2007**



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

### **Managing General Agency Agreement**

The Company entered into a managing general agency (MGA) agreement with ASI Underwriters Corp. (ASI Underwriters) effective June 1, 2006, whereby ASI Underwriters provided policy management services, including underwriting and claims administration for personal lines, and claims administration for all lines. ASI Underwriters received a fee of \$25 per policy plus the commission calculated as 8% of the written premium and 5% of incurred non catastrophe losses and 1% of incurred catastrophe losses.

This agreement had a term of one year, which was automatically renewed for consecutive one-year terms. During the first year, neither party could terminate without cause. After the first year either party may terminate, with or without cause at any time, by providing to the other party written notice of termination at least 90 days prior to effective date of termination.

### **Managing General Agency Agreement**

The Company entered into an 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 fee of \$25 per policy plus the commission calculated as 10% of the written premium and 5% of incurred non catastrophe losses and 1% of incurred catastrophe losses.

This agreement had a term of one year, which was automatically renewed for consecutive one-year terms. During the first year, neither party could terminate without cause. After the first

year either party may terminate, with or without cause at any time, by providing the other party written notice of termination at least 90 days prior to effective date of termination.

### **Administration Agreement**

The Company entered into an agreement with ARX Holding Corp. (ARX) effective November 1, 2006, whereby ARX provided certain services and personnel to the Company. The fee was paid on a monthly basis within 20 days of the end of the month in an amount necessary to reimburse ARX for the expenses of providing services.

### **FIDELITY BOND**

The Company maintained fidelity bond coverage up to \$1,000,000 with a deductible of \$25,000, which adequately covered the suggested minimum amount of coverage for the Company as recommended 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 6% of each employee's compensation were made each pay period. The Company's contribution for 2007 was \$15,500.

## 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>\$340,215</u>
TOTAL SPECIAL DEPOSITS		<u>\$300,000</u>	<u>\$340,215</u>

## INSURANCE PRODUCTS AND RELATED PRACTICES

### **Territory**

The Company was authorized to write the following lines of business: Fire, Allied lines, Homeowners' multi peril, Commercial multi peril, Inland marine, and Other liability. During 2007, the Company only wrote Commercial multi peril and Inland marine. The Company did not write Fire, Allied lines, Homeowners' multi peril, or Other liability business. Since the Company did not write business in all authorized lines, the Company was in violation of Section 624.430, Florida Statutes. Section 624.430, Florida Statutes, states that any insurer who does not write any premiums in a line or kind of insurance within a calendar year, shall have that line or kind of insurance removed from its certificate of authority.

### **Subsequent Event:**

Effective January 1, 2008, the Company entered into a quota share reinsurance agreement with Home Pointe Insurance Company whereby the Company assumed 100% of Home Pointe's premium and liability in the homeowners' and dwelling fire products on a going-forward basis.

Therefore, the Company was assuming or writing direct business in all authorized lines as required by Section 624.430, Florida Statutes.

### **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 procedures 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 had no assumed reinsurance contracts during the period under examination.

### **Ceded**

#### Excess of Loss

Under agreements covering the period from June 1, 2007 through May 31, 2008, the Company had per occurrence excess of loss coverage in three layers. The Company's retention was \$8,500,000 and the coverage purchased was 100% up to \$87,500,000. Coverage was provided by a variety of reinsurers in amounts ranging from 4% to 20%.

### Multi-line Excess Per Risk

Under agreements covering the period from June 1, 2007 through May 31, 2008, the Company had excess per risk coverage for property business. The Company's retention was \$650,000 and the coverage purchased was each risk, each loss up to \$10,000,000; each loss occurrence up to \$10,000,000; and all loss occurrences up to \$15,000,000. Coverage was provided by a variety of reinsurers in amounts ranging from 5% to 20%.

### Florida Hurricane Catastrophe Fund

The Company participated in the Florida Hurricane Catastrophe Fund which provided hurricane-only excess catastrophe coverage as required under Section 215.555, Florida Statutes.

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 2006 and 2007, 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 December 17, 2007. This agreement was in accordance with Rule 69O-143.042, Florida Administrative Code.

### **Investment Advisory Agreement**

At inception, the Company entered into an existing agreement which the Company's affiliates had with Gen Re - New England Asset Management dated July 1, 2005. Under this agreement, Gen Re - New England Asset Management managed investments within guidelines approved by the Board of Directors.

### **Information Technology Report**

INS Services, Inc. performed a computer systems evaluation on the Company. Results of the evaluation were noted in the Information Technology (IT) 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, 2007, 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, 2007**

	Per Company	Examination Adjustments	Per Examination
Bonds	\$65,692,474		\$65,692,474
Cash:	12,103,886		12,103,886
Interest and dividend income due and accrued	725,778		725,778
Premiums and considerations:			
Uncollected premiums	2,212,102		2,212,102
Deferred premiums	5,979		5,979
Reinsurance recoverable			0
Net deferred tax asset	1,623,487		1,623,487
Guaranty funds receivable or on deposit	89,075		89,075
Receivable from parents, subsidiaries and affiliates	5,050		5,050
	<hr/>		
Totals	\$82,457,831	\$0	\$82,457,831
	<hr/>		

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

**DECEMBER 31, 2007**

	Per Company	Examination Adjustments	Per Examination
Losses	\$3,236,714		\$3,236,714
Loss adjustment expenses	485,507		485,507
Commissions payable, contingent commissions	1,033,560		1,033,560
Other expenses	550,524		550,524
Taxes, licenses and fees	1,158,550		1,158,550
Current federal and foreign income taxes	182,776		182,776
Unearned premiums	23,612,572		23,612,572
Advance premiums	69,644		69,644
Funds held by Company under reinsurance treaties	(1,057,916)		(1,057,916)
Payable to parent, subsidiaries and affiliates	418,458		418,458
Total Liabilities	<u>\$29,690,389</u>	<u>\$0</u>	<u>\$29,690,389</u>
Common capital stock	\$1,000		\$1,000
Surplus note	25,000,000		25,000,000
Gross paid in and contributed surplus	24,999,000		24,999,000
Unassigned funds (surplus)	<u>2,767,440</u>		<u>2,767,440</u>
Surplus as regards policyholders	<u>\$52,767,440</u>		<u>\$52,767,440</u>

**AMERICAN CAPITAL ASSURANCE CORP.  
Statement of Income**

**DECEMBER 31, 2007**

<b>Underwriting Income</b>		
Premiums earned		\$20,758,172
	<b>Deductions:</b>	
Losses incurred		3,316,128
Loss expenses incurred		486,527
Other underwriting expenses incurred		14,041,886
Aggregate write-ins for underwriting deductions		0
Total underwriting deductions		<u>\$17,844,541</u>
Net underwriting gain or (loss)		\$2,913,631
<b>Investment Income</b>		
Net investment income earned		\$1,744,246
Net realized capital gains or (losses)		<u>(20,894)</u>
Net investment gain or (loss)		\$1,723,352
<b>Other Income</b>		
Total other income		<u>\$0</u>
Net income before dividends to policyholders and before federal and foreign income taxes		\$4,636,983
Dividends to policyholders		<u>0</u>
Net Income, after dividends to policyholders, but before federal and foreign income taxes		\$4,636,983
Federal and foreign income taxes incurred		<u>2,623,600</u>
Net Income		\$2,013,383
<b>Capital and Surplus Account</b>		
Surplus as regards policyholders, December 31 prior year		\$49,445,453
Net Income		\$2,013,383
Net unrealized capital gains or losses		0
Change in deferred income tax		1,330,101
Change in non-admitted assets		(21,498)
Examination Adjustment		<u>0</u>
Change in surplus as regards policyholders for the year		<u>\$3,321,986</u>
Surplus as regards policyholders, December 31 current year		<u><u>\$52,767,439</u></u>

## COMMENTS ON FINANCIAL STATEMENTS

### Liabilities

**Losses and Loss Adjustment Expenses** \$3,722,221

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, 2007, make a reasonable provision for all unpaid loss and loss expense obligations of the Company under the terms of its policies and agreements.

The actuary for the firm of INS Consultants, Inc. reviewed the Company's stated reserves and was in concurrence with that opinion.

### Capital and Surplus

The amount reported by the Company of \$52,767,440, exceeds 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, 2007**

Surplus as Regards Policyholders  
December 31, 2007, per Annual Statement \$52,767,440

	<u>PER COMPANY</u>	<u>PER EXAM</u>	<u>INCREASE (DECREASE) IN SURPLUS</u>
ASSETS:			
No adjustments			0
LIABILITIES:			
No adjustments			0
Net Change in Surplus:			<u>0</u>
Surplus as Regards Policyholders December 31, 2007, Per Examination			<u><u>\$52,767,440</u></u>

## **SUMMARY OF FINDINGS**

### **Compliance with previous directives**

This is the first examination of this Company.

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

There were no comments or recommendations for corrective action in the current examination.

## **SUBSEQUENT EVENTS**

On October 22, 2007 the Company signed a letter of intent to purchase Home Pointe Insurance Company. The Company filed a Form A seeking approval of the transaction with the Office on October 29, 2007. On January 23, 2008, the Company purchased Home Point Insurance Company, a Florida property and casualty insurer.

## 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, 2007, consistent with the insurance laws of the State of Florida.

Per examination findings, the Company's Surplus as regards policyholders was \$52,767,440 in compliance with Section 624.408, Florida Statutes.

In addition to the undersigned, Barry Armstrong, CFE, Supervisor, Pat Casey Davis, CFE, CPA, Examiner in Charge, Bill Holmes, CFE, Financial Examiner, Lori Ruggiero, CFE, CIE, Financial Examiner, Samita Lamsal, Financial Examiner, and Mike Young, Financial Examiner participated in this examination. We also recognize INS Consultants, Inc. and INS Services, Inc. participation in the examination.

Respectfully submitted,

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Kethessa Carpenter, CPA  
Financial Examiner/Analyst Supervisor  
Florida Office of Insurance Regulation