

REPORT ON EXAMINATION

**CAPITAL ASSURANCE
COMPANY, INC.**

ST. PETERSBURG, FLORIDA

AS OF

DECEMBER 31, 2010

BY THE

FLORIDA OFFICE OF INSURANCE REGULATION

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Tallahassee, Florida

December 9, 2011

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 Rule 690-138.005, Florida Administrative Code, and in accordance with the practices and procedures promulgated by the National Association of Insurance Commissioners (NAIC), we have conducted an examination of December 31, 2010, of the financial condition and corporate affairs of:

**CAPITAL ASSURANCE COMPANY, INC.
7901 4th STREET NORTH, SUITE 203
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, 2006, through December 31, 2010. The Company was last examined by representatives of the Florida Office of Insurance Regulation (Office) as of December 31, 2005. This examination commenced with planning at the Office from October 18, 2011, to October 20, 2011. The fieldwork commenced on October 31, 2011, and was concluded as of December 9, 2011.

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.

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

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

SUMMARY OF SIGNIFICANT FINDINGS

Current Exam Findings

There were no material findings or exceptions noted during the examination as of December 31, 2010.

Prior Examination Findings

There were no findings, exceptions, or corrective action to be taken by the Company for the examination as of December 31, 2005.

HISTORY

General

The Company was incorporated in Florida on August 15, 1978, and commenced business on October 1, 1978, as Federal Assurance Company. The Company was acquired by Ryder Systems, Inc., approximately at the time of its incorporation. The name was subsequently changed on June 23, 1982, to Capital Assurance Company, Inc.

Skandia Direct Operations Corporation (SAC), a Delaware corporation, took ownership of the Company on January 2, 1990, after purchasing all of shares of the Company's capital stock from Ryder Systems, Inc., pursuant to a Stock Purchase Agreement dated October 6, 1989.

In 1996, the Company was placed in runoff as part of a stated business decision by its ultimate parent to exit property and casualty business worldwide, with all policies being non-renewed no later than April 7, 1997. All outstanding shares of the Company were sold by SAC to IF Skadeforsakring Holding AB (ISHA), a Swedish insurance holding company on December 30, 2005.

On August 28, 2008, Sun Gulf Holdings, Inc. (Sun) acquired 100% of the Company and its sister company, Capital Assurance Services, Inc. (CASI). Sun is ultimately owned by Enstar Group Limited. CASI was the appointed run-off manager for the Company pursuant to a written agreement between the companies. CASI provides for all services related to the run-off and has its administrative offices in St. Petersburg, Florida.

In accordance with Section 624.401(1), Florida Statutes, the Company's Certificate of Authority was active for only the Allied Lines line of business. All other lines of business were withdrawn in June 1990.

Dividends to Stockholders

The Company did not declare or pay dividends during the period of examination.

Subsequent Event: On June 2, 2011, the Office approved the Company's request for a \$10 million dividend distribution and return of capital, which the Company paid its shareholder on June 20, 2011.

Capital Stock and Capital Contributions

As of December 31, 2010, the Company's capitalization was as follows:

Number of authorized common capital shares	23,500
Number of shares issued and outstanding	23,500
Total common capital stock	\$2,350,000
Par value per share	\$100.00

Control of the Company was maintained by its parent, Sun, who owned 100 percent of the stock issued by the Company, who in turn, was 100 percent owned ultimately by Enstar Group Limited, a Bermuda company.

Surplus Debentures

The Company did not have any surplus debentures during the period of this examination.

Acquisitions, Mergers, Disposals, Dissolutions, and Purchase or Sales through Reinsurance

The Company had no acquisitions, mergers, disposals, dissolutions, and purchases or sales through reinsurance during the period of this examination.

CORPORATE RECORDS

The recorded minutes of the shareholder and Board of Directors (Board) were reviewed for the period under examination. The recorded minutes of the Board adequately documented its meetings and approval of Company transactions and events, including the authorization of investments as required by Section 625.304, Florida Statutes.

Conflict of Interest

The Company adopted a policy statement requiring annual disclosure of conflicts of interest in accordance with the NAIC Financial Condition Examiners Handbook adopted by Rule 69O-138.001, Florida Administrative Code.

MANAGEMENT AND CONTROL

Management

In lieu of the annual shareholder meeting for the election of directors, the sole stockholder signed a consent statement duly electing the directors of the Company. Those directors serving as of December 31, 2010, were:

Directors

Name and Location	Principal Occupation
Karl John Wall Tierra Verde, Florida	President and COO, Enstar (US) Inc.
Robert Barry Carlson East Greenwich, Rhode Island	Executive Vice President, Enstar (US) Inc.
Donna Lynn Stolz Tampa, Florida	Executive Vice President/CAO, Enstar (US) Inc.
Andrea Jill Giannetta Providence, Rhode Island	Attorney, Vice President/Reinsurance Counsel, Enstar (US), Inc.
James Grajewski Tierra Verde, Florida	Executive Vice President, Enstar (US) Inc.

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

Senior Officers

Name	Title
Karl John Wall	President and CEO
Robert Barry Carlson	Treasurer
Thomas John Balkin	Secretary
Andrea Jill Giannetta	Senior Vice President
James Grajewski	Senior Vice President

The Company had not established an audit committee in accordance with Section 624.424 (8) (c), Florida Statutes. The Company obtained a waiver of this requirement from the Office.

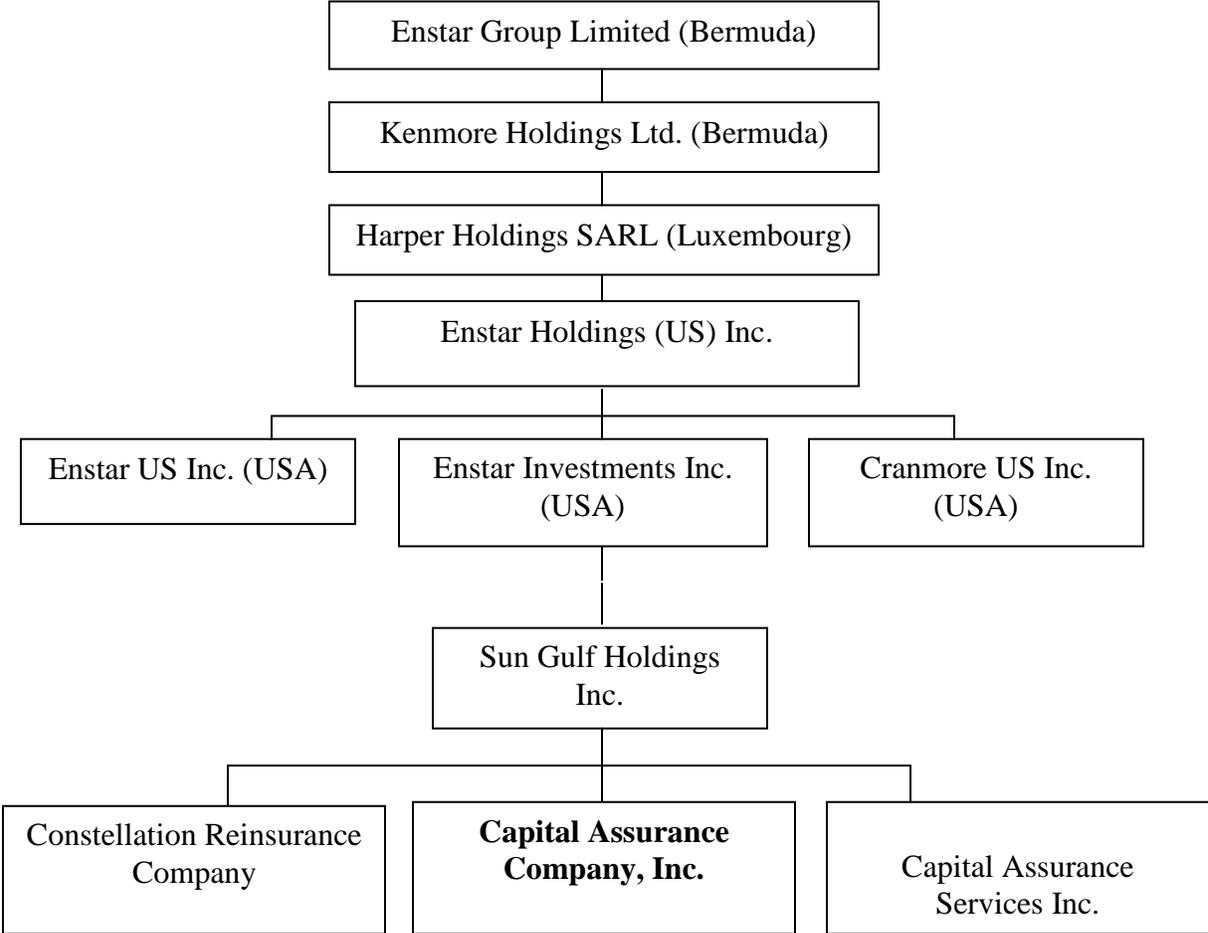
Affiliated Companies

The latest holding company registration statement was filed with the State of Florida on May 16, 2010, as required by Section 628.801, Florida Statutes, and Rule 69O-143.046, Florida Administrative Code.

An organizational chart as of December 31, 2010, reflecting the holding company system is shown below. Schedule Y of the Company's 2010 annual statement provided a list of all related companies of the holding company group.

**CAPITAL ASSURANCE COMPANY, INC.
ORGANIZATIONAL CHART**

DECEMBER 31, 2010*



*Ownership was 100% at all levels at examination date.

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

Tax Allocation Agreement

The Company, along with its parent and other named US affiliates, filed a consolidated federal income tax return with Eastar Holding (US) Inc. (Holding). On December 31, 2010, the method of allocation between the Company and Holdings. was on a separate-entity basis. Each member of the group recorded an inter-company income tax receivable or payable to the parent. Within thirty days of the remittance by the parent of any income tax payment to the taxing authorities balances are to be settled.

Facilities and Services Agreement

The Company had a Facilities and Service Agreement with its affiliate, CASI. The nature and purpose of this agreement was to provide certain services, including underwriting and claims handling, and facilities, including the use of office equipment, and the furnishing of office space by CASI to the Company. During 2010, the Company reported that it paid fees totaling \$936,000 to CASI under the terms of the agreement.

FIDELITY BOND

The Company maintained fidelity bond coverage up to \$1,000,000 with a single loss deductible of \$25,000, which reached the suggested minimum as recommended by the NAIC. Subsequent to 2010 year-end it was increased to \$5,000,000. The Company was named as a subsidiary on the policy and the amounts exceed the NAIC recommended minimum fidelity coverage.

PENSION, STOCK OWNERSHIP AND INSURANCE PLANS

The Company had no employees, and participated in no pension, stock ownership, or insurance plans.

TERRITORY AND PLAN OF OPERATIONS

The Company has been in run off since 1997 and not written insurance coverage or renewed any business. It still maintains licenses in Alabama and Florida.

Treatment of Policyholders

At the date of the examination, the Company had two direct claims, one of which has since been settled and no new business since 1997.

COMPANY GROWTH

The Company is long-term runoff and continues to work toward complete dissolution of all the Company's business.

Profitability of Company

The following table shows the profitability trend of the Company for the period of examination, as reported in the filed annual statement.

	2010	2009	2008	2007	2006
Premiums Earned	0	0	0	(7,948)	0
Net Underwriting Gain/(Loss)	5,691,614	6,612,189	(3,826,029)	(4,961)	(5,337)
Net Income	4,235,792	6,087,746	(3,036,003)	1,983,065	863,625
Total Assets	26,878,336	29,648,191	30,570,727	38,116,356	39,561,746
Total Liabilities	10,269,404	17,345,063	24,345,446	23,389,916	26,699,120
Surplus As Regards Policyholders	16,608,930	12,303,127	6,225,281	14,726,440	12,862,626

LOSS EXPERIENCE

The Company has been in runoff since April 7, 1997, and all business written by the Company was non-renewed. During the current examination period, the Company has continued to reduce its loss reserves and settle claims on business written prior to being placed in runoff.

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 assumed no new business during the period of this examination. Prior to June 30, 1997, the Company assumed risks on an excess of loss and quota share basis from several non-affiliated insurers and as of the examination date, loss reserves carried on those treaties total approximately 90% of the Company's remaining outstanding loss reserves. The examination actuary considered these exposures during review of loss reserves.

Ceded

The Company has not entered into any reinsurance contracts for the cession of business during the period of this examination. All treaties have been in run-off since June 30, 1997. 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.

The Company was exempt from a CPA audit in accordance with Section 624.424(8)(b), Florida Statutes.

The Company's accounting records were maintained by CASI under the provisions of the Facilities and Services Agreement discussed earlier. Those records were kept on computerized systems.

The Company and non-affiliates had the following agreements:

Custodial Agreement

As of the examination date, the Company had a custodial agreement with UBS Financial Services which was terminated in early 2011.

Effective February 1, 2011, a new custodian agreement with the Bank of New York Mellon was put in place to protect the Company's invested assets. The agreement was in compliance with Rule 69O-143.042, Florida Administrative Code.

Independent Auditor Agreement

The Company was exempt from Rule 69O-137.002 (7) (c), Florida Administrative Code, which requires an external independent CPA firm to perform the annual audit of its financial statements. Therefore, the Company had no independent auditor agreement.

INFORMATION TECHNOLOGY REPORT

Paul Berkebile, CISA, CFSA, CRISC, and Claude B. Granese, CPA, IT specialist both from INS Services, Inc. performed an evaluation of the information technology and computer systems of the Company. Results of the evaluation were contained in the Information Technology Report provided to the Company.

STATUTORY DEPOSITS

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

<u>State</u>	<u>Description</u>	<u>Par Value</u>	<u>Market Value</u>
FLORIDA	US Treasury Note	\$ 250,000	\$ 276,838
	US Treasury Note	<u>1,325,000</u>	<u>1,503,160</u>
TOTAL FLORIDA DEPOSITS		<u>\$1,575,000</u>	<u>\$1,779,998</u>
ALABAMA	Industrial & Misc. Bond	\$ 100,000	\$ 107,750
TOTAL SPECIAL DEPOSITS		<u>\$1,675,000</u>	<u>\$1,887,748</u>

FINANCIAL STATEMENTS PER EXAMINATION

The following pages contain financial statements showing the Company's financial position as of December 31, 2010, 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."

CAPITAL ASSURANCE COMPANY, INC.
Assets

DECEMBER 31, 2010

	Per Company	Examination Adjustments		Per Examination
Bonds	\$ 18,155,757		\$	18,155,757
Cash and short-term investments	8,396,102			8,396,102
Investment income due & accrued	240,728			240,728
Reinsurance:				
Amounts recoverable from reinsurers	78,997			78,997
Receivables from parent, subsidiaries & affiliates	6,752			6,752
Totals	\$ 26,878,336	\$ -	\$	26,878,336

CAPITAL ASSURANCE COMPANY, INC.
Liabilities, Surplus and Other Funds

DECEMBER 31, 2010

	Per Company	Examination Adjustments	Per Examination
Losses	\$ 4,846,668		\$ 4,846,668
Reinsurance payable on paid losses and loss adjustment expense	471,592		471,592
Loss adjustment expenses	2,218,597		2,218,597
Other expenses	92,000		92,000
Taxes, licenses and fees	365,381		365,381
Current federal income taxes	1,789,879		1,789,879
Provision for reinsurance	20,643		20,643
Payable to parent, subsidiaries and affiliates	464,644		464,644
Total liabilities	<u>\$ 10,269,404</u>		<u>\$ 10,269,404</u>
Common capital stock	\$2,350,000		\$2,350,000
Gross paid in and contributed surplus	9,563,835		9,563,835
Unassigned funds (surplus)	4,695,095		4,695,095
Surplus as regards policyholders	<u>\$ 16,608,930</u>		<u>\$ 16,608,930</u>
Total liabilities, capital and surplus	<u>\$ 26,878,334</u>	<u>\$ -</u>	<u>\$ 26,878,334</u>

CAPITAL ASSURANCE COMPANY, INC.
Statement of Income

DECEMBER 31, 2010

Underwriting Income		
Premiums earned		\$ -
	DEDUCTIONS:	
Losses incurred		(4,095,076)
Loss expenses incurred		(1,751,925)
Other underwriting expenses incurred		155,387
Total underwriting deductions		<u>\$ (5,691,614)</u>
Net underwriting gain or (loss)		\$5,691,614
Investment Income		
Net investment income earned		\$ 333,923
Net realized capital gains or (losses)		134
Net investment gain or (loss)		<u>\$ 334,057</u>
Other Income		
Net gain or (loss) from agents' or premium balances charged off		\$ -
Aggregate write-ins for miscellaneous income		0
Total other income		<u>\$ -</u>
Net income before dividends to policyholders and before federal & foreign income taxes		\$ 6,025,671
Dividends to policyholders		<u>0</u>
Net Income, after dividends to policyholders, but before federal & foreign income taxes		\$ 6,025,671
Federal & foreign income taxes		<u>\$ 1,789,879</u>
Net Income		\$ 4,235,792
Capital and Surplus Account		
Surplus as regards policyholders, December 31 prior year		<u>\$ 12,303,128</u>
Gains and (Losses) in Surplus		
Net Income		\$ 4,235,792
Net unrealized capital gains or losses		
Change in net deferred income taxes		(567,927)
Change in non-admitted assets		567,927
Change in provision for reinsurance		70,013
Examination Adjustment		
Change in surplus as regards policyholders for the year		<u>\$ 4,305,804</u>
Surplus as regards policyholders, December 31 current year		<u><u>\$ 16,608,933</u></u>

A comparative analysis of changes in surplus is shown below.

CAPITAL ASSURANCE COMPANY, INC.
Comparative Analysis of Changes in Surplus

DECEMBER 31, 2010

	Per Company	Per Examination	Increase (Decrease) in Surplus
Surplus as Regards Policyholders as of December 31, 2010 per Annual Statement			<u>\$ 16,608,930</u>
Assets			
No adjustment			
Liabilities			-
No adjustment			
Net Change in Surplus			<u>-</u>
Surplus as Regards Policyholders as of December 31, 2010 per Examination			<u><u>\$ 16,608,930</u></u>

COMMENTS ON FINANCIAL STATEMENTS

Liabilities

Losses and Loss Adjustment Expenses (LAE) \$7,065,265

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, 2010, made a reasonable provision for all unpaid loss and loss expense obligations of the Company under the terms of its policies and agreements.

The Office consulting actuary, Robert W. Gardner, FACS, MAAA of INS Consultants, Inc. (INS), reviewed the loss and loss adjustment expense work papers provided by the Company and determined that the Company was over reserved by \$0.4 million. However, no adjustments were made as the amount was immaterial.

Capital and Surplus

The amount of Capital and Surplus reported by the Company of \$16,608,930, exceeded the minimum of \$4,000,000 required by Section 624.408, Florida Statutes.

CONCLUSION

The insurance examination practices and procedures as promulgated by the NAIC have been followed in ascertaining the financial condition of **Capital Assurance Company, Inc.** as of December 31, 2010, consistent with the insurance laws of the State of Florida.

Per examination findings, the Company's surplus as regards policyholders was \$16,608,930, which exceeded the minimum of \$4,000,000 required by Section 624.408, Florida Statutes.

In addition to the undersigned, Hails W. Taylor, CFE, Senior Insurance Examiner, of INS Regulatory Insurance Services, Inc., and Basilous Poulos, MBA, CIA, CGAP, of the Office participated in the examination. We also recognize Robert W. Gardner, FCAS, MAAA and Michael Morro, ACAS, MAAA actuaries from INS Consultants, Inc. along with Paul Berkebile, CISA, CFSA, CRISC and Claude B. Granese, CPA, IT specialists from INS Services, Inc. also participated in the examination.

Respectfully submitted,

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