

REPORT ON EXAMINATION

OF

SEVEN SEAS INSURANCE COMPANY,

INC.

RIVIERA BEACH, FLORIDA

AS OF

DECEMBER 31, 2003

BY THE

OFFICE OF INSURANCE REGULATION

TABLE OF CONTENTS

| | |
|--|----|
| LETTER OF TRANSMITTAL | - |
| SCOPE OF EXAMINATION..... | 1 |
| Status of Adverse Findings from Prior Examination..... | 2 |
| HISTORY | 3 |
| General | 3 |
| Capital Stock..... | 3 |
| Profitability..... | 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 |
| AFFILIATED COMPANIES | 6 |
| Tax Allocation Agreement | 6 |
| Cost Sharing Agreement..... | 6 |
| ORGANIZATIONAL CHART | 7 |
| FIDELITY BOND AND OTHER INSURANCE | 8 |
| PENSION, STOCK OWNERSHIP, AND INSURANCE PLANS..... | 8 |
| STATUTORY DEPOSITS | 8 |
| INSURANCE PRODUCTS AND RELATED PRACTICES..... | 8 |
| Territory and Plan of Operation..... | 9 |
| Treatment of Policyholders | 9 |
| REINSURANCE | 10 |
| Assumed | 10 |
| Ceded | 10 |
| ACCOUNTS AND RECORDS | 10 |
| Custodial Agreement..... | 11 |

| | |
|---|----|
| CPA Agreement | 11 |
| Risk-Based Capital..... | 11 |
| | |
| FINANCIAL STATEMENTS PER EXAMINATION..... | 12 |
| Assets | 13 |
| Liabilities, Surplus and Other Funds | 14 |
| Statement of Income | 15 |
| | |
| COMMENTS ON FINANCIAL STATEMENTS..... | 16 |
| Liabilities | 16 |
| | |
| COMPARATIVE ANALYSIS OF CHANGES IN SURPLUS..... | 17 |
| | |
| SUMMARY OF FINDINGS | 18 |
| | |
| CONCLUSION | 19 |

Tallahassee, Florida
May 28, 2004

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 (FS), 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, 2003, of the financial condition and corporate affairs of:

**SEVEN SEAS INSURANCE COMPANY, INC.
821 AVENUE E
RIVIERA BEACH, FLORIDA 33404**

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, 2001 through December 31, 2003. The Company was last examined by representatives of the Florida Office of Insurance Regulation (Office) as of December 31, 2000. This examination commenced with planning at the Office on March 29, 2004, to April 2, 2004. The fieldwork commenced on April 5, 2004, and was concluded as of May 28, 2004. The examination included any material transactions and/or events occurring subsequent to the examination date and noted during the course of the examination.

This financial examination was a statutory financial examination conducted in accordance with the Financial Examiners Handbook, Accounting Practices and Procedures Manual and annual statement instructions promulgated by the NAIC as adopted by Rules 690-137.001(4) and 690-138.001, Florida Administrative Code (FAC), with due regard to the statutory requirements of the insurance laws and rules of the State of Florida.

In this examination, emphasis was directed to the quality, value and integrity of the statement assets and the determination of liabilities, as those balances affect the financial solvency of the Company.

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 Company's independent audit reports and certain work papers prepared by the Company's independent certified public accountant (CPA) were reviewed and utilized where applicable within the scope of this examination.

We valued and/or verified the amounts of the Company's assets and liabilities as reported by the Company in its annual statement as of December 31, 2003. Transactions subsequent to year-end 2003 were reviewed where relevant and deemed significant to the Company's financial condition.

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

The following is a summary of significant adverse findings contained in the Office's prior examination report as of December 31, 2000, along with resulting action taken by the Company in connection therewith.

Custody Agreement

The Company had a custodial agreement with the Bank of America for the safekeeping of its securities. The custodial agreement did not include all provisions required by Rule 69O-143.042, FAC. In addition, the agreement was governed by the laws of the State of California, instead of the State of Florida. The new custodial agreement executed in October 2004 was in compliance with Rule 69O-143.042, FAC.

HISTORY

General

The Company was incorporated in Florida on April 21, 1989, under the laws of the State of Florida, as a stock property and casualty insurer and commenced business on June 1, 1989, with the name of Seven Seas Insurance Company, Inc.

In accordance with Section 624.401(1), FS, the Company was authorized to transact the following insurance coverage, in the State of Florida, on December 31, 2003:

Ocean Marine

Inland Marine

The articles of incorporation and the bylaws were not amended during the period covered by this examination.

Capital Stock

As of December 31, 2003, the Company's capitalization was as follows:

| | |
|--|-----------|
| Number of authorized common capital shares | 20,000 |
| Number of shares issued and outstanding | 10,010 |
| Total common capital stock | \$750,750 |
| Par value per share | \$75.00 |

Control of the Company was maintained by its parent, Birdsall, Inc., (parent) who owned 100 percent of the stock issued by the Company, who in turn was 100 percent owned by NICOR Corporation, an Illinois corporation. NICOR Inc. was a publicly traded company.

Profitability of Company

The Company has reported five years of net income and net underwriting profits.

Dividends to Stockholders

In accordance with Section 628.371, FS, the Company declared and paid dividends to its stockholders during this examination:

| <u>Year</u> | <u>Amount</u> |
|-------------|---------------|
| 2001 | \$3,190,000 |
| 2002 | \$2,130,000 |
| 2003 | \$2,500,000 |

Management

The annual shareholder meeting for the election of directors was held in accordance with Sections 607.1601 and 628.231, FS. Directors serving as of December 31, 2003, were:

Directors

| Name and Location | Principal Occupation |
|---|--|
| John H. Birdsall III Charlottesville, Virginia | Private Investor |
| George Behrens Naperville, Illinois | Vice President NICOR, Inc. |
| Thomas L. Fisher Aurora, Illinois | Chairman, President & CEO NICOR, Inc. |
| Kathleen H. Halloran Naperville, Illinois | Vice President NICOR, Inc. |
| Richard Murrell Palm Beach Gardens, Florida | President & CEO Tropical Shipping |
| Russ M. Strobel Naperville, Illinois | President & CEO NICOR Gas & NICOR, Inc. |

The board of directors in accordance with the Company's bylaws, appointed the following senior officers:

Senior Officers

| Name | Title |
|----------------------|--------------------------|
| Richard Murrell | President* |
| Thomas M. Black | Executive Vice President |
| George M. Behrens | Treasurer |
| Kathleen L. Halloran | Secretary |

*James K. McIntire became president of Seven Seas Insurance Company in February 2004.

The Company did not utilize any internal committees.

As of December 31, 2003, the Company did not maintain an audit committee. However, the Company's ultimate parent, NICOR, Inc., had an audit committee, which allowed the Company to be in compliance with Section 624.424(8), FS.

Conflict of Interest Procedure

The Company had adopted a policy statement requiring annual disclosure of conflicts of interest in accordance with Section 607.0832, FS. No exceptions were noted during this examination period.

Corporate Records

The recorded minutes of the shareholder, board of directors, and executive and investment committee meetings were reviewed for the period under examination. The recorded minutes of the board adequately documented its meetings and approval of Company transactions in accordance with Section 607.1601, FS, including the authorization of investments as required by Section 625.304, FS.

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

There were no acquisitions, mergers, disposals, dissolutions, and purchase or sales through reinsurance during the current examination period.

Surplus Debentures

The Company had no surplus debentures during the current examination period.

AFFILIATED COMPANIES

The Company was a member of an insurance holding company system as defined by Rule 69O-143.045(3), FAC. The latest holding company registration statement was filed with the State of Florida on April 30, 2003, as required by Section 628.801, FS, and Rule 69O-143.046, FAC.

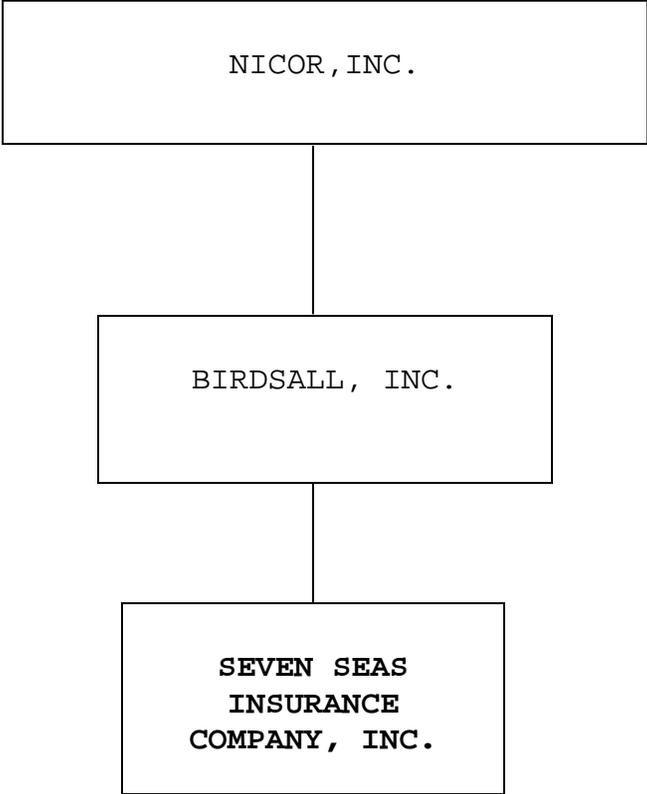
The following agreements were in effect between the Company and its affiliates:

Cost Sharing Agreement

On October 1, 1999, the Company entered into a cost sharing agreement with its parent. The agreement provided that the Company would reimburse the parent for its portion of the shared administrative, office, and personnel expenses. The contract also provided that the Company would reimburse the parent for its portion of the consolidated state and federal taxes. The method of allocation of income taxes between the companies was based upon separate return calculations.

A simplified organizational chart as of December 31, 2003, reflecting the holding company system is shown below. Schedule Y of the Company's 2003 annual statement provided a list of all related companies of the holding company group.

**SEVEN SEAS INSURANCE COMPANY, INC.
ORGANIZATIONAL CHART
DECEMBER 31, 2003**



FIDELITY BOND AND OTHER INSURANCE

The Company, along with several affiliated companies was named on a fidelity bond policy with coverage of \$10,000,000. Information was not available to compute the amount of coverage required for all companies covered under this policy; however, the amount of coverage required for the Company was only \$150,000.

PENSION, STOCK OWNERSHIP, AND INSURANCE PLANS

The Company had a pension/ retirement savings plan through its parent, Birdsall Inc.

STATUTORY DEPOSITS

The following security was deposited with the State of Florida as required by Section 624.411, FS:

| State | Description | Par Value | Market Value |
|-------|--------------------|------------|--------------|
| FL | CD, 1.1%, 06/03/04 | \$ 150,000 | \$ 150,000 |

INSURANCE PRODUCTS AND RELATED PRACTICES

The Company provided ocean cargo insurance primarily to shippers and consignees who transported cargo on vessels owned or operated under charter by affiliate. The majority of all premiums written by the Company were generated by an affiliate, Tropical Shipping, Inc., a Delaware company. The Company wrote coverage for the following three types of cargo insurance:

- 1.) Insured bills of lading – For regular Tropical Shipping Inc.'s Shippers and consignees.
- 2.) Open Cargo Policy – Covers marine cargo shipments on or through Tropical Shipping, Inc. or other ocean carriers.
- 3.) Special Cargo Policy – For regular insured bill of lading customers using other carriers.

The cost of insurance under both policies was based upon actual value shipped. Rates were generally determined from policy to policy, by commodity shipped, the type of packaging used, the points of origin and destination and modes of transport.

The cargo insured was covered from the point of origin to the point of destination, or “warehouse to warehouse”. The insurance premium was considered earned and recognized as revenue once the vessel carrying the cargo reached its port of destination and the insured cargo was released to the consignee.

Territory and Plan of Operation

The Company was authorized to transact insurance in the State of Florida only, in accordance with Section 624.401(2), FS.

Treatment of Policyholders

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

REINSURANCE

The reinsurance agreement reviewed was found to comply with NAIC standards with respect to the standard insolvency clause, arbitration clause, transfer of risk, reporting and settlement information deadlines.

Assumed

The Company did not assume reinsurance risk as of December 31, 2003.

Ceded

The Company ceded risk on an excess of loss basis using Willis Marine Limited, London, England to place its business with reinsurers and engaged Aon Risk Services, Inc. of Florida, Miami, Florida to co-broker the business. At December 31, 2003, the Company retained \$100,000 and ceded business through four excess of loss layers. The four layers of excess coverage combine for a \$7,900,000 excess of \$100,000. The reinsurance was placed with several Lloyd's of London syndicates and other alien reinsurers.

The excess of loss contract was reviewed by the Company's appointed actuary and was utilized in determining the ultimate loss opinion.

ACCOUNTS AND RECORDS

An independent CPA audited the Company's statutory basis financial statements annually for the years 2001, 2002 and 2003, in accordance with Section 624.424(8), FS. Supporting work papers were prepared by the CPA as required by Rule 69O-137.002, FAC.

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 incorrectly reported the NAIC designation for some of its "PE" bonds. The Company also did not complete Schedule E, Part 3 as required by the NAIC Annual Statement Instruction Manual. Also, the Company reported the wrong items in the commissions payable line of the annual statement.

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

The Company and non-affiliates had the following agreements:

Custodial Agreement

The Company had a custodial agreement with Bank of America for the safekeeping of its securities. The custodial agreement executed in October 2004 met the requirements of Rule 690-143.042, FAC.

Independent Auditor Agreement

The Company engaged Deloitte and Touche for the purpose of auditing and reporting on the balance sheet and statutory financial statement of the Company.

Risk-Based Capital

The Company reported its risk-based capital at an adequate level.

FINANCIAL STATEMENTS PER EXAMINATION

The following pages contain financial statements showing the Company's financial position as of December 31, 2003, 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."

SEVEN SEAS INSURANCE COMPANY, INC.
Assets

DECEMBER 31, 2003

| Classification | Per Company | Examination Adjustments | Per Examination |
|--|-------------|----------------------------|-----------------|
| Bonds | \$7,190,122 | \$0 | \$7,190,122 |
| Cash: | | | |
| On deposit | 33,920 | | 33,920 |
| Agents' Balances: | | | |
| Uncollected premium | 368,170 | | 368,170 |
| Deferred premium | 0 | | 0 |
| EDP Equipment | 2,467 | | 2,467 |
| Interest and dividend income due & accrued | 112,669 | | 112,669 |
| Aggregate write-in for other than invested assets | 71,940 | | 71,940 |
| | <hr/> | | |
| Totals | \$7,779,288 | \$0 | \$7,779,288 |
| | <hr/> <hr/> | | |

SEVEN SEAS INSURANCE COMPANY, INC.
Liabilities, Surplus and Other Funds

DECEMBER 31, 2003

| Liabilities | Per Company | Examination Adjustments | Per Examination |
|--|--------------------|----------------------------|--------------------|
| Losses | \$705,074 | | \$705,074 |
| Loss adjustment expenses | 34,978 | | 34,978 |
| Contingent commissions | 122,739 | | 122,739 |
| Unearned premium | <u>43,916</u> | | <u>43,916</u> |
| Total Liabilities | \$906,707 | | \$906,707 |
| Common capital stock | \$750,750 | | \$750,750 |
| Gross paid in and contributed surplus | 1,000,000 | | 1,000,000 |
| Unassigned funds (surplus) | <u>5,121,831</u> | | <u>5,121,831</u> |
| Surplus as regards policyholders | <u>\$6,872,581</u> | | <u>\$6,872,581</u> |
| Total liabilities, capital and surplus | <u>\$7,779,288</u> | \$0 | <u>\$7,779,288</u> |

SEVEN SEAS INSURANCE COMPANY, INC.
Statement of Income

DECEMBER 31, 2003

Underwriting Income

| | |
|---|--------------------|
| Premiums earned | \$7,761,549 |
| DEDUCTIONS: | |
| Losses incurred | 1,515,570 |
| Loss expenses incurred | 374,140 |
| Other underwriting expenses incurred | 979,713 |
| Aggregate write-ins for underwriting deductions | 0 |
| Total underwriting deductions | <u>\$2,869,423</u> |
| Net underwriting gain or (loss) | \$4,892,126 |

Investment Income

| | |
|--|------------------|
| Net investment income earned | \$403,484 |
| Net realized capital gains or (losses) | 0 |
| Net investment gain or (loss) | <u>\$403,484</u> |

Other Income

| | |
|---|--------------------|
| Net income before dividends to policyholders and before federal & foreign income taxes | \$5,295,609 |
| Dividends to policyholders | 0 |
| Net Income, after dividends to policyholders, but before federal & foreign income taxes | <u>\$5,295,609</u> |
| Federal & foreign income taxes | <u>1,853,463</u> |
| Net Income | \$3,442,146 |

Capital and Surplus Account

| | |
|--|-------------|
| Surplus as regards policyholders, December 31 prior year | \$6,171,603 |
|--|-------------|

Gains and (Losses) in Surplus

| | |
|--|---------------------------|
| Net Income | 3,442,146 |
| Net unrealized capital gains or losses | 0 |
| Change in non-admitted assets | (237,262) |
| Dividends to stockholders | (2,500,000) |
| Aggregate write-ins for gains and losses in surplus | 3,905 |
| Examination Adjustment | 0 |
| Change in surplus as regards policyholders for the year | <u>\$700,980</u> |
| Surplus as regards policyholders, December 31 current year | <u><u>\$6,872,583</u></u> |

COMMENTS ON FINANCIAL STATEMENTS

Losses and Loss Adjustment Expenses

\$740,052

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, 2003, make a reasonable provision for all unpaid loss and loss expense obligations of the Company under the terms of its policies and agreements.

The Office actuary reviewed work papers provided by the Company and was in concurrence with this opinion.

**SEVEN SEAS INSURANCE COMPANY, INC.
Comparative Analysis of Changes in Surplus**

DECEMBER 31, 2003

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 per December 31, 2003, Annual Statement | \$6,872,581 |
|---|-------------|

| | <u>PER</u> <u>COMPANY</u> | <u>PER</u> <u>EXAM</u> | <u>INCREASE</u> <u>(DECREASE)</u> <u>IN SURPLUS</u> |
|--|------------------------------|---------------------------|---|
| ASSETS: | | | |
| No adjustments | | | |
| LIABILITIES: | | | |
| No adjustments | | | |
| Net Change in Surplus: | | | 0 |
| Surplus as Regards Policyholders December 31, 2003, Per Examination | | | \$6,872,581 |

SUMMARY OF FINDINGS

Compliance with previous directives

The Company has taken the necessary actions to comply with the comments made in the 2000 examination report issued by the Office.

CURRENT EXAMINATION COMMENTS AND CORRECTIVE ACTION

The following is a brief summary of items of interest and corrective action to be taken by the Company regarding findings in the examination as of December 31, 2003.

Accounts and Records

The Company reported incorrect bond designations for some of its "PE" securities. **The Company is directed to report in the future the correct security designations in accordance with the NAIC Securities Valuation Office.**

The Company did not complete Schedule E, Part 3 of the annual statement according to the NAIC annual statement instruction manual. **The Company is directed in the future to complete Schedule E, Part 3 of the annual statement for its special deposit with the State of Florida in accordance with annual statement instructions.**

The Company reported the items and amounts that make up commissions payable on the wrong line of the annual statement. **The Company is directed in the future to include these items and similar items under other expenses of the annual statement in accordance with annual statement instructions.**

CONCLUSION

The customary insurance examination practices and procedures as promulgated by the NAIC have been followed in ascertaining the financial condition of **Seven Seas Insurance Company, Inc.** as of December 31, 2003, consistent with the insurance laws of the State of Florida.

Per examination findings, the Company's surplus as regards policyholders was \$6,872,581, which was in compliance with Section 624.408, FS.

In addition to the undersigned, John Berry, Financial Examiner/Analyst Supervisor participated in the examination.

Respectfully submitted,

Maurice Fuller
Financial Examiner/Analyst II
Florida Office of Insurance Regulation