



COMMONWEALTH OF MASSACHUSETTS
OFFICE OF CONSUMER AFFAIRS AND BUSINESS REGULATION
DIVISION OF INSURANCE

REPORT OF EXAMINATION OF THE
ARBELLA PROTECTION INSURANCE COMPANY

Quincy, Massachusetts

As of December 31, 2015

NAIC GROUP CODE 0586

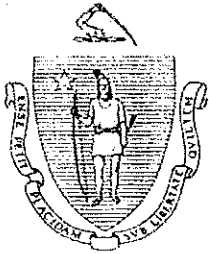
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ARBELLA PROTECTION INSURANCE COMPANY

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COMMONWEALTH OF MASSACHUSETTS
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DIVISION OF INSURANCE

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ACTING COMMISSIONER OF INSURANCE

April 26, 2017

Honorable Gary D. Anderson
Acting Commissioner of Insurance
Commonwealth of Massachusetts
Division of Insurance
1000 Washington Street, Suite 810
Boston, MA 02118-6200

Honorable Commissioner:

Pursuant to your instructions and in accordance with Massachusetts General Laws, Chapter 175, Section 4, an examination has been made of the financial condition and affairs of the

ARBELLA PROTECTION INSURANCE COMPANY

at its home office located at 1100 Crown Colony Drive, Quincy, MA, 02269-9103. The following report thereon is respectfully submitted.

SCOPE OF EXAMINATION

The Arbella Protection Insurance Company ("Company") was last examined as of December 31, 2010 by the Massachusetts Division of Insurance ("Division"). The current examination was conducted by the Division and covers the five year period from January 1, 2011 through December 31, 2015, including any material transactions and/or events occurring subsequent to the examination date and noted during the course of this examination.

A separate examination of Covenant Insurance Company, which is a member of the Arbella Insurance Group, was conducted by the Connecticut Insurance Department. Concurrent with this examination, the following insurance affiliates in the Arbella Insurance Group were also examined and separate reports of examinations have been issued by the Division:

Arbella Mutual Insurance Company ("Arbella Mutual")
Arbella Indemnity Insurance Company ("Indemnity")
Commonwealth Mutual Insurance Company
Commonwealth Reinsurance Company

The examination was conducted in accordance with standards and procedures established by the National Association of Insurance Commissioners ("NAIC") Financial Condition (E) Committee and prescribed by the current NAIC *Financial Condition Examiners Handbook*, the examination standards of the Division and with Massachusetts General Laws. The Handbook requires that we plan and perform the examination 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.

All accounts and activities of the Company were considered in accordance with the risk-focused examination process. This may include assessing significant estimates made by management and evaluating management's compliance with Statutory Accounting Principles. The examination does not attest to the fair presentation of the financial statements included herein. If, during the course of the examination an adjustment is identified, the impact of such adjustment will be documented separately following the Company's financial statements.

This examination report includes significant findings of fact, as mentioned in the Massachusetts General Laws, Chapter 175, Section 4, and general information about the insurer and its financial condition. There may be other items identified during the examination that, due to their nature (e.g., subjective conclusions, proprietary information, etc.), are not included within the examination report but separately communicated to other regulators and/or the Company.

The Company is audited annually by Ernst & Young LLP, an independent certified public accounting firm. The firm expressed unqualified opinions on the Company's financial statements for the calendar years 2011 through 2015. A review and use of the Certified Public Accountants' workpapers were made to the extent deemed appropriate and effective. Representatives from the firm of Baker Tilly Virchow Krause, LLP ("Baker Tilly") were retained by the Division to evaluate the adequacy and effectiveness of the IT systems controls to determine the level of reliance to be

Arbella Protection Insurance Company

placed on the information generated by the data processing systems. Lewis & Ellis, Inc. was contracted by Baker Tilly to review the adequacy of the Company's loss and loss adjustment expense reserves as of December 31, 2015.

SUMMARY OF SIGNIFICANT FINDINGS OF FACT

The examination included a review to verify the current status of findings commented upon in the Report of Examination as of December 31, 2010. There were no significant findings during the previous examination and there are no significant findings related to the current examination.

COMPANY HISTORY

General

The Company was incorporated under the laws of Massachusetts on November 17, 1992 and commenced business on January 1, 1993. The start-up of the Company was part of an agreement with the Division to take over part of the business of Attleboro Mutual Insurance Company, which was in receivership.

Capital Stock

The Company has 97,500 common shares authorized of \$28 par value and 92,674 shares are issued and outstanding, all owned by Arbella, Inc.

Dividends to Stockholder

The Company paid dividends to their sole stockholder, Arbella, Inc., in 2012 for \$4,898,535 and in 2011 for \$9,500,000.

MANAGEMENT AND CONTROL

Annual Meeting of Stockholders

In accordance with the bylaws, the Annual Meeting of the Stockholders shall be held on a date to be determined by the Board of Directors and is to be within six months after the end of year.

Board of Directors

The bylaws of the Company provide that the business and affairs of the Company shall be managed by the Board of Directors except as otherwise provided by the law, Articles of Organization, or the bylaws. The Board of Directors shall consist of not fewer than five members and shall hold office until the next annual meeting of stockholders and until his or her successors shall have been elected and qualified.

Arbella Protection Insurance Company

At December 31, 2015 the Board was comprised of five directors which are in compliance with the Company's bylaws. The director's names and business affiliation were as follows:

<u>Director</u>	<u>Business Affiliation</u>
Patricia P. Bailey	Consultant
Francis X. Bellotti	Consultant
Janet R. Corcoran	Chief Operating Officer and Executive Vice President Arbella Service Company
John F. Donohue	President and Chief Executive Officer Arbella Mutual Insurance Company
Christopher E. Hall	Treasurer, Chief Financial Officer and Executive Vice President - Arbella Mutual Insurance Company

Officers

The bylaws of the Company provide that the officers of the Company shall be a President, a Treasurer, a Secretary and other officers as deemed necessary. Pursuant to the bylaws, the officers of the Company are elected by the Board of Directors at the first meeting of the Board of Directors held after the Annual Meeting.

The elected officers and their respective titles at December 31, 2015 follow:

<u>Name</u>	<u>Title</u>
John F. Donohue	Chairman, Board of Directors, President, Chief Executive Officer and Assistant Secretary
Francis X. Bellotti *	Vice Chairman, Board of Directors
Christopher E. Hall	Treasurer, Chief Financial Officer and Executive Vice President
Eileen S. Currie	Senior Vice President, Commercial Lines
Gail Eagan	Senior Vice President and General Counsel
James S. Hyatt	Senior Vice President, Personal Lines
Lynellen M. Ramirez	Chief Actuary and Vice President
Beverly J. Tangvik	Secretary

* Francis Bellotti was not listed as an Officer on the Jurat page of the 2015 Annual Statement.

Arbella Protection Insurance Company

Committees of the Board

The bylaws state that the Board of Directors ("Board") may elect an Executive Committee and may form an Audit Committee and shall elect other committees as may be required from time to time. The Company has shared Board committees with Arbella Mutual. As of the date of this examination, the Company operated with designated Audit, Compensation, Executive, Investment, Planning and Technology Committees. The minutes of all of the committee meetings for the period covered by the examination were reviewed.

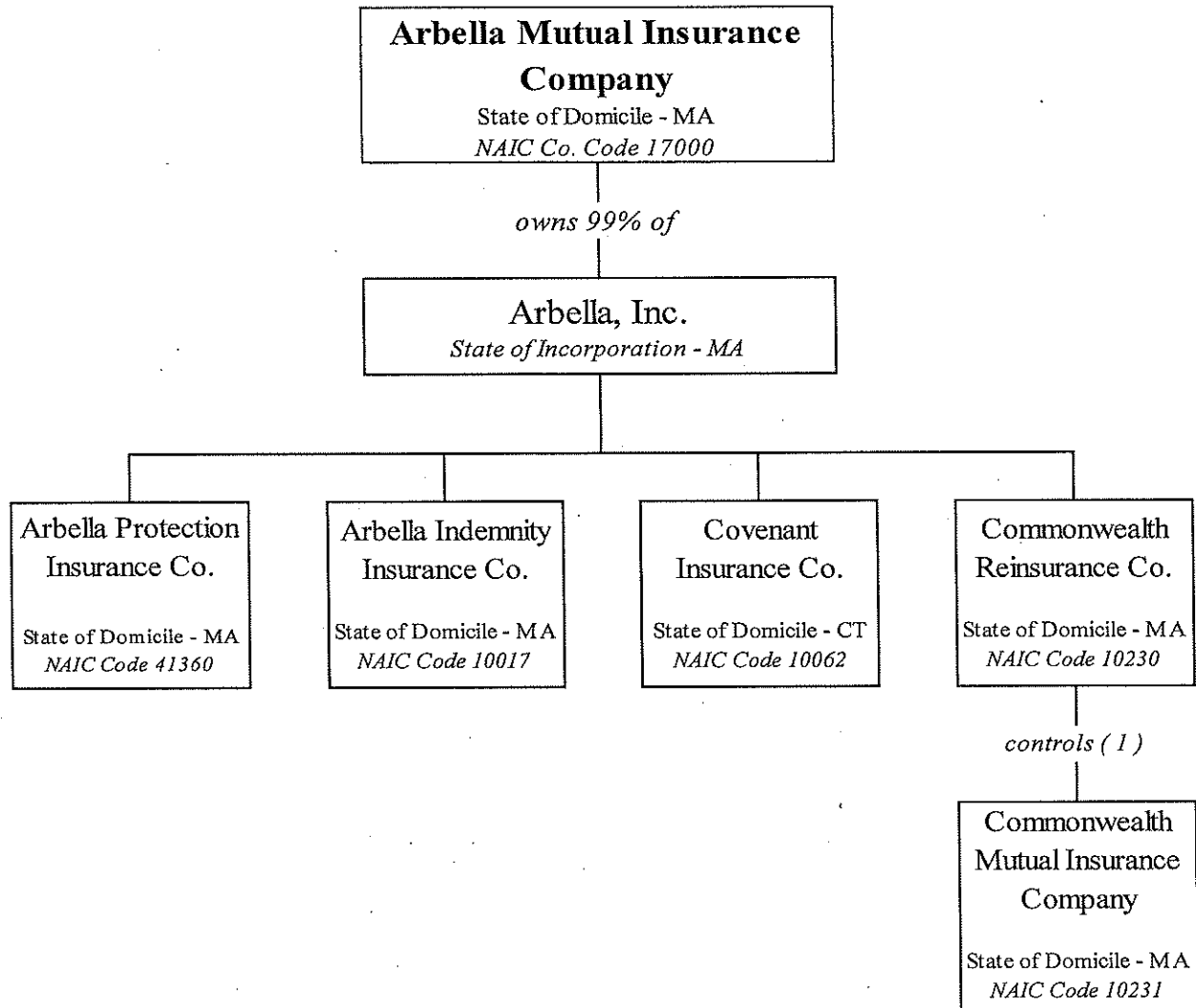
Holding Company

As stated in the Insurance Holding Company System Form B, as filed with the Massachusetts Division of Insurance, the Company is a member of a holding company system and is subject to the registration requirements of Chapter 175, Section 206C and 211 CMR 7.00 of the Massachusetts General Laws. Arbella Mutual Insurance Company is defined as the "ultimate controlling person".

Organization Chart

The Company's insurance affiliates are shown on the organization chart below and the Company's other affiliates including various insurance agencies are not shown. At December 31, 2015, the Company is a member of the following organizational structure:

Arbella Protection Insurance Company



(1) - Commonwealth Reinsurance Company controls Commonwealth Mutual Insurance Company through a reinsurance agreement, which terminated in 2014 in connection with the winding down of the two companies. See the Subsequent Events section for further details.

Transactions and Agreements with Subsidiaries and Affiliates

The Company owns 99.0% of Arbella, Inc., an insurance holding company. Arbella, Inc. directly owns the four insurance companies shown on the organization chart above. Arbella Protection owns 100% of Arbella Specialty Brokerage, Inc. In addition Arbella Inc. owns 100% of Arbella Capital Corporation, Arbella Service Company, Inc., AMIC Insurance Agency, Inc. and its subsidiary, Arbella Service Center, and is the sole member of the Arbella Insurance Group Charitable Foundation, Inc. Arbella Inc. owns two insurance agencies in Massachusetts, Viveiros Insurance Agency, Inc. and Bearingstar Insurance Agency, Inc.

Arbella Protection Insurance Company

Intercompany Pooling Agreement

The Company participates in an intercompany pooling arrangement ("Pool") with Arbella Mutual, Arbella Indemnity and Covenant Insurance Company in which it shares in the Pool's combined underwriting results and related balance sheet accounts. After processing its external reinsurance, each affiliated pooled company cedes its remaining net underwriting activity to the Company, which subsequently retrocedes the pooled results to the participants based on their percentage share of the Pool. Refer to the following chart for the percentages of the Pool participants as of the examination date.

<u>Company</u>	<u>Pool Percent</u>
Arbella Mutual Insurance Company	76%
Arbella Protection Insurance Company	16%
Covenant Insurance Company	5%
Arbella Indemnity Insurance Company	3%

Management Agreement

The Company and its affiliates ("Participants") are participants in a Services Agreement pursuant to which Arbella Service Company, Inc. provides administrative, operational and managerial services to all the individual companies. The Participants have agreed to a method to allocate the costs of the services which is based on generally accepted accounting principles. The settlement terms among the companies are in accordance with statutory accounting guidance.

Tax Sharing Agreement

The Company files a consolidated tax return with Arbella Mutual and its subsidiaries. Since 1996, the Company and its affiliates have been participants ("Participants") to a Tax Allocation Agreement ("Agreement") for the purpose of establishing a method for allocating the consolidated tax liability of the Participants and for reimbursing the Company for the payment of such tax liability. The Agreement provides that all subsidiaries of the Company shall be subject to the Agreement.

TERRITORY AND PLAN OF OPERATION

The Company is licensed to write business in seven Northeastern states: Connecticut, Massachusetts, New Hampshire, New York, Pennsylvania (*), Rhode Island and Vermont, but is only actively writing business in Connecticut, Massachusetts, New Hampshire, and Rhode Island. The Company primarily writes insurance coverage for workers' compensation, commercial automobile lines, other commercial business including commercial package, business owners policies, and commercial umbrella, and homeowners.

* - The Company voluntarily surrendered its Pennsylvania license effective February 2017.

Arbella Protection Insurance Company

Treatment of Policyholders – Market Conduct

During the financial examination of the Company, the Division's Market Conduct Department initiated a comprehensive market conduct examination of the Company for the period January 1, 2015 through December 31, 2015. The market conduct examination was called pursuant to authority in M.G.L. Chapter 175, Section 4. The market conduct examination was conducted at the direction of, and the overall management and control of, the market conduct examination staff of the Division. Representatives from the firm of Rudmose and Noller Advisors, LLC were engaged to complete certain agreed upon procedures which were developed using the guidance and standards of the NAIC Market Regulation Handbook, the market conduct examination standards of the Division, and the Commonwealth of Massachusetts insurance laws, regulations and bulletins. The business areas that were reviewed under the market conduct examination are Company Operations/Management; Complaint Handling; Marketing and Sales; Producer Licensing; Policyholder Services; Underwriting and Rating and Claims. Each business area reviewed includes the identification and evaluation of the insurer's internal controls

REINSURANCE

The Company and its affiliates participate in the intercompany pooling agreement described above. Assumed and ceded reinsurance with unaffiliated companies is also subject to the inter-company pooling agreement, as described below.

Ceded Reinsurance

The Company and its insurance affiliates utilize and share the cost of a common reinsurance program to reduce loss exposures from catastrophic and individual risks. The Company has catastrophe excess of loss contracts that provide coverage in excess of the Company's retention of \$25 million up to \$570 million. The Company has an aggregate catastrophe treaty providing coverage in excess of \$7.5 million up to \$22.5 million per occurrence excess and otherwise recoverable deductible of \$15 million. There are contracts for property and liability excess of loss contracts providing coverage up to \$10 million in excess of \$1.5 million. The workers' compensation contract provides coverage in excess of the Company's retention of \$1.5 million up to \$10 million. In addition, the Group purchased facultative reinsurance and catastrophic workers compensation protection for risk in excess of its property and liability excess of loss treaty limits. Lastly, the Group purchases various reinsurance to reduce insurance risk from its umbrella, boiler and machinery and other product offerings.

In addition, the Company serves as one of the four servicing carriers on behalf of Commonwealth Automobile Reinsurers ("CAR"). Under its contract, the Company underwrites business from assigned agents and cedes 100% of the insurance risk to CAR.

Assumed Reinsurance

The Company assumes business from the Massachusetts FAIR Plan and the Massachusetts Workers' Compensation Assigned Risk Pool.

Arbella Protection Insurance Company

FINANCIAL STATEMENTS

The following financial exhibits are based on the statutory financial statements prepared by management and filed by the Company with the Division and present the financial condition of the Company for the period ending December 31, 2015. The financial statements are the responsibility of Company management.

Statement of Assets, Liabilities, Surplus and Other Funds as of December 31, 2015

Statement of Income as of December 31, 2015

Statement of Capital and Surplus for the Year Ended December 31, 2015

Reconciliation of Capital and Surplus for the Five-Year Period Ended December 31, 2015

Arbella Protection Insurance Company
Statement of Assets, Liabilities, Surplus and Other Funds
As of December 31, 2015

Assets	<u>As Reported by the Company</u>
Bonds	\$ 150,809,620
Common stocks	8,541
Cash and short-term investments	4,788,919
Other invested assets	<u>564,700</u>
Subtotals, cash and invested assets	156,171,780
Investment income due and accrued	1,636,415
Premiums and considerations:	
Uncollected premiums and agents' balances in the course of collection	7,409,086
Deferred premiums, agents' balances and installments booked but deferred and not yet due	83,503,779
Amounts recoverable from reinsurers	35,308,119
Current federal income tax recoverable	2,315,402
Net deferred tax asset	8,813,931
Aggregate write-ins for other-than-invested assets	<u>19,607,869</u>
Total Assets	<u>\$ 314,766,380</u>

Arbella Protection Insurance Company
Statement of Assets, Liabilities, Surplus and Other Funds (Continued)
As of December 31, 2015

Liabilities	<u>As Reported by the Company</u>
Losses	\$ 59,034,239
Reinsurance payable on paid loss and LAE	21,421,940
Loss adjustment expenses	11,618,372
Commissions payable	4,470,914
Other expenses	4,693,270
Unearned premiums	68,947,389
Advance premiums	1,925,481
Dividends declared and unpaid: Policyholders	35,000
Ceded reinsurance premiums payable	43,646,669
Funds held by company under reinsurance treaties	24,508
Drafts outstanding	3,596,879
Payable to parent, subsidiaries and affiliates	4,240,184
Aggregate write-ins for liabilities	671,204
Total Liabilities	<u>224,326,049</u>
Common capital stock	2,594,872
Gross paid in and contributed surplus	55,863,191
Unassigned funds (surplus)	31,982,268
Surplus as regards policyholders	<u>90,440,331</u>
Total Liabilities, Capital and Surplus	<u>\$ 314,766,380</u>

Arbella Protection Insurance Company
Statement of Income
For the Year Ended December 31, 2015

	<u>As Reported by the Company</u>
Premiums earned	\$ 123,698,910
Deductions:	
Losses incurred	89,033,227
Loss expenses incurred	12,655,998
Other underwriting expenses incurred	40,106,821
Total underwriting deductions	<u>141,796,046</u>
Net underwriting gain (loss)	<u>(18,097,136)</u>
 Net investment income earned	 5,190,767
Net realized capital gains	<u>90,028</u>
Net investment gain	<u>5,280,795</u>
 Net gain (loss) from agents' balances or premium balances charged off	 (230,719)
Finance and service charges not included in premiums	 1,924,157
Aggregate write-ins for miscellaneous income	<u>(404,069)</u>
Total other income	<u>1,289,369</u>
 Net income before dividends to policyholders and before federal and foreign income taxes	 (11,526,971)
Dividends to policyholders	<u>35,000</u>
 Net income, after dividends to policyholders and before federal and foreign income taxes	 (11,561,971)
Federal and foreign income taxes incurred	<u>(2,421,041)</u>
 Net Income	 <u>\$ (9,140,930)</u>

Arbella Protection Insurance Company
Capital and Surplus
For the Year Ended December 31, 2015

	<u>As Reported by the Company</u>
Surplus as regards policyholders, December 31, 2014	\$ 97,816,930
Net income	(9,140,930)
Change in net unrealized capital gains	7,541
Change in net deferred tax	2,906,720
Change in nonadmitted assets	<u>(1,149,932)</u>
Change in surplus as regards policyholders for the year	<u>(7,376,600)</u>
Surplus as regards policyholders, December 31, 2015	<u>\$ 90,440,331</u>

Arbella Protection Insurance Company
Reconciliation of Capital and Surplus
For the Five Year Period Ended December 31, 2015

	2015	2014	2013	2012	2011
Capital and surplus, December 31, prior year	\$ 97,816,930	\$ 85,685,859	\$ 79,470,011	\$ 72,407,010	\$ 95,901,963
Net income	(9,140,930)	14,179,221	6,806,756	10,149,217	(15,752,814)
Change in net unrealized capital gains or (losses)	7,541				13,094
Change in net deferred income tax	2,906,720	(2,419,360)	(977,024)	(2,433,844)	5,009,303
Change in nonadmitted assets	(1,149,932)	371,210	386,116	2,189,148	(3,264,536)
Cumulative effect of changes in accounting principles				2,057,015	
Dividends to stockholders				(4,898,535)	(9,500,000)
Net change in capital and surplus for the year	(7,376,601)	12,131,070	6,215,848	7,063,001	(23,494,953)
Capital and surplus, December 31, current year	<u>\$ 90,440,331</u>	<u>\$ 97,816,930</u>	<u>\$ 85,685,859</u>	<u>\$ 79,470,011</u>	<u>\$ 72,407,010</u>

ANALYSIS OF CHANGES IN FINANCIAL STATEMENTS RESULTING FROM THE EXAMINATION

There have been no changes made to the financial statements as a result of the examination.

COMMENTS ON FINANCIAL STATEMENT ITEMS

As a result of the examination, no significant issues with non-compliance, adverse findings, or material changes to the financial statements were identified.

The Division engaged the consulting actuaries from Lewis & Ellis, Inc. to review the reasonableness of the Loss and Loss Adjustment Expense Reserves (the "Reserves") of the Company as of December 31, 2015. The review was conducted in a manner consistent with the Code of Professional Conduct and Qualification Standards of the American Academy of Actuaries and the Standards of Practice adopted by the Actuarial Standards Board.

Lewis & Ellis's actuarial review utilized year-end paid and incurred loss data developed through December 31, 2015. The tables below summarize a comparison of Lewis & Ellis's range of reasonable net estimates for the Reserves to the Company's carried net reserves as of December 31, 2015.

	Low Point of Range	Central Estimate	High Point of Range
Lewis & Ellis Total Net Loss & LAE Reserves	\$61,608,960	\$67,845,440	\$74,181,120
Total Company Carried Net Loss & LAE Reserves	70,653,120	70,653,120	70,653,120
Difference	9,044,160	2,807,680	(3,528,000)

The Company's total net carried reserves are above Lewis & Ellis's central estimate and below their high point. Therefore the Division concludes the Company's reserves are a reasonable estimate of their ultimate liability.

SUBSEQUENT EVENTS

During 2016, Commonwealth Reinsurance Company ("Comm Re") converted to a non-insurance company and was renamed Arb CR, Inc. On December 28, 2016, Arb CR, Inc. was dissolved. The transaction had no impact on the Group's capital. Consequently, there is no longer any affiliation to Commonwealth Mutual Insurance Company, an entity previously included on the Group's organizational chart as a result of its former controlling arrangements with Comm Re.

SUMMARY OF RECOMMENDATIONS

There were no significant recommendations noted by the examination team for improvements in process, activities and/or controls that should be noted in this report. Recommendations of a lesser degree will be communicated to the Board of Directors in the Company's Management Letter.

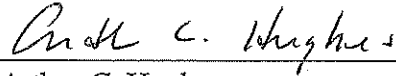
Arbella Protection Insurance Company

SIGNATURE PAGE

Acknowledgement is made of the cooperation and courtesies extended by the officers and employees of the Company during the examination.



Kenneth R. Plumb, CPA, CFE
Supervising Examiner
Commonwealth of Massachusetts
Division of Insurance



Arthur C. Hughes
Examiner-in-Charge
Commonwealth of Massachusetts
Division of Insurance