

COMMONWEALTH OF MASSACHUSETTS
Office of Consumer Affairs and Business Regulation
DIVISION OF INSURANCE

One South Station • Boston, MA 02110-2208
(617) 521-7794 • FAX (617) 521-7475
TTY/TDD (617) 521-7490
<http://www.mass.gov/doi>

DEVAL L. PATRICK
GOVERNOR

TIMOTHY P. MURRAY
LIEUTENANT GOVERNOR

DANIEL O'CONNELL
SECRETARY OF HOUSING AND
ECONOMIC DEVELOPMENT

DANIEL C. CRANE
DIRECTOR

NONNIE S. BURNES
COMMISSIONER OF INSURANCE

March 30, 2007

The Honorable Alfred W. Gross
Chairman, NAIC Financial Condition (E) Committee
Commissioner, Bureau of Insurance
Commonwealth of Virginia
PO Box 1157
1300 East Main Street
Richmond, VA 23219

The Honorable Thomas E. Hampton
Secretary, Northeast Zone
Commissioner, Dept. of Insurance, Securities, and Banking
Government of the District of Columbia
810 First Street, N. E., Suite 701
Washington, DC 20002

The Honorable Nonnie S. Burnes
Commissioner of Insurance
The Commonwealth of Massachusetts
One South Station, 5th Floor
Boston, MA 02110

Honorable Commissioners:

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

ARBELLA INDEMNITY INSURANCE COMPANY

at its statutory home office at 1100 Crown Colony Drive, Quincy, Massachusetts 02269. The following report thereon respectfully is submitted:

SCOPE OF EXAMINATION

Arbella Indemnity Insurance Company (hereinafter referred to as “Arbella” or the “Company”) was last examined as of December 31, 2000, under the Association Plan of the National Association of Insurance Commissioners (“NAIC”) by the Massachusetts Division of Insurance (the “Division”). The current Association examination was performed by the Division under the authority of Section 4, Chapter 175 of the Massachusetts General Laws, and covers the five year period from January 1, 2001, through December 31, 2005, including any material transactions and/or events subsequent to the examination date as noted during the course of this examination.

Concurrent examinations were also conducted of four other Massachusetts domiciled insurers of the Arbella Insurance Group: Arbella Mutual Insurance Company (“AMIC”), Arbella Protection Insurance Company (“APIC”), Commonwealth Mutual Insurance Company (“CMIC”), Commonwealth Reinsurance Company (“CRC”), (collectively, the “Group”) each of which is the subject of a separate examination report.

The examination was conducted in accordance with standards established by the Financial Condition (E) Committee of the NAIC as well as with the requirements of the NAIC Financial Condition Examiner’s Handbook, the examination standards of the Division and with Massachusetts General Laws. The principal focus of the examination was as of December 31, 2005, and the year 2005 activity, however transactions both prior and subsequent thereto were reviewed as deemed appropriate.

In addition to a review of the financial condition of the Company, the examination included a review of the Company’s business policies and practices, corporate records, reinsurance treaties, conflict of interest disclosure statements, fidelity bonds and other insurance, employees’ pension and benefits plans, disaster recovery plan and other pertinent matters to provide reasonable assurance that the Company was in compliance with applicable laws, rules and regulations. In planning and conducting the examination, consideration was given to the concepts of materiality and risk and examination efforts were directed accordingly.

The Company is audited annually by Ernst & Young LLP (“E&Y”), an independent certified public accounting firm, in accordance with 211 CMR 23.00. E&Y expressed unqualified audit opinions on the Company’s statutory basis financial statements for each of the years they audited the Company during the examination period (2001 through 2005). The E&Y workpapers for the year 2005 audit were reviewed as part of the examination process and used to assist in the planning of the examination, to supplement work performed by the Division and KPMG, and expedite the overall examination process.

Representatives from the independent certified public accounting firm of KPMG LLP (“KPMG”) were engaged to complete certain agreed upon procedures, including a review and evaluation of the adequacy of the Company’s loss and loss adjustment expense reserves as of December 31, 2005.

HISTORY

General

The Company was incorporated on April 4, 1994, under the laws of the Commonwealth of Massachusetts as a wholly-owned subsidiary of AMIC and commenced business on June 1, 1994. During 1994, all of the Company's common stock was contributed and ownership of the Company was transferred to Arbella, Inc., a holding company which is 99.3% owned by AMIC. The Group operates solely in the New England region and collectively writes private passenger auto, commercial auto, commercial lines, homeowners, personal umbrella and workers' compensation products primarily through independent agents.

The Company is duly organized under Section 47 of Chapter 175 of the Massachusetts General laws to provide coverage for all commercial lines, workers' compensation, and personal lines other than life.

Effective January 1, 2002, the Company entered into an intercompany pooling agreement with its Massachusetts domiciled affiliates. Under the terms of this agreement the Company, APIC, and CRC cede 100% of their net book to the AMIC. AMIC retains 75% of the pooled underwriting results and retrocedes the remaining 25% back to the other pool participants, including the Company, based on the percentages listed in the following table. Percentages have not changed since the pool's inception:

The Company	4%
AMIC	75%
APIC	18%
CRC*	3%
Total	100%

* CMIC cedes 100% of its net book to CRC and CRC retrocedes 100% of this book to the Pool.

The Company has not made any significant changes to its articles of incorporation or its by-laws during the period covered by this examination. Additionally, there have not been any name changes, mergers, or any other material changes to its corporate structure since the last examination except as discussed below in Acquisitions, Affiliation and Other Transactions.

Capital Stock

The ownership of the Company resides with its stockholder, Arbella, Inc., a down stream holding company of AMIC, which controls the Company through the election of the Board of Directors. The Company has 400,000 shares authorized of \$10.00 par value common stock and 200,000 issued and outstanding. The stock is 100% owned by Arbella, Inc.

Growth of Company

The growth of the Company for the years 2001 through 2005 is shown in the following schedule, which was prepared from the Company's statutory annual statements.

<u>Year</u>	<u>Admitted Assets</u>	<u>Net Written Premium</u>	<u>Capital & Surplus</u>
2005	\$ 45,398,750	\$ 24,803,006	\$ 15,867,469
2004	42,644,257	23,764,302	14,358,213
2003	40,909,575	24,121,652	12,316,658
2002	43,269,940	27,024,413	11,583,790
2001	35,039,668	10,610,887	11,943,019

MANAGEMENT

Annual Meeting of Stockholder

In accordance with Article 1, Section 2 of the Company's by-laws, the annual meeting of the stockholder entitled to vote, shall be held on a date to be determined by the Board of Directors within six months after the end of each fiscal year (last day of December of each year).

Board of Directors

The by-laws 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 by-laws. 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.

At December 31, 2005, the Board of Directors was comprised of five members, which is in compliance with the Company by-laws. Directors duly elected and serving at December 31, 2005, with business affiliations, follows:

<u>Director</u>	<u>Business Affiliation</u>	<u>Residence</u>
Patricia P. Bailey	Consultant	Santa Fe, New Mexico
Francis X. Bellotti	Arbella Insurance Group	Quincy, Massachusetts
Thomas S. Carpenter	Executive Vice President and Chief Actuary	Mansfield, Massachusetts
John F. Donohue	Chairman, Board of Directors	Belmont, Massachusetts
Douglas R. Jones	President, Chief Executive Officer, Assistant Secretary	Georgetown, Massachusetts

The by-laws do not specify the number of meetings to be held during a given calendar year. The by-laws contain provisions allowing for special meetings. Additionally, the by-laws allow the Board of Directors to take action by written consent and/or telephone conference. The minutes of the Board of Directors meetings indicated that meetings were held at least four times per year during the examination period. At any meeting of the Board of Directors a majority of the directors constitutes a quorum. The minutes indicated that a quorum was obtained at all meetings of the Board of Directors held during the examination period.

Committees of the Board

The by-laws state that the Board of Directors may elect an Executive Committee and may elect such other committees as may be required from time to time. The Board of Directors of Arbella, Inc. elects committees each year and the Board of Directors votes each year to direct and authorize the committees of Arbella, Inc. to act as advisory committees to the Boards of Directors of the subsidiary companies of Arbella, Inc. As of the date of this examination, Arbella, Inc. operated with designated Audit, Automation, Compensation, Executive, Investment and Planning Committees. We reviewed the meeting minutes for the committees for the period covered by this examination.

Officers

The by-laws of the Company provide that the officers of the Company shall be a President, Treasurer, Clerk, the Secretary, and any other officers as the Board of Directors deems necessary. Pursuant to the by-laws, the officers of the Company are elected by the Board of Directors at their first meeting following the annual meeting of the stockholder or special meeting in lieu thereof. The elected officers and their respective titles at December 31, 2005 are as follows:

<u>Officer</u>	<u>Title</u>
John F. Donohue	Chairman, Board of Directors
Douglas R. Jones	President, Chief Executive Officer, Assistant Secretary
Robert P. Medwid	Executive Vice President, Chief Financial Officer, Treasurer
Thomas S. Carpenter	Executive Vice President and Chief Actuary
Gail Eagan (1)	Vice President and General Counsel
Beverly T. Kenneally	Secretary and Clerk

(1) elected November, 2005

Conflict of Interest Procedures

The Company has established procedures for the disclosure to the Board of Directors of any material interest or affiliation on the part of any officer or director, which is in or is likely to conflict with his/her official duties. Annually, each officer and director completes a questionnaire disclosing any material conflicts of interest.

Corporate Records

Articles of Incorporation and By-laws

The Company's articles of organization and by-laws were reviewed and indicate that no significant changes have been made to these documents since the prior examination.

Disaster Recovery and Business Continuity

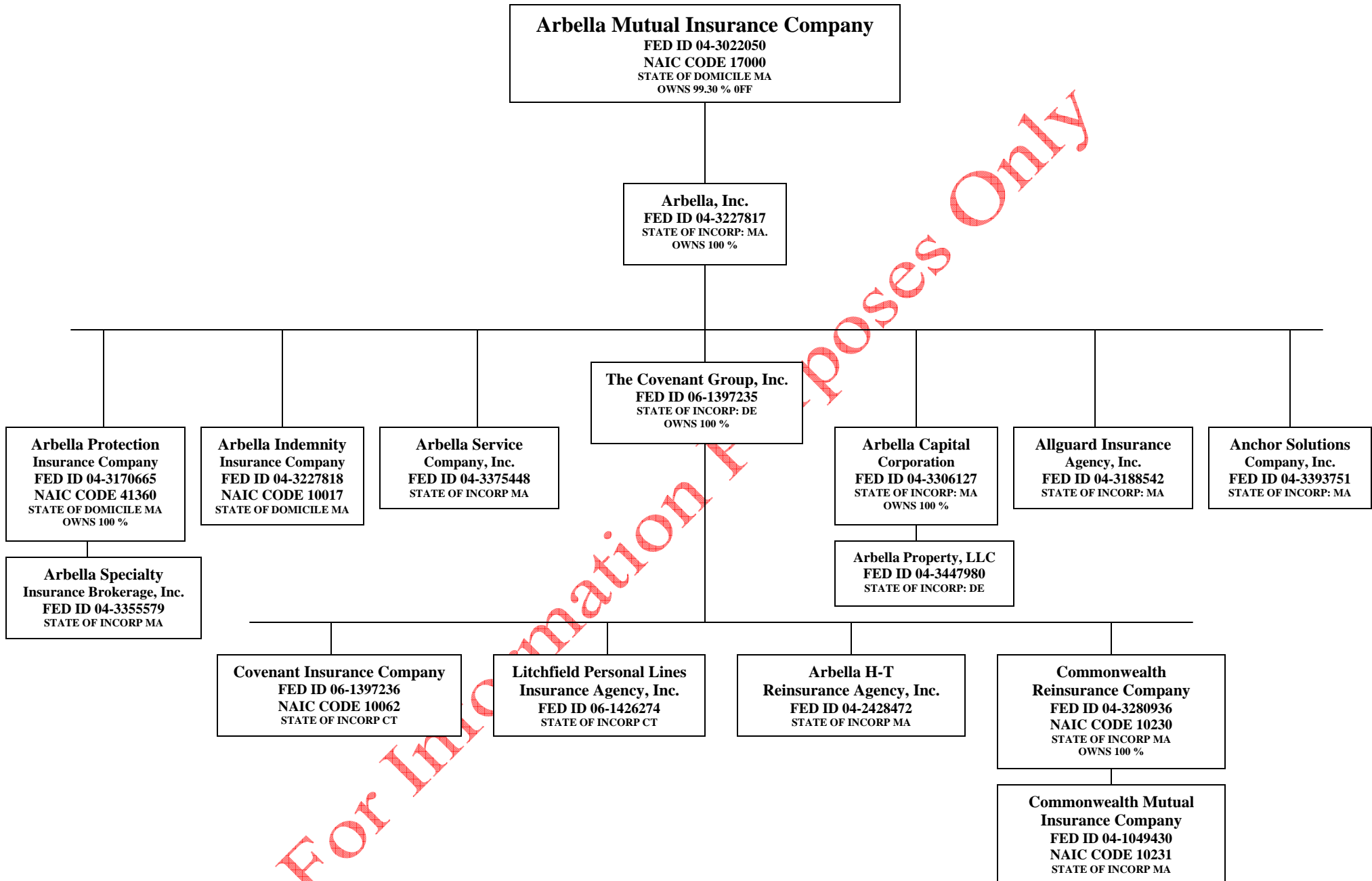
The Company provides for the continuity of management and operations in the event of a catastrophe or national emergency in accordance with M.G.L. c. 175 ss. 180M-180Q.

AFFILIATED COMPANIES

The Company's insurance affiliates include the following Massachusetts domiciled property and casualty insurance companies: AMIC, APIC, CRC and CMIC. Covenant Insurance Company ("CIC") is domiciled in the State of Connecticut.

Organization Chart

An organization chart of Arbella Mutual Insurance Company and subsidiaries is presented below.



Acquisitions, Affiliations and Other Transactions

During the period January 1, 2000, through December 31, 2005, the Company's material transactions included the following items:

- The Company recorded a cumulative effect of adoption of Codification which resulted in an adjustment that increased unassigned surplus as of January 1, 2001, by \$840,000, primarily as a result of recording a net deferred tax asset.
- Effective April 2, 2002, the Group received a rating of B++ from A.M. Best. Previously, the Group's A.M. Best rating was A-.

INTERCOMPANY AGREEMENTS

Management Agreement

Effective January 1, 1998, the Company entered into a management agreement with Arbella Service Company ("Service"), a wholly owned subsidiary of Arbella, Inc. whereby Service provides the Company (and its affiliates) with management services including data processing and system support, underwriting, marketing, claims, actuarial, cash and investment management, personnel, legal, accounting, and other such management oversight as is required and requested by the Company for the necessary and efficient management of its operation.

Tax Sharing Agreement

The Company files a consolidated tax return with AMIC and its subsidiaries. The Company has executed a tax sharing agreement effective January 1, 1996, which provides for the allocation of taxes based upon the separate return calculations with current credit for net losses incurred by any one of the companies to the extent such losses are utilized in the consolidated return.

FIDELITY BOND AND OTHER INSURANCE

The Company and its affiliates maintain fidelity coverage with an authorized Massachusetts insurer, under a financial institutions bond designed for insurance companies, consistent with M.G.L. c. 175 s. 60. The Company, a member of the Group, is covered by a blanket fidelity bond with an aggregate liability of \$6,000,000 and a single loss limit of liability of \$3,000,000 and a single loss deductible of \$25,000. Coverage is provided by insurers licensed in the Commonwealth of Massachusetts and was in force as of December 31, 2005. The aggregate limit of liability exceeds the NAIC suggested minimum as well as Massachusetts General Law requirements. Other coverage provided under the bond includes assorted loss of property coverage, losses due to forgery and counterfeit currency losses, and computer systems fraud. The Company

has further protected its interest and property by policies of insurance covering other insurable risks.

PENSION, INSURANCE PLANS AND EMPLOYEE WELFARE

Retirement and Deferred Compensation Plans

The Company has no employees, however, it does participate in a qualified defined contribution retirement plan (retirement plan) for which all employees of Service are eligible to participate on the first month following their attainment of age 18 and completion of eleven months of service. The retirement plan is allocated to various companies within the Group under a Generally Accepted Accounting Practices (“GAAP”) cost sharing arrangement.

The Company has no employees, however, it does participate in a qualified 401K savings plan which uses the same eligibility requirements as the retirement plan. Under the terms of this plan employees contribute from 1% to 60% of their annual earnings, with the sponsor matching 100% of the employee’s first 3% and a 50% match for the next 2%, subject to Internal Revenue Service (“IRS”) annual limitations. The cost of this plan is allocated to various companies within the Group under a GAAP cost sharing arrangement.

The Company has no employees, however, it does participate in a defined contribution plan, which provides certain postretirement health and life insurance benefits. Substantially all employees may become eligible for these benefits if they reach retirement age (62) while working for Service, and have at least five years of service credit. Annually, the plan sponsor determines the amount of money it will contribute that year towards the cost of the benefits for the individuals that are currently retired. The sponsor retains the right to change or modify the plan at any time and makes no promise to current employees that it will annually contribute to the cost of their postretirement benefits.

Stock Option Plan

Arbella, Inc. has an incentive bonus and stock option plans for senior management as well as the Board of Directors for shares of Arbella, Inc. Under the terms of these plans, each option granted can be used to purchase one share of Arbella, Inc.’s stock. There are 4,289,375 shares reserved for issuance under these plans as of December 31, 2005.

STATUTORY DEPOSITS

The statutory deposits of the Company as of December 31, 2005, were as follows:

<u>Location</u>	<u>Description of Deposit</u>	<u>Par Value</u>	<u>Statement Value</u>	<u>Market Value</u>
Massachusetts	U.S. Treasury Note 5.25% due 2/15/2029	\$ 50,000	\$ 55,715	\$ 54,562
Massachusetts	U.S. Treasury Note 7.50% due 11/15/2016	50,000	55,640	62,813
Rhode Island	U.S. Treasury Note 5.125% due 5/15/2016	1,750,000	1,755,160	1,783,898

INSURANCE PRODUCTS AND RELATED PRACTICES

Territory and Plan of Operation

As of December 31, 2005, the Company is authorized and licensed to write all personal and commercial lines (except life) and workers' compensation in Massachusetts, all lines except life in Rhode Island, and all personal lines in Connecticut. Although licensed in Connecticut and Rhode Island, the Company is not currently writing business in those states.

Rating and Statistical Reporting

The significant rating and statistical organizations to which the Company subscribes include the Workers' Compensation Rating and Inspection Bureau of Massachusetts, the Insurance Service Office, the National Council on Compensation Insurance, and Commonwealth Automobile Reinsurers.

SUBSEQUENT EVENTS

There were no details noted as "subsequent events", the disclosure of which in this Examination Report were considered appropriate.

REINSURANCE

The Company and its insurance affiliates utilize and share the cost of a common reinsurance program to reduce loss exposures from catastrophe as well as individual risks. The Group maintains treaties for property excess of loss, casualty excess of loss, workers' compensation excess of loss and umbrella treaties placed directly with General Reinsurance Company. Additionally the Group maintains a facultative treaty with Hartford Steam Boiler for machinery and equipment coverage. The Group utilizes the services of a reinsurance broker, Guy Carpenter, to place certain catastrophe reinsurance. The Company remains contingently liable to the extent that its reinsurers are unable to meet their obligations under the reinsurance agreements.

Ceded Reinsurance

Property Per Risk Excess of Loss Treaty

This reinsurance agreement with Gen Re covers homeowners property losses as follows: 1st layer: \$1,000,000 xs \$1,000,000; 2nd layer: \$4,000,000 xs \$2,000,000. The limit for other property losses is: 1st layer: \$800,000 xs \$1,200,000; 2nd layer: \$4,000,000 xs \$2,000,000.

Casualty Per Risk Excess of Loss Treaty

This reinsurance agreement with Gen Re covers casualty losses as follows: 1st layer \$800,000 xs \$1,200,000; 2nd layer: \$4,000,000 xs \$2,000,000.

Property Catastrophe Excess of Loss Treaty

This reinsurance agreement is placed with various subscribing reinsurers through a broker, Guy Carpenter, as follows:

1st layer: \$25,000,000 xs \$25,000,000; 2nd layer: \$120,000,000 xs \$50,000,000; 3rd layer: \$50,000,000 xs \$170,000,000.

Assumed Reinsurance

As an issuer of Massachusetts workers' compensation insurance, the Company must participate in a mandatory residual market workers' compensation pool, Massachusetts Workers' Compensation Assigned Risk Pool (the "Pool"). The Company is required to assume from Pool a percentage of premiums, losses and expenses generated by the Pool.

Intercompany Reinsurance

As previously noted on January 1, 2002, the Company entered into an intercompany pooling agreement with several of its affiliates. Under the terms of this agreement the Company, APIC and CRC cede 100% of their net book to the AMIC. AMIC retains 75% of the pooled underwriting results and retrocedes the remaining 25% to the other pool participants.

In order for CIC to receive the same claims paying ability rating as the Group, there is an inter-company reinsurance agreement whereby CIC cedes 100% of its direct written premium to the Company. The Company retrocedes this premium to the AMIC and the AMIC simultaneously retrocedes the premium to CIC. Because there is no net impact to any of the companies, this transfer has been eliminated from this statement.

ACCOUNTS AND RECORDS

The internal control structure was discussed with management through questionnaires and through transaction testing and a review of the work performed by the Company's independent Certified Public Accountants. No material deficiencies were noted.

The NAIC provides a questionnaire covering the evaluation of the controls in the information systems (IS) environment. The Company operates on information systems owned, operated and maintained by the Company. The NAIC Exhibit C Questionnaire was completed by the Company. These independent work products were reviewed by the Division as part of the evaluation of the adequacy of the IS controls. No material deficiencies were noted.

The Company maintains its accounts and records on an electronic data processing basis. All entries are input to this data processing system, which then generates general ledger and supporting reports as well as other reports common to the insurance industry.

FINANCIAL STATEMENTS

The following financial statements are presented on the basis prescribed by the NAIC Accounting Practices and Procedures Manual which are the principal accounting practices and procedures promulgated by the National Association of Insurance Commissioners and the Commonwealth of Massachusetts Division of Insurance:

- Statement of Assets, Liabilities, Surplus and Other Funds, December 31, 2005;
- Statement of Income for the Year Ended December 31, 2005;
- Statement of Capital and Surplus for the Year Ended December 31, 2005;
- Reconciliation of Capital and Surplus for the Five Year Period Ended December 31, 2005.

Arbella Indemnity Insurance Company
Statement of Assets, Liabilities, Surplus and Other Funds
December 31, 2005

	Per Annual Statement	Examination Adjustments	Per Examination	Note
<u>Assets</u>				
Bonds	\$ 33,081,891	\$ -	\$ 33,081,891	
Common stocks	92,100		92,100	
Cash	(83,436)		(83,436)	
Short-term investments	1,553,219		1,553,219	
Investment income due and accrued	421,347		421,347	
Uncollected premiums	347,837		347,837	
Deferred premiums	6,608,906		6,608,906	
Net deferred tax asset	1,100,000		1,100,000	
Receivables from parent, subsidiaries and affiliates	2,255,833		2,255,833	
Other assets	21,053		21,053	
Total assets	<u>\$ 45,398,750</u>	<u>\$ -</u>	<u>\$ 45,398,750</u>	
<u>Liabilities, Surplus and Other Funds</u>				
Losses	\$ 13,506,207	\$ 861,000	\$ 14,367,207	1
Loss adjustment expenses	1,930,875	(861,000)	1,069,875	1
Commissions payable	845,559		845,559	
Taxes, licenses and fees	53,096		53,096	
Current federal income taxes	847,000		847,000	
Unearned premiums	11,829,588		11,829,588	
Advance premiums	342,786		342,786	
Dividends declared and unpaid - policyholders	150,000		150,000	
Other liabilities	26,170		26,170	
Total liabilities	<u>29,531,281</u>	<u>-</u>	<u>29,531,281</u>	
Common capital stock	2,000,000		2,000,000	
Gross paid in and contributed surplus	8,650,000		8,650,000	
Unassigned funds	5,217,469		5,217,469	
Surplus as regards policyholders	<u>15,867,469</u>	<u>-</u>	<u>15,867,469</u>	
Total liabilities, surplus and other funds	<u>\$ 45,398,750</u>	<u>\$ -</u>	<u>\$ 45,398,750</u>	

Arbella Indemnity Insurance Company
Statement of Income
for the Year Ended December 31, 2005

	Per Annual <u>Statement</u>	Examination <u>Adjustments</u>	Per <u>Examination</u>	<u>Note</u>
Premiums earned	\$ 24,192,169	\$ -	\$ 24,192,169	
Losses incurred	13,147,989	861,000	14,008,989	1
Loss expenses incurred	2,440,626	(861,000)	1,579,626	1
Other underwriting expenses incurred	8,069,834		8,069,834	
Net underwriting gain	533,720	-	533,720	
Net investment income earned	1,714,506		1,714,506	
Net realized capital gains and (losses)	14		14	
Net investment gain or (loss)	1,714,520	-	1,714,520	
Net gain or (loss) from agents' or premium balances charged off	(99,005)		(99,005)	
Finance or service charges	584,360		584,360	
Miscellaneous income	(163,525)		(163,525)	
Net income before dividends and taxes	2,570,070	-	2,570,070	
Dividends to policyholders	16,595		16,595	
Net income before taxes	2,553,475	-	2,553,475	
Federal income taxes incurred	847,000		847,000	
Net income	\$ 1,706,475	\$ -	\$ 1,706,475	

Arbella Indemnity Insurance Company
Statement of Capital and Surplus
for the Year Ended December 31, 2005

	Per Annual <u>Statement</u>	Examination <u>Adjustments</u>	Per <u>Examination</u>	<u>Note</u>
Surplus as regards policyholders, December 31, 2004	\$ 14,358,213	\$ -	\$ 14,358,213	
Net income	1,706,475		1,706,475	
Change in net deferred income tax	(3,000)		(3,000)	
Change in nonadmitted assets	113,883		113,883	
Prior period tax adjustment	(308,102)		(308,102)	
Change in surplus as regards policyholders for the year	1,509,256	-	1,509,256	
Surplus as regards policyholders, December 31, 2005	<u>\$ 15,867,469</u>	<u>\$ -</u>	<u>\$ 15,867,469</u>	

For Information Purposes Only

Arbella Indemnity Insurance Company
Reconciliation of Capital and Surplus
for the Five Year Period Ended December 31, 2005

	2005 *	2004	2003	2002	2001
Surplus as regards policyholders, December 31, prior year	\$ 14,358,213	\$ 12,316,658	\$ 11,583,790	\$ 11,943,019	\$ 11,233,451
Net income	1,706,475	1,865,704	674,970	(368,359)	(130,149)
Change in net deferred income tax	(3,000)	160,000	-	-	-
Change in nonadmitted assets	113,883	15,851	57,898	9,130	(283)
Cumulative effect of changes in accounting principles	-	-	-	-	840,000
Prior period tax adjustment	(308,102)	-	-	-	-
Change in surplus as regards policyholders for the year	1,509,256	2,041,555	732,868	(359,229)	709,568
Surplus as regards policyholders, December 31, current year	\$ 15,867,469	\$ 14,358,213	\$ 12,316,658	\$ 11,583,790	\$ 11,943,019

* As per Examination

NOTES TO FINANCIAL STATEMENT

NOTE 1:

The Company's Annual Statement, as filed, did not reflect a reclassification necessary to bring the Loss Reserves and Reserve for Loss Adjustment Expenses into agreement with the actuarial analysis prepared by the Company's Appointed Actuary. This examination reclassified those amounts in both the liabilities and in the underwriting expenses. There was no effect on Surplus.

NOTE 2:

As part of the examination by the Division, KPMG was directed to review the reasonableness of the reserves for loss and loss adjustment expenses of the Company as of December 31, 2005.

The review was conducted in a manner consistent with the Code of Professional Conduct and the Qualification Standards of the American Academy of Actuaries and the Standards of Practice adopted by the Actuarial Standards Board.

The results of KPMG's actuarial review indicated that the Company's reserves at December 31, 2005 fell within the range of reasonable estimates for all unpaid loss and loss adjustment expense obligations of the Company under the terms of its policies and reinsurance agreements.

The following table summarizes the reserve ranges as developed by KPMG, the selected point estimate reserve and the Company's carried loss and loss adjustment expense reserves as of December 31, 2005, for each reserve category (all amounts in millions of dollars).

Net of Reinsurance

<u>Reserve Category</u>	<u>Low End of Range</u>	<u>KPMG Selection</u>	<u>High End of Range</u>	<u>Company Carried</u>
Loss Reserves	\$ 11.6	\$ 12.6	\$ 13.9	\$ 13.5
Loss Adjustment Expense Reserve	<u>2.5</u>	<u>2.6</u>	<u>2.7</u>	<u>1.9</u>
Total Loss and Loss Adjustment Expense Reserves	<u>\$ 14.1</u>	<u>\$ 15.2</u>	<u>\$ 16.6</u>	<u>\$ 15.4</u>

Gross of Reinsurance

<u>Reserve Category</u>	<u>Low End of Range</u>	<u>KPMG Selection</u>	<u>High End of Range</u>	<u>Company Carried</u>
Loss Reserves	\$ 13.8	\$ 15.0	\$ 16.6	\$ 16.3
Loss Adjustment Expense Reserve	<u>3.0</u>	<u>3.3</u>	<u>3.4</u>	<u>2.3</u>
Total Loss and Loss Adjustment Expense Reserves	<u>\$ 16.8</u>	<u>\$ 18.3</u>	<u>\$ 20.0</u>	<u>\$ 18.6</u>

The following table summarizes the reserve ranges as developed by KPMG, the selected point estimate reserve and the Arbella Insurance Group carried loss and loss adjustment expense reserves as of December 31, 2005, for each reserve category (all amounts in millions of dollars).

<u>Reserve Category</u>	<u>Low End of Range</u>	<u>KPMG Selection</u>	<u>High End of Range</u>	<u>Company Carried</u>
Net Loss Reserves	\$ 289.8	\$ 314.8	\$ 347.2	\$ 337.7
Net Defense & Cost Containment Expense Reserves	52.2	53.8	56.0	32.7
Net Adjusting & Other Expense Reserves	<u>13.3</u>	<u>14.4</u>	<u>15.2</u>	<u>15.6</u>
Total Net Loss and Loss Adjustment Expense Reserves	<u>\$ 355.3</u>	<u>\$ 383.0</u>	<u>\$ 418.4</u>	<u>\$ 386.0</u>
<u>Reserve Category</u>	<u>Low End of Range</u>	<u>KPMG Selection</u>	<u>High End of Range</u>	<u>Company Carried</u>
Gross Loss Reserves	\$ 344.2	\$ 375.9	\$ 414.9	\$ 405.6
Gross Defense & Cost Containment Expense Reserves	67.4	69.8	73.1	42.4
Gross Adjusting & Other Expense Reserves	<u>13.3</u>	<u>14.4</u>	<u>15.2</u>	<u>16.6</u>
Total Gross Loss and Loss Adjustment Expense Reserves	<u>\$ 424.9</u>	<u>\$ 460.1</u>	<u>\$ 503.2</u>	<u>\$ 464.6</u>

CONCLUSION

The undersigned gratefully acknowledges the participation of the following members of the Massachusetts Division of Insurance in this examination:

Yvette P. Nelson-Smith
Steven C. Tsimitsos

Insurance Examiner II
Insurance Examiner II

The undersigned also express their appreciation for the courteous cooperation of the officers and employees of the Company in the course of the examination.

Respectfully submitted,

Hilton A. Irizarry, CFE
Examiner-in-Charge
Commonwealth of Massachusetts

Kenneth R. Brenner, CPA
Supervising Examiner
Commonwealth of Massachusetts