THE COMMONWEALTH OF MASSACHUSETTS

OFFICE OF CONSUMER AFFAIRS AND BUSINESS REGULATION

DIVISION OF INSURANCE

REPORT OF EXAMINATION

OF THE

COFACE NORTH AMERICA INSURANCE COMPANY

EAST WINDSOR, NEW JERSEY

as of DECEMBER 31, 2005

N.A.I.C. COMPANY CODE 31887

EMPLOYER ID NUMBER 20-0527783

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May 25, 2007

The Honorable Alfred W. Gross
Chair, Financial Condition (E) Committee, NAIC
Commissioner of Insurance
The Commonwealth of Virginia

State Corporation Commission
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The Honorable Steve Goldman
Secretary, Northeastern Zone, NAIC
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The Honorable Nonnie S. Burnes
Commissioner of Insurance
The Commonwealth of Massachusetts
Office of Consumer Affairs and Business Regulation
Division of Insurance
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Honorable Commissioners:

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

COFACE NORTH AMERICA INSURANCE COMPANY

at its home office located at 50 Millstone Road, Building 100, Suite 360, East Windsor, New Jersey 08520. The following report thereon is respectfully submitted.

SCOPE OF EXAMINATION

This is the first examination of Coface North America Insurance Company ("Company" or "Coface") since it was acquired by Coface North America Holding Company. The current National Association of Insurance Commissioners ("NAIC") association examination was conducted by the Massachusetts Division of Insurance ("Division") covering the period from December 30, 2003 (date of acquisition) through December 31, 2005, and included a review of certain Company, practices, processes and controls subsequent to the examination date.

The examination was conducted in accordance with standards and procedures established by the NAIC Financial Condition (E) Committee and prescribed by the NAIC *Financial Condition Examiners Handbook*, the examination standards of the Division, and Massachusetts General Laws. The principal focus of the examination was activity as of and for the year ended December 31, 2005; 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, treatment of policyholders, 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 was audited for 2005 by McGladrey & Pullen ("M&P"), and for 2006, by KPMG LLP ("KPMG"), both independent certified public accounting firms. M&P expressed an unqualified opinion on the Company's statutory financial statements for calendar year 2005, while KPMG has not yet issued the 2006 audit report. During the examination, review and use of M&P's workpapers were made to the extent deemed appropriate and effective. M&P noted a reportable condition regarding internal controls known as a material weakness and issued a letter to the Company's Board of Directors on May 23, 2006. The letter notes that bank accounts were not always reconciled timely. A second weakness noted that formal financial statement closing procedures had not been developed. The Company states that these internal control weaknesses resulted from requirements to meet quarterly reporting deadlines for the Company's parent necessitating that the final month of activity for each quarter be estimated. Bank reconciliations using actual, instead of estimated activity, were prepared; however; they were not timely. See the Accounts and Records Section and the Comments and Recommendations Section for additional discussion.

The Division retained the independent consulting actuarial services of Milliman, Inc. ("Milliman") to evaluate the adequacy of the Company's loss and loss adjustment expense reserves as of December 31, 2005. An evaluation of the adequacy and effectiveness of controls over information systems was completed by the Division to determine the level of reliance to be placed on summary information generated by the data processing systems.

For a summary of findings contained within this Report, refer to the Comments and Recommendations Section.

HISTORY

General

The Company is organized under the laws of the Commonwealth of Massachusetts. On December 30, 2003 Factory Mutual Insurance Company ("Factory Mutual") sold 100% of the issued and outstanding capital stock of Arkwright Insurance Company ("Arkwright") to Coface North America Holding Company ("CHC") for the purchase price of $7,150,000 including $5,400,000 in cash and investments. All liabilities of Arkwright were assumed by Factory Mutual. Arkwright was then renamed Coface and remains domiciled in Massachusetts.

CHC owns and operates a managing general underwriter ("MGU") that underwrites trade credit insurance business for CNA/Continental Insurance Company ("CNA"). CNA informed CHC that it wished to exit the trade credit insurance business. Consequently this book of business has incrementally been re-written by Coface as it has become licensed in more jurisdictions. As of today, approximately 10% of CHC's business is still underwritten through the MGU and reinsured from CNA to Coface S.A., a French based affiliate of the Company. The Company expects to move the remaining business to the Company over the next two years when the remaining state licenses are obtained.

For 2005, Coface S.A. was owned by Natexis Banques Populaires ("Natexis"), a French bank providing financing, investment banking, and other bank services. The parent of Natexis is Banque Federale des Banques Populaires ("BFBP") a French bank holding company. In November 2006 certain entities owned by the French bank Caisse Nationale des Caisses d'Epargne et de Prevoyance ("CNCE") merged into Natexis. Natexis was the surviving entity, and was renamed Natixis ("Natixis"). Thus, as of November 2006, the Company's ultimate parent is Natixis with BFBP and CNCE each owning 34.4% of Natixis. The remaining shares are publicly traded.

Capital Stock

The Articles of Organization for the Company authorized 26,000 shares of capital stock with $100 par value. All shares are issued and outstanding. All outstanding shares are held by CHC.

Dividends to Stockholder

In the period of examination, the Board of Directors has not issued dividends to the Company's sole stockholder.

Growth of the Company

The growth of the Company from the years 2003 through 2005 is indicated in the following schedule which was prepared from information in the Company's Annual Statements and examination adjustments:

Year	Admitted Assets	Liabilities	Surplus and Other Funds
2005	$ 40,862,065	$ 24,390,788	$ 16,471,277
2004	19,694,369	7,845,887	11,848,482
2003	5,400,027	0	5,400,027

Management

Annual Meeting

In accordance with the Company's bylaws, the annual meeting of shareholders shall be held on the second Thursday of April each year for the election of the board of directors. If an annual meeting shall not have been held on the date fixed in the bylaws, a special meeting in lieu of an annual meeting may be held with all the force and effect of an annual meeting. One-fifth of the shareholders shall be necessary to constitute a quorum. The corporate records document that for each year in the examination period, the requirement for an annual meeting was satisfied with an action by consent of the Company's sole shareholder.

Board of Directors

According to the bylaws, the Company's business shall be managed by a board of directors which may exercise all of the powers of the Company except those exclusively conferred upon or reserved solely to the shareholders. The board of directors may determine the number of directors on the board. The directors shall be elected at the annual meeting of shareholders or the special meeting in lieu of the annual meeting. Each director shall hold office until the next annual meeting of the stockholders and until a successor shall have been duly elected and qualified, but any director may resign. If the office of a director becomes vacant, the directors may fill any vacancy on the board of directors between annual meetings. Any vacancy at the time of the annual meeting may be determined by the shareholders. A director must be an officer or eligible to hold such office pursuant to any rules of eligibility and tenure adopted by the board of directors.

At December 31, 2005, the Company's board of directors, their business or professional affiliations, and residential addresses follow:

Name of Director	Business Affiliation	Residence
Michael J. Ferrante	President and Chief Executive Officer, Coface	West Windsor, New Jersey
Corine J. Troncy	Executive Vice President, Sales, Coface	New York, New York
Kenneth Moyle	Senior Vice President, Underwriting and Claims, Coface	Freehold, New Jersey
Pierre Fournel	Treasurer and Chief Financial Officer, Coface	New York, New York
Friedrich von Krusenstiern	Secretary and General Counsel, Coface	Brookline, Massachusetts

The bylaws do not specify the number of meetings of the board of directors to be held during a year and they allow the board of directors to take action by consent or telephonic meetings. At any meeting of the board of directors, a majority of the directors in attendance at any meeting shall constitute a quorum. The Company used consent actions to complete its business during the examination period.

Committees of the Board of Directors

The bylaws allow that the directors may elect from their number an executive committee, a finance committee, an audit committee and such other committees as they may determine. In accord therewith, on December 31, 2005, the board of directors appointed an investment committee to monitor the performance of the Company's investments and authorize the purchase and/or sale of securities. The membership of the investment committee consists of Director Ferrante, Director Fournel, Director Moyle, Director von Krusenstiern and Mr. Gary Scharf, Director of Statutory/GAAP Reporting. Although the Company did not obtain timely approval by the Board of Directors of Company investments as required by MGL Chapter 175 Section 64, the Company's board of directors has subsequently ratified the 2006 actions of the investment committee.

Officers

According to the Company's bylaws, the board of directors shall elect the officers of the Company. The officers of the Company shall be the chairman of the board of directors, the president, the treasurer, the secretary, one or more vice chairmen of the board of directors, one or more executive vice presidents and one or more senior vice presidents.

Generally, the powers and duties of the Company's officers are those commonly incident to the respective office. Such powers and duties are set forth in the bylaws and are subject to action of the board of directors. The president shall be the chief executive officer, unless the board of directors determines that the chairman of the board of directors shall be the chief executive officer, who shall have general supervision and control of the Company's business. Subject to the direction of the board of directors, the treasurer shall have custody of Company funds and securities and the general supervision of bank accounts. The secretary shall keep the articles of organization, the bylaws, and the records of all meetings and consents of shareholders and the board of directors.

Key officers and management of the Company at December 31, 2005 are as follows:

Name of Officer:	Title:
Michael J. Ferrante	President and Chief Executive Officer
Corine J. Troncy	Executive Vice President, Sales
Kenneth Moyle	Senior Vice President, Underwriting and Claims
Pierre Fournel	Treasurer and Chief Financial Officer
Friedrich von Krusenstein	General Counsel & Secretary
John Goggin	Vice President, Domestic and International Underwriting
Chris Germe	Vice President, Information Systems
Celine Hartmanshenn	Vice President Strategic Accounts
Dora M. Gonczy	Vice President
Hans Christian Freidrich Volbehr	Vice President
Christopher J. Short	Vice President
Gary Scharf	Director of Statutory Accounting/GAAP Reporting
Anthony Logiudice	Director for Taxes and Internal Control
Evette Mikhail	Director of Accounting

Conflict of Interest Procedures

The Company has an established procedure for the reporting of any material interest or affiliation on the part of any officer or director or responsible employee, which is in or is likely to conflict with his/her official duties. The Company began requiring officers and directors to file conflict of interest disclosure forms in March 2006.

Corporate Records

Articles of Incorporation and Bylaws

The articles of organization ("Articles") of the Company have been amended once since the acquisition of Arkwright on December 30, 2003. This amendment took effect on April 14, 2006. The bylaws of the Company were amended June 16, 2004. The Articles and the bylaws were read and reviewed.

Disaster Recovery and Business Continuity

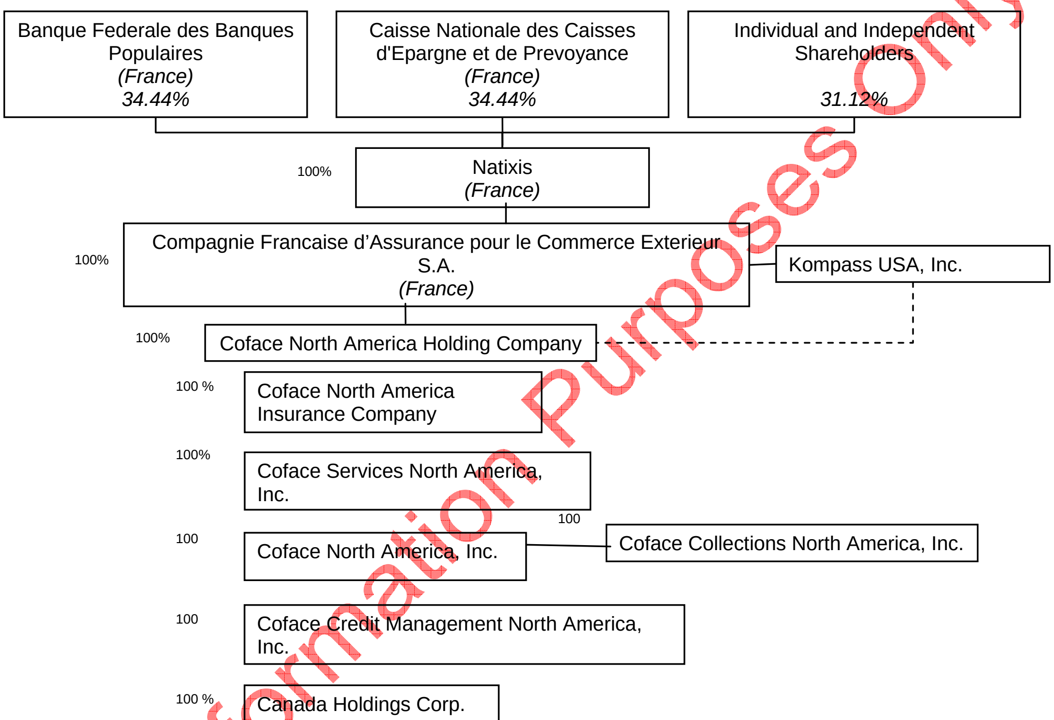
The Company provides for the continuity of management in the event of a catastrophe or national emergency in accordance with MGL Chapter 175 Sections 180M through 180Q. An evaluation of the Company's information technology systems and control environment indicated that it has a formal plan to address disaster recovery and business continuity. However, the Company has not tested the plan. See the Comments and Recommendations Section.

Board of Directors Minutes

The board of directors meeting consents for the period under examination and subsequent to the examination date indicated that all actions were taken in accordance with the Company's bylaws. The Company has not historically obtained approval by the Board of Directors of the top five most highly compensated officers or directors and any other officer or director who has compensation exceeding $150,000 as required by MGL Chapter 175 Section 35. The Company obtained such approval on January 1, 2007, and has agreed to prospectively obtain such approval as required.

AFFILIATED COMPANIES

As stated in the Insurance Holding Company System Form B and Form C as filed with the Division, the Company is a member of a holding company system and is subject to the registration requirements of Section 206C of MGL Chapter 175 and Regulation 211 CMR 7.00. Effective with the reorganization in November 2006, the corporate organization of which the Company is a member is as follows**:**



<u>Transactions and Agreements with Subsidiaries and Affiliates</u>

Administrative Services Agreement

Beginning in January 2005, substantially all personnel previously employed by Coface North America, Inc. were transferred to the Company. In addition, the Company purchased fixed assets related to the employees who were transferred to the Company. The assets and employee transfers were made as a result of the transfer of the book of business to the Company and declining role of the MGU. The Company shares certain employee, operating and overhead expenses with affiliated companies and is reimbursed for the affiliates' share of such expenses. The Company also pays certain licensing fees to Coface Services North America, Inc. for use of its credit evaluation database and underwriting system.

The Company's administrative services agreement referenced in its April 27, 2006 Form B filing does not reflect actual intercompany administrative services between the Company and Coface North America, Inc. or other affiliates. As a result, the Company's billings and payments in 2005 and 2006 to or from its affiliates for certain services rendered or incurred have not been supported by a written agreement. Additionally, cash settlements for services rendered or incurred have not always been made timely. As a result, the Company filed a Form D on May 24, 2007 which included a proposed Expense Allocation Agreement for the Company and its affiliates. For further discussion, see the Comments and Recommendations Section.

Reinsurance Agreements

See the Reinsurance Section for a discussion of intercompany reinsurance agreements.

Tax Sharing Agreement

The Company's Federal income tax return is included in the consolidated Federal income tax return of Coface North America Holding Company. Although the Company did not previously adopt a written intercompany tax sharing agreement with its parent, it filed a Form D on May 24, 2007 which included a proposed Tax Sharing Agreement for the Company and its affiliates.

FIDELITY BONDS AND OTHER INSURANCE

The Company maintains fidelity coverage with an authorized Massachusetts insurer, consistent with Section 60 of MGL Chapter 175. The aggregate limit of liability exceeds the NAIC suggested minimum.

The Company has further protected its interests and property by additional policies of insurance covering other insurable risks. Insurance coverage is provided by insurers licensed in the Commonwealth of Massachusetts and was in-force as of December 31, 2005.

DEFINED CONTRIBUTION PLAN

The Company's affiliate, Coface North America, Inc. sponsors a defined contribution plan covering all of the Company's employees. Each employee may contribute to the plan ("elective contributions") subject to Internal Revenue Service limits. The Company contributes equal to 70% of each employee's elective contributions up to 6% of the employee's salary. In 2005 the Company also provided a discretionary benefit of 3-5% based on each employee's age. The Company's portion of the defined contribution plan expense was $165,614 in 2005.

STATUTORY DEPOSITS

The Company's statutory deposits as of December 31, 2005 are as follows:

Jurisdiction	Description of Deposit	Par Value	Statement Value	Market Value
Arizona	U.S Treasury Note 3.125% Due 1/31/07	$550,000	$543,616	$542,311
Georgia	U.S Treasury Note 2.75% Due 7/31/06	50,000	49,726	49,530
Kansas	U.S Treasury Note 2.75% Due 7/31/06	100,000	99,452	99,059
Louisiana	U.S Treasury Note 2.75% Due 7/31/06	70,000	69,616	69,341
Massachusetts	U.S Treasury Note 2.75% Due 7/31/06	1,500,000	1,491,782	1,485,885
North Carolina	U.S Treasury Note 2.75% Due 7/31/06	120,000	119,303	118,871
North Carolina	U.S Treasury Note 2.375% Due 8/15/06	180,000	180,267	177,786
Rhode Island	U.S Treasury Note 1.875% Due 12/31/05	500,000	500,000	500,000
South Carolina	U.S Treasury Note 2.75% Due 7/31/06	125,000	124,315	123,824
Tennessee	U.S Treasury Note 5.5% Due 2/15/08	150,000	153,930	153,357
		$3,345,000	$3,332,007	$3,319,964

INSURANCE PRODUCTS AND RELATED PRACTICES

Policy Forms and Underwriting Practices

The Company sells trade credit insurance and political risk insurance policies. The Company's policyholders are typically distributors or wholesalers of goods to retail establishments and other businesses. There are no sales of insurance products to individual consumers. Trade credit coverage typically covers 30-90 day accounts receivable unpaid due to insolvency. At the time the creditor enters bankruptcy, the policyholder may choose to file a claim. The Company's trade credit underwriting includes an assessment of the policyholder's credit granting process and bad debt experience. Additionally, the Company's underwriting department reviews the policyholder's customers' credit risk. Policies are typically one year, and may include specific named customers or "named buyers" while others include all buyers meeting specific requirements. Premium is based upon a rate for the amount of coverage purchased, or a rate based on a policyholder's monthly sales activity.

Political risk coverage on trade receivables is offered using the same trade credit policy forms with a political risk rider, and also using negotiated and customized policy forms for large policyholders. In connection with the latter, political risk coverage is provided with regard to the nonpayment of trade receivables, confiscation, expropriation, nationalization and deprivation of property and non-performance of contractual obligations. The Company's underwriting focuses on country risk by considering its political, economic and legal environment.

Territory and Plan of Operation

The Company currently is licensed to write business in 30 states and the District of Columbia. It provides coverage through its network of 85 exclusive captive agents who are managed by five regional managing agents. All managing agents and captive agents are independent contractors and not employees of the Company. The agents also sell other Coface services offered by affiliated companies.

Treatment of Policyholders

Claim Settlement Practices

All claims are adjudicated in the Company's home office. First notice of a claim typically is reported when a policyholder is aware of a customer's delinquency or insolvency. When the policyholder has knowledge of a customer's insolvency as determined by a legal proceeding, the policyholder is required to notify the Company. If the policyholder does not have knowledge of the insolvency prior to policy expiration, the claim may be filed within 20 days of the expiration. Under the terms of the policy, a policyholder also has the option of filing past due accounts as a claim where unpaid accounts receivable less than 90 days past due are assigned to the Company for collection. The Company charges fees for the assignments that are based upon amounts collected as set forth in the policy. Individual notices filed with the Company regarding losses are accumulated against the *Primary Loss* (deductible). When the *Primary Loss* is reached the policyholder requests and completes a *Statement of Claim* (proof of loss). Claims are to be paid in 60 days after receipt of the *Statement of Claim*, once the claim is determined to be "in good order". The Company has no outstanding claim litigation with any policyholders and has not experienced any formal complaints regarding its claims practices. Procedures performed in conjunction with the claims testwork indicated that the Company investigates and settles claims timely.

Dividends to Policyholders

In the period of examination, the Board of Directors did not authorize any dividends to be paid to the Company's policyholders.

REINSURANCE

Ceded Reinsurance

The Company has entered into a quota share reinsurance agreement with Coface S.A., effective December 31, 2003. Under the quota share agreement, the Company cedes 50% of premiums written and received a ceding commission of 50.6% and 46.3% during 2005 and 2004, respectively. The Company recognized $10,003,268 and $2,527,731 of ceding commission income from premiums ceded during 2005 and 2004, respectively.

The Company did not record a deferred ceding commission as required by the *NAIC Accounting Practices and Procedures Manual ("APP Manual") SSAP 62, Paragraph 51.* The Division and the Company have agreed to a methodology for calculating the deferred ceding commission, which the Company has agreed to use for future financial statements. As a result, an examination adjustment to record a deferred ceding commission was made as noted in Note 4. See also the Comments and Recommendations Section.

The Company has also entered into a stop-loss reinsurance agreement with Coface S.A. The Company retains net ultimate losses up to a maximum limit of 56% of the net retained earned premium. In addition, the Company has entered into an excess of loss agreement with Coface S.A. that limits the Company's retention on any one loss per policy to a maximum of 10% of the Company's capital and surplus. The Company annual premium for the excess of loss agreement is $10,000.

The following table summarizes the effect of the ceded reinsurance on premiums written for 2005.

	Premium Written	Unearned Premium
Direct	$39,543,639	$18,080,198
Ceded – Quota share	19,824,974	9,040,099
Ceded – Stop loss	828,000	0
Net	$18,890,665	$ 9,040,099

The Company's reinsurance contracts did not originally contain all of the required terms noted in *APP Manual SSAP 62* such as an insolvency clause and arbitration clause. The Company filed a Form D on January 11, 2007 to amend its contracts to include such required items. Such Form D was deemed approved by the Division. In addition, the examination noted that the Company did not timely settle reinsurance balances with affiliates in 2005. However, in 2006, reinsurance balances with affiliates were settled quarterly.

Assumed Reinsurance

The Company assumes a very small amount of reinsurance from a U.S. Agency, the Oversees Private Investment Corporation ("OPIC"). OPIC was established as an agency of the U.S. Government in 1971 and helps U.S. businesses invest overseas and fosters economic development in new and emerging markets. In addition, Coface S.A. operates as a branch for business written in Canada. For the Canadian branch activity, the ultimate net loss in excess of 56% of the net retained earned premium income is assumed by the Company pursuant to a stop-loss reinsurance treaty. Assumed premiums from OPIC and Coface S.A.'s Canadian branch were $106,310 and $45,000, respectively in 2005.

ACCOUNTS AND RECORDS

The internal control structure was discussed with management through questionnaires and through a review of work performed by M&P, who issued a material weakness letter to the Company's Board of Directors on May 23, 2006. The letter notes that bank accounts were not always reconciled timely. A second weakness noted that formal financial statement closing procedures had not been developed. The Company notes that these problems resulted from requirements to meet the quick quarterly close for the Company's parent necessitating that the final month of activity for each quarter be estimated, while statutory reporting reflected actual results.

The Company has added significant staff in 2006 to address these concerns. The examination reviewed bank and account reconciliations for selected months and noted that the Company has made significant improvement in completing timely reconciliations and identifying reconciling items. However, for one account we noted that the Company was not always timely investigating reconciling items. As a result of our review, the Company has implemented a new procedure to ensure that any potential income statement or surplus impact reconciling items are timely identified and evaluated. A new report will be prepared monthly identifying these items. For more discussion, see the Comments and Recommendations Section.

The Company's premiums receivable and commissions payable accounts have not been reconciled and researched timely. The Company has only recently begun performing such procedures in a timely manner. For more discussion, see the Comments and Recommendations Section.

The NAIC Evaluation of Controls in Information Systems Questionnaire was completed by the Company and reviewed to evaluate the adequacy of the controls in the Company's information systems. For further discussion, see the Comments and Recommendations Section.

In accordance with 211 C.M.R. 23.00, the books and records of the Company are audited annually by a firm of independent certified public accountants. For 2005 M&P completed the audit. In 2006, KPMG has been retained to complete the audit, which is ongoing.

FINANCIAL STATEMENTS

The following financial statements are presented on the basis of accounting practices prescribed or permitted by the Division and the NAIC as of December 31, 2005:

Statement of Assets, Liabilities, Surplus and Other Funds as of December 31, 2005

Statement of Income (Loss) for the Year Ended December 31, 2005

Reconciliation of Surplus and Other Funds from Inception and for the Three Years in the Period Ended December 31, 2005

Statement of Assets, Liabilities, Surplus and Other Funds
as of December 31, 2005

Assets	Per Company	Examination Changes	Per Examination	Notes
Bonds	$ 3,326,264	$ 0	$ 3,326,264	
Cash and short-term investments	19,619,457	111,942	19,731,399	(2)
Subtotals, cash and invested assets	22,945,721	111,942	23,057,663	
Investment income due and accrued	142,432		142,432	
Uncollected premiums and agents' balances in course of collection	10,896,547	(716,223)	10,180,324	(2,3)
Amounts recoverable from reinsurers	1,876,988		1,876,988	
Net deferred tax asset	1,060,131	335,282	1,395,413	(7)
Receivables from parent, subsidiaries and affiliate	4,209,245	747,627 (747,627)	4,209,245	(3,3A)
Total Assets	$ 41,131,064	$ (268,999)	$ 40,862,065	

Statement of Assets, Liabilities, Surplus and Other Funds
as of December 31, 2005

Liabilities	Per Company	Examination Changes	Per Examination	Notes
Losses	$ 5,163,027	$ 0	$ 5,163,027	(1)
Loss adjustment expenses	66,874		66,874	(1)
Commissions payable, contingent commissions, and other similar charges	3,634,076	(1,024,986)	2,609,090	(3, 5, 6)
Other expenses	917,669		917,669	
Taxes, licenses and fees	263,401		263,401	
Unearned premiums	9,040,099		9,040,099	
Deferred ceding commission	-	1,132,495	1,132,495	(4)
Ceded reinsurance premiums payable	2,992,830	542,539	3,535,369	(5)
Payable to parent, subsidiaries and affiliates	1,633,521	29,243	1,662,764	(6)
Total Liabilities	23,711,497	679,291	24,390,788	
Common capital stock	2,600,000		2,600,000	
Gross paid-in and contributed surplus	18,283,310		18,283,310	
Unassigned funds (surplus)	(3,463,743)	(948,290)	(4,412,033)	(3,3A,4,6,7)
Surplus as regards policyholders	17,419,567	(948,290)	16,471,277	
Total Liabilities, Surplus and Other Funds	$ 41,131,064	$ (268,999)	$ 40,862,065	

Statement of Income (Loss)
for the Year Ended December 31, 2005

	Per Company	Examination Changes	Per Examination	Notes
Premiums earned	$ 13,855,284	$ 0	$ 13,855,284	
Deductions:				
Losses incurred	6,301,175		6,301,175	
Loss expenses incurred	96,000		96,000	
Other underwriting expenses incurred	9,374,787	535,945	9,910,732	(3, 4, 6)
Total underwriting deductions	15,771,962	535,945	16,307,907	
Net underwriting gain (loss)	(1,916,678)	(535,945)	(2,452,623)	
Net investment income earned	482,919		482,919	
Net investment gain	482,919	0	482,919	
Net gain (loss) before dividends to policyholders, after capital gains tax, and before all other federal and foreign income taxes	(1,433,759)	(535,945)	(1,969,704)	
Net income (loss)	$ (1,433,759)	$ (535,945)	$ (1,969,704)	

Reconciliation of Surplus and Other Funds from Inception and for the Three Years in the Period Ended December 31, 2005

	2005*	2004	2003
Surplus as regards policyholders as of December 31, prior year	$ 11,848,482	$ 5,400,027	$ 0
Net income (loss)	(1,969,704)	(2,316,529)	-
Change in net deferred income tax	867,213	785,400	-
Change in non-admitted assets	(1,433,521)	(344,919)	-
Paid-in surplus	7,158,807	8,324,503	5,400,027
Net change in surplus as regards policyholders for the year	4,622,795	6,448,455	5,400,027
Surplus as regards policyholders as of December 31, current yea	$ 16,471,277	$ 11,848,482	$ 5,400,027

* Per Examination

NOTES TO FINANCIAL STATEMENTS

NOTE 1:

Losses	$ 5,163,027
Loss Adjustment Expenses	$ 66,874
Losses and Loss Adjustment Expenses	$ 5,229,901

As part of the examination, the Division engaged the consulting actuarial services of Milliman to perform an actuarial review of the loss and loss adjustment expense reserves carried by the Company as of December 31, 2005. Their review principally included a review of the reasonableness of the assumptions, selections, and methodologies used by KPMG in its actuarial report on the calculation of the reserve estimates for the Company.

The following table summarizes KPMG's gross reserve ranges and selected point estimate reserves:

KPMG Gross Loss and Loss Adjustment Expense Reserves

Reserve Category	Low	Point	High	Company Carried
Losses + LAE	$9,054,958	$9,847,111	$10,614,725	$10,459,802

Similarly, on a net basis, the following table summarizes KPMG's reserve ranges and selected point estimate reserves, and the Company's carried loss and loss adjustment expense reserves as of December 31, 2005.

KPMG Net Loss and Loss Adjustment Expense Reserves

	Estimates by KPMG			
Reserve Category	Low	Point	High	Company Carried
Losses + LAE	$4,527,479	$4,923,555	$5,307,362	$5,229,901

In the course of analyses, Milliman reviewed KPMG's actuarial methodologies, actuarial assumptions and selections, and the Schedule P reconciliation. Milliman noted that KPMG estimated losses by underwriting year and used a variety of actuarially accepted estimation methods. Milliman concluded that KPMG's actuarial methodologies and actuarial assumptions and selections were reasonable. Regarding the Schedule P reconciliation, Milliman noted that KPMG reconciled the data in total and not by accident year. Milliman concluded that minor differences in the data were not material. Finally, Milliman concluded that based upon its review, they believe that the gross and net loss and loss adjustment expense reserves estimated by KPMG and the Company, are reasonable.

NOTE 2:

	Dr (Cr)
Cash and short-term investments	$111,942
Uncollected premiums and agents' balances in course of collection	($111,942)

The 2005 audited financial statements reflect a reclassification of amounts reported in the 2005 annual statement to apply cash received against uncollected premiums and agents' balances in course of collection.

NOTE 3:

	Dr (Cr)
Receivables from parent, subsidiaries and affiliates	$747,627
Commissions payable, contingent commissions, and other similar charges	($72,300)
Other underwriting expenses incurred	($71,046)
Uncollected premiums and agents' balances in course of collection	($604,281)

An examination adjustment was made to record an intercompany receivable for commission advances due from its affiliate, which the Company recorded in uncollected premiums as a suspense item.

NOTE 3A:

	Dr (Cr)
Unassigned funds (surplus)	$747,627
Receivables from parent, subsidiaries and affiliates	($747,627)

An examination adjustment was made to non-admit the intercompany receivable recorded in Note 3 since it was billed in May 2007.

NOTE 4:

	Dr (Cr)
Other underwriting expenses	$1,132,495
Deferred ceding commission	($1,132,495)

The Company did not properly record a deferred ceding commission as required by *AAP Manual SSAP 62, Paragraph 51*. The adjustment records this deferred income.

NOTE 5:

	Dr (Cr)
Commissions payable, contingent commissions, and other similar charges	$542,539
Ceded reinsurance premiums payable	($542,539)

The 2005 audited financial statements reflect a reclassification of amounts reported in the 2005 annual statement to correct an error in which commissions payable, contingent commissions, and other similar charges were overstated and ceded reinsurance premiums payable were understated.

NOTE 6:

	Dr (Cr)
Commissions payable, contingent commissions, and other similar charges	$554,747
Other underwriting expenses	($525,504)
Payable to parent, subsidiaries and affiliates	($29,243)

Commissions payable, contingent commissions, and other similar charges were adjusted to reflect the actual liability at December 31, 2005.

NOTE 7:

	Dr (Cr)
Net deferred tax asset	$335,282
Unassigned funds (surplus)	($335,282)

The adjustment records the deferred tax impact of the examination adjustments.

COMMENTS AND RECOMMENDATIONS

Bank Reconciliations

With regard to the conditions noted in the material weakness letter issued May 23, 2006, the Company has added significant staff in 2006 to address these concerns. While the examination noted that the Company has made significant improvement in completing timely bank reconciliations and identifying reconciling items, for one account, reconciling items were not always timely investigated. As a result of the examination, the Company has implemented a new procedure to ensure that any potential income statement or surplus impact reconciling items are timely identified and evaluated. A new report will be prepared monthly identifying these items. The Company should ensure that these procedures are timely performed.

Premiums Receivable and Commissions Payable Accounts

The Company's premiums receivable and commissions payable accounts have not been reconciled and researched timely. The Company has only recently begun performing such procedures on a timely manner. The Company should ensure that the premiums receivable and commissions payable detail are properly reviewed monthly and reconciled to the general ledger. Unusual items should be researched and adjusted as necessary to ensure that the general ledger is not misstated. Also, a supervisor should complete an in-depth and timely review of the research and reconciliation efforts.

Schedule P Loss Data

The Company prepared its 2006 Annual Statement Schedule P showing loss data on an "underwriting year basis" rather than an "accident year basis." Premiums were properly reported on an earned basis. As a result of this reporting, Schedule P – Part 2 incorrectly shows material adverse development of the Company's incurred losses. The Company is re-filing its 2006 Annual Statement Schedule P in accordance with the Annual Statement Instructions, which requires loss data to be reported on an "accident year basis." The Company has agreed to use this methodology for all future Schedule P filings and should ensure that this methodology is properly used for all future Schedule P filings.

Deferred Ceding Commission

The Company did not record a deferred ceding commission as required by the *APP Manual SSAP 62, Paragraph 51*. The Division and the Company have agreed to a methodology for calculating the deferred ceding commission, which the Company has agreed to use for future financial statements. The Company should ensure that this methodology is properly used for calculating this deferred income in future financial statements.

Reinsurance Contracts

The Company's reinsurance contracts did not originally contain all of the required terms noted in *APP Manual SSAP 62* such as an insolvency clause and arbitration clause. The Company has filed a Form D on January 11, 2007 to amend its contracts to include such required items. Future contracts should also include these key elements.

The examination also noted that the Company did not timely settle reinsurance balances with affiliates in 2005. However, in 2006, reinsurance balances with affiliates were settled quarterly. The Company should ensure that all future intercompany reinsurance balances are settled at least quarterly.

Intercompany Administrative Services Agreement

The Company's administrative services agreement referenced in its April 27, 2006 Form B filing did not reflect actual intercompany administrative services between the Company and Coface North America, Inc. or other affiliates. As a result, the Company's billings and payments in 2005 and 2006 to or from its affiliates for certain services rendered or incurred have not been supported by a written agreement. Additionally, cash settlements for services rendered or incurred have not always been made timely. The Company should establish an appropriate intercompany agreement to ensure proper reporting in accordance with *APP Manual SSAPS 25 and 70*. The allocation methods should be supportable and substantially reflect actual costs incurred or services rendered. Finally, the Company should ensure it settles all intercompany receivables and payables at least quarterly. The Company filed a Form D on May 24, 2007 which included a proposed Expense Allocation Agreement for the Company and its affiliates.

Intercompany Tax Sharing Agreement

The Company's Federal income tax return is included in the consolidated Federal income tax return of Coface North America Holding Company. Although the Company did not previously adopt a written intercompany tax sharing agreement with its parent, it filed a Form D on May 24, 2007 which included a proposed Tax Sharing Agreement for the Company and its affiliates.

Compensation Approval by the Board of Directors

The Company has not historically obtained approval by the Board of Directors of top five most highly compensated officers or directors and any other officer or director who has compensation exceeding $150,000 as required by MGL Chapter 175 Section 35. The Company obtained such approval on January 1, 2007, and agreed to prospectively obtain such approval as required.

Investment Approval

The Company established an investment committee of the Board of

by the Board of Directors

Directors on December 31, 2005. The Company did not obtain timely approval by the Board of Directors of Company investments as required by MGL Chapter 175 Section 64. The Company's Board of Directors has subsequently ratified the 2006 actions of the investment committee, and the Company has agreed to prospectively have the Board of Director's quarterly ratify the actions of the investment committee.

Non-admitted Over 90 Day Receivables

The Company should ensure that its non-admitted over 90 day receivable analysis is properly completed including the use of accurate unearned premium amounts applied against these receivables.

Deferred Tax Disclosures

The Company's 2005 annual statement included errors in the deferred tax disclosures. The errors were not significant. The Company should work closely with the independent auditors to ensure that future financial statement disclosures are complete and accurate.

Annual Statement Allocation of Expenses

The Company has allocated few expenses to investments expenses and loss adjustment expenses in the Underwriting and Investment Exhibit-Part 3 Expenses to the Annual Statement. As the Company grows, the Company should consider a cost allocation study to evaluate appropriate allocation of expenses.

Criminal Background Checks

The Company has not historically conducted criminal background checks on prospective employees to ensure compliance with the Federal Law regarding the hiring of a felon without approval of the Commissioner of Insurance. The Company has agreed to begin conducting criminal background checks on prospective employees.

Information Technology Controls and Processes

The Company recently hired an outside consultant to conduct an information technology review. The report noted several areas for improvement including the following:

- Server room fire and power failure protection
- Systems access security
- Segregation of duties among system development staff
- Password design and compliance with password change policies
- Adopting written procedures for changes to hardware
- Compliance with and documentation of procedures for application change management
- Updating procedures over anti-virus software
- Developing procedures to prevent the use of unauthorized software
- Testing of the Company's disaster recovery plan and
- Adoption of an information technology privacy policy.

The Company has addressed several of these items and should consider making enhancements to their information technology controls and processes to address the remaining items.

CONCLUSION

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

The assistance rendered by Rudmose & Noller Advisors, LLC who participated in this examination hereby is acknowledged.

John A. Turchi, CFE, CPCU
Supervising Examiner and Examiner-in-Charge
Commonwealth of Massachusetts