



**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, 2011**

**NAIC COMPANY CODE 31887**

**EMPLOYER ID NUMBER 20-0527783**

## Coface North America Insurance Company

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

1000 Washington Street, Suite 810 • Boston, MA 02118-6200  
(617) 521-7794 • Toll free (877) 563-4467  
<http://www.mass.gov/doi>

**DEVAL L. PATRICK**  
GOVERNOR

**TIMOTHY P. MURRAY**  
LIEUTENANT GOVERNOR

**GREGORY BIALECKI**  
SECRETARY OF HOUSING AND  
ECONOMIC DEVELOPMENT

**BARBARA ANTHONY**  
UNDERSECRETARY OF CONSUMER AFFAIRS  
AND BUSINESS REGULATION

**JOSEPH G. MURPHY**  
COMMISSIONER OF INSURANCE

April 28, 2013

Honorable Joseph G. Murphy  
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 ("M.G.L."), 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 08520-1419. The following report thereon is respectfully submitted.

## **SCOPE OF EXAMINATION**

Coface North America Insurance Company ("Company" or "Coface") was last examined as of December 31, 2006 by the Massachusetts Division of Insurance (the "Division"). The current examination was also conducted by the Division and covers the five-year period from January 1, 2007 through December 31, 2011, including any material transactions and/or events occurring subsequent to the examination date and noted during the course of this examination.

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 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. An examination also includes assessing the principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation, management's compliance with Statutory Accounting Principles and annual statement instructions, when applicable to domestic state regulations. All accounts and activities of the Company were considered in accordance with the risk-focused examination process.

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 bond and other insurance, employees' 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 is audited annually by KPMG LLP, an independent certified public accounting firm. The firm expressed unqualified opinions on the Company's financial statements for the calendar years 2007 through 2011. A review and use of the Certified Public Accountants' workpapers were made to the extent deemed appropriate and effective. An independent actuarial consulting firm, Milliman, Inc. ("Milliman") was retained by the Division to evaluate the adequacy of the Company's loss and loss adjustment expense reserves as of December 31, 2011. Additionally, the Division reviewed the adequacy and effectiveness of the IT systems controls to determine the level of reliance to be placed on the information generated by the data processing systems.

## **SUMMARY OF SIGNIFICANT FINDINGS**

For a summary of findings contained within this report, refer to the "Summary of Recommendations" section on page 20. The previous report of examination recommended the Company enhance its controls and processes related to timely completion of bank reconciliation, proper aging and non-admitting premium receivables, increasing the Company's internal audit focus over financial and compliance controls, and timely settlement of intercompany balances. The Company implemented new controls and processes to address the Comments and Recommendations from the prior examination.

## **SUBSEQUENT EVENTS**

The Company insures commercial trade credit risks, which may include large risks. A few large claims may result in material adverse deviation of reserves. During the financial crisis of 2008 and 2009, the Company experienced higher than usual ultimate loss ratios on direct and assumed business. In the years following the financial crisis, due to continued economic weakness in the U.S. and global economies, the Company maintained conservative estimates of ultimate loss ratios. Based upon redundant reserve development of prior years' reserves and stable economic indicators, the Company recognized favorable loss development of approximately \$24.8 million during 2012.

## **COMPANY 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 ("CNAHC") for the purchase price of \$7,150,000. All liabilities of Arkwright were assumed by Factory Mutual. Arkwright was then renamed Coface and remained domiciled in Massachusetts. As a licensed property and casualty insurer, the Company is subject to the provisions of Massachusetts General Laws ("M.G.L."), Chapter 175, Section 4 and other Massachusetts insurance laws.

Prior to acquiring Arkwright, CNAHC owned and operated a managing general underwriter ("MGU") that underwrote trade credit insurance business for CNA/Continental Insurance Company. Beginning in 2004, CNA/Continental Insurance Company no longer wished to be the risk bearing entity for the trade credit insurance business, so as policies expired, the book of business was incrementally written by Coface as it became licensed in more U.S. jurisdictions. As of December 31, 2011, the Company is licensed in the District of Columbia and all states except Hawaii.

CNAHC is controlled by its immediate parent, Compagnie Francaise d'Assurance pour le Commerce Extérieur S.A. ("Coface S.A."); its intermediate parent, the publicly traded French bank Natixis; and its ultimate parent BPCE, the second largest French bank holding company.

## Coface North America Insurance Company

Natixis provides financing, investment banking, and other bank services. BPCE is a retail bank that also provides other banking, financial and real estate financing services.

Coface S.A. has a significant history in trade credit insurance in France and Europe, beginning shortly after World War II, and together with its affiliates are global leaders in providing receivables management products. Coface S.A. and its subsidiaries are the world's third largest trade credit insurer.

### Capital Stock

The Company's Articles of Organization authorized 26,000 shares of capital stock with \$100 par value. All shares are issued and outstanding. All outstanding shares are held by CNAHC. Since December 31, 2006, CNAHC contributed \$20,000,000 and \$3,000,000 in 2007 and 2009, respectively, in additional paid-in capital to the Company. With this infusion of funds, paid-in capital totaled \$2,600,000, and the gross paid-in and contributed surplus totaled \$49,283,310 as of December 31, 2011.

### Dividends to Stockholders

The Company did not pay any dividends to its stockholder during the five-year period of the examination and had no dividend payable at year-end.

## **CORPORATE RECORDS**

### Board of Directors Minutes

The minutes of meetings of the Board of Directors and its Committees for the period under examination were read and they indicated that all meetings were held in accordance with the Company's bylaws and the Laws of the Commonwealth of Massachusetts. Activities of the Committees were ratified at meetings of the Board of Directors.

In accordance with an action by unanimous written consent of the Board of Directors without a meeting dated July, 1, 2008, the Board of Directors adopted a resolution that the prior Report of Examination was reviewed and accepted by the Board.

### Articles of Incorporation and Bylaws

The Articles of Incorporation ("Articles") of the Company have been amended twice since the acquisition of Arkwright on December 30, 2003. The Company changed its name to its present name on the same day as the acquisition and this was subsequently approved by the Division on January 27, 2004. A second amendment to the Articles authorizing an additional class of business was adopted by the Company on March 27, 2006 and subsequently approved by the Division on April 13, 2006. The bylaws of the Company were also amended on June 16, 2004 to reflect the change of the Company's name previously authorized by the Company on December 30, 2003 and then subsequently approved by the Division on January 27, 2004. The Articles and the bylaws were read and reviewed.

### Conflict of Interest Procedures

The Company has a policy pertaining to conflict of interest. In support of its answer to Question 14 of Part 1 Common Interrogatories of the annual statement, the Company has an established procedure for the disclosure to the Board of Directors 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. Annually, each officer or director or responsible employee completes a questionnaire disclosing any material conflicts of interests. The completed questionnaires were reviewed and no discrepancies were noted to contradict the Company's response to the General Interrogatory regarding conflicts of interests reported in the Company's 2011 Annual Statement.

### 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., Chapter 175, Sections 180M-180Q.

## **MANAGEMENT AND CONTROL**

### 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, 2011, the Company's Board of Directors consisted of the following Company officers:

<u>Name of Director</u>	<u>Title</u>
Michael J. Ferrante	President and Chief Executive Officer
Kerstin Braun	Executive Vice President, Sales
Kenneth Moyle	Executive Vice President, Underwriting
Daniel Shultis	Treasurer and Chief Financial Officer
Friedrich von Krusenstiern	Secretary and General Counsel

## Coface North America Insurance Company

### 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 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 Shultis, Director Moyle, Director von Krusenstiern and Mr. Gary Scharf, Director of Statutory/GAAP Reporting.

### 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. The Board of Directors fulfills the functions of an audit committee that are delegated by the Company's ultimate parent, BCPE.

Officers of the Company at December 31, 2011, in addition to those directors above are as follows:

<u>Name of Officer</u>	<u>Title</u>
Zulfikar Bhura	Vice President, Information Systems
Christopher Short	Vice President, International
Michael Harasek	Vice-President, Claims

### Affiliated Companies

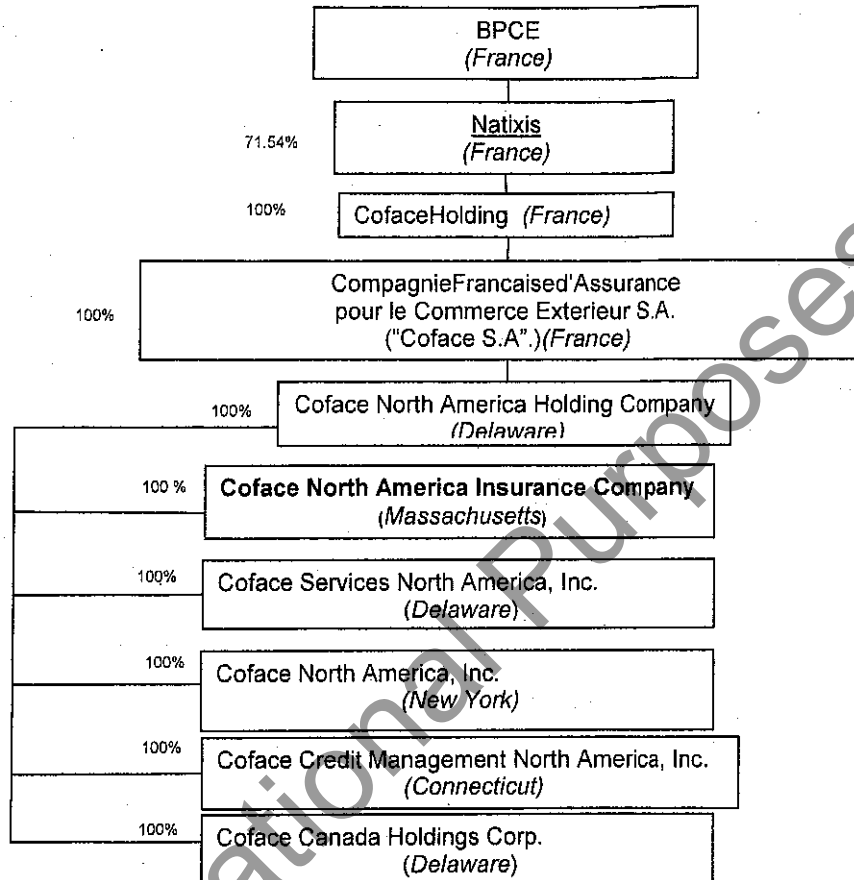
As stated in the Insurance Holding Company System Form B and Form C as filed with the Division, the Company is a member of a holding company system and is subject to the registration requirements of Section 206C of M.G.L., Chapter 175 and Regulation 211 CMR 7.00. BPCE is the "ultimate controlling person" for the Company.



## Coface North America Insurance Company

### Organization Chart

A summary of ownership and relationship of the Company and its affiliated companies as of Year 2013 is illustrated below:



### Transactions and Agreements with Subsidiaries and Affiliates

#### *Administrative Services Agreements*

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 fees to Coface Services North America, Inc. for credit and financial information, which the Company uses for its credit evaluations.

The Company pays Coface S.A. and other affiliated entities group management and staff costs associated with reimbursement of expatriate employees and head office expenses. The Company has remitted payments to Coface S.A. for such services since 2008. On January 4, 2013, the Company executed a Head Office Management Fees Agreement ("Head Office Agreement"). The Head Office Agreement covers such services for the period commencing January 1, 2011 and

## Coface North America Insurance Company

is annually renewable. In addition, payments made under the Head Office Agreement include a profit margin of 5.6%. The Company did not make a required Form D filing referencing the Head Office Agreement until November 20, 2012. As a result of the delinquent Form D filing, the Company's payments to Coface S.A. since 2008 were not supported by a written agreement or approved Form D filing. See the Summary of Recommendations Section for additional discussion.

### *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 subject to a tax sharing agreement.

## **FIDELITY BONDS AND OTHER INSURANCE**

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

The Company has further protected its interests and property by policies of insurance covering other insurable risks. Coverage is provided by insurers licensed in the Commonwealth of Massachusetts, and the policies were in force as of December 31, 2011.

## **PENSIONS, STOCK OWNERSHIP AND INSURANCE PLANS**

### Defined Contribution Plan

The Company participates in the Natixis/CofaceUS Group 401(k) Retirement Plan. This plan is available to 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. The Company's portion of the defined contribution plan expense was \$150,141 in 2011.

## **TERRITORY AND PLAN OF OPERATION**

The Company currently is licensed to write business in the District of Columbia and all states except Hawaii. The Company writes insurance through four regional independent agencies. Each agency employs insurance agents, who exclusively sell Coface services and other services offered by affiliated companies.

### Policy Forms and Underwriting Practices

The Company primarily sells trade credit insurance and, to a lesser extent, 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 debtor 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.

### Treatment of Policyholders

#### *Claim Settlement Practices*

All claims are adjudicated in the Company's principal 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 unusual claim related litigation with any policyholders and has not experienced significant complaints regarding its claims practices. Procedures performed in conjunction with the claims test work 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.

**GROWTH OF COMPANY**

The growth of the Company for the years 2007 through 2011 is shown in the following schedule, which was prepared from the Company's annual statements.

<u>Year</u>	<u>Admitted Assets</u>	<u>Liabilities</u>	<u>Surplus</u>	<u>Direct Premiums Written</u>	<u>Net Premiums Written</u>
2011	\$127,265,119	\$77,960,096	\$49,305,023	\$93,392,622	\$41,490,653
2010	109,742,633	59,976,816	49,765,817	71,894,889	31,176,188
2009	109,740,750	60,732,247	49,008,503	74,699,272	35,589,607
2008	101,986,490	52,749,038	49,237,452	79,910,110	38,103,946
2007	94,976,804	44,570,166	50,406,638	71,489,436	33,807,400

**REINSURANCE****Ceded Reinsurance**

The Company entered into a quota share reinsurance agreement with a sliding scale ceding commission with Coface S.A., effective December 31, 2003, which has been renewed each year. Under the quota share agreement, the Company cedes 50% of premiums written and received a provisional ceding commission of 47% during 2011. The Company recognized \$17,998,901 of ceding commission income from premiums ceded during 2011. The Company's deferred ceding commission liability was \$269,853 as of December 31, 2011. The Company recorded a contingent commission liability of \$6,774,811 as of December 31, 2011.

The Company also entered into a stop-loss reinsurance agreement with Coface S.A. The Company retains net ultimate losses up to a maximum limit of 60% of the net retained earned premium. The Company ceded \$5,142,028 of premium for the stop-loss agreement during 2011. In addition, the Company 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's premium for the 2011 excess of loss agreement was \$77,625.

The following table summarizes the effect of the ceded reinsurance on premiums written for 2011:

	<u>Premium Written</u>	<u>Unearned Premium</u>
Direct and Assumed	\$ 93,392,622	\$ 33,808,802
Ceded – Quota share	46,682,316	16,904,401
Ceded – Stop loss	5,142,028	0
Ceded – Excess of loss	77,625	0
Net	<u>\$ 41,490,653</u>	<u>\$ 16,904,401</u>

Assumed Reinsurance

The Company assumes a small amount of reinsurance from unaffiliated reinsurers which amounted to \$1,399,222 in assumed premium written for the year ended December 31, 2011.

**ACCOUNTS AND RECORDS**

The internal control structure was discussed with management through questionnaires, interviews and through a review of the work performed by the Company's Independent Certified Public Accountants. Testing of key underwriting and claim internal controls was performed. No material deficiencies were noted.

The NAIC provides a questionnaire covering the evaluation of the controls in the IT systems environment. The questionnaire was completed by the Company and reviewed by the Division to evaluate the adequacy of the IT controls. In addition to the questionnaire, interviews with Company staff were conducted to gather supplemental information and corroborate the Company's responses to the questionnaire. A review was also made of the documentation supporting Management and Organization Controls, Application Systems Development and Maintenance Controls, Operating and Processing Controls, Logical and Physical Security Controls, Contingency Planning Controls, Personal Computer, Local Area Network, Wide Area Network and Internet 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. No material exceptions were noted.

The books and records of the Company are audited annually by KPMG LLP, independent Certified Public Accountants, in accordance with 211 CMR 23.00.

**STATUTORY DEPOSITS**

The Company's statutory deposits as of December 31, 2011 are as follows:

Jurisdiction	Description of Deposit	Par Value	Statement Value	Market Value
Arizona	U.S Treasury Note 2.375% Due 2/28/15	\$125,000	\$123,714	\$132,627
Florida	U.S Treasury Note 1.125% Due 1/15/12	550,000	549,994	550,192
Florida	U.S Treasury Note 3.000% Due 2/28/17	550,000	543,385	608,267
Georgia	U.S Treasury Note 2.375% Due 2/28/15	50,000	49,486	53,051
Massachusetts	U.S Treasury Note 2.375% Due 2/28/15	2,000,000	1,979,429	2,122,040
Missouri	U.S Treasury Note 2.375% Due 2/28/15	350,000	346,400	371,357
Nevada	U.S Treasury Note 2.375% Due 2/28/15	225,000	222,686	238,730
New Hampshire	U.S Treasury Note 2.375% Due 2/28/15	500,000	494,857	530,510
New Mexico	U.S Treasury Note 2.375% Due 2/28/15	230,000	227,634	244,034
North Carolina	U.S Treasury Note 2.375% Due 2/28/15	300,000	296,914	318,306
Rhode Island	U.S Treasury Note 2.375% Due 2/28/15	500,000	494,857	530,510
South Dakota	U.S Treasury Note 2.375% Due 2/28/15	125,000	123,714	132,628
Tennessee	U.S Treasury Note 2.375% Due 2/28/15	150,000	156,238	159,153
Virginia	U.S Treasury Note 2.375% Due 2/28/15	225,000	222,686	238,730
Wyoming	U.S Treasury Note 2.375% Due 2/28/15	225,000	234,357	238,730
	Totals:	<u>\$6,105,000</u>	<u>\$6,066,351</u>	<u>\$6,468,865</u>

**FINANCIAL STATEMENTS**

The following financial statements are presented on the basis of accounting practices prescribed or permitted by the Division of Insurance and by the NAIC as of December 31, 2011:

Statement of Assets, Liabilities, Surplus and Other Funds as of December 31, 2011

Statement of Income for the Year Ended December 31, 2011

Statement of Capital and Surplus for the Year Ended December 31, 2011

Reconciliation of Capital and Surplus for Each Year in the Five-Year Period Ended December 31, 2011

For Informational Purposes Only

Coface North America Insurance Company  
Statement of Assets, Liabilities, Surplus and Other Funds  
As of December 31, 2011

Assets	As Reported by the Company	Examination Changes	Per Statutory Examination
Bonds	\$ 65,650,910	\$ 0	\$ 65,650,910
Cash	34,193,899		34,193,899
Subtotals, cash and invested assets	99,844,809	0	99,844,809
Investment income due and accrued	634,737		634,737
Premiums and considerations:			
Uncollected premiums and agents' balances in course of collection	20,121,589		20,121,589
Reinsurance:			
Amounts recoverable from reinsurers	2,524,049		2,524,049
Net deferred tax asset	2,996,583		2,996,583
Receivables from parent, subsidiaries and affiliates	1,143,352		1,143,352
Total Assets	<u>\$ 127,265,119</u>	<u>\$ 0</u>	<u>\$ 127,265,119</u>



Coface North America Insurance Company  
Statement of Assets, Liabilities, Surplus and Other Funds (continued)  
As of December 31, 2011

Liabilities	As Reported by the Company	Examination Changes	Per Statutory Examination	Notes
Losses	\$ 33,755,587	\$ 0	\$ 33,755,587	(1)
Loss adjustment expenses	1,450,461		1,450,461	(1)
Commissions payable, contingent commissions and other similar charges	11,739,954		11,739,954	
Other expenses	1,503,754		1,503,754	
Taxes, licenses and fees	279,732		279,732	
Current federal and foreign income taxes	113,148		113,148	
Unearned premiums	16,904,401		16,904,401	
Ceded reinsurance premiums payable	7,095,305		7,095,305	
Payable to parent, subsidiaries and affiliates	5,064,376		5,064,376	
Aggregate write-ins for liabilities	53,378		53,378	
Total Liabilities	<u>77,960,096</u>	<u>0</u>	<u>77,960,096</u>	
Common capital stock	2,600,000		2,600,000	
Gross paidin and contributed surplus	49,283,310		49,283,310	
Unassigned funds (surplus)	(2,578,287)		(2,578,287)	
Surplus as regards policyholders	<u>49,305,023</u>		<u>49,305,023</u>	
Total Liabilities, Surplus and Other Funds	<u>\$127,265,119</u>	<u>\$ 0</u>	<u>\$ 127,265,119</u>	

Coface North America Insurance Company  
Statement of Income  
For the Year Ended December 31, 2011

	As Reported by the Company	Examination Changes	Per Statutory Examination
Premiums earned	\$ 38,728,346	\$ 0	\$ 38,728,346
Deductions:			
Losses incurred	15,192,463		15,192,463
Loss adjustment expenses incurred	2,074,997		2,074,997
Other underwriting expenses incurred	22,063,933		22,063,933
Total underwriting deductions	39,331,393	0	39,331,393
Net underwriting gain (loss)	(603,047)	0	(603,047)
Net investment income earned	1,065,291		1,065,291
Net investment gain (loss)	1,065,291	0	1,065,291
Net income before dividends to policyholders, after capital gains tax and before all other federal and foreign income taxes	462,244	0	462,244
Federal and foreign income taxes incurred	607,957	0	607,957
Net income (loss)	\$ (145,713)	\$ 0	\$ (145,713)

Coface North America Insurance Company  
Statement of Capital and Surplus  
For the Year Ended December 31, 2011

	As Reported by the Company	Examination Changes	Per Statutory Examination
Surplus as regards policyholders, December 31 prior year	\$ 49,765,817	\$ 0	\$ 49,765,817
Net income (loss)	(145,713)		(145,713)
Change in net deferred income tax	1,075,279		1,075,279
Change in nonadmitted assets	(1,403,970)		(1,403,970)
Aggregate write-ins for gains and losses in surplus: Prior period adjustment	13,610		13,610
Change in surplus as regards policyholders for the year	(460,794)	0	(460,794)
Surplus as regards policyholders, December 31 current year	<u>\$ 49,305,023</u>	<u>\$ 0</u>	<u>\$ 49,305,023</u>

Coface North America Insurance Company  
Reconciliation of Capital and Surplus  
For Each Year in the Five-Year Period Ended December 31, 2011

	2011	2010	2009	2008	2007
Capital and surplus, December 31 prior year	\$ 49,765,817	\$ 49,008,503	\$ 49,237,452	\$ 50,406,638	\$ 23,474,018
Net income (loss)	(145,713)	(680,683)	(2,177,230)	(942,396)	4,112,392
Paid-in surplus	-	-	3,000,000	-	20,000,000
Change in net deferred income tax	1,075,279	(649,362)	161,879	(945,276)	(229,842)
Change in nonadmitted assets	(1,403,970)	2,087,359	(897,501)	718,486	3,050,070
Prior period adjustment	13,610		(316,097)		
Net change in capital and surplus for the year	(460,794)	757,314	(228,949)	(1,169,186)	26,932,620
Capital and surplus, December 31 current year	\$ 49,305,023	\$ 49,765,817	\$ 49,008,503	\$ 49,237,452	\$ 50,406,638

## COMMENTS ON FINANCIAL STATEMENT ITEMS

### Note 1 - Summary of Loss and Loss Adjustment Expense Reserves ("Loss and LAE Reserves")

The Division engaged Milliman, Inc. to review the reasonableness of the loss and LAE reserves of the Company as of December 31, 2011. 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.

Coface held net loss and LAE reserves of approximately \$35.2 million as of December 31, 2011. These reserves are net of anticipated salvage and subrogation and assumed and ceded reinsurance.

Milliman's actuarial review utilized accident year paid and incurred loss data at annual valuations through December 31, 2011. Milliman's actuarial central estimate of the net loss and LAE reserves is \$25.6 million. Milliman also calculated a range of estimates that it considered reasonable and acceptable. The overall reasonable range of estimates extends from \$23.0 million to \$37.5 million.

The results of Milliman's actuarial review indicated that the Company's recorded net loss and LAE reserves at December 31, 2011 fell within the range of reasonable estimates for all unpaid loss and LAE obligations of the Company under the terms of its policies and reinsurance agreements. Milliman determined that the estimates are reasonable.

The table below summarizes a comparison of Milliman's range of reasonable estimates for Loss and LAE Reserves to the Company's net carried Loss and LAE Reserves as of December 31, 2011. All amounts shown are in thousands (000's omitted):

	Low Point of Range	Selected Estimate	High Point of Range
Milliman Estimate	\$23,018	\$25,629	\$37,483
Company Carried	35,205	35,205	35,205
Company Carried Over / (Under) Milliman	12,187	9,576	(2,278)

## **SUMMARY OF RECOMMENDATIONS**


As noted in the Affiliated Companies section of this report, the Company did not file a required Form D for an intercompany cost allocation agreement that has been in place since 2008. In addition, the charges were not supported by a written agreement as required by the *NAIC Accounting Practices and Procedures Manual* ("APP Manual") SSAP 25, Paragraph 6. The related intercompany charges for years 2008-2011 were \$856,382, \$794,333, \$842,603 and \$1,106,131, respectively. In addition, the 2011 charges included a markup for profit margin to the parent of 5.6%. The lack of written agreement and Form D filing appear to be an oversight by management and internal control deficiency, rather than a means to obtain illegal dividends or advances from the Company. Accordingly, the Company shall complete the following required actions:

1. The Company's Internal audit department shall perform a semi-annual review of non-reinsurance related payments made by the Company to any affiliated entity and determine whether such payments are properly covered by a written intercompany agreement ("Internal Audit") during the twelve month period following the date of this report of examination ("First Year"). The Internal Audit findings ("Audit Findings") shall be reported to the Division concurrently with the filing of its second quarter and annual financial statement filings during the First Year. After the First Year, such Internal Audits shall be performed once a year and the Internal Audit Findings relating to such Internal Audits shall be reported to the Division concurrently with the first annual financial statement filing.
2. The Company's General Counsel shall certify that Audit Findings have been submitted to, and received by, the Board of Directors of the Company. The form of such certification shall be submitted to the Division for approval ("Certificate") and thereafter an executed Certificate shall be submitted with each Audit Finding filed with the Division.

**ACKNOWLEDGEMENT**

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  
Deputy Commissioner,  
Financial and Market Regulation  
Examiner-In-Charge  
Commonwealth of Massachusetts  
Division of Insurance