



**THE COMMONWEALTH OF MASSACHUSETTS**  
**OFFICE OF CONSUMER AFFAIRS AND BUSINESS**  
**REGULATION**

**DIVISION OF INSURANCE**

*REPORT OF EXAMINATION OF THE*  
**EMPLOYERS SECURITY ASSURANCE COMPANY**

**Burlington, Massachusetts**

**As of December 31, 2008**

**NAIC GROUP CODE 2498**

**NAIC COMPANY CODE 13083**

**EMPLOYERS ID NO. 26-1665309**

# EMPLOYERS SECURITY ASSURANCE COMPANY

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**COMMONWEALTH OF MASSACHUSETTS**  
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COMMISSIONER OF INSURANCE

April 26, 2010

The Honorable Alfred Gross, Chairman  
Financial Condition (E) Committee, NAIC  
Commissioner of Insurance  
Bureau of Insurance  
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The Honorable Paulette Thabault, Secretary  
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The Honorable Joseph G. Murphy  
Commissioner of Insurance  
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Honorable Commissioners:

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

**EMPLOYERS SECURITY ASSURANCE COMPANY**

at its home office located at 54 Third Avenue, Burlington, MA, 01803. The following report thereon is respectfully submitted.

## **SCOPE OF EXAMINATION**

Employers Security Assurance Company (hereinafter referred to as “Company” or “ESAC”) is being examined for the first time under the association plan of the *National Association of Insurance Commissioners* (“NAIC”) by the Massachusetts Division of Insurance (“Division”). The current association plan examination was conducted by the Division and covers the period from January 1, 2008 through December 31, 2008, including any material transactions and/or events occurring subsequent to the examination date and noted during the course of this examination.

Concurrent with this examination, the following insurance affiliates in the Associated Industries of Massachusetts Mutual Insurance Company (“A.I.M. Mutual”) group were also examined and separate Reports of Examination have been issued:

Associated Industries of Massachusetts Mutual Insurance Company  
Massachusetts Employers Insurance Company  
Employers Security Assurance Company

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 consistent with Massachusetts General Laws (“M.G.L.”). The principal focus of the examination was 2008 activity; however, transactions 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, 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 Ernst & Young LLP, an independent certified public accounting firm. The firm expressed an unqualified opinion on the Company’s financial statements for the calendar year 2008. A review and use of the Certified Public Accountants’ work papers was made to the extent deemed appropriate and effective. An independent certified public accounting and actuarial firm, KPMG LLP, was retained by the Division to evaluate the adequacy of the Company’s loss and loss adjustment expense reserves as of December 31, 2008. An evaluation of the adequacy and effectiveness of the Information Technology Systems’ controls was done to determine the level of reliance to be placed on summary information generated by the data processing systems.

## **HISTORY**

### **General**

On January 17, 2008, A.I.M. Mutual contributed \$3,000,000 in capital and surplus to form a wholly owned subsidiary, Employers Security Assurance Company. ESAC was issued a Certificate of Authority to write workers' compensation and employers' liability coverages in Massachusetts on January 17, 2008.

### **Capital Stock**

ESAC has authorized and issued 30,000 shares of \$20.00 par value common stock, all of which is owned by A.I.M. Mutual.

### **Dividends to Shareholders**

The Company has not declared or paid dividends to stockholders during the examination period.

### **Dividends to Policyholders**

During the examination period, the Company has not declared or paid dividends to policyholders.

### **Management**

#### *Annual Meeting*

In accordance with the by-laws, the annual meeting of the Company is held on the first Tuesday in May. Stockholders holding not less than a majority of the then issued and outstanding shares of the common stock shall constitute a quorum. The minutes indicated that a quorum was obtained at the annual meeting held during the examination period.

#### *Board of Directors*

The by-laws provide that the business and affairs of the Company shall be managed by the board of directors except as otherwise provided by the Articles of Incorporation or by a valid shareholder agreement. The board of directors shall consist of not less than three or more than twelve directors with the number of directors determined at each annual meeting coinciding with the expiration of one or more director's term. Each director holds office until the annual meeting of the stockholders in the years designated by the Incorporators of the Corporation. Upon expiration or resignation, his/her successor is elected at the next annual meeting.

## Employers Security Assurance Company

At December 31, 2008 the board was comprised of five directors, which is in compliance with the Company's by-laws. Directors duly elected and serving at December 31, 2008, with business affiliations, follow:

<u>Director</u>	<u>Business Affiliation</u>
John J. Gould, Chairman	Vice Chairman Associated Industries of Massachusetts
Robert R. Cella	Vice President Operations A.I.M. Mutual Insurance Company
Richard C. Lord	President and CEO Associated Industries of Massachusetts
John A. Myers	President and CEO A.I.M. Mutual Insurance Company
Gregory R. Shah	Vice President and Secretary/Treasurer A.I.M. Mutual Insurance Company

The by-laws do not specify the number of meetings of directors to be held during the year. The minutes of the board of directors indicate that a meeting was held during the examination period. The by-laws provide that at any meeting of the board a majority of the directors then in office shall constitute a quorum. The minutes indicate that a quorum was present at the meeting of the board of directors held during the examination period.

The board of directors appointed two committees in accordance with the by-laws. The members of each committee at December 31, 2008 follow:

### *Investment Committee*

Michael J. Riley, Chairman  
John J. Gould  
John A. Myers

### *Audit Committee*

Ralph P. Schlenker, Chairman  
John J. Gould  
Michael G. Faucher

## Employers Security Assurance Company

### *Officers*

The by-laws of the Company provide that the officers of the Company shall be a president, a secretary, a clerk, a treasurer, a Chairman of the board and other officers as deemed necessary. Pursuant to the by-laws, the officers of the Company are elected by the board of directors. Vacancies among the officers shall be filled by the board of directors.

The elected officers and their respective titles at December 31, 2008 follow:

<u>Name</u>	<u>Title</u>
John J. Gould	Chairman of the Board
John A. Myers	President and Chief Executive Officer
Gregory R. Shah	Vice President and Secretary/Treasurer
Robert R. Cella	Vice President Operations
Thomas J. Crupi	Vice President Loss Control
Michael P. Kelley	Vice President Claim

### Conflict of Interest Procedures

The Company has adopted a policy statement pertaining to conflicts of interest in accordance with Question 13 of the General 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, which conflicts or is likely to conflict with his or her official duties.

Annually, each officer and director completes a questionnaire disclosing any material conflicts of interest. The completed questionnaires were reviewed, and no discrepancies were noted in the responses to the General Interrogatories regarding conflicts of interest as reflected in the Company's 2008 Annual Statement.

### Corporate Records

#### *Articles of Incorporation and By-laws*

The by-laws and Articles of Incorporation thereto were read. There were no changes to the by-laws or Articles of Incorporation during the exam period.

#### *Disaster Recovery and Business Continuity*

The Company does provide 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.

## Employers Security Assurance Company

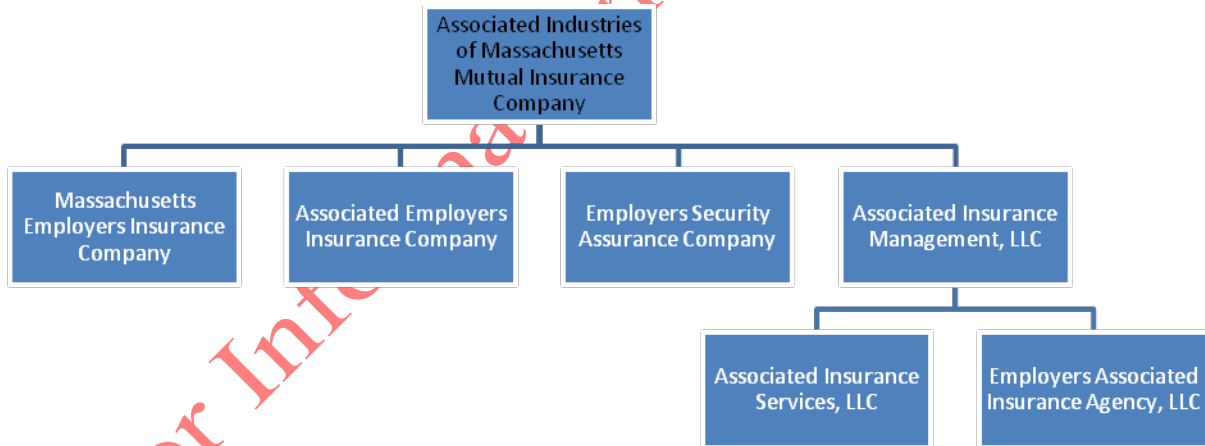
### *Board of Directors Minutes*

The minutes of the board of directors meetings for the period under statutory examination were read. The minutes indicated that the meeting was held in accordance with the Company's by-laws and the laws of the Commonwealth of Massachusetts.

### **AFFILIATED COMPANIES**

Per Form B, as filed with the Massachusetts Division of Insurance, the Company is a member of a holding company system and is subject to the registration requirements of M.G.L. c175, s206C of the Massachusetts General Laws. A.I.M. Mutual is the "ultimate controlling person".

### Organization Chart





## Employers Security Assurance Company

### Transactions and Agreements with Subsidiaries and Affiliates

#### *Management Agreement*

In 2008, ESAC entered into a management service agreement with Associated Insurance Management, LLC (“AIM, LLC”). Under the terms of the agreement AIM, LLC will provide all services necessary to run the business operations of ESAC. These services include but are not limited to underwriting, claims and accounting services. ESAC reimburses AIM, LLC 100% for the costs of running the business. In addition, if the board determines that there are excess funds available for distribution to its policyholders, then AIM, LLC shall be entitled to receive 5% of any distributions paid or credited to the policyholders.

ESAC also entered into a licensing agreement with Associated Industries of Massachusetts, Inc. (“AIM”) in 2008. Under the agreement, ESAC is permitted to use the Licensed Marks of AIM. These marks are “A.I.M.” and “Associated Industries of Massachusetts” and the A.I.M. logo. In return for the use of these marks, ESAC pays to AIM a royalty of 3% of Earned Premiums for each calendar year provided that the maximum annual royalty payable shall be equal to the amount, if any, by which \$1,200,000 exceeds the sum of the royalty payable by A.I.M. Mutual, AEIC and MEIC.

#### *Tax Sharing Agreement*

The Company participates in a tax allocation agreement with its parent, A.I.M. Mutual. The allocation method is based upon the respective tax liability of each member computed as if a separate return were filed, in accordance with the Internal Revenue Code.

### **FIDELITY BOND AND OTHER INSURANCE**

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

The Company has further protected its interests and property by purchasing policies of insurance covering other insurable risks. Coverage is provided by insurers licensed in the Commonwealth of Massachusetts and was in force as of December 31, 2008

### **INSURANCE PRODUCTS AND RELATED PRACTICES**

#### Territory and Plan of Operation

The Company is licensed to write workers’ compensation and employers’ liability insurance in Massachusetts only. The company writes business through brokers.

## Employers Security Assurance Company

### Treatment of Policyholders

#### *Policyholder Complaints*

During the course of the examination, a general review was made of the manner in which the Company conducts its business practices and fulfills its contractual obligations to policyholders and claimants. This review was limited in nature and was substantially narrower than a full scope market conduct examination.

During the claims test work, it was noted that the Company investigates and settles claims on a timely and fair basis. There were no complaints against the company for the exam period.

## REINSURANCE

### Pooling Agreement

ESAC participates in a pooling agreement with A.I.M. Mutual. The agreement became effective in 2008. Under the agreement, ESAC cedes 100% of its net retained business to A.I.M. Mutual. They do not assume any business from the pool.

### Assumed Reinsurance

ESAC's participation in the involuntary pool, Massachusetts Workers' Compensation Assigned Risk Pool, is included with A.I.M. Mutual.

### Ceded Business

ESAC cedes a small portion of its direct business to outside reinsurers. This is briefly summarized below.

#### Guy Carpenter Excess of Loss 2008

Layer	Reinsurance	Retention
First \$2,000,000	\$1,000,000	\$1,000,000
Next \$8,000,000	\$8,000,000	\$0
Next \$15,000,000	\$15,000,000	\$0

## SUBSEQUENT EVENTS

In January 2010, ESAC re-domesticated to the state of New Hampshire. The name was changed to New Hampshire Employers Insurance Company.

## **ACCOUNTS AND RECORDS**

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

The NAIC provides a questionnaire covering the evaluation of the controls in the Information Technology environment. The questionnaire was completed by the Company and reviewed by the Division to evaluate the adequacy of the Information Technology controls. No material deficiencies were noted.

The Company uses an automated general ledger system. Trial balances were traced from the general ledger and supporting documents to the 2008 annual statement. No material exceptions were noted.

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

## **FINANCIAL STATEMENTS**

The following financial statements are presented on the basis of accounting practices prescribed or permitted by the Division of Insurance of the Commonwealth of Massachusetts and by the *National Association of Insurance Commissioners* as of December 31, 2008:

Statement of Assets, Liabilities and Surplus and Other Funds as of December 31, 2008

Underwriting and Investment Exhibit of Income for the Year Ended December 31, 2008

Reconciliation of Capital and Surplus, For the Period Ended December 31, 2008

# Employers Security Assurance Company

## Statement of Assets, Liabilities and Other Funds as of December 31, 2008

Assets	Per Company	Examination Changes	Per Statutory Examination	Notes
Bonds	\$ 2,957,153	\$ 0	\$ 2,957,153	
Cash and short term investments	143,590		143,590	
Subtotal cash and invested assets	3,100,743	0	3,100,743	
Investment income due and accrued	26,381		26,381	
<b>TOTAL ASSETS</b>	<b>\$ 3,127,124</b>	<b>\$ 0</b>	<b>\$ 3,127,124</b>	
 Liabilities				
Other expenses	\$ 1,272	\$ 0	\$ 1,272	
Current federal and foreign income taxes	31,401		31,401	
Provision for reinsurance	(6,996)		(6,996)	
Amounts withheld for account of others	10,620		10,620	
Payable to parent, subsidiaries and affiliates	39,429		39,429	
Total liabilities	75,726	0	75,726	
Common capital stock	600,000		600,000	
Gross paid in and contributed surplus	2,400,000		2,400,000	
Unassigned funds	51,398		51,398	
Total surplus	3,051,398	0	3,051,398	
<b>TOTAL LIABILITIES AND SURPLUS</b>	<b>\$ 3,127,124</b>	<b>\$ 0</b>	<b>\$ 3,127,124</b>	

# Employers Security Assurance Company

## Underwriting and Investment Exhibit Statement of Income the Year Ended December 31, 2008

	Per Company	Examination Changes	Per Statutory Examination	Notes
Premiums earned	\$ 0	\$ 0	\$ 0	
Deductions				
Losses incurred	0		0	
Total underwriting deductions	0	0	0	
Net underwriting gain (loss)	0	0	0	
Net investment income earned	82,799		82,799	
Net investment gain (loss)	82,799	0	82,799	
Net income before dividends to policyholders	82,799	0	82,799	
Net income before federal taxes	82,799		82,799	
Federal and foreign taxes incurred	31,401		31,401	
Net Income	\$ 51,398	\$ 0	\$ 51,398	

# Employers Security Assurance Company

## Reconciliation of Capital and Surplus For the Year Ended December 31, 2008

	<u>2008</u>
Capital and Surplus, December 31, prior year	\$ 0
Net income	51,398
Capital changes:	
Paid in	600,000
Surplus adjustments:	
Paid in	<u>2,400,000</u>
Net change in capital and surplus for the year	<u>3,051,398</u>
Capital and Surplus, December 31, current year	<u><u>\$ 3,051,398</u></u>

**NOTES TO THE FINANCIAL STATEMENTS**

**Note 1: Loss and Loss Adjustment Expense Reserves**

The Division retained the services of KPMG LLP to provide an actuarial evaluation of the Loss and Loss Adjustment Expense reserves recorded by the company. The table below shows the findings resulting from their actuarial evaluation of the company on a gross of reinsurance basis.

**Loss & Loss Adjustment Expense Reserve as of December 31, 2008  
(000's omitted)**

<u>Low</u>	KPMG Indicated <u>Selected</u>	<u>High</u>	<u>Company Carried</u>
174	208	246	208

The reserves carried by the company agree with the selected amount determined by KPMG LLP. These reserves are ceded 100% to A.I.M. Mutual Insurance Company per the pooling agreement.

### ACKNOWLEDGEMENT

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

The assistance rendered by the following Massachusetts Division of Insurance examiners who participated in this examination is hereby acknowledged:

Linda Dow, Financial Examiner II  
Brian Knowlton, Financial Examiner II

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Raffaele J. Ciaramella, Jr., CFE  
Supervising Examiner  
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