



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

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April 5, 2010

The Honorable Alfred W. Gross
Chairman, NAIC Financial Condition (E) Committee
Commissioner
The Commonwealth of Virginia
Virginia State Corporation Commission
Bureau of Insurance
PO Box 1157
Richmond, Virginia 23218

The Honorable Paulette Thabault
Secretary, NAIC Northeastern Zone
Commissioner
The State of Vermont
Department of Banking,
Insurance, Securities & Health
Care Administration
Insurance Division
89 Main Street
Montpelier, Vermont 05620-3101

The Honorable Joseph G. Murphy
Commissioner of Insurance
The Commonwealth of Massachusetts
Division of Insurance
1000 Washington Street – Suite 810
Boston, Massachusetts 02118-6200

Honorable Commissioners:

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

SAFETY PROPERTY AND CASUALTY INSURANCE COMPANY

at its statutory home office located at 20 Custom House Street, Boston, Massachusetts 02110. The following report thereon respectfully is submitted.

SCOPE OF EXAMINATION

Period Covered By Examination

Safety Property and Casualty Insurance Company ("Company") has not been previously examined according to the Association Plan of the National Association of Insurance Commissioners ("NAIC") by the Massachusetts Division of Insurance ("Division"). The Division made the present examination by authority of Section 4, Chapter 175 of Massachusetts General Law, under the NAIC Association Plan. This examination covers the transactions of the Company from inception through December 31, 2008, with notation of significant events occurring through the date of this report.

This examination was conducted at the same time and in conjunction with the Division's statutory financial condition examination of the Company's parent Safety Insurance Company ("SIC") and related company Safety Indemnity Insurance Company ("SInd"). A separate market conduct examination is being performed on the Company, SIC and SInd by the Division.

Examination Procedure Employed

The examination was conducted in accordance with standards and procedures established by the NAIC Financial Condition (E) Committee and prescribed by the current NAIC Financial Condition Examiners Handbook.

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 is audited annually by an independent certified public accounting firm. The Company was audited by PricewaterhouseCoopers LLP ("PwC") for all of the years under examination. The firm expressed unqualified opinions on the Company's financial statements for the years ending December 31, 2006 through 2008. Review and use of PwC's workpapers were made to the extent deemed appropriate and effective.

The Division engaged the consulting actuarial advisory services of the Actuarial Advisory Services Unit of Ernst & Young LLP ("E&Y") to perform an actuarial review of the Company's loss and loss adjustment expense reserves.

Safety Property and Casualty Insurance Company

The Division's information systems auditor evaluated the adequacy and effectiveness of the Company's information systems controls to determine the level of reliance to be placed on summary information generated by the data processing systems.

This Report of Examination is written on an exception basis. Explanations of and details pertaining to various phases of the examination will be found herein. Unless it is specifically noted otherwise, all references to the accounts, activities, and transactions of the Company are as of December 31, 2008.

HISTORY

General

The Company was organized and incorporated on December 5, 2006, under the laws of the Commonwealth of Massachusetts, as a stock company titled "Safety Property and Casualty Insurance Company"; it commenced business on January 1, 2007. As a subsidiary of Safety Insurance Company ("SIC"), the Company is part of the Safety Insurance Group ("Group"). Effective September 2007, the Company began writing ultra preferred homeowners business for the Group.

At December 31, 2008, the Company is a corporation in the stock form of organization that operates as a property and casualty insurance company. It has been licensed in Massachusetts since its inception and in New Hampshire since 2007.

Capital Stock

In 2006, SIC purchased 175,000 no par value shares of the Company for a price of \$1.75 million and at the same time, made a capital contribution of \$7.3 million to its newly formed subsidiary. At December 31, 2008, the authorized and outstanding capital stock of the Company consisted of 175,000 shares of no par value common stock. All of the outstanding stock is held by SIC. Safety Insurance Group, Inc. ("SIG"), a Delaware corporation publically traded on the NASDAQ Global Select Market under the symbol "SAFT," owns all of the outstanding stock of SIC.

Dividends To Stockholders

In the examination period, the Company paid no stockholder dividends to its sole shareholder.

Growth Of The Company

The growth of the Company throughout the examination period is indicated in the following schedule which was prepared from information in the Company's Annual Statements:

| DEC. 31, | ADMITTED ASSETS | LIABILITIES | CAPITAL AND SURPLUS | PREMIUMS EARNED | LOSSES AND LAE INCURRED | NET INCOME |
|-------------|--------------------|--------------|---------------------------|--------------------|-------------------------------|---------------|
| 2008 | \$34,085,195 | \$21,422,658 | \$12,662,537 | \$17,296,675 | \$11,094,684 | \$1,824,618 |
| 2007 | 33,236,648 | 22,298,191 | 10,938,457 | 18,276,211 | 11,234,783 | 1,128,844 |
| 2006 | 9,170,084 | 115,627 | 9,054,457 | 0 | 0 | 4,898 |

MANAGEMENT

Meetings of Stockholders

According to the Company's By-laws, the annual meeting of stockholders shall be held on the third Wednesday in April of each year. At any meeting of the stockholders, the holders of a majority in interest of all stock issued, outstanding, and entitled to vote at a meeting shall constitute a quorum. Each stockholder shall have one vote for each share of stock entitled to vote owned by such stockholder of record. A stockholder may vote either in person or by written proxy. Minutes document that a quorum was obtained at each annual meeting held during the examination period.

Special meetings of stockholders may be called by the President or by the Board of Directors, and shall be called by the Secretary upon written application of one or more stockholders who hold shares representing at least ten per cent of the capital stock entitled to vote at such meeting. A written notice of each meeting of stockholders shall be given at least seven days before the meeting and shall state the place, date, time, and purposes of the meeting.

Board of Directors

According to the Company's By-laws, the business of the Company shall be managed under the direction of the Board of Directors, who shall have and may exercise all of the powers of the Company except such as are reserved to the stockholders by law, by the Company's Articles of Organization, or by the By-laws. Directors shall be elected by a plurality of the votes cast at annual meetings of stockholders and each Director so elected shall hold office until the next annual meeting and until a successor is duly elected and qualified, or until his earlier resignation or removal. Any Director may resign at any time upon notice to the Company. Directors need not be stockholders. The By-laws, however, do not specify rules or procedures for the election of a Chairman of the Board.

Safety Property and Casualty Insurance Company

At December 31, 2008, the Company's Board of Directors was composed of five persons, which is in compliance with the Company's By-laws and the General Laws of Massachusetts. The members of the Board, with their business or professional affiliations and their residential addresses, are as follows:

| <u>Name of Director:</u> | <u>Business Affiliation:</u> | <u>Residence:</u> |
|----------------------------|---|----------------------------|
| David Francis Brussard | President and Chief | Boston, |
| William Joseph Begley, Jr. | Vice President, Treasurer, and | Norwell, |
| Daniel D. Loranger | Vice President, MIS | Boxford, Massachusetts |
| Edward Norman Patrick, Jr. | Vice President, Underwriting Clerk and Secretary | Westwood, Massachusetts |
| David E. Krupa | Vice President, Claims | Raynham, Massachusetts |

The business affiliations listed above are positions held with the Company unless otherwise noted. Directors of the Company also serve simultaneously in similar capacities as Directors and Officers of SIC and Safety Indemnity Insurance Company ("SInd").

The By-laws do not specify the number of meetings of the Board of Directors to be held during a year. Regular meetings of the Board of Directors may be held at such places and times as the Directors may from time to time determine; a regular meeting of the Board of Directors shall be held without notice immediately after and at the same place as the annual meeting of stockholders. Special meetings of the Board of Directors may be held at any time and place when called by the President, the Treasurer, or one or more Directors. At any meeting of the Board of Directors, a majority of the Directors then in office shall constitute a quorum for the transaction of business. The minutes indicated that a quorum was obtained for all meetings of the Board of Directors held during the examination period.

Committees of the Board of Directors

According to the Company's By-laws, the Board of Directors may, by the affirmative vote of a majority of the Directors then in office, appoint an executive committee or other committees consisting of one or more Directors and may by vote delegate to any such committee some or all of its powers except those which by law, the Articles of Organization, or the By-laws, it may not delegate. The Board of Directors shall have power at any time to fill vacancies in, change the membership of, or discharge any such committee. The Board of Directors shall have the power to rescind any action of any committee, but no such rescission shall have retroactive effect.

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The Company has an Investment Committee composed of Directors David F. Brussard and William J. Begley, Jr., and A. Richard Caputo, Jr., a member of the Board of Directors of SIG. Minutes of the Investment Committee documented regular meetings of these Investment Committee members with representatives of the Company's investment advisor/manager, Deutsche Asset Management ("Deutsche").

The Company does not have a formal audit committee. This function is addressed by the Audit Committee of its ultimate parent company, SIG.

The Company has an Executive Committee composed of senior management which meets weekly to address various aspects of the day-to-day operations of the Company. Additionally, according to the Chief Financial Officer of the Company, functional committees and staff make formal presentations to the Executive Committee at regular intervals on specific topics or various aspects of the Company's business. Minutes of such meetings are not formally maintained.

Officers

According to the Company's By-laws, the officers of the Company shall consist of a President, a Treasurer, a Secretary, and such other officers and agents, with duties and powers, as the Board of Directors may in its discretion determine. The President, the Treasurer, and the Secretary shall be elected annually by the Directors at their first meeting following the annual meeting of stockholders; other officers may be chosen by the Directors at such meeting or at any other meeting. The term of office for each officer shall be one year or until respective successors are elected and qualified or until earlier resignation or removal.

An officer may but need not be a director or stockholder and no officer shall be a Director solely by virtue of being an officer.

The By-laws state that the President shall be the Chief Executive Officer of the Company. Except as otherwise voted by the Board of Directors, the President shall preside at all meetings of the stockholders and of the Board of Directors at which he is present. The President shall have such duties and powers as are commonly incident to the office and such duties and powers as the Board of Directors shall from time to time designate. In addition to what is defined explicitly in the By-laws, the Company's officers shall have such powers and duties as generally pertain to their respective offices, as well as such powers and duties as from time to time may be conferred by the Board of Directors. Except as otherwise required or prohibited by law, any two or more offices may be held by the same person.

The minutes of the Board of Directors document that the Officers of the Company are elected each year. The Officers of the Company at December 31, 2008, were as follows:

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| <u>Name of Officer:</u> | <u>Title:</u> |
|----------------------------|---|
| David Francis Brussard | President, Chief Executive Officer, and Director |
| William Joseph Begley, Jr. | Vice President, Treasurer, Chief Financial Officer, and Director |
| James D. Berry | Vice President – Insurance Operations |
| George M. Murphy | Vice President – Marketing |
| Janet Kelleher Catino | Assistant Vice President and Controller |
| Robert John Kerton | Vice President - Claims |
| David Ernest Krupa | Vice President - Claims and Director |
| Daniel David Loranger | Vice President - Management Information Systems and Chief Information Officer and Director |
| Edward Norman Patrick, Jr. | Vice President – Underwriting, Clerk, Secretary, and Director |

The Company's Officers listed above simultaneously held similar positions in SIC and SInd.

Conflict Of Interest Procedure

The Company has a written Code of Business Conduct and Ethics with an established procedure for disclosure to the Board of Directors of any material interest or affiliation of any Officer or Director which is likely to conflict with his or her official duties. Annually, each Director of the Company completes and signs a questionnaire disclosing any material conflicts of interest. Since SIG became a publicly traded entity, extensive disclosure filings are made annually by its Directors, many of whom share common directorships with other entities in the Group. No exceptions were noted in the examination's review of the forms supporting the Company's responses to the General Interrogatories in its Annual Statements.

Corporate Records

The By-laws and the Articles of Organization of the Company were read.

Although the Company has disaster recovery and business continuity plans, its By-laws do not contain explicit provisions for the continuity of operations in the event of a national emergency; hence, under such circumstances, the succession of officers will be as prescribed in Sections 180M through 180Q of MGL Chapter 175.

Minutes of the meetings of the Board of Directors held throughout the examination period were reviewed. Votes and authorizations over the examination period were found to be in order and the records indicated that the Company appeared to be conducting its affairs in compliance with its By-laws and the Laws of the Commonwealth of Massachusetts.

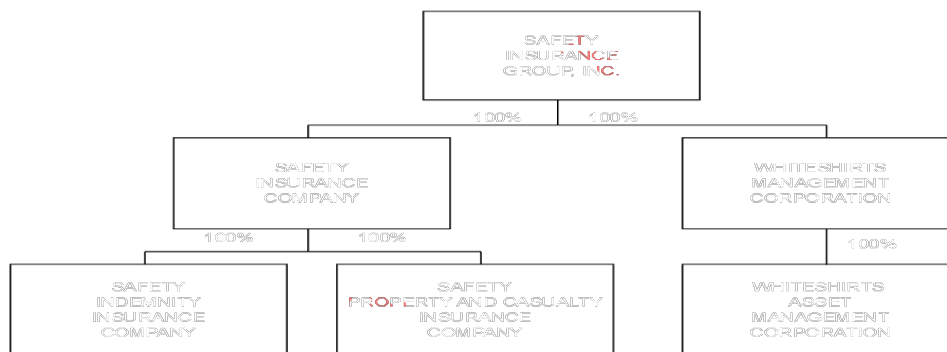
AFFILIATED COMPANIES

Holding Company Filings

The Company is a member of an insurance holding company system as defined in Section 206 of MGL Chapter 175 and is subject to the registration requirements thereof. During the examination period, the Company filed Form B with the Division pursuant to Regulation 211 CMR 7.00 and Section 206C of MGL Chapter 175. Ultimate control of the holding company system is held by the owners of SIG, a Delaware corporation, the sole business of which is ownership of the group.

Chart Of Organization

The ownership interests and hierarchy of companies in this corporate organization at December 31, 2008, are represented as follows:



Acquisitions, Mergers Or Sales

In the examination period, there occurred some significant transactions involving the Company in acquisitions, mergers, disposals, dissolutions, and purchases or sales through reinsurance, key of which are summarized as follows:

- ◆ The Company was organized and incorporated on December 5, 2006, as a stock company under the laws of the Commonwealth of Massachusetts. In December of 2006, the SIC purchased 175,000 no par value shares of the Company for a price of \$1.75 million and at the same time, made a capital contribution of \$7.3 million.
- ◆ Effective January 1, 2007, the Company and SIC entered into an Administrative Service Agreement, pursuant to which the Company receives certain administrative and managerial services from SIC, as compensation for which the Company pays the actual

costs and expenses incurred by SIC for providing such services. This agreement remains in effect to date.

- ◆ Effective on January 1, 2007, an existing pooling agreement between SIC and SInd was amended to include the Company. As amended, the agreement applies the pool participation percentages of 90% for SIC, 7% for SInd, and 3% for the Company to the net liabilities of the pooled companies (that is, reserves for unearned premiums, losses, and loss adjustment expenses, net of salvage and subrogation and third party reinsurance cessions). Prior to January 1, 2007, the pool participation percentages were 95% for SIC, 5% for SInd, and 0% for SPC. Assets equaling the net change in liabilities as a result of the changes to the pool participation percentages were transferred between companies as of the effective date of the amendment. This agreement remains in effect to date.

Summary Of Cost-Sharing Agreements

The two predominant cost-sharing agreements involving the Company are a management services agreement and an inter-company reinsurance pooling agreement. Both are described briefly among the following summaries:

- ◆ The Company and SIC entered into an Administrative Service Agreement effective on January 1, 2007, pursuant to which the Company receives certain administrative and managerial services from SIC, for which as compensation SPC pays the actual costs and expenses incurred by SIC for providing such services. This agreement remains in effect to date.
- ◆ Effective on January 1, 2007, an existing pooling agreement between SIC and SInd was amended to include the Company. As amended, the agreement applies the pool participation percentages of 90% for SIC, 7% for SInd, and 3% for the Company to the net liabilities of the pooled companies (that is, reserves for unearned premiums, losses, and loss adjustment expenses, net of salvage and subrogation and third party reinsurance cessions). Prior to 1/1/2007, the pool participation percentages were 95% for SIC, 5% for SInd, and 0% for the Company. Assets equaling the net change in liabilities as a result of the changes to the pool participation percentages were transferred between companies as of the effective date of the amendment. This agreement remains in effect to date.
- ◆ The Company has a written tax allocation agreement. The Company files its Federal Income Tax Return on a consolidated basis with SIG and all of SIG's subsidiaries. The consolidated tax liability of SIG and subsidiaries is allocated on the basis of each corporation's proportionate contributions to consolidated taxable income. Any corporation which incurs a loss receives a credit in recognition of the benefit that the loss brings to other corporations through the filing of a consolidated return. The Company had no net losses carried forward as of December 31, 2008.

FIDELITY BONDS AND OTHER INSURANCE

The By-laws of the Company specify that the Secretary, the Treasurer, and each Assistant Secretary and each Assistant Treasurer shall give bond for the faithful performance of his duties to the Company in such amount as the Directors shall prescribe, which amount shall be at least \$10,000 for the Secretary and the Treasurer, and \$1,000 for each Assistant Secretary and each Assistant Treasurer. Any other officer may be required by the Directors to give bond for the faithful performance of his duties to the Company in such amount and with such sureties as the Directors may determine. For its key executive officers, the Company maintains a fidelity bond with an authorized Massachusetts insurer, consistent with its By-laws and Section 60 of MGL Chapter 175.

The Company is specified among the named insureds on a financial institutions bond with a policy limit of \$10.0 million which provides coverage to SIG and subsidiaries; this specifically provides dishonesty coverage. The aggregate limit of liability exceeds the NAIC suggested minimum. The Company and its affiliates have further protected their interests and property by other policies of insurance covering various insurable risks. Coverage is provided by insurers licensed in Massachusetts and was in force as of December 31, 2008.

PENSION AND INSURANCE PLANS

The Company has no retirement, deferred compensation, or other post-retirement benefit plans. The Company itself did not have employees as all personnel were provided to the Company by SIC under a management services agreement. Health, life, retirement, and stock ownership benefits were provided to those employees through SIC.

STATUTORY DEPOSITS

In Massachusetts no statutory deposit is required of this domestic company as of December 31, 2008. The state of New Hampshire holds a statutory deposit of the Company in the form of a U.S. Treasury Note with par value of \$500,000 at 4.625% which matures on July 31, 2012. At December 31, 2008, this security had a statement value of \$505,433 and a fair value of \$525,000.

INSURANCE PRODUCTS AND RELATED PRACTICES

Territory and Plan of Operation

A review of the Certificate of Authority indicated that the Company is a corporation duly organized under the laws of the Commonwealth of Massachusetts. The Company is authorized to write the following lines of insurance coverages: fire, ocean and inland marine, boiler, accident – all kinds, liability and automobile liability, glass, water damage and sprinkler leakage, elevator property damage and collision, burglary, robbery, theft, repair –

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replacement, reinsurance (except life), comprehensive motor vehicle and aircraft, personal property floater, and certain other extensions of coverage. The Company has limited its writings primarily to homeowners insurance. The vast majority of Company business is on a direct billing basis and the Company uses a lock-box collection system for premiums.

The Company writes the Group's ultra preferred homeowners business.

TREATMENT OF POLICYHOLDERS – MARKET CONDUCT

During the financial examination of the Company, the Division's Market Conduct Department initiated a comprehensive market conduct examination of the Company for the period January 1, 2007, through December 31, 2007. The market conduct examination was called pursuant to authority in M.G.L. c.175 s.4.

The market conduct examination is being conducted at the direction of, and under the overall management and control of, the market conduct examination staff of the Division. Representatives from the firm of Eide Bailly were engaged to complete certain agreed upon procedures which were developed using the guidance and standards of the NAIC Market Regulation Handbook, the market conduct examination standards of the Division, and the Commonwealth of Massachusetts insurance laws, regulations and bulletins.

The basic business areas that are being reviewed under this market conduct examination are Company Operations/Management; Complaint Handling; Marketing and Sales; Producer Licensing; Policyholder Services; Underwriting and Rating; Claims, in addition to an assessment of the Company's internal control environment. Once this market conduct examination is completed a Report on the Comprehensive Market Conduct Examination of the Company for the period January 1, 2007, through December 31, 2007 will be issued and become available as a public document.

REINSURANCE

The Company does not assume reinsurance from non-affiliated companies; its reinsurance is limited to an inter-company pooling arrangement.

Inter-Company Pooling Agreement and Reinsurance Ceded to Affiliates:

Effective on January 1, 2007, an existing pooling agreement between SIC and SInd was amended to include the Company. As amended, the agreement applies the pool participation percentages of 90% for SIC, 7% for SInd, and 3% for the Company to the net liabilities of the pooled companies (that is, reserves for unearned premiums, losses, and loss adjustment expenses, net of salvage and subrogation and third party reinsurance cessions). Assets equaling the net change in liabilities as a result of the changes to the pool participation percentages were transferred between companies as of the effective date of the amendment. This agreement remains in effect to date.

ACCOUNTS AND RECORDS

The Company's accounting and record-keeping are extensively automated. The Company maintains its records, ledgers, and accounts on a computerized accounting system. Trial balances were traced from the general ledger and supporting documents to annual statements. No material exceptions were noted.

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 the year ended December 31, 2008, the Company was audited by PwC.

The Company's claims inventory was tested on a sample basis for completeness and accuracy. No material errors or exceptions were detected.

The NAIC Evaluation of Controls in Information Systems Questionnaire was completed by the Company. The Division's IT Auditor reviewed the Company's management responses to the NAIC IS Questionnaire and interviewed key management personnel in the Company's Information Technology Department. In addition to such interviews, various internal audit reports and audit workpapers of PwC were reviewed. The Company has internal control procedures in place to protect its data processing and information, and it has comprehensive disaster recovery and business continuity plans in place.

The internal control structure was discussed with management through questionnaires and through a review of the workpapers of the Company's independent certified public accounting firm. PwC's workpapers on the Company's compliance with the Sarbanes-Oxley Act of 2002 were reviewed for findings, conclusions, and recommendations on all financially significant system environment controls (design, installation, and maintenance) for those facilities that support the equipment controlling the environmental conditions for IT as well as communication facilities.

FINANCIAL STATEMENTS

The following pages present a Statement of Assets, Liabilities, Surplus and Other Funds as determined by this examination, showing the financial condition of the Company as of December 31, 2008. The statement is followed by supporting statements and reconciliations presented in the following order:

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

Statement of Income For the Year Ended December 31, 2008

Capital and Surplus Account As of December 31, 2008

Reconciliation of Capital and Surplus For Each Years in the Three Year Period Ended December 31, 2008

Safety Property and Casualty Insurance Company

Safety Property and Casualty Insurance Company Statement of Assets, Liabilities, Surplus and Other Funds December 31, 2008

| | As Reported by Company | Examination Changes | Per Statutory Examination | Notes |
|--|---------------------------|------------------------|------------------------------|-------|
| <u>Assets</u> | | | | |
| Bonds | \$ 27,651,467 | \$ - | \$ 27,651,467 | |
| Cash | 4,097,650 | | 4,097,650 | |
| Cash and invested assets | 31,749,117 | - | 31,749,117 | |
| Investment income due and accrued | 227,374 | | 227,374 | |
| Uncollected premiums | 56,844 | | 56,844 | |
| Deferred premiums | 1,349,165 | (1,124,063) | 225,102 | 2 |
| Net deferred tax asset | 702,695 | | 702,695 | |
| Receivables from parent, subsidiaries and affiliates | | 1,124,063 | 1,124,063 | 2 |
| Total assets | \$ 34,085,195 | \$ - | \$ 34,085,195 | |
| <u>Liabilities, Surplus and Other Funds</u> | | | | |
| <u>Liabilities</u> | | | | |
| Losses | \$ 10,165,964 | | \$ 10,165,964 | 1 |
| Loss adjustment expenses | 1,566,122 | | 1,566,122 | 1 |
| Commissions payable | 366,604 | | 366,604 | |
| Taxes, licenses and fees | 1,412 | | 1,412 | |
| Unearned premiums | 8,042,253 | | 8,042,253 | |
| Advance premium | 10,693 | | 10,693 | |
| Ceded reinsurance premiums payable | 652,337 | | 652,337 | |
| Equities and deposits in pools and associations | 617,273 | | 617,273 | |
| | 21,422,658 | - | 21,422,658 | |
| <u>Surplus and Other Funds</u> | | | | |
| Common capital stock | 1,750,000 | | 1,750,000 | |
| Gross paid in and contributed surplus | 7,300,000 | | 7,300,000 | |
| Unassigned funds (surplus) | 3,612,537 | | 3,612,537 | |
| Surplus as regards policyholders | 12,662,537 | - | 12,662,537 | |
| Total liabilities, surplus and other funds | \$ 34,085,195 | \$ - | \$ 34,085,195 | |

Safety Property and Casualty Insurance Company

Safety Property and Casualty Insurance Company

Statement of Income

For the Year Ended December 31, 2008

| | As Reported by Company | Examination Changes | Per Statutory Examination | Notes |
|---|---------------------------|------------------------|------------------------------|-------|
| Premiums earned | \$ 17,296,675 | \$ - | \$ 17,296,675 | |
| Deductions: | | | | |
| Losses incurred | 9,537,526 | | 9,537,526 | |
| Loss adjustment expenses incurred | 1,557,158 | | 1,557,158 | |
| Other underwriting expenses incurred | 5,088,212 | | 5,088,212 | |
| Total underwriting deductions | 16,182,896 | - | 16,182,896 | |
| Net underwriting gain (loss) | 1,113,779 | - | 1,113,779 | |
| Net investment income earned | 1,563,706 | | 1,563,706 | |
| Net realized gains (losses), net of capital gains tax | (33,382) | | (33,382) | |
| Net investment gain (loss) | 1,530,324 | - | 1,530,324 | |
| Finance and service charges not included in premiums | 7,345 | | 7,345 | |
| Total other income | 7,345 | - | 7,345 | |
| Net income before dividends to policyholders and before federal and foreign income taxes | 2,651,448 | - | 2,651,448 | |
| Dividend to policyholders | - | | - | |
| Net income after dividends to policyholders but before federal and foreign income taxes | 2,651,448 | - | 2,651,448 | |
| Federal and foreign income taxes | 826,830 | | 826,830 | |
| Net income | \$ 1,824,618 | \$ - | \$ 1,824,618 | |

Safety Property and Casualty Insurance Company

Safety Property and Casualty Insurance Company Statement of Capital and Surplus For the Year Ended December 31, 2008

| | As Reported by Company | Examination Changes | Per Statutory Examination | Notes |
|---|---------------------------|------------------------|------------------------------|-------|
| Surplus as regards policyholders, December 31, 2007 | \$ 10,938,457 | \$ - | \$ 10,938,457 | |
| Net income | 1,824,618 | - | 1,824,618 | |
| Net change in unrealized capital gains or (losses) | (31,537) | | (31,537) | |
| Change in net deferred income tax | (94,364) | | (94,364) | |
| Change in nonadmitted assets | 25,363 | | 25,363 | |
| Change in surplus as regards policyholders for the year | 1,724,080 | - | 1,724,080 | |
| Surplus as regards policyholders, December 31, 2008 | \$ 12,662,537 | \$ - | \$ 12,662,537 | |

For Information Purposes Only

Safety Property and Casualty Insurance Company

Safety Property and Casualty Insurance Company Reconciliation of Capital and Surplus For Each Year in the Three Year Period Ended December 31, 2008

| | <u>2008 *</u> | <u>2007</u> | <u>2006</u> |
|--|----------------------|----------------------|---------------------|
| Balance, beginning of period | \$ 10,938,457 | \$ 9,054,457 | \$ - |
| Net income (loss) | 1,824,618 | 1,128,844 | 4,898 |
| Net change in unrealized capital gains or (losses) | (31,537) | | |
| Change in net deferred income tax | (94,364) | 894,382 | (441) |
| Change in nonadmitted assets | 25,363 | (139,226) | |
| Capital change: Paid in | | | 1,750,000 |
| Surplus change: Paid in | | | 7,300,000 |
| Balance, end of period | <u>\$ 12,662,537</u> | <u>\$ 10,938,457</u> | <u>\$ 9,054,457</u> |

* Per Statutory Examination

NOTES TO FINANCIAL STATEMENTS

Note 1:

| | |
|---------------------------------|----------------------|
| Losses | \$ 10,165,964 |
| Loss Adjustment Expenses | \$ 1,566,122 |

The Company's Board of Directors appointed an actuary from the Actuarial Consulting Services Unit of PwC, the Company's independent certified public accounting firm, to render a Statement of Actuarial Opinion as of December 31, 2008, on the Company's loss and loss adjustment expense (LAE) reserves. Among the items in the Opinion for the Company and in the similar Opinion for SIC and for SInd, the appointed actuary specifically listed the following amounts for each respective insurer separately; they are shown herein on a combined basis for ease of general reference:

| | SIC | SInd | Company | Combined |
|---|---------------|--------------|--------------|---------------|
| Reserve for Unpaid Losses | \$304,978,929 | \$23,720,583 | \$10,165,964 | \$338,865,476 |
| Reserve for Unpaid Loss Adjustment Expenses | 46,983,624 | 3,654,283 | 1,566,122 | 52,204,029 |
| Aggregate Total – Net Basis | \$351,962,553 | \$27,374,866 | \$11,732,086 | \$391,069,505 |
| Reserve for Unpaid Losses | \$367,218,000 | \$28,562,000 | \$12,240,000 | \$408,020,000 |
| Reserve for Unpaid Loss Adjustment Expenses | 53,585,000 | 4,168,000 | 1,786,000 | 59,539,000 |
| Aggregate Total – Direct and Assumed | \$420,803,000 | \$32,730,000 | \$14,026,000 | \$467,559,000 |

After reviewing the above reserves and other items, the Company's appointed actuary concluded that, in his opinion, the amounts identified above:

1. meet the requirements of the insurance law of Massachusetts;
2. were computed in accordance with accepted loss reserving standards and principles; and
3. make a reasonable provision for all unpaid loss and loss adjustment expense obligations of the Company under the terms of its policies and agreements.

As part of the examination, the Division engaged the consulting actuarial advisory services of Ernst & Young, LLP, an independent firm. The consulting actuaries for the Division prepared independent estimates for the Company's loss and LAE liabilities as of December 31, 2008, using data evaluated as of March 31, 2009, (the Company's appointed actuary relied on data evaluated as of December 31, 2008,). The consulting actuaries also updated their independent estimates for the Company's loss and LAE liabilities as of December 31, 2008, based on actual versus expected loss emergence analysis results using data as of December 31, 2009.

The consulting actuaries summarized the results of their analysis of the loss and LAE liabilities in the following table:

Safety Property and Casualty Insurance Company

| | | Carried | | Indicated by Ernst & Young | | |
|------------------------------|-------|----------------|--|----------------------------|----------------|-------------|
| | | <u>Reserve</u> | | <u>Low</u> | <u>Central</u> | <u>High</u> |
| | | | | | | |
| Safety Insurance Company | Gross | \$420,802 | | \$324,295 | \$352,947 | \$383,851 |
| With 90% of Pooled Business | Net | 351,953 | | 261,628 | 284,109 | 308,841 |
| | | | | | | |
| Safety Indemnity Ins Company | Gross | 32,729 | | 25,223 | 27,451 | 29,855 |
| With 7% of Pooled Business | Net | 27,375 | | 20,349 | 22,097 | 24,021 |
| | | | | | | |
| Safety P&C Insurance Company | Gross | 14,027 | | 10,810 | 11,765 | 12,795 |
| With 3% of Pooled Business | Net | 11,732 | | 8,721 | 9,470 | 10,295 |
| | | | | | | |
| Group Combined | Gross | \$467,558 | | \$360,328 | \$392,163 | \$426,501 |
| | Net | 391,070 | | 290,698 | 315,676 | 343,157 |

In conclusion, the consulting actuaries noted that the indicated net Loss and LAE liability range for the combined group is \$290.7 million to \$343.2 million. The net carried reserve at December 31, 2008, exceeds the “High” end of the consulting actuaries estimated liability range by \$47.9 million and the “Central” estimate by \$74.4 million on a group combined basis. They also observed that the Group has consistently reported favorable loss and LAE development in each of the past four years and during the year of 2009 reported favorable development of approximately \$40 million on year-end 2008 loss and LAE reserves.

Had the reserves been booked at the “High” end of the consulting actuaries’ range, the Loss and LAE reserve in the accompanying financial statements would have been \$1.4 million lower, the incurred losses would have been \$1.4 million lower and, assuming a 35.0% tax rate, Surplus would have increased by approximately \$0.9 million.

Note 2:

Receivable from parent, subsidiaries and affiliates

\$ 1,124,063

During the course of the examination, it was noted that cash belonging to Safety Property and Casualty Insurance Company was inadvertently deposited to an account owned by Safety Insurance Company. This error was corrected in January of 2009.

ACKNOWLEDGEMENT

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

The assistance rendered by the following Division examiner who participated in this examination is hereby acknowledged:

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