

Report of Examination of

**James River Insurance Company**  
Columbus, Ohio

As of December 31, 2009

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Columbus, Ohio  
August 6, 2010

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Commissioner  
Chairman, Financial Condition (E) Committee  
National Association of Insurance Commissioners  
Division of Insurance  
State of Virginia  
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Honorable Paulette Thabault  
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Helena, Montana 59601

Honorable Mary Jo Hudson  
Director  
Ohio Department of Insurance  
50 West Town Street  
3<sup>rd</sup> Floor – Suite 300  
Columbus, Ohio 43215

Dear Madams and Sirs:

In accordance with Section 3901.07 of the Ohio Revised Code "ORC", the Ohio Department of Insurance ("Department") conducted an examination of

**James River Insurance Company**

an Ohio domiciled, stock, property and casualty insurance company, hereinafter referred to as the "Company." The examination was conducted at the Company's home office, located at 6641 West Broad Street, Suite 300, Richmond, Virginia.

**Scope of Examination**

The Department last examined the Company as of December 31, 2004. The current examination covers the period of January 1, 2005 through December 31, 2009.

The Department conducted the examination in accordance with the National Association of Insurance Commissioners ("NAIC") Financial Condition Examiners Handbook. The Handbook requires that the Department plan and perform the examination to evaluate the Company's financial condition and identify prospective risks including corporate governance, identify and assess inherent risks and evaluate 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.

For each year during the period under examination, the certified public accounting firm of Ernst & Young LLP ("E&Y") provided an unqualified opinion based on statutory accounting principles. Relevant work performed by E&Y during its annual audit of the Company was reviewed during the examination and incorporated into the examination work papers.

## Management and Control

### Board of Directors

Management of the Company is vested in its Board of Directors, which was comprised of the following members as of the examination date.

<u>Name</u>	<u>Principal Occupation</u>
Joseph F. Morris, Jr.	Chief Executive Officer
Bruce E. Short	Chief Financial Officer
Richard J. Schmitzer	Chief Underwriting Officer
John G. Clarke	Senior Vice President – Marketing
Gregg T. Davis	Chairman of the Board, Executive Vice President of James River Group

### Officers

As of the examination date, the following officers were elected and serving in accordance with the Company's Bylaws:

<u>Name</u>	<u>Title</u>
Joseph F. Morris, Jr.	President
Denise L. Husted	Treasurer
Steven P. Earhart	Secretary
Gregg T. Davis	Chairman of the Board
Bruce E. Short	Vice President, Chief Financial Officer

### Insurance Holding Company System

The Company is a member of a holding company system as defined in Section 3901.32 of the ORC. The following displays the chain of ownership of the insurance companies as of December 31, 2009:

Franklin Holdings, Ltd. (Bermuda)  
    Franklin Holdings II, Ltd. (Bermuda)  
        James River Group, Inc. (Delaware)  
            James River Management Company (Delaware)  
            James River Insurance Company (Ohio)  
                James River Casualty Company (Virginia)  
            Stonewood Insurance Company (North Carolina)  
            Stonewood Insurance Management Company, Inc. (Delaware)  
            Potomac Risk Services, Inc. (Virginia)  
            JRG Reinsurance Company, Ltd. (Bermuda)

### Territory and Plan of Operations

Except for the State of Ohio, the Company is licensed to transact business in all states and the District of Columbia. The Company works with broker administrators to write their casualty business.

The following schedule illustrates the Company's premium written in 2009 by line of business:

	Direct	Assumed	Ceded	Net	Percent
Other liability - occurrence	63,967,743	4,767	49,561,350	14,411,160	31.5%
Allied lines	3,540,565	38,898,476	30,540,419	11,898,622	26.0%
Other liability – claims-made	32,009,954	5,400	23,345,908	8,669,446	19.0%
Products liability - occurrence	18,460,842	0	13,017,387	5,443,455	11.9%
Medical professional liability – claims-made	11,810,110	0	8,484,067	3,326,043	7.3%
Product liability – claims-made	6,867,719	0	4,919,772	1,947,947	4.3%
All other lines	<u>1,404,412</u>	<u>0</u>	<u>1,304,422</u>	<u>99,990</u>	<u>0.0%</u>
Totals	<u>138,061,345</u>	<u>38,908,643</u>	<u>131,173,325</u>	<u>45,796,663</u>	<u>100.0%</u>

### Significant Operating Results

The Company reported the following net underwriting results, reported in thousands, during the examination period:

	2009	2008	2007	2006	2005
Premiums earned	<u>\$ 51,183</u>	<u>\$ 54,624</u>	<u>\$ 203,082</u>	<u>\$ 174,357</u>	<u>\$ 94,000</u>
Losses incurred	16,753	16,763	82,752	73,169	46,857
Loss adjustment expense incurred	19,773	18,895	34,466	28,861	16,515
Underwriting expense incurred	<u>9,542</u>	<u>897</u>	<u>50,061</u>	<u>40,503</u>	<u>25,053</u>
Total underwriting deductions	<u>46,068</u>	<u>36,555</u>	<u>167,279</u>	<u>142,533</u>	<u>88,425</u>
Net underwriting gain	<u>\$ 5,115</u>	<u>\$ 18,069</u>	<u>\$ 35,803</u>	<u>\$ 31,824</u>	<u>\$ 5,575</u>
Pure loss ratio	32.7%	30.7%	40.7%	42.0%	49.8%
Loss adjustment expense ratio	<u>38.6%</u>	<u>34.6%</u>	<u>17.0%</u>	<u>16.6%</u>	<u>17.6%</u>
Loss ratio	71.4%	65.3%	57.7%	58.6%	67.4%
Underwriting expense ratio	<u>20.8%</u>	<u>-17.7%</u>	<u>24.5%</u>	<u>22.2%</u>	<u>21.0%</u>
Combined ratio	<u>92.2%</u>	<u>47.6%</u>	<u>82.2%</u>	<u>80.8%</u>	<u>88.4%</u>

## **Reinsurance**

Certain premiums and losses are ceded to and assumed from unaffiliated and affiliated insurance companies under various excess of loss and quota share reinsurance contracts. Prior to January 1, 2008, the Company and Stonewood Insurance Company (“SIC”) were participants to an intercompany reinsurance pooling agreement. One hundred percent of all direct business, net of reinsurance with non-affiliates, written by the two companies was ceded to the pool, with the Company and SIC assuming 80% and 20% of the underwriting results, respectively. On January 1, 2008, the Company and SIC terminated the intercompany pooling arrangement.

Effective January 1, 2008, the Company entered into a 70% quota share reinsurance arrangement with JRG Reinsurance Company Ltd. In 2009, the Company entered into a quota share reinsurance agreement with its newly acquired wholly owned subsidiary, James River Casualty Company. Under the agreement, the Company assumes 90% of the net retained premiums and losses of JRCC and pays a 35% commission on assumed premiums written.

Reinsurance coverage is tailored to fit the various primary and excess products written by the Company and includes a combination, of excess of loss and quota share treaties. The retention level per occurrence for primary casualty is up to \$2.0 million per occurrence and for excess casualty, it is approximately \$750,000 per occurrence. The retention level per risk for primary property and excess property is \$1.0 million per risk and \$2.0 million per risk, respectively. The combination of property catastrophe and per risk reinsurance treaties provides coverage for a single occurrence of up to approximately \$50.0 million as of December 31, 2009. The total coverage includes a \$45.0 million excess of \$5.0 million catastrophe cover, which provides coverage in excess of the Company’s 500-year probable maximum loss.

All contracts contained an insolvency clause, intermediary clause, errors and omission clause, arbitration clause and a service of suit clause applicable to foreign reinsurers, which meet the guidelines prescribed by the National Association of Insurance Commissioners (“NAIC”).

## **Financial Statements**

The financial condition and the results of its operations for the five year period under examination as reported and filed by the Company with the Department and audited by the Company’s external auditors, are reflected in the following:

Statement of Assets, Liabilities, Capital and Surplus  
Statement of Income  
Statement of Changes in the Capital and Surplus Account

**Statement of Assets, Liabilities, Capital and Surplus  
December 31, 2009**

<b><u>Admitted assets</u></b>	
Bonds	\$ 332,271,212
Common stocks	6,757,173
Cash	12,275,589
Other invested assets	16,212,108
Receivables for securities	<u>555,738</u>
Total cash and invested assets	368,071,820
Investment income due and accrued	3,465,074
Uncollected premiums and agents' balances in the course of collection	42,927,384
Amounts recoverable from reinsurers	19,384,337
Current federal and foreign income tax recoverable	300,702
Net deferred tax asset	7,074,603
Receivables from parent, subsidiaries and affiliates	67,705
Aggregate write-ins for other than invested assets	
Insurance receivable	<u>1,597,245</u>
Total admitted assets	<u>\$ 442,888,869</u>

**Liabilities**

Losses	\$ 136,812,797
Reinsurance payable on paid losses and loss adjustment expenses	23,961,132
Loss adjustment expenses	62,480,919
Unearned premiums	15,653,813
Ceded reinsurance premiums payable	10,599,324
Provision for reinsurance	84,000
Payable for securities	712,319
Aggregate write-ins for liabilities:	
Other liabilities	91,164
Deferred ceding commission	2,644,679
Excise tax payable	<u>84,771</u>
Total liabilities	253,124,917

**Capital and Surplus**

Aggregate write-ins for special surplus funds:	
Additional admitted deferred tax assets	3,328,124
Common capital stock	3,547,500
Gross paid in and contributed surplus	134,601,871
Unassigned funds	<u>48,286,457</u>
Surplus as regards policyholders	<u>189,763,952</u>
Total liabilities, capital and surplus	<u>\$ 442,888,869</u>

**Statement of Income**  
**As of December 31, 2009**

Premium earned	\$ 51,183,454
Losses incurred	16,753,277
Loss adjustment expenses	19,773,463
Other underwriting expenses incurred	<u>9,542,303</u>
Net underwriting gain	<u>5,114,411</u>
Net investment income earned	16,828,080
Net realized capital gains or (losses)	<u>(4,511,589)</u>
Net investment gain	<u>12,316,491</u>
Aggregate write-ins for miscellaneous income:	
Miscellaneous income	<u>2,723</u>
Total other income	<u>2,723</u>
Net income before dividends to policyholders and federal income taxes	17,433,625
Federal income taxes incurred	<u>3,241,092</u>
Net income	<u>\$ 14,192,533</u>

**Statement of Changes in the Capital and Surplus Account**  
(In thousands)

<u>Capital and Surplus</u>	<u>2009</u>	<u>2008</u>	<u>2007</u>	<u>2006</u>	<u>2005</u>
Capital & surplus, prior year end	<u>\$ 179,262</u>	<u>\$ 189,400</u>	<u>\$ 184,238</u>	<u>\$ 122,564</u>	<u>\$ 57,529</u>
Net income	14,193	16,288	35,818	28,316	5,478
Change in net unrealized capital gains or (losses)	5,708	(5,295)	(760)	95	-
Change in net deferred income tax	(253)	636	3,841	3,966	4,234
Change in non-admitted assets	6,077	(7,525)	(1,933)	(4,462)	(2,844)
Change in provision for reinsurance	1,777	2,758	(3,488)	759	(1,833)
Paid in surplus	-	-	-	33,000	60,000
Dividends to stockholders	(17,000)	(17,000)	(28,316)	-	-
Net change in capital and surplus	<u>10,502</u>	<u>(10,138)</u>	<u>5,162</u>	<u>61,674</u>	<u>65,035</u>
Capital and surplus, current year end	<u>\$ 189,764</u>	<u>\$ 179,262</u>	<u>\$ 189,400</u>	<u>\$ 184,238</u>	<u>\$ 122,564</u>

## Notes to Financial Statements

### Investments

The Company's investment portfolio consists primarily of investment grade bonds and is in compliance with Section 3925.08 of the ORC. The investments were valued in accordance with the relevant Statements of Statutory Accounting Principles and the NAIC Securities Valuation Office.

### Loss and Loss Adjustment Expense Reserves

Brian D. Haney, FCAS, MAAA, of the Company certified the total reserves for year 2005 and the Company had an outside actuary, Ollie L. Sherman, Jr., FCAS, MAAA, certify the total reserves for examination years 2006 to 2009.

Mary D. Miller, Assistant Director, Product Regulation and Actuarial Services of the Department, reviewed the actuarial studies performed and determined the loss and loss adjustment expense ("LAE") reserves presented in the Company's 2009 annual statement appear to make a reasonable provision for the Company's loss and LAE reserves.

### Conclusion

The balance sheet contained in this Report of Examination reflects the financial condition of the Company as of December 31, 2009, and is summarized as follows:

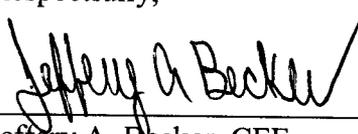
Total Admitted Assets	<u>\$442,888,869</u>
Liabilities	\$253,124,917
Surplus as Regards Policyholders	<u>189,763,952</u>
Total Liabilities and Surplus as Regards Policyholders	<u>\$442,888,869</u>

### Acknowledgement

Appreciation is expressed for the assistance extended by the officers and employees of the Company during the course of this examination.

In addition to the undersigned, the following representatives of the Department participated in this examination: Louis F. Radecky, CPA (inactive), David T. Finkler, CPA; Kim Somogyi, CPA; Richard Clayton, CFE; Rick Rhoades, CPA (inactive); Mary D. Miller, FCAS, MAAA; Bradley Schroer; Jeffrey Ferris, AES, CISA and Floyd Meeks, AES, CISA.

Respectfully,



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Jeffery A. Becker, CFE

Examiner-In-Charge  
Office of Risk Assessment  
Ohio Department of Insurance



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William C. Harrington, CFE, CPA (inactive)  
Chief Examiner  
Office of Risk Assessment  
Ohio Department of Insurance

Verification

As required by Section 3901.07 of the Ohio Revised Code, the undersigned hereby attest to the best of their knowledge and belief that the attached is a true Report of Examination as of December 31, 2009.

Jeffery A. Becker  
Examiner-In-Charge

8/6/10  
Date

William C. Harrington  
Chief Examiner

8/06/10  
Date

State of Ohio

County of Franklin

Personally appeared before me the above named, Jeffery A. Becker, personally known to me, who executed the above instrument and that the statements and answers contained therein are true and correct to the best of his/her knowledge and belief.

Subscribed and sworn to before me this 6 day of August, 2010.

Elizabeth Chase

(Notary Public)  
**ELIZABETH CHASE**  
NOTARY PUBLIC, STATE OF OHIO  
MY COMMISSION EXPIRES MAY 22, 2012  
My Commission Expires

State of Ohio

County of Franklin

Personally appeared before me the above named, William C. Harrington, personally known to me, who executed the above instrument and that the statements and answers contained therein are true and correct to the best of his/her knowledge and belief.

Subscribed and sworn to before me this 6 day of August, 2010.

Elizabeth Chase  
(Notary Public)

**ELIZABETH CHASE**  
NOTARY PUBLIC, STATE OF OHIO  
MY COMMISSION EXPIRES MAY 22, 2012  
My Commission Expires