

Report of Examination of

Falls Lake National Insurance Company
Columbus, Ohio

As of December 31, 2014

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Columbus, Ohio
October 23, 2015

Honorable Mary Taylor
Lt. Governor/Director
Ohio Department of Insurance
50 West Town Street
3rd Floor – Suite 300
Columbus, Ohio 43215

Dear Madam:

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

Falls Lake National 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 6131 Falls of Neuse Rd, Suite 306, Raleigh, North Carolina.

Scope of Examination

The Department last examined the Company as of December 31, 2011. The Department’s current examination covers the period from and including January 1, 2012 through December 31, 2014.

The Department, as the lead regulator of James River Group and the examination facilitator, led the multi-state coordinated examination. In addition to the Department, the North Carolina Insurance Department and the Virginia Bureau of Insurance also participated on the examination. The examination was conducted in accordance with the National Association of Insurance Commissioners Financial Condition Examiners Handbook (“Handbook”). The Handbook requires that the Department plan and perform the examination to evaluate the Company’s financial condition, assess corporate governance, identify current and prospective risks of the Company and evaluate system controls and procedures used to mitigate those risks. An examination also includes identifying and evaluating significant risks that could cause an insurer’s surplus to be materially misstated both currently and prospectively.

All accounts and activities of the Company were considered in accordance with the risk-focused examination process. This may include assessing significant estimates made by management and evaluating management’s compliance with Statutory Accounting Principles. The examination does not attest to the fair presentation of the financial statements included herein. If, during the course of the examination an adjustment is

identified, the impact of such adjustment will be documented separately following the Company's financial statements.

This examination report includes significant findings of fact, as mentioned in the ORC Section 3901.07 and general information about the insurer and its financial condition. There may be other items identified during the examination that, due to their nature (e.g., subjective conclusions, proprietary information, etc.), are not included within the examination reports but separately communicated to other regulators and/or the Company.

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>
Michael E. Crow	Senior Vice President-Finance and Chief Accounting Officer, James River Group, Inc.
Gregg T. Davis	Chief Financial Officer, James River Group Holdings, Ltd.
Thomas R. Fauerbach	Chief Financial Officer and Chief Actuary, Falls Lake Insurance Companies
Steven J. Hartman	President and Chief Executive Officer, Falls Lake Insurance Companies
Joseph R. Raia	Controller, Falls Lake Insurance Companies

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>
Gregg T. Davis	Chairman
Steven J. Hartman	President and Chief Executive Officer
Thomas R. Fauerbach	Secretary and Chief Financial Officer
Michael E. Crow	Treasurer

Insurance Holding Company System

The Company is a member of a holding company system as defined in Section 3901.32 of the ORC. James River Group Holdings, Ltd., a publicly traded insurance holding company, is the ultimate controlling party of the insurance holding company system.

James River Group Holdings, Ltd.

 JRG Reinsurance Company, Ltd.

 Franklin Holdings II Capital Trust I

 James River Group, Inc.

 Potomac Risk Services, Inc.

 James River Insurance Company

 James River Casualty Company

 James River Management Company, Inc.

 Falls Lake National Insurance Company

 Falls Lake Fire and Casualty Company

 Stonewood Insurance Company

 Falls Lake General Insurance Company

 Falls Lake Insurance Management Company, Inc.

Territory and Plan of Operations

The Company was licensed to transact business in the District of Columbia and the following states:

Alabama	Alaska	Arizona	Arkansas	Colorado
Delaware	Florida	Georgia	Hawaii	Idaho
Illinois	Indiana	Iowa	Kansas	Kentucky
Louisiana	Maryland	Massachusetts	Michigan	Minnesota
Mississippi	Missouri	Montana	Nebraska	Nevada
New Hampshire	New Jersey	New Mexico	New York	North Carolina
North Dakota	Ohio	Oklahoma	Oregon	Pennsylvania
Rhode Island	South Carolina	South Dakota	Tennessee	Texas
Utah	Vermont	Virginia	Washington	West Virginia
Wisconsin	Wyoming			

The Company writes workers' compensation, specialty property and casualty program business and individual risks that fit management's rating criteria on an admitted basis.

Reinsurance

Effective January 1, 2013, the Company participates in an intercompany pooling agreement with its United States affiliates. After each affiliate cedes 70% of its net business to JRG Reinsurance Company, Ltd., the remaining 30% is subject to the intercompany pooling. The pooling participation percentages are as follows:

James River Insurance Company	75.0%
Falls Lake National Insurance Company	13.0%
Stonewood Insurance Company	6.0%
James River Casualty Company	5.0%
Falls Lakes General Insurance Company	<u>1.0%</u>
	100.0%

Financial Statements

The financial condition and the results of its operations for the three 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
December 31, 2014**

Admitted assets

Bonds	\$ 6,798,070
Common stocks	40,323,931
Cash and short-term investments	<u>2,254,068</u>
Total cash and invested assets	49,376,069
Investment income due and accrued	20,737
Uncollected premiums and agents' balances in the course of collection	17,964,065
Deferred premiums, agents' balances and installments booked but deferred and not yet due	9,185,861
Amounts recoverable from reinsurers	10,160,891
Funds held by or deposited with reinsured companies	176,294,270
Current federal and foreign income tax recoverable and interest thereon	303,982
Net deferred tax asset	857,976
Receivables from parent, subsidiaries and affiliates	<u>167,407</u>
Total admitted assets	<u>\$ 264,331,258</u>

**Statement of Liabilities, Capital and Surplus
December 31, 2014**

Liabilities

Losses	\$ 11,706,425
Reinsurance payable on paid losses and loss adjustment expenses	10,888,240
Loss adjustment expenses	7,682,312
Commissions payable, contingent commissions and other similar charges	2,781,557
Other expenses	290,065
Taxes, licenses and fees	874,476
Unearned premiums	3,818,601
Ceded reinsurance premiums payable	20,144,134
Funds held by company under reinsurance treaties	155,810,651
Amounts withheld or retained by company for account of others	21,813
Provision for reinsurance	667,000
Payable to parent, subsidiaries and affiliates	21,553
Aggregate write-in for liabilities	
Deferred ceding commission	42,308
Policyholder deposits	<u>26,710</u>
Total liabilities	214,775,845

Capital and Surplus

Common capital stock	4,200,000
Gross paid in and contributed surplus	38,558,551
Unassigned funds	<u>6,796,862</u>
Surplus as regards policyholders	<u>49,555,413</u>
Total liabilities, capital and surplus	<u>\$ 264,331,258</u>

Statement of Income
As of December 31, 2014

Premiums earned	<u>\$ 8,787,949</u>
Losses incurred	2,239,163
Loss adjustment expenses	2,718,727
Other underwriting expenses	<u>3,093,600</u>
Net underwriting gain	736,459
Net investment income earned	<u>66,804</u>
Net investment gain	<u>66,804</u>
Net loss from agents' or premium balances charged off	(27)
Finance and service charges not included in premiums	<u>347</u>
	<u>320</u>
Net income, after dividends to policyholders, after capital gains tax and before all other federal and foreign income taxes	<u>803,583</u>
Federal and foreign income taxes incurred	<u>172,672</u>
Net income	<u>\$ 630,911</u>

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

<u>Capital and Surplus</u>	<u>2014</u>	<u>2013</u>	<u>2012</u>
Capital & surplus, prior year end	<u>\$ 47,741</u>	<u>\$ 42,077</u>	<u>\$ 8,128</u>
Net income (loss)	631	(24)	(320)
Change in net unrealized capital gains less capital gains tax	1,891	4,775	(2,071)
Change in net deferred income tax	(99)	2,145	-
Change in non-admitted assets	28	(1,202)	(15)
Change in provision for reinsurance	(637)	(30)	-
Paid-in capital	-	-	1,199
Paid-in surplus	-	-	<u>35,156</u>
Net change in capital and surplus	<u>1,814</u>	<u>5,664</u>	<u>33,949</u>
Capital and surplus, current year end	<u>\$ 49,555</u>	<u>\$ 47,741</u>	<u>\$ 42,077</u>

Notes to Financial Statements

Investments

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

Loss and Loss Adjustment Expense Reserves

The Company's Board of Directors appointed Sean P. McDermott, FCAS, MAAA, of Towers Watson to render a Statement of Actuarial Opinion ("Opinion") on the total reserves. Mr. McDermott prepared an Actuarial Report supporting the Opinion in conjunction with the preparation of the Company's December 31, 2014 Annual Statement.

Thomas Botsko, ACAS, MAAA, the Department's Chief Property and Casualty Actuary, reviewed the Actuarial Report and performed other procedures as considered necessary to evaluate the loss and loss adjustment expense ("LAE") reserves. Mr. Botsko concluded the reserves fall within a reasonable range of reserve estimates at December 31, 2014.

Conclusion

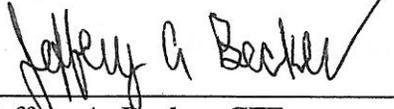
The balance sheet contained in this Report of Examination reflects the financial condition of the Company as of December 31, 2014, and is summarized as follows:

Total Admitted Assets	<u>\$ 264,331,258</u>
Liabilities	214,775,845
Surplus as Regards Policyholders	<u>49,555,413</u>
Total Liabilities and Surplus as Regards Policyholders	<u>\$ 264,331,258</u>

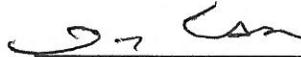
Acknowledgement

In addition to the aforementioned and undersigned, the following representatives of the Department participated in this examination: Methuselah Nyangoro, AES, CFE, CPA; Kim Somogyi, AES, CPA, Richard Morris, CPA and Bradley Schroer.

Respectfully,



Jeffery A. Becker, CFE
Examiner-In-Charge
Office of Risk Assessment
Ohio Department of Insurance



David Cook, CFE
Assistant Chief Examiner
Office of Risk Assessment
Ohio Department of Insurance

Verification

As required by Section 3901.07 of the ORC, 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, 2014.

Jeffery A Becker
Examiner-In-Charge

11/9/15
Date

[Signature]
Assistant Chief Examiner

11/9/15
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 knowledge and belief.

Subscribed and sworn to before me this 9 day of November, 2015.

Elizabeth Chase

(Notary Public)
ELIZABETH CHASE
NOTARY PUBLIC, STATE OF OHIO
~~MY COMMISSION EXPIRES MAY 22, 2017~~
My Commission Expires

State of Ohio

County of Franklin

Personally appeared before me the above named, David Cook, 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 knowledge and belief.

Subscribed and sworn to before me this 9 day of November, 2015.

Elizabeth Chase

(Notary Public)
ELIZABETH CHASE
NOTARY PUBLIC, STATE OF OHIO
~~MY COMMISSION EXPIRES MAY 22, 2017~~
My Commission Expires