

REPORT ON EXAMINATION

OF THE

SENECA INSURANCE COMPANY

AS OF

DECEMBER 31, 2005

DATE OF REPORT

MAY 1, 2007

EXAMINER

JAINARINE TILAKDHARRY

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STATE OF NEW YORK
INSURANCE DEPARTMENT
25 BEAVER STREET
NEW YORK, NEW YORK 10004

May 1, 2007

Honorable Eric Dinallo
Superintendent of Insurance
Albany, New York 12257

Sir:

Pursuant to the requirements of the New York Insurance Law, and in compliance with the instructions contained in Appointment Number 22521 dated June 27, 2006 attached hereto, I have made an examination into the condition and affairs of Seneca Insurance Company, Inc. as of December 31, 2005, and submit the following report thereon.

Wherever the designations "the Company" or "Seneca" appear herein without qualification, they should be understood to indicate Seneca Insurance Company, Inc.

Wherever the term "Department" appears herein without qualification, it should be understood to mean the New York Insurance Department.

The examination was conducted at the Company's home offices located at 160 Water Street, New York, New York 10038.

1. SCOPE OF EXAMINATION

The previous examination was conducted as of December 31, 2000. This examination covered the five-year period from January 1, 2001 through December 31, 2005. Transactions occurring subsequent to this period were reviewed where deemed appropriate by the examiner.

The examination comprised a verification of assets and liabilities as of December 31, 2005. The examination included a review of income, disbursements and company records deemed necessary to accomplish such analysis or verification and utilized, to the extent considered appropriate, work performed by the Company's independent certified public accountants ("CPA"). A review or audit was also made of the following items as called for in the Examiners Handbook of the National Association of Insurance Commissioners ("NAIC"):

- History of Company
- Management and control
- Corporate records
- Fidelity bond and other insurance
- Territory and plan of operation
- Growth of Company
- Business in force by states
- Loss experience
- Reinsurance
- Accounts and records
- Financial statements

A review was also made to ascertain what action was taken by the Company with regard to comments and recommendations contained in the prior report on examination.

This report on examination is confined to financial statements and comments on those matters, which involve departures from laws, regulations or rules, or which are deemed to require explanation or description.

2. DESCRIPTION OF COMPANY

The Company was incorporated on March 29, 1978, under the laws of New York as Eagle Star Insurance Company of America. It was formed to serve as the corporate vehicle in the domestication of the United States Branch of the Eagle Star Insurance Company, Ltd., London, England, which entered the United States through the State of New York in 1916. The Company was licensed and the domestication became effective as of July 1, 1978. The present title was adopted on April 8, 1987.

On October 8, 1993, a new holding company, Sen-Tech International Holdings, Inc. ("Sen-Tech") was formed. On April 26, 2000, Sen-Tech entered into a merger agreement to be acquired by Crum and Forster Holding Inc., which is a subsidiary of Fairfax Financial Holdings Limited. The transaction was completed on August 31, 2000, with the acquirer being North River Insurance Company, which is a wholly-owned subsidiary of Crum and Forster Holding Inc.

Capital paid-in is \$4,800,000 consisting of 24,000 shares of \$200 par value per share common stock. Gross paid in and contributed surplus is \$26,275,566. The Company's gross paid-in and contributed surplus increased by \$1,844,105 during the examination period, as follows:

| <u>Year</u> | <u>Description</u> | <u>Amount</u> |
|-------------|---|----------------------|
| 2000 | Beginning gross paid in and contributed surplus | \$ 24,431,461 |
| 2002 | Surplus contribution | <u>1,844,105</u> |
| 2005 | Ending gross paid in and contributed surplus | \$ <u>26,275,566</u> |

A. Management

Pursuant to the Company's charter and by-laws, management of the Company is vested in a board of directors consisting of not less than thirteen nor more than twenty-one members. The board meets four times during each calendar year. At December 31, 2005, the board of directors was comprised of the following members:

Names and ResidencePrincipal Business Affiliation

Nikolas Antonopoulos
Basking Ridge, NJ

Chairman of the Board & Chief Executive Officer,
United States Fire Insurance Company

Joseph F. Braunstein, Jr.
Yardley, PA

President,
United States Fire Insurance Company

Harvey Child
Greenville, PA

Chief Executive Officer,
Bail USA, Inc.

Donald R. Fischer
Wyckoff, NJ

Senior Vice President-Underwriting,
United States Fire Insurance Company

Dennis J. Hammer
Somerville, NJ

Senior Vice President & Controller,
United States Fire Insurance Company

Mary J. Hughes
Randolph, NJ

Senior Vice President-Underwriting,
United States Fire Insurance Company

Paul Kush
Souderton, PA

Senior Vice President-Claims,
United States Fire Insurance Company

Albert B. Lewis
New York, NY

Attorney,
D'Amato & Lynch

Douglas M. Libby
New York, NY

President, Chairman of the Board & Chief Executive
Officer,
Seneca Insurance Company, Inc.

Kim E. Piersol
Skillman, NJ

Senior Vice President-Actuarial,
United States Fire Insurance Company

Mary Jane Robertson
Morristown, NJ

Executive Vice President, Treasurer & Chief Financial
Officer,
United States Fire Insurance Company

Chris I. Stormo
Ledgewood, NJ

Vice President,
Seneca Insurance Company, Inc.

Marc T. A. Wolin
Merrick, NY

Vice President, Treasurer, Chief Financial Officer &
Secretary,
Seneca Insurance Company, Inc.

A review of the minutes of the board of directors' meetings held during the examination period indicated that the meetings were generally well attended with the exception of Mary Jeanne Hughes who attended only 25% of the meetings in 2005 for which she was eligible to attend.

Members of the board have a fiduciary responsibility and must evince an ongoing interest in the affairs of the insurer. It is essential that board members attend meetings consistently and set forth their views on relevant matters so that the board may reach appropriate decisions. Individuals who fail to attend at least one-half of the regular meetings do not fulfill such criteria.

It is recommended that board members who are unable or unwilling to attend meetings consistently should resign or be replaced.

As of December 31, 2005, the principal officers of the Company were as follows:

| <u>Name</u> | <u>Title</u> |
|------------------|--|
| Douglas M. Libby | President and Chief Executive Officer |
| Marc T. A. Wolin | Chief Financial Officer, Treasurer and Secretary |

B. Territory and Plan of Operation

As of December 31, 2005, the Company was licensed to write business in all states and the District of Columbia.

As of the examination date, the Company was authorized to transact the kinds of insurance as defined in the following numbered paragraphs of Section 1113(a) of the New York Insurance Law:

| <u>Paragraph</u> | <u>Line of Business</u> |
|------------------|-------------------------------|
| 4 | Fire |
| 5 | Miscellaneous property damage |
| 6 | Water damage |
| 7 | Burglary and theft |
| 8 | Glass |
| 9 | Boiler and machinery |
| 10 | Elevator |
| 12 | Collision |
| 13 | Personal injury liability |
| 14 | Property damage liability |

| <u>Paragraph</u> | <u>Line of Business</u> |
|------------------|--|
| 15 | Workers' compensation and employers' Liability |
| 16 | Fidelity and surety |
| 19 | Motor vehicle and aircraft physical damage |
| 20 | Marine and inland marine |
| 21 | Marine protection and indemnity |

In addition, the Company is licensed to transact such workers' compensation insurance as may be incident to coverages contemplated under paragraphs 20 and 21 of Section 1113(a), including coverages described in the Longshoremen's and Harbor Workers' Compensation Act (Public Law No. 803, 69th Congress, as amended; 33 USC Section 901 et seq. as amended). The Company is also licensed to write special risk insurance pursuant to Section 6302 of the New York Insurance Law.

Based on the lines of business for which the Company is licensed and the Company's current capital structure, and pursuant to the requirements of Articles 13 and 41 of the New York Insurance Law, the Company is required to maintain a minimum surplus to policyholders in the amount of \$3,700,000.

The following schedule shows the direct premiums written by the Company both in total and in New York for the period under examination:

| <u>Calendar</u> | | | <u>Percentage of Premiums</u> |
|-----------------|-----------------------|----------------------------|-------------------------------|
| <u>Year</u> | <u>New York State</u> | <u>Total United States</u> | <u>Written in New York</u> |
| 2001 | \$30,513,182 | \$142,624,173 | 21.39% |
| 2002 | \$40,254,882 | \$105,898,199 | 38.01% |
| 2003 | \$48,776,550 | \$118,768,437 | 41.07% |
| 2004 | \$57,067,880 | \$134,087,505 | 42.56% |
| 2005 | \$44,161,095 | \$129,570,728 | 34.08% |

The Company's primary lines of business written are commercial multi peril, fire, other liability, workers compensation, inland marine and surety (bail bonds). The business is largely produced through branches in New York, Kentucky, Colorado and Virginia.

C. Reinsurance

Assumed reinsurance accounted for 4.62% of the Company's gross premium written at December 31, 2005. During the period covered by this examination, the Company's assumed reinsurance business has increased since the last examination. The Company's assumed reinsurance program consists of property and casualty coverage assumed on a quota share basis, pursuant to the terms of a ninety percent quota share treaty with Seneca Specialty Insurance Company, a wholly owned subsidiary domiciled in Arizona. The Company utilizes reinsurance accounting as defined in the NAIC Statement of Statutory Accounting Principles ("SSAP") No. 62 for its assumed reinsurance business.

The company has structured its ceded reinsurance program to limit its maximum exposure to any one risk as follows:

| <u>Type of Contract</u> | <u>Cession</u> |
|--|--|
| Umbrella Liability | 80% quota share of the first \$1,000,000 net loss, each occurrence. \$4,000,000 excess of \$1,000,000 net loss, each occurrence. \$5,000,000 excess of \$5,000,000, net loss, each occurrence. |
| Property Variable Quota Share | Up to 50% of \$2,000,000 per risk, limit 40% of \$4,000,000 per occurrence. |
| Workers' Compensation Quota Share (Safety Association Fund business only) | 50% quota share of ultimate net loss on policies written from 1/1/92 – 12/31/97. |
| Workers' Compensation Excess of Loss (Safety Association Fund business only) | First layer: \$250,000 excess of \$250,000 ultimate net loss, each occurrence. Second layer: \$500,000 excess of \$500,000 ultimate net loss, each occurrence. |
| Environmental Liability Quota Share | 42.5% of \$1,000,000 each loss and/or in the aggregate, any one policy. |
| Workers' Compensation Excess of Loss | First layer: \$3,000,000 excess of \$2,000,000 each occurrence. Second layer: \$5,000,000 excess of \$5,000,000 each occurrence. |
| Inland Marine Property Excess of Loss | First layer: \$500,000 excess of \$500,000 each risk, limit \$1,500,000 each occurrence. Second layer: \$1,000,000 excess of \$1,000,000 each risk, limit \$3,000,000 each occurrence. |
| Technology Errors and Omissions | 32.5% quota share of up to \$1,000,000 each loss. |

| <u>Type of Contract</u> | <u>Cession</u> |
|--|---|
| | \$4,000,000 excess of \$1,000,000 each loss. \$3,000,000 excess of \$5,000,000 each loss. |
| Equipment Breakdown | 100% up to \$25,000,000 any one accident, any one policy. |
| <u>Multiple Line Excess of Loss</u> | |
| First layer | <ul style="list-style-type: none"> a. Casualty: \$500,000 excess of \$500,000 each occurrence. (Excluding Umbrella, D&O, E&O, Environmental and Workers' compensation policies) b. Property: \$500,000 excess of \$500,000 each risk, limit \$1,000,000 each occurrence. c. Boiler and Machinery: \$500,000 excess of \$500,000 each risk. d. Basket: \$500,000 excess of \$500,000 each common loss occurrence (in the event of loss under both a and b) |
| Second layer | <ul style="list-style-type: none"> a. Casualty: Other than workers compensation (Clash) - \$3,000,000 excess of \$1,000,000 each occurrence involving more than one policy (General and Auto Liability). Workers compensation - \$1,000,000 excess of \$1,000,000 each occurrence and \$2,000,000 excess of \$10,000,000 each occurrence. b. Property: \$1,000,000 excess of \$1,000,000 each risk, limit \$3,000,000 each occurrence. |
| Property Capacity Excess of Loss (Includes business written by the Inland Marine or Property Departments, excludes business written by the Custom Property and Excess and Surplus Property division.) | <ul style="list-style-type: none"> a. Property: \$3,000,000 excess if \$2,000,000 each risk, limit \$6,000,000 each occurrence. b. Inland Marine: \$3,000,000 excess if \$2,000,000 each risk, limit \$6,000,000 each occurrence. |
| Property Excess of Loss (Business written by the Company's Custom Property and Excess and Surplus Property Division) | <p>First layer: \$500,000 excess of \$500,000 each loss, each risk, limit \$1,500,000 any one loss occurrence.</p> <p>Second layer: \$4,000,000 excess of \$1,000,000 each loss, each risk, limit \$8,000,000 any one loss occurrence.</p> |
| Property Catastrophe | \$24,000,000 excess of \$1,000,000 ultimate net loss, each and every loss occurrence. |

Reinsurance agreements with affiliates were reviewed for compliance with Article 15 of the New York Insurance Law. It was noted that not all affiliated reinsurance agreements were filed with the Department pursuant to the provisions of Section 1505(d) (2) of the New York Insurance Law which states that:

“Transactions between a domestic controlled insurer and any person in its holding company system may not be entered into unless the insurer has notified the superintendent in writing of its intention to enter into any such transaction at least thirty days prior thereto, or such shorter period as he may permit and he has not disapproved it within such period...

(2) reinsurance treaties or agreements...”

It is recommended that the Company comply with Section 1505(d) (2) of the New York Insurance Law and notify the superintendent in writing of its intention to enter into any transactions at least thirty days prior thereto, or such shorter period as may permit, with any person in its holding company system.

It is the Company's policy to obtain the appropriate collateral for its cessions to unauthorized reinsurers. Letters of credit and trust accounts obtained by the Company to take credit for cessions to unauthorized reinsurers were reviewed for compliance with Department Regulations 133 and 114, respectively. No exceptions were noted.

All ceded reinsurance agreements in effect as of the examination date were reviewed and found to contain the required clauses, including an insolvency clause meeting the requirements of Section 1308 of the New York Insurance Law.

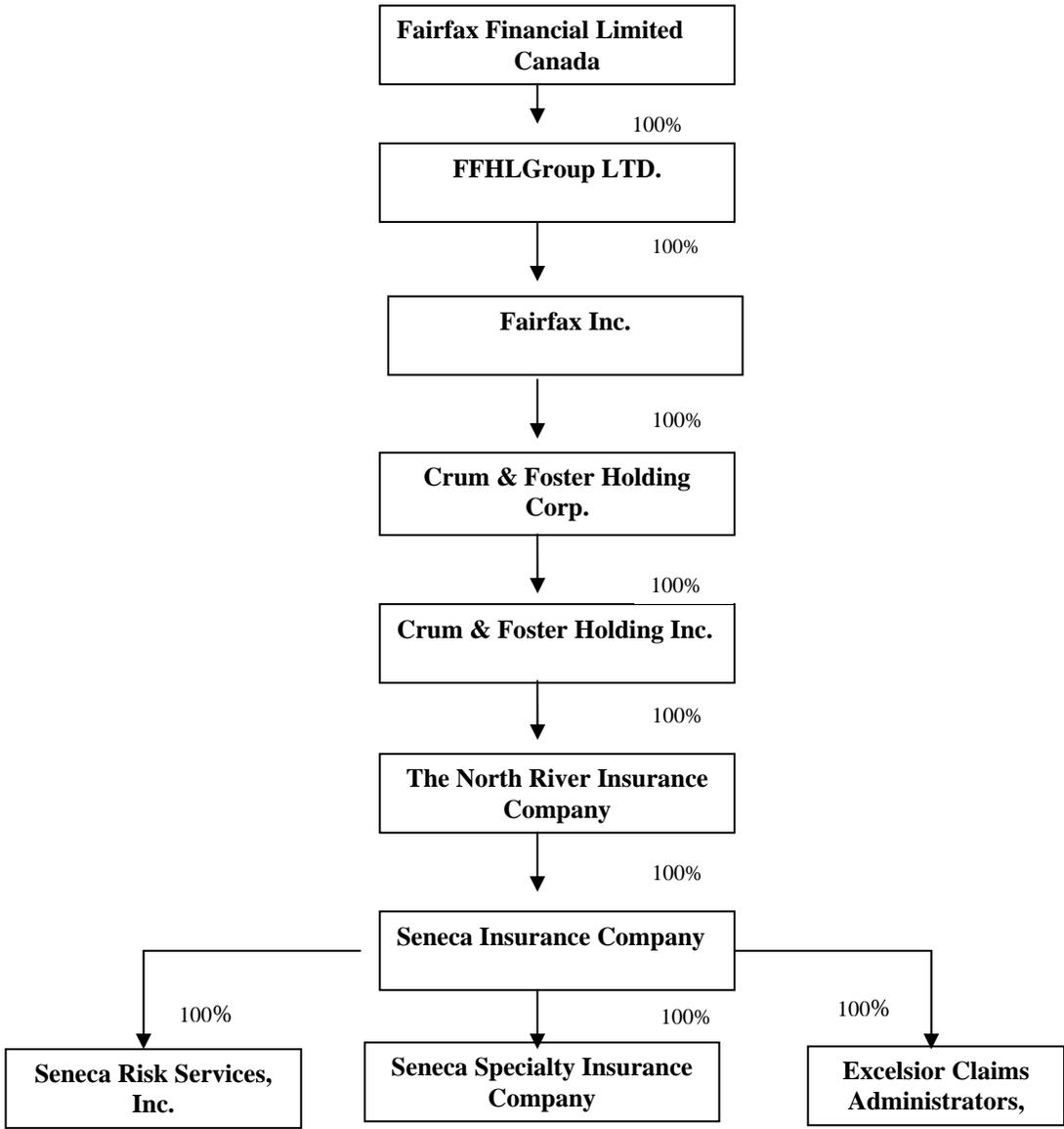
Examination review of the Schedule F data reported by the Company in its filed annual statement was found to accurately reflect its reinsurance transactions. Additionally, management has represented that all material ceded reinsurance agreements transfer both underwriting and timing risk as set forth in SSAP No. 62. Representations were supported by appropriate risk transfer analyses and an attestation from the Company's Chief Executive Officer pursuant to Department Circular Letter No. 8 (2005). Additionally, examination review indicated that the Company was not a party to any finite reinsurance agreements. All ceded reinsurance agreements were accounted for utilizing reinsurance accounting as set forth in paragraphs 25 and 26 of SSAP No. 62.

D. Holding Company System

The Company is a member of the Fairfax Financial Holding, Limited (“FFH”), (Canada). The Company is a wholly-owned subsidiary of North River, a New Jersey corporation, which is ultimately controlled by Fairfax Inc.

A review of the holding company registration statements filed with this Department indicated that such filings were complete and were filed in a timely manner pursuant to Article 15 of the New York Insurance Law and Department Regulation 52.

The following is an abridged chart of the holding company system at December 31, 2005:



At December 31, 2005, the Company was party to the following agreements with other members of its holding company system. All of these agreements were have been filed and non-disapproved by this Department pursuant to the provisions of Section 1505(d) of the New York Insurance Law.

1. Tax Allocation Agreement

Pursuant to the terms of this agreement, the Company filed a consolidated federal income tax return with its parent company Fairfax, Inc. The agreement was approved by the Department and became effective January 31, 2000.

2. Claims Adjustment Agreement

Effective April 29, 1994, the Company entered into a claims adjustment agreement with Excelsior Claims Administrators, Inc. (“Excelsior”). Pursuant to the terms of the agreement, Excelsior performs various claims services on behalf of the Company.

3. Administrative Services Agreement

Effective January 31, 2000, the Company entered into an administrative services agreement with United States Fire Insurance Company. Pursuant to the terms of the agreement each party agreed to provide certain underwriting, claims, policy administration and general services for each other.

4. Investment Administration Agreement

Effective August 31, 2000, the Company entered into an investment administration agreement with Fairfax Financial Holdings Limited (“Fairfax Financial”). Pursuant to the terms of this agreement, Fairfax Financial performs various functions relative to the administration of the Company’s investment portfolio.

5. Investment Management Agreement

Effective October 1, 2002, the Company entered into an investment management agreement with Hamblin Watsa Investment Counsel Ltd. (“Hamblin Watsa”) and Fairfax Financial Holdings Limited. Pursuant to this agreement, Hamlin Watsa performs all functions relative to the management of the Company’s investment portfolio. The agreement was amended on January 1, 2005.

6. Expense Sharing and Reimbursement with Seneca Specialty Insurance Company

The Company shares certain expenses with its subsidiary, Seneca Specialty Insurance Company. Although the Company has established procedures for the allocation of joint expenses, it does not have a formal, written expense sharing agreement with Seneca Specialty Insurance Company.

It is recommended that that the Company formalize a cost sharing agreement setting forth provisions that would serve as guidelines to properly allocate, reimburse and settle the cost of shared expenses with Seneca Specialty Insurance Company. The allocation method of shared expenses should be consistent with the provisions of Department Regulation 30.

E. Abandoned Property Law

Section 1316 of the New York Abandoned Property Law provides that amounts payable to a resident of this state from a policy of insurance, if unclaimed for three years, shall be deemed to be abandoned property. Such abandoned property shall be reported to the Comptroller on or before the first day of April each year. Such filing is required of all insurers regardless of whether or not they have any abandoned property to report.

The Company's abandoned property reports for the period of this examination were all filed on a timely basis pursuant to the provisions of Section 1316 of the New York Abandoned Property Law. However, the Company made a "negative" report of Abandoned Property for year ended December 31, 2005, instead of reporting an amount for Abandoned Property to the Comptroller.

Subsequent to the examination date, on November 16, 2006, the Company filed "Verification and Checklist for Unclaimed Property" for the period ended September 30, 2006 and reported amount of abandoned property to the Comptroller.

It is recommended that the Company comply with Section 1316 of the New York Abandoned Property Law and report the proper amount to the Comptroller.

F. Significant Operating Ratios

The following ratios have been computed as of December 31, 2005, based upon the results of this examination:

| | |
|--|--------|
| Net premiums written in 2005 to surplus as regards policyholders | 1:1 |
| Liabilities to liquid asset (cash and invested assets less investment in affiliates) | 69.39% |
| Premiums in course of collection to surplus as regards policyholders | 3.47% |

All of the above ratios fall within the benchmark ranges set forth in the Insurance Regulatory Information System of the National Association of Insurance Commissioners.

The underwriting ratios presented below are on an earned/incurred basis and encompass the five-year period covered by this examination:

| | <u>Amount</u> | <u>Ratio</u> |
|--------------------------------------|----------------------|----------------|
| Losses incurred | \$183,570,716 | 38.85% |
| Loss adjustment expenses incurred | 49,091,458 | 10.39 |
| Other underwriting expenses incurred | 192,425,224 | 40.72 |
| Net underwriting gain | <u>47,439,356</u> | <u>10.04</u> |
| Premium earned | <u>\$472,526,754</u> | <u>100.00%</u> |

G. Accounts and Records

1. Custodian Agreement

Seneca Insurance Company entered into a custodian agreement with The Bank of New York on September 30, 1996. A review of agreement revealed that it did not contain several covenants prescribed by the NAIC Financial Condition Examiners Handbook, Part 1, Section IV-J:

It is recommended that the Company amend its custodial agreement to include the safeguards and provisions per the NAIC Financial Condition Examiners Handbook, Part 1, Section IV- J.

Subsequent to the examination date, on September 13, 2006, the Company amended its custodial agreement with The Bank of New York to meet the requirements of the NAIC Financial Condition Examiners Handbook.

3. FINANCIAL STATEMENTS

A Balance Sheet

The following shows the assets, liabilities and surplus as regards policyholders as of December 31, 2005 as determined by this examination and as reported by the Company:

| Assets | <u>Assets</u> | <u>Assets Not Admitted</u> | <u>Net Admitted Assets</u> |
|--|----------------------|--------------------------------|--------------------------------|
| Bonds | \$187,938,517 | | \$187,938,517 |
| Common stocks | 32,694,132 | | 32,694,132 |
| Cash, cash equivalents and short-term investments | 33,809,030 | | 33,809,030 |
| Subtotals, cash and invested assets | 254,441,679 | | 254,441,679 |
| Investment income due and accrued | 2,932,863 | | 2,932,863 |
| Uncollected premiums and agents' balances in the course of collection | 3,664,863 | \$245,036 | 3,419,827 |
| Deferred premiums, agents' balances and installments booked but deferred and not yet due | 19,399,009 | | 19,399,009 |
| Amounts recoverable from reinsurers | 1,652,901 | | 1,652,901 |
| Net deferred tax asset | 9,056,126 | 3,735,548 | 5,320,578 |
| Electronic data processing equipment and software | 562,455 | 141,417 | 421,038 |
| Furniture and equipment, including health care delivery assets | 97,917 | 97,917 | |
| Aggregate write-ins for other than invested assets | <u>399,863</u> | <u>152,188</u> | <u>247,675</u> |
| Total assets | <u>\$292,207,676</u> | <u>\$4,372,106</u> | <u>\$287,835,570</u> |

Liabilities, surplus and other fundsLiabilities

| | | |
|---|-------------------|----------------------|
| Losses | | \$84,184,603 |
| Loss adjustment expenses | | 27,095,803 |
| Commissions payable, contingent commissions and other similar charges | | 954,492 |
| Other expenses (excluding taxes, licenses and fees) | | 3,097,310 |
| Taxes, licenses and fees (excluding federal and foreign income taxes) | | 2,304,453 |
| Current federal and foreign income taxes | | 4,197,413 |
| Unearned premiums | | 55,280,022 |
| Ceded reinsurance premiums payable (net of ceding commissions) | | 3,675,187 |
| Funds held by company under reinsurance treaties | | 113,388 |
| Amounts withheld or retained by company for account of others | | 425,208 |
| Provision for reinsurance | | 186,864 |
| Payable to parent, subsidiaries and affiliates | | 13,698 |
| Aggregate write-ins for liabilities | | <u>656,732</u> |
| Total liabilities | | \$182,185,173 |
| <u>Surplus and other funds</u> | | |
| Common capital stock | \$ 4,800,000 | |
| Gross paid in and contributed surplus | 26,275,566 | |
| Unassigned funds (surplus) | <u>74,574,831</u> | |
| Surplus as regards policyholders | | <u>105,650,397</u> |
| Total liabilities, surplus and other funds | | <u>\$287,835,570</u> |

NOTE: The Internal Revenue Service is currently conducting audits of the Company's consolidated federal income tax returns for tax years covering 2003 and 2004. The examiner is unaware of any potential exposure of the Company to any tax assessment and no liability has been established herein relative to such contingency.

B. Underwriting and Investment Exhibit

Surplus as regards policyholders increased \$56,106,053 during the five-year examination period January 1, 2001 through December 31, 2005, detailed as follows:

Statement of Income

Underwriting Income

| | | |
|--------------------------------------|--------------------|--------------------|
| Premiums earned | | \$ 472,526,754 |
| Deductions: | | |
| Losses incurred | \$183,570,716 | |
| Loss adjustment expenses incurred | 49,091,458 | |
| Other underwriting expenses incurred | <u>192,425,224</u> | |
| Total underwriting deductions | | <u>425,087,398</u> |
| Net underwriting gain | | \$47,439,356 |

Investment Income

| | | |
|---|-------------------|---------------------|
| Net investment income earned | \$30,164,182 | |
| Net realized capital gain | <u>26,129,376</u> | |
| Net investment gain | | <u>56,293,558</u> |
| Net income before dividends to policyholders and before federal and foreign income taxes | | \$103,732,914 |
| Dividends to policyholders | | <u>106,055</u> |
| Net income after dividends to policyholders but before federal and foreign income taxes | | \$103,626,859 |
| Federal and foreign income taxes incurred | | <u>35,980,768</u> |
| Net income | | <u>\$67,646,091</u> |

Capital and Surplus Account

| | | | |
|--|-----------------------------|------------------------------|----------------------|
| Surplus as regards policyholders per report on examination as of December 31, 2000 | | | \$49,544,344 |
| | <u>Gains in Surplus</u> | <u>Losses in Surplus</u> | |
| Net income | \$67,646,091 | \$ 0 | |
| Net unrealized capital gains or (losses) | 4,942,614 | | |
| Change in net deferred income tax | 1,238,125 | | |
| Change in nonadmitted assets | 258,256 | | |
| Change in provision for reinsurance | 411,321 | | |
| Cumulative effect of changes in accounting principles | 3,398,923 | | |
| Surplus adjustments: paid in | 1,844,105 | | |
| Dividends to stockholders | <u> </u> | <u>23,633,382</u> | |
| Total gains and losses | <u>\$79,739,435</u> | <u>\$23,633,382</u> | |
| Net increase (decrease) in surplus | | | <u>56,106,053</u> |
| Surplus as regards policyholders per report on examination as of December 31, 2005 | | | <u>\$105,650,397</u> |

4. LOSSES AND LOSS ADJUSTMENT EXPENSES

The examination liability for the captioned items of \$111,280,406 is the same as reported by the Company as of December 31, 2005. The examination analysis was conducted in accordance with generally accepted actuarial principles and practices and was based on statistical information contained in the Companies internal records and in its filed annual statements.

5. MARKET CONDUCT ACTIVITIES

In the course of this examination, a review was made of the manner in which the Company conducts its business and fulfills its contractual obligations to policyholders and claimants. The review was general in nature and is not to be construed to encompass the more precise scope of a market conduct investigation, which is the responsibility of the Market Conduct Unit of the Property Bureau of this Department.

The general review was directed at practices of the Company in the following areas:

- A. Sales and advertising
- B. Underwriting
- C. Rating
- D. Claims and complaint handling

No problem areas were encountered.

6. COMPLIANCE WITH PRIOR REPORT ON EXAMINATION

The prior report on examination contained six recommendations as follows (page numbers refer to the prior report):

| <u>ITEM</u> | <u>PAGE NO.</u> |
|---|-----------------|
| A. <u>Accounts and Records</u> | |
| 1. <u>Bail Bond Accounting</u> | |
| i. It is recommended that the Company discontinue its current bail bond accounting practices and record only the portions received and establish an unearned premium reserve on that amount. | 11 |
| The Company has complied with this recommendation. | |
| ii. It is recommended that the Company report an unearned premium reserve on its bail bond business in all future filed financial statements. | 11 |
| The Company has complied with this recommendation. | |
| iii. It is recommended that the Company include only reinsurance transactions on Schedule F of its filed financial statements. | 11 |
| The Company has complied with this recommendation. | |
| iv. The Company is not in compliance of Section 243.2(d) of Department Regulation 152 since its managing general agent failed to maintain complete records. It is recommended that the Company require Bail USA to conduct periodic audits of its subagents. It is also recommended that the Company enforce the provisions of its MGA contract relative to the maintenance of records, including collateral records. | 12 |
| The Company has partially complied with this recommendation. A similar comment is made in this report. | |
| 2. <u>Loss Stratification</u> | |
| It is recommended that the Company make an effort to provide the information necessary for the completion of the Department's loss stratification exhibit. | 12-13 |
| The Company provided adequate information for the completion of the Department's loss stratification exhibit. | |

| | |
|-------------|-----------------|
| <u>ITEM</u> | <u>PAGE NO.</u> |
|-------------|-----------------|

| | |
|----------------------------------|--|
| B. <u>Abandoned Property Law</u> | |
|----------------------------------|--|

| | |
|---|----|
| It is recommended that the Company comply with Section 1316 of the New York Abandoned Property Law. | 13 |
|---|----|

The Company has partially complied with this recommendation. A similar comment is made in this report.

7. SUMMARY OF COMMENTS AND RECOMMENDATIONS

| | |
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| <u>ITEM</u> | <u>PAGE NO.</u> |
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| A. <u>Management</u> | |
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| It is recommended that board members who are unable or unwilling to attend meetings consistently should resign or be replaced. | 5 |
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| B. <u>Reinsurance</u> | |
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| It is recommended that the Company comply with Section 1505(d) (2) of the New York Insurance Law and notify the superintendent in writing of its intention to enter into any transactions at least thirty days prior thereto, or such shorter period as may permit, with any person in its holding company system. | 9 |
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| C. <u>Accounts and Records</u> | |
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| i. It is recommended that the Company formalize a cost sharing agreement setting forth provisions that would serve as guidelines to properly allocate, reimburse and settle the cost of shared expenses with Seneca Specialty Insurance Company. The allocation method of shared expenses should be consistent with the provisions of Department Regulation 30. | 13 |
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| ii. It is recommended that in the future, the Company should comply with Section 1316 of the New York Abandoned Property Law and report the proper amount to the Comptroller. | 13 |
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| iii. It is recommended that the Company amend its custodial agreement to include the safeguards and provisions per the NAIC Financial Condition Examiners Handbook, Part 1, Section IV- J. | 14 |
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Appointment No 22521

STATE OF NEW YORK
INSURANCE DEPARTMENT

I, HOWARD MILLS, Superintendent of Insurance of the State of New York,
pursuant to the provisions of the Insurance Law, do hereby appoint:

Jainarine Tilakdharry

as proper person to examine into the affairs of the

SENECA INSURANCE COMPANY, INC.

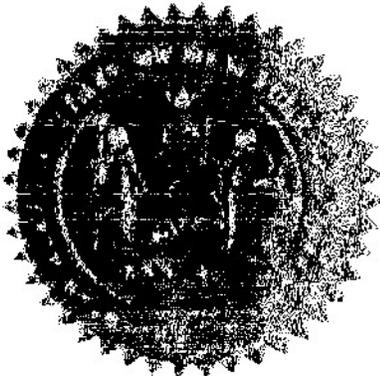
and to make a report to me in writing of the condition of the said

Incorporated

with such other information as he shall deem requisite.

In Witness Whereof, I have hereunto subscribed by the
name and affixed the official Seal of this Department, at
the City of New York,

this 27th day of June, 2006



A handwritten signature in cursive script, appearing to read "Howard Mills".

HOWARD MILLS
Superintendent of Insurance