

REPORT ON EXAMINATION

OF THE

XL INSURANCE COMPANY OF NEW YORK, INC.

AS OF

DECEMBER 31, 2005

DATE OF REPORT

APRIL 27, 2007

EXAMINER

JAMES CALL

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

April 27, 2007

Honorable Eric R. 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 22430 dated October 28, 2005 attached hereto, I have made an examination into the condition and affairs of XL Insurance Company of New York, Inc. as of December 31, 2005, and submit the following report thereon.

Wherever the designations "the Company" or "XLINY" appear herein without qualification, they should be understood to indicate XL Insurance Company of New York, 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 main administrative office located at 70 Seaview Avenue, Stamford, CT 06902-6040.

1. SCOPE OF EXAMINATION

The previous examination was conducted as of December 31, 1999. An examination was conducted as of December 31, 2002; however, it was decided to update the examination to as of December 31, 2005. This examination covered the six-year period from January 1, 2000 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, a New York domiciled insurer, originally known as Great Lakes American Reinsurance Company (“GLARC”) was incorporated under the Laws of New York State on September 23, 1994 and was licensed to transact business on October 1, 1994. At the time of its incorporation in 1994, GLARC was a member of the Munich Reinsurance Group and a wholly-owned subsidiary of the Great Lakes Reinsurance Company (“GLRC”). GLRC was a federal Canadian company, established in 1951, under the laws of the Dominion of Canada. On August 28, 1981, a United States Branch (“Branch”) was established under the laws of the State of New York. The Branch was a wholly-owned subsidiary of GLRC and was under the management of Great Lakes Re Management Corporation, a New York business corporation also wholly-owned by GLRC.

Folksamerica Holding Company and Folksamerica Reinsurance Company filed an application to acquire Great Lakes American Reinsurance Company, which was approved by the Department on July 15, 1997. Effective August 25, 1997, the name of the Company was changed to Folksamerica General Insurance Company. Also in 1997, the Company entered into a transfer and assumption agreement with Folksamerica Reinsurance Company. Under this agreement, all of the assets and liabilities of the Company were transferred to Folksamerica Reinsurance Company. As part of this agreement, the Company entered into a loss portfolio transfer.

On March 5, 1998, X.L. America, Inc. (“XLA”), a U.S. holding company formed by XL Capital Ltd, a Cayman Islands holding company, purchased Folksamerica General Insurance Company. The name was then changed to X.L. Insurance Company of America, Inc. on May 7, 1998 and, effective April 9, 1999, to XL Insurance Company of New York, Inc. (“XLINY”).

On June 18, 1999, XL Capital Ltd acquired NAC Re Corporation (“NAC Re”) in a pooling of interest stock transaction. Subsequent to this acquisition, a reorganization plan was submitted to the Department. As part of this restructuring, NAC Re acquired 100% of the common stock of XLINY from XLA. Effective July 1, 1999, the Company became a participant in an intercompany reinsurance pooling agreement with various affiliated companies, with XL Reinsurance America Inc. functioning as the pool leader.

XLINY was subsequently acquired by XL Reinsurance America Inc. (“XLRA”) in September 1999. In June 2003, the outstanding shares of XLINY were contributed to Greenwich Insurance

Company (“Greenwich”) by XLRA, and then were contributed by Greenwich to XL Insurance America, Inc.

At December 31, 2005, the capital paid in was \$6,000,000 consisting of 400,000 shares of common stock at \$15 par value per share. Gross paid in and contributed surplus was \$63,908,815. Gross paid in and contributed surplus decreased by \$29,937,766 during the examination period, as follows:

<u>Year</u>	<u>Description</u>		<u>Amount</u>
12/31/1999	Beginning gross paid in and contributed surplus		\$93,846,581
2000	Surplus paid-in	\$16,000,000	
2000	Transferred to capital (retirement of repurchased shares)	(65,000,000)	
2002	Surplus paid-in	9,000,000	
2003	Capital contribution from X.L. America, Inc.	<u>\$10,062,234</u>	
	Net decrease during exam period		<u>(29,937,766)</u>
2005	Ending gross paid in and contributed surplus		<u>\$63,908,815</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 nineteen members. The by-laws provide that the board shall have at least two regular meetings, in addition to the annual meeting of the board of directors, in each calendar year. At December 31, 2005, the board of directors was comprised of the following thirteen members:

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Steven Peter Agosta Rye, NY	Vice President and Secretary, NAC Re Corporation
	Vice President, General Counsel and Secretary, XL Reinsurance America Inc.
Richard Stephen Banas Lexington, KY	Senior Vice President, XL Insurance Company of New York, Inc., XL Insurance America, Inc., and Greenwich Insurance Company
Lee Larkin Bennett	Senior Vice President,

Name and ResidencePrincipal Business Affiliation

Avon, CT

XL Insurance Company of New York, Inc.,
 XL Insurance America, Inc. and
 Greenwich Insurance Company

David Brian Duclos
 Exton, PA

President and Chief Executive Officer,
 XL Insurance Company of New York, Inc. and
 XL Insurance America, Inc.

Senior Vice President,
 Greenwich Insurance Company

Janet Ericson Duncan
 West Hartford, CT

Senior Vice President,
 XL Insurance Company of New York, Inc.,
 XL Insurance America, Inc.,
 Greenwich Insurance Company and
 X.L. America, Inc.

Penny Ann Foltz
 Wilmington, DE

Senior Vice President,
 XL Insurance Company of New York, Inc.,
 Greenwich Insurance Company and
 X.L. America, Inc.

Alan Lester Hunte
 Shelton, CT

Vice President and Controller,
 XL Insurance Company of New York, Inc.,
 XL Insurance America, Inc.,
 XL Reinsurance America, Inc. and
 Greenwich Insurance Company

Dennis Patrick Kane
 Island Heights, NJ

Senior Vice President,
 XL Insurance Company of New York, Inc. and
 XL Insurance America, Inc.

President and Chief Executive Officer,
 Greenwich Insurance Company

Robert Paul Klepper
 Asheville, NC

Senior Vice President,
 XL Insurance Company of New York, Inc.,
 XL Insurance America, Inc.,
 Greenwich Insurance Company and
 XL Insurance (Bermuda) Ltd.

Kenneth Peter Meagher
 Ridgefield, CT

Vice President, General Counsel and Secretary,
 XL Insurance Company of New York, Inc.,
 XL Insurance America, Inc. and
 Greenwich Insurance Company

Assistant Secretary,

Name and ResidencePrincipal Business Affiliation

	XL Reinsurance America Inc. Vice President and Assistant Secretary, NAC Re Corporation and X.L. America, Inc.
Richard Harold Miller New Fairfield, CT	Senior Vice President, XL Insurance Company of New York, Inc., XL Insurance America, Inc. and Greenwich Insurance Company Executive Vice President, Chief Financial Officer and Treasurer, NAC Re Corporation and X.L. America, Inc.
David Bruce Porteus Portland, CT	Senior Vice President, XL Insurance Company of New York, Inc., XL Insurance America, Inc. and Greenwich Insurance Company
Michael Allan Zauderer Carmel, NY	Vice President, XL Insurance Company of New York, Inc., XL Insurance America, Inc., Greenwich Insurance Company and XL Reinsurance America Inc. Assistant Treasurer, NAC Re Corporation

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 Lee Larkin Bennett, who attended less than 50% of the meetings for which he 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. A similar recommendation was included in the prior report. It is noted that the board member cited above for poor attendance has since been replaced.

The Company was unable to provide signed statements from each of the members of its board of directors indicating that he or she had received and read the prior report on examination of the Company. Section 312(b) of the New York Insurance Law requires that a copy of the report on examination of the Company “shall be furnished by such insurer or other person to each member of its board of directors and each such member shall sign a statement which shall be retained in the insurer's files confirming that such member has received and read such report.”

It is recommended that the Company furnish each member of the board with a copy of the report on examination and retain a signed statement from each board member that he or she has received and read such report pursuant to the provisions of Section 312(b) of the New York Insurance Law.

Article III, Section 3.01 of the Company’s by-laws states, in part, that “not less than three of the Directors shall be residents of the State of New York.” As of December 31, 2005, only two directors were residents of New York. It is recommended that the Company either ensure that at least three of its directors are residents of the State of New York pursuant to the provisions of Article III, Section 3.01 of its by-laws or that it amend its charter and by-laws to require that only two directors be residents of the State of New York as permitted pursuant to Section 1201(a)(5)(B)(vi) of the New York Insurance Law.

Article III, Section 3.14 of the Company’s by-laws states, in part, that “the Board of Directors shall elect from among its members a Chairman and one or more Vice Chairmen...” As of the examination date, the Company’s board of directors had not elected a chairman or vice chairman. It is recommended that the board of directors elect from among its members a chairman and one or more vice chairmen, pursuant to the provisions of Article III, Section 3.14 of its by-laws.

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

<u>Name</u>	<u>Title</u>
David B. Duclos	President and Chief Executive Officer
Kenneth P. Meagher	Vice President, General Counsel and Secretary
Gabriel G. Carino	Vice President and Treasurer
Richard S. Banas	Senior Vice President
Lee L. Bennett	Senior Vice President
Janet E. Duncan	Senior Vice President
Penny A. Foltz	Senior Vice President
Dennis P. Kane	Senior Vice President

<u>Name</u>	<u>Title</u>
Robert P. Klepper	Senior Vice President
James K. Miller	Senior Vice President
Richard H. Miller	Senior Vice President
David B. Porteus	Senior Vice President

B. Territory and Plan of Operation

As of December 31, 2005, the Company was licensed to write business in thirty-five 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>
3	Accident and health
4	Fire
5	Miscellaneous property
6	Water damage
7	Burglary and theft
8	Glass
9	Boiler and machinery
10	Elevator
11	Animal
12	Collision
13	Personal injury liability
14	Property damage liability
15	Workers' compensation and employers' liability
16	Fidelity and surety
17	Credit
19	Motor vehicle and aircraft physical damage
20	Marine and inland marine
21	Marine protection and indemnity
22	Residual value

The Company is also authorized to write workers' compensation insurance as may be incident to coverages contemplated under paragraphs 20 and 21 of Section 1113(a) of the New York Insurance Law, including insurances described in the Longshoremen's and Harbor Workers' Compensation Act (Public Law No. 803, 69 Cong. as amended; 33 USC Section 901 et seq. as amended).

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 policyholders' surplus in the amount of \$6,400,000 (includes Article 63 requirement). The Company had no direct premiums written during the period under examination.

C. Reinsurance

Assumed reinsurance accounted for 100% of the Company's gross premium written at December 31, 2005. During the examination period, January 1, 2000 through December 31, 2005, the Company wrote no direct business and assumed the following amount of business:

2000	\$41,336,555
2001	47,803,874
2002	45,143,045
2003	19,956,447
2004	25,200,909
2005	<u>23,788,464</u>
Total	<u>\$68,945,820</u>

The business assumed was attributable to the Company's inter-company pooling agreement.

Inter-Company Pooling Agreement

Effective July 1, 1999, the Company participates in an inter-company pooling agreement with various affiliated companies, with XLRA functioning as pool leader. Effective January 1, 2002, the pooling agreement was amended to provide that cessions to the pool would occur on a gross of external reinsurance basis. Effective January 1, 2003 the inter-company pooling agreement was amended to change the pooling percentages. The agreement and subsequent amendments thereto were submitted to and non-disapproved by the Department.

Under the inter-company pooling agreement, 100% of all members' gross premium, losses, insurance expenses and other related underwriting activity of the pool members are ceded to XLRA, except for finite reinsurance produced by XLRA's finite reinsurance business unit and primary financial guaranty. XLRA purchases external reinsurance on behalf or itself and its pool members for business that was written by the pool members and XLRA. Seventy five percent of the premium and losses net of external reinsurance is then ceded to XL Re Ltd (an affiliate) under a quota share

reinsurance treaty. The net after the cession to XL Re Ltd is then pooled and a retrocession made to each pool member in proportion to its pool year participation percentage.

All ceded reinsurance balances related to the external ceded reinsurance contracts are recorded in the statutory financial statements of XLRA, and all reinsurers which are parties to the contracts are included in XLRA's Schedule F. Only XLRA has a contractual right of direct recovery from non-affiliate reinsurers per the terms of the reinsurance agreements placed by XLRA on behalf of itself and its pool members. Any Schedule F penalty is shared by the pool members in accordance with their pool year participation percentages. XLRA and each of the pool members have an option of establishing a "Funds Withheld Balance", which may be maintained until cancellation of the agreement. The Funds withheld balance, pursuant to the pooling agreement, at any given time shall be equal to net premiums due, less net paid losses, and less net underwriting expenses, but exclusive of investment costs.

Pool membership and participation at the beginning and end of the exam period was as follows:

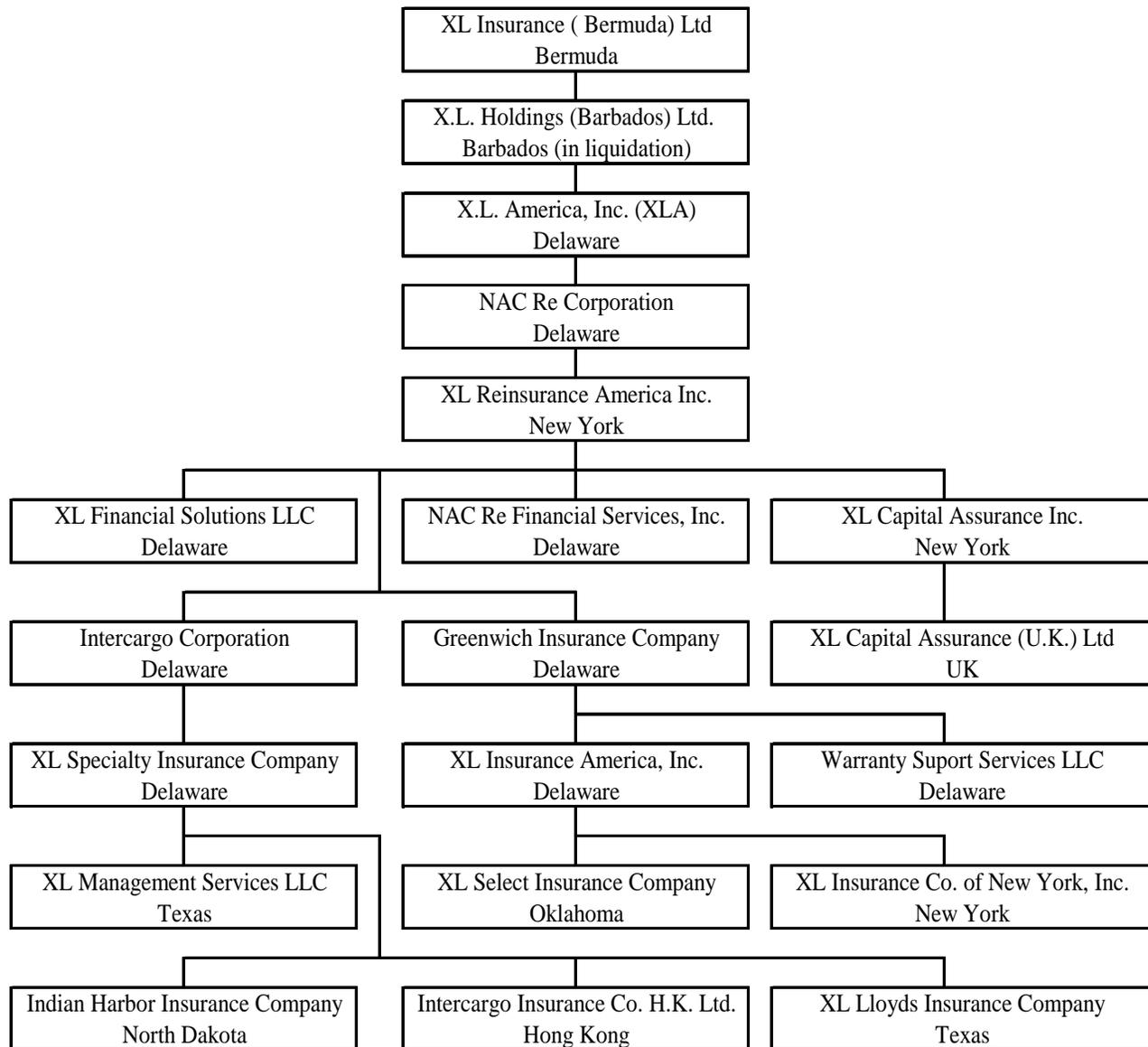
	<u>12/31/1999 –</u> <u>12/31/2002</u>	<u>1/1/2003 –</u> <u>12/31/2005</u>
XL Reinsurance America Inc.	76%	65%
Greenwich Insurance Company	5%	12%
XL Insurance America, Inc.		10%
XL Select Insurance Company		2%
XL Insurance Company of New York, Inc.	7%	3%
XL Specialty Insurance Company	7%	6%
Indian Harbor Insurance Company	5%	2%
Total	100%	100%

D. Holding Company System

The Company is a member of the X.L. America, Inc. Group. The Company is a wholly owned subsidiary of XL Insurance America, Inc., a property and casualty insurance company domiciled in the State of Delaware, which is ultimately controlled by XL Capital Ltd, a Cayman Islands holding company.

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.

A complete organization chart as of December 31, 2005, which details members of the system, is shown in Appendix A. The following is an abridged chart of the holding company system at December 31, 2005:



In addition to the intercompany pooling arrangement previously discussed in the reinsurance section of this report, the Company was a party to the following agreements with other members of its holding company system at December 31, 2005:

Second Amended and Restated General Services Agreement

This agreement is between XLA, the service provider, XLINY and the pool companies, as well as various other affiliated insurance and non-insurance entities of XLA. XLA provides management and general services such as legal and auditing, data processing, and regulatory compliance to the affiliates. The effective date of the agreement is January 1, 2003. The agreement filed with the Department pursuant to Section 1505 of the New York Insurance Law and was found to be non-objectionable.

Amended and Restated General Services Agreement

This agreement is between XL Global Services, Inc., as service provider, XLA with various insurance and non-insurance affiliates, including XLINY. XL Global Services, Inc. is to provide various information technology services, reinsurance services, actuarial services, human resource services and miscellaneous services. The agreement has an effective date of January 1, 2003. The agreement was filed with the Department pursuant to Section 1505 of the New York Insurance Law and non-objected to on January 24, 2003.

Management Agreement

XL Investment Management Ltd. provides investment management, financial advisory and related administrative services to XLINY. XL Investment Management Ltd. has the authority, subject to the terms of the agreement, to act on behalf of the Company in all such matters, including the power to retain and terminate investment managers, agents and subcontractors, pursuant to an agreement substantially in the form of the master investment management agreement appended to this agreement. The agreement was filed with the Department pursuant to Section 1505 of the New York Insurance Law. The agreement was non-objected to on November 8, 2004, but did not become effective until July 26, 2005.

Fifth Amended Tax sharing and Payment Agreement

This tax sharing and payment agreement with an effective date of April 1, 2004 is between XL Insurance America, Inc., the United States parent of XLINY and various insurance and non-insurance affiliates. The agreement was filed with the Department pursuant to Section 1505 of the New York Insurance Law and non-objected to on April 8, 2004.

Department Circular Letter No. 33 (1979) states that intercompany tax settlements should be made within 30 days of the filing the actual consolidated federal corporate income tax return. The Company filed its consolidated tax return on September 15, 2006 (after obtaining an automatic 6 month extension using form 7004). The Company is not in compliance with Circular Letter No. 33 (1979) as the balance was not settled with XL Insurance America, Inc. until December 2006. Additionally, the Company's fifth amended tax sharing and payment agreement stipulates the parent shall pay to each such member, whose losses or tax credits were utilized, its allocable portion of such excess amount within 30 days after the filing of the consolidated return. The Company is not in compliance with the agreement, as settlement of the intercompany balances did not occur until December 2006. It was also noted during the review of general ledger transactions that a payable to XL Insurance America, Inc., related to the 1999 federal tax return, had been outstanding for several years before being paid and thus was not settled according to the tax agreement.

It is recommended that the Company settle its federal income tax related intercompany balances in accordance with Department Circular Letter No. 33 (1979) and the Company's fifth amended tax sharing and payment agreement.

E. Significant Operating Ratios

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

Net premiums written to surplus as regards policyholders	60%	
Liabilities to liquid assets (cash and invested assets less investments in affiliates)	159%	*
Premiums in course of collection to surplus as regards policyholders	13%	
Estimated current reserve deficiency to policyholder surplus	28%	*
Gross Change in Policyholder Surplus	-10%	*
Net Change in Adjusted Policyholder Surplus	-10%	*

The above ratios denoted with an asterisk fall outside the benchmark ranges set forth in the Insurance Regulatory Information System of the National Association of Insurance Commissioners. The liabilities to liquid assets ratio exceeded the NAIC benchmark mainly because approximately 43% of the Company's assets were Funds held by or deposited with reinsured companies, which is not considered a liquid asset. The Company utilizes the Funds Held Account pursuant to its inter-company pooling agreement as described in Section 2(C) "Reinsurance" of this report. Estimated current reserve deficiency to policyholder surplus exceeded the NAIC benchmark of less than 25% as a result of examination adjustments. Prior to the examination adjustments, this ratio was 11%. Both the gross change in policyholder surplus ratio and the net change in adjusted policyholder surplus ratio exceeded the minimum NAIC benchmark of greater than negative 10% as a result of examination changes. Prior to the examination adjustments both of these ratios were calculated at 6%.

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

	<u>Amounts</u>	<u>Ratios</u>
Losses and loss adjustment expenses incurred	\$129,229,694	99.76%
Other underwriting expenses incurred	26,512,373	20.47
Net underwriting loss	(26,204,875)	<u>(20.23)</u>
Premiums earned	\$129,537,192	<u>100.00%</u>

F. Accounts and Records

The Company reports all financial accounting transactions using the Peoplesoft General Ledger application. Statutory financial statements are prepared utilizing the Freedom software package. Enterprise Portfolio System ("EPS") is utilized for the Company's investments. The Company additionally utilizes WINs, Genius and Phoenix as its primary commercial insurance processing systems for U.S. business. Functions include policy and claim administration. These systems also serve as source systems for policy production, financial reporting, and statistical reporting. Systems for reinsurance accounting include Destiny and RSG. Standardized insurance accounting procedures are employed in transactions involving premiums, losses, expenses and valuation of assets and liabilities resulting from the operations of the Company.

During the course of the review of the Company's accounts and records the operational and organizational controls in place were analyzed. In general, it appears the Company has a sufficient

level of controls in place. However, the following record keeping deficiencies were noted during the course of the current examination:

i. Financial Statement Preparation and Disclosure

Management incorrectly posted escheatable funds to “Amounts withheld or retained by company for the account of others.” The escheatable funds should have been reported as “aggregate write ins for liabilities.”

It was also noted during exam that one of the sixteen operating business units within the X.L. America, Inc. Group, the Global Risk operating business unit, had been incorrectly posting cash receipts and disbursements to “Advance premiums.” The Company should instead have been posting to “Remittances and items not allocated.” The Company’s reported accrued retro premium amount in its 2005 Annual Financial Statement, note No. 24 does not agree with the amount reported on page 2 of the statement.

It is recommended that the Company follow the NAIC Annual Statement Instructions when completing its annual statements and classify financial statement items into the proper account.

ii. Documentation Supporting Balance Sheet Amounts

During review of “Other expenses”, it was noted that the Company did not provide the detail to support the banking fees accrual that was part of the “Other expenses” accrual at December 31, 2005.

During the examination review of “Ceded commissions”, the Company was unable to provide valid support for general ledger account No. 208723 - Ceded profit commission (debit balance) in the amount of \$98,625 as of December 31, 2005.

It is recommended that the Company maintain supporting detailed records and produce same upon examination for any amounts it reports in its financial statements, henceforth.

iii. Escheatable Funds

The Company's (negative) abandoned property reports for 2004 and 2005 were not filed pursuant to the provisions of Section 1316 of the New York Abandoned Property Law.

It is recommended that the Company file its abandoned property reports pursuant to the provisions of Section 1316 of the New York Abandoned Property Law.

iv. Settlement of Inter-Company Balances

The Company does not have a comprehensive process in place to age and settle intercompany balances in a timely manner. The detail data making up the intercompany balance transactions is maintained only in the source underwriting systems and the Company does not have a process in place within these subsystems to age the intercompany balances. It was also noted that the Element Reinsurance Ltd. (XL Weather and Energy) balance had not been settled during 2006. The Company has indicated that it would be using a new general ledger system in 2007, which will allow for a greater level of detail to be captured within the general ledger. The Company has initiated a global task force to address the issue as the settlement process involves more than one intercompany account and more than one currency.

It is recommended that the Company develop and implement a comprehensive process to age and settle intercompany account balances in a timely manner.

v. Classification of Expenses

The NAIC Property and Casualty Annual Statement Instructions for Uniform Classifications of Expenses of Property and Casualty Insurers states the following:

- Fees and expenses of examination by insurance departments or other governmental agencies are to be included in “Taxes licenses and fees.” The Company recorded account No. 223018 – “State examination fees under other expenses.”
- Any other taxes not assignable under A, B, C and not otherwise excluded should be recorded in “Taxes, licenses and fees.” The Company reported the accrual for account No. 234110 – “Federal excise taxes in other expenses.”

It is recommended that the Company properly classify expenses according to the NAIC Property and Casualty Annual Statement Instructions for Uniform Classifications of Expenses of Property and Casualty Insurers.

vi. Accounting Issues

During review of the Company’s data files, it was noted that the Company uses various cutoff dates for recognizing written premiums from its operating business units. Although the Company

uses the cutoff dates to recognize its written premium, the Company used the December 31, 2005 date in calculating its unearned premium reserve (“UPR”). This accounting underestimates the Company’s year-end UPR for annual statement reporting purposes. The NAIC Accounting Practices and Procedures Manual Statements of Statutory Accounting Principles, SSAP No. 53, paragraph 5 indicates that:

“written premiums for all other written contracts, excluding workers' compensation contracts, shall be recorded as of the effective date of the contract. Upon recording written premium, a liability, the unearned premium reserve shall be established to reflect the amount of premium for the portion of the insurance coverage that has not expired”.

It is recommended that the Company set up accruals for both written premium and unearned premium reserve that represent the written premium and the unearned premium reserve from the cutoff dates to year-end.

As part of the Company's early close process the Company posts claim payments made after the close of the claims subsystems but before the reporting date, as Remittances and items not allocated. According to SSAP No. 67, paragraph 9, the Remittances and items not allocated account is for unidentified cash receipts otherwise known as suspense accounts. Claim payments made subsequent to the subsystem closing, but prior to the reporting date should be recorded as adjusting entries to the claim reserves at year-end.

It is recommended that the Company properly classify claims paid after the early close as reductions to outstanding loss reserves and not as “Remittances and items not allocated”.

Per results of the examination’s premium data testing, it was noted that the X.L. America, Inc. Group incorrectly posted advanced premiums. Both the XL Global Risk and XL Programs operating business units record premium with effective dates after year-end as written premium. The written premium was offset by unearned premium for the same amount. The SSAP No. 53, paragraph 13 states that:

“Advanced premiums result when the policies have been processed, and the premium has been paid prior to the effective date. These advance premiums are reported as a liability in the statutory financial statements and not considered income until due. Such amounts are not included in written premium or the unearned premium reserve.”

It is recommended that the Company comply with SSAP No. 53, paragraph 13 when recording advance premiums.

vii. CPA Contract

The Company's contract with its external auditors for 2005 was not in compliance with the requirements of Department Regulation 118, as it did not contain all the required language nor was it executed by both parties.

It is recommended that the Company ensure that all future contracts entered into with its independent certified public accountants comply with Department Regulation 118 and are properly executed.

viii. Directors and Officer ("D&O") Coverage – Regulation 110

XL Capital Ltd, the ultimate parent company of XLINY has a D&O indemnity policy covering the Company. The certificate of insurance as shown does not contain coinsurance amounts for directors and officers as required by Department Regulation 110.

The Company is subject to the requirements of Department Regulation 110 under Part 72.1(c) which states that:

"Retention amounts and coinsurance are both required, in accordance with this Part, for D&O indemnification policies issued to corporations formed under the Insurance Law, Religious Corporations Law, Cooperative Corporations Law, Transportation Corporations Law, or any other law of this state, where provisions of such laws make such corporations subject to BCL section 727 or N-PCL section 727."

The directors and officers policy covering the Company is not in compliance with Department Regulation 110 regarding the minimum coinsurance percentage amount specified in Part 72.4.

It is recommended that the directors and officers policy covering the Company be brought into compliance with Department Regulation 110 regarding the minimum coinsurance percentage for D&O indemnity coverage as specified in Part 72.4 as regards the New York domiciled insurers.

ix. Information Systems Review

The following weaknesses were noted during the review of the Company's Information Technology ("IT") systems and controls:

- The Company's WINS IT system does not make use of automated tools to ensure that the source code used corresponds to the most recent version of the program; and, the Company's Financial Data Repository ("FDR") application does not use automated controls for checking out and checking in source code to ensure that only one programmer modifies a program's source code. Lack of strong controls around production source code increases the risk of unauthorized access and use of the automated systems.
- During the period under examination, it was noted during review and testing, the Company had weak access controls. Weak access controls increase the risk of unauthorized access to computing resources that could result in compromising servers, storage tapes, and sensitive data that is present in the server room.
- Internal audit noted that the claims department maintains a manual diary, and recommended that the diary/log should be electronic to facilitate the consistent tracking of claims files for review, and to provide for the future expansion of the Department. Management indicated that an electronic diary is planned for implementation during the first quarter of 2006.
- During the review of documentation controls for one application, it was noted that the organization does not have a documentation standards manual; utilize a documentation check-off list and specify a minimum level of documentation to ensure that all required documentation is prepared, approved, and maintained for all systems and/or programs. Documentation controls help ensure that accurate and relevant documentation is prepared for all new systems and for changes to existing systems and/or programs.
- During the review of the Company's system security authorization process, it was noted that the Company does not use a system security authorization form, but alternatively relies on the new hire process to evidence initial access approval, and thereafter, on the periodic re-certification process to ensure user access is commensurate with job responsibilities. For 55 of 76 (72%) users tested, the Company could not provide supporting documentation to enable testing. Consequently, the sample error rate was too high to permit calculation of an upper error limit for the attributes associated with this test.
- Additionally, during the review of the Company's application security authorization process, it was noted that the Company does not use a standard process to document user application access. One application uses an application authorization form. Another application uses a different form to authorize initial access. No evidence was provided to indicate that six other applications use an application authorization form. For 45 of 76 (59%) users tested, the Company did not provide supporting documentation to enable testing. Consequently, the sample error rate was too high

to permit calculation of an upper error limit for the attributes associated with this test.

- The review of the Company's Sarbanes Oxley ("SOX") testing revealed that weekly virus scans were not run for all weeks in a recent month for three of the ten users sampled. The Company could incur risks associated with the loss and corruption of data, disclosure of sensitive information, and productivity losses associated with reduced service levels, and platform and data recovery efforts.
- During the review of the Company's business contingency plan, the IT examiners noted that the plans for a number of the Company's facilities are not current or complete. In one case, issues identified during 2003 walkthroughs of the plans remained open. In one other case, plans for that facility were not available. Without current and complete business continuity plans, the Company is at risk of being unable to recover and/or function in a timely manner from a disaster.
- During the review of the Company's documentation for disaster recovery, the IT examiners noted that the Company did not have a comprehensive, executable disaster recovery plan. Additionally, the list of applications to be recovered was incomplete, and did not contain data from four critical applications. The names of specific individuals authorized to declare a disaster on behalf of the Company was not documented in the plan and the Company's WAN was not tested in 2005. Review of internal audit reports revealed that one financially significant application disaster recovery plan was last tested two years ago and a formally documented disaster recovery plan was unavailable for another application.

It is recommended that the Company address the weaknesses noted in the IT review, as noted above, in order to strengthen controls and security within its IT environment.

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:

<u>Assets</u>	<u>Examination</u>		<u>Company</u>		Surplus Increase (Decrease)
	<u>Assets</u>	Assets Not <u>Admitted</u>	Net Admitted <u>Assets</u>	Net Admitted <u>Assets</u>	
Bonds	\$52,012,924	\$ 0	\$52,012,924	\$52,012,924	\$ 0
Cash, cash equivalents and short-term investments	2,709,099	0	2,709,099	2,709,099	0
Investment income due and accrued	318,762	0	318,762	318,762	0
Uncollected premiums and agents' balances in the course of collection	7,200,924	1,836,520	5,364,404	5,501,214	(136,810)
Deferred premiums, agents' balances and installments booked but deferred and not yet due	13,123,365	0	13,123,365	13,123,365	0
Accrued retrospective premiums	200,137	20,014	180,123	200,137	(20,014)
Funds held by or deposited with reinsured companies	61,883,578	0	61,883,578	59,416,708	2,466,870
Net deferred tax asset	10,680,971	6,515,137	4,165,834	4,647,639	(481,805)
Guaranty funds receivable or on deposit	244,632	0	244,632	244,632	0
Receivables from parent, subsidiaries and affiliates	7,074	0	7,074	7,074	0
Aggregate write-ins for other than invested assets	<u>859,454</u>	<u>127,159</u>	<u>732,295</u>	<u>809,530</u>	<u>(77,235)</u>
Totals assets	<u>\$149,240,920</u>	<u>\$8,498,830</u>	<u>\$140,742,090</u>	<u>\$138,991,084</u>	<u>\$1,751,006</u>

Liabilities, Surplus and Other Funds

<u>Liabilities</u>	<u>Examination</u>	<u>Company</u>	Surplus Increase (Decrease)
Losses and loss adjustment expenses	\$73,244,623	\$66,438,646	\$(6,805,977)
Reinsurance payable on paid losses and loss adjustment expenses	1,148,198	1,148,198	0
Commissions payable, contingent commissions and other similar charges	754,224	643,021	(111,203)
Other expenses (excluding taxes, licenses and fees)	2,284,299	2,284,299	0
Taxes, licenses and fees (excluding federal and foreign income taxes)	826,258	826,258	0
Current federal and foreign income taxes	276,989	276,989	0
Unearned premiums	12,409,863	12,331,531	(78,332)
Advance premiums	3,073,487	3,073,487	0
Amounts withheld or retained by company for account of others	55,201	55,201	0
Remittances and items not allocated	(4,923,768)	(4,923,768)	0
Provision for reinsurance	3,907,781	3,517,354	(390,427)
Payable to parent, subsidiaries and affiliates	2,508,590	2,508,590	0
Aggregate write-ins for liabilities	<u>3,831,692</u>	<u>3,799,540</u>	<u>(32,152)</u>
Total liabilities	<u>\$99,397,437</u>	<u>\$91,979,346</u>	<u>\$(7,418,091)</u>
 <u>Surplus and Other Funds</u>			
Common capital stock	\$6,000,000	\$6,000,000	\$ 0
Gross paid in and contributed surplus	63,908,815	63,908,815	0
Unassigned funds (surplus)	<u>(28,564,162)</u>	<u>(22,897,077)</u>	<u>(5,667,085)</u>
Surplus as regards policyholders	<u>\$41,344,653</u>	<u>\$47,011,738</u>	<u>\$(5,667,085)</u>
 Total liabilities, surplus and other funds	 <u>\$140,742,090</u>	 <u>\$138,991,084</u>	 <u>\$ 1,751,006</u>

NOTE: The Internal Revenue Service (“IRS”) has completed its audits of the Company’s consolidated Federal Income Tax returns through tax year 2002. All material adjustments, if any, made subsequent to the date of examination and arising from said audits, are reflected in the financial statements included in this report. There are no current IRS tax audits. The Internal Revenue Service has not yet begun to audit tax returns covering tax years 2003 through 2005. 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 \$28,493,405 during the six-year examination period January 1, 2000 through December 31, 2005, detailed as follows:

Underwriting Income

Premiums earned		\$129,537,192
Deductions:		
Losses and loss adjustment expenses incurred	\$129,229,694	
Other underwriting expenses incurred	26,389,394	
Aggregate write-ins for underwriting deductions	<u>122,979</u>	
Total underwriting deductions		<u>155,742,067</u>
Net underwriting gain or (loss)		\$(26,204,875)

Investment Income

Net investment income earned	\$20,669,789	
Net realized capital gain	<u>(508,998)</u>	
Net investment gain or (loss)		20,160,791

Other Income

Net gain or (loss) from agents' or premium balances charged off	\$13,703	
Aggregate write-ins for miscellaneous income	<u>2,003,570</u>	
Total other income		<u>2,017,273</u>
Net income before dividends to policyholders and before federal and foreign income taxes		\$(4,026,811)
Dividends to policyholders		<u>6,959</u>
Net income after dividends to policyholders but before federal and foreign income taxes		\$(4,033,770)
Federal and foreign income taxes incurred		<u>(2,561,508)</u>
Net Income		<u>\$(1,472,262)</u>

C. Capital and Surplus Accounts

Surplus as regards policyholders per report on examination as of December 31, 1999			\$11,368,990
	<u>Gains in Surplus</u>	<u>Losses in Surplus</u>	
Net income		\$ 1,472,262	
Change in net deferred income tax		3,633,511	
Change in nonadmitted assets		575,615	
Change in provision for reinsurance		3,092,868	
Cumulative effect of changes in accounting principles	\$ 1,238,940		
Surplus adjustments paid in	35,062,234		
Surplus adjustments transferred to capital (stock dividend)		65,000,000	
Change in treasury stock	65,000,000		
Change in funds held under reinsurance treaties	2,466,870		
Aggregate write-ins for gains and losses in surplus	<u>0</u>	<u>18,125</u>	
Total gains or losses in surplus	<u>\$103,768,044</u>	<u>\$73,792,381</u>	
Net increase (decrease) in surplus			<u>29,975,663</u>
Surplus as regards policyholders per report on examination as of December 31, 2005			<u>\$41,344,653</u>

4. **UNCOLLECTED PREMIUMS AND AGENTS' BALANCES IN THE COURSE OF COLLECTION**

The examination admitted asset of \$5,364,404 is \$136,810 less than the \$5,501,214 reported by the Company as of December 31, 2005. During the review of Agents' balances, it was noted that the Company failed to book \$2,857,495 for the XL Specie OBU as a 90 day overdue balance at December 31, 2005. This is a pooled amount of which the XLINY had a 3% share or \$85,725.

The Company was not able to age the agents' balance for Vianet Program in the OBU XL Programs due to a lack of policy level detail received from the MGA. Therefore, the total balance of \$1,702,841 for Vianet Program has been non-admitted. The Company's share of this pooled amount was \$51,085.

It is recommended that the Company ensure that they post all non-admitted premium receivable balances in compliance with SSAP No. 6.

5. ACCRUED RETROSPECTIVE PREMIUMS

The examination admitted asset of \$180,123 is \$20,014 less than the \$200,137 reported by the Company as of December 31, 2005. SSAP No. 66, paragraph 9 requires that the Company, at a minimum, non-admit either 10% or an amount calculated using factors listed under Section d of paragraph 9 of any accrued retrospective premiums not offset by retrospective return premiums, other liabilities to the same party (other than loss and loss adjustment expense reserves), or collateral, not otherwise used. It was noted during review that the Company could not provide documentation to determine if there were offsets. The examination has non-admitted 10% of the reported balance of \$6,671,231 to comply with the requirements of SSAP No 66, paragraph 9. The Company's share of the pooled adjustment of \$667,123 is 3% or \$20,014.

It is recommended that the Company perform a review each year to determine if any accrued retrospective premiums should be non-admitted per the requirements of SSAP No. 66, paragraph 9 and that the Company retain the necessary documentation to substantiate the recorded balance.

6. FUNDS HELD BY OR DEPOSITED WITH REINSURED COMPANIES

The examination admitted asset of \$61,883,578 is \$2,466,870 more than the \$59,416,708 reported by the Company as of December 31, 2005. During the exam period, XL Reinsurance America Inc. over ceded a total of \$172,486,819 in reserves (on a pooled basis that was associated mainly with the 2003 accident year), to XL Re Ltd., an affiliate. The over-cession pertained to a 75% quota share agreement in effect between XL Re Ltd and XL Reinsurance America Inc. on behalf of itself and its pool members. Part of the correcting entries made by XLRA in 2006 was to increase "Reinsurance amounts recoverable from reinsurers" by \$82,229,016 of which XLINY has a 3% pooling share. Pursuant to the Company's pooling agreement, settlements of pooled balances are run through the Company's Funds held account. Overall surplus effect to the pool was a decrease of \$90,257,803. See Section 9 "Losses and loss adjustment expenses" for additional information.

It is recommended that the Company take steps to implement controls to ensure future cessions are allocated correctly and ensure that future financial statements are completed correctly in compliance with the NAIC Annual Statement Instructions.

7. NET DEFERRED TAX ASSET

The examination admitted asset of \$4,165,834 is \$481,805 less than the \$4,647,639 reported by the Company as of December 31, 2005.

The examination calculation is based upon SSAP No. 10, as modified by Department Regulation 172. Based on XLINY's September 30, 2005 Quarterly Statement, its gross Deferred Tax Asset ("DTA") as of December 31, 2005 would be limited to \$4,165,834.

It is recommended that the Company calculate its "Net deferred tax asset" in accordance with SSAP No. 10, as modified by Department Regulation 172.

8. AGGREGATE WRITE-INS FOR OTHER THAN INVESTED ASSETS

The examination admitted asset of \$ 732,295 is \$77,235 less than the \$809,530 reported by the Company as of December 31, 2005. It was noted during the review of the Company's deductible recoverable that thirty-four of the balances had negative receivable amounts. Twelve of these were in the Genius system and twenty-two were from the old GAIN system. The Company acknowledged that the negative recoverable balances occur when the cash received does not exactly match the balance outstanding or where there needs to be additional investigation and clean-up done as it appears that cash may have been applied to the wrong claim number or the Company has received cash that was applied in Genius when the corresponding claim entry was made in GAIN.

The examination also noted that the Company had balances in Genius of \$2,496,493 and in GAIN of \$195,463.79, which were over 90 days past due. These amounts were non-admitted for examination purposes in accordance with SSAP No. 65, paragraph 37, which states that "Deductible recoverables that are greater than ninety days old shall be non-admitted." After application of cash received that was not processed against these balances of \$117,447, the non-admitted portion for the pool was \$2,574,510. The Company's portion of this balance was \$77,235.

It is recommended that the Company comply with SSAP No. 65, paragraph 37, and non-admit uncollateralized recoverables with balances over 90 days past their contractual due date, or billing date if no contractual due date has been established.

9. LOSSES AND LOSS ADJUSTMENT EXPENSES

The examination liability for the captioned items of \$73,244,623 is \$6,805,977 more than the \$66,438,646 reported by the Company in its December 31, 2005, filed annual statement. The examination change is due to the following:

As noted in Section 6 “Funds held by or deposited with reinsured companies” above, during the exam period, XL Reinsurance America Inc. over-ceded a total of \$172,486,819 in reserves (on a pooled basis), to XL Re Ltd, an affiliate. The over-cession pertained to a 75% quota share agreement in effect between XL Re Ltd and XL Reinsurance America Inc. on behalf of itself and its pool members. The Company made correcting entries in 2006. The Company’s share of the \$172,486,819 was \$5,174,605.

As disclosed in Notes to Financial Statements No. 25 of the Company’s 2006 Annual Statement, the Company reserves showed a deficiency after taking into account the one time adjustment associated with the over-cession. Based on a review of the deficiency, the examination has increased the liability for losses for the pooled companies by \$32,325,000. The Company’s portion of the increase was \$975,000.

Review of XL Capital Group Internal Audit Department reports noted a finding relating to re-allocation of ceded Incurred by not reported (“IBNR”) losses, disclosed in a report dated July 6, 2005. This finding described a company practice of re-allocating the portion of ceded IBNR attributable to insolvent reinsurers, to solvent reinsurers, thereby taking credit in Schedule F and as part of this captioned liability for IBNR recoverables due from insolvent reinsurers.

Further examination inquiry into this issue resulted in the Company providing supporting documentation detailing re-allocated IBNR totaling \$21,879,054 in the 2005 Annual Statement Schedule F, and \$13,435,545 in the 2004 Schedule F. The Company stated that no re-allocation was made in 2003. The recognition of reinsurance recoverable assets or recoverable liabilities due from insolvent reinsurers is contrary to the requirements of SSAP No. 62, paragraphs 17, 26 and 58.

The Company provided a schedule detailing the ceded IBNR balances due from insolvent reinsurers at December 31, 2005 and December 31, 2004, along with a listing of solvent reinsurers to whom balances were re-allocated. According to management, the Company wrote off IBNR balances due from insolvent reinsurers in the amount of \$29,190,276 in 2006 and discontinued this

practice. The write-off included the reallocated balances carried at December 31, 2005 as well as current balances reported in the first six months of 2006. The Company's portion of the \$21,879,054 for 2005 was \$656,372.

It is recommended that the Company comply with SSAP No. 62, paragraphs 17, 26 and 58 by not taking credit in Schedule F and the loss reserve liability for ceded IBNR recoverables due from insolvent reinsurers.

The examination analysis of the loss and loss adjustment expense reserves was conducted in accordance with generally accepted actuarial principles and was based on statistical information contained in the Company's internal records and in its filed annual statements.

10. COMMISSIONS PAYABLE

The examination liability of \$754,224 is \$111,203 more than the \$643,021 reported by the Company in its December 31, 2005, filed annual statement. XLINY was unable to provide valid support for general ledger account #208723 - Ceded profit commission (debit balance) in the amount of \$3,287,498 as of December 31, 2005. The Company's portion of this pooled account was \$98,625.

Also, the Company did not accrue for the profit sharing commission payable to Heartland Crop for the Crop Hail and MPCl business written in 2005. Heartland Crop had a 45% profit sharing commission on the business. The estimated liability for the profit sharing commission due on 2005 business was \$11,180,443 before reinsurance. After the 85% quota share and the 75% quota share with XL Re Ltd, the net liability for the pool should have been \$419,266. The Company's portion of this pooled account was \$12,578.

It is recommended that the Company establish proper procedures to ensure that it records proper accruals for its obligations and maintain adequate records to support account balances recorded in the general ledger and in financial statements filed with this Department.

11. UNEARNED PREMIUMS

The examination liability of \$12,409,863 is \$78,332 more than the \$12,331,531 reported by the Company in its 2005 filed annual statement. It was noted during the examination that the Company incorrectly calculated unearned premiums reserve (“UPR”) for the XL Professional OBU on "run-off" policies. The Company underwrites directors and officers liability, employment practices liability and insurance agents/brokers/company errors and omissions coverages. Run-off policies occur when an event changes the original make-up of the company (i.e. acquisition, change of Board members or merger), which causes the original board of directors to be left without D&O coverage. The original D&O policy goes into run-off upon the trigger event and the unearned premium is returned to the client. A run-off premium is charged to provide an extended reporting period, normally for three to six years, for coverage to the directors for the original policy period up to the date of the event. This is done because the exposure period is in the past, and the policy premium received for the run-off policy is not subject to the return premium process. The run-off endorsement states that the premium is fully earned on the date of the event and will not be returned to the client if the endorsement is cancelled. The Company was not carrying any UPR on this type of policy. This is contrary to the requirements of SSAP No. 65, paragraph 7 that states:

“When a reporting entity issues an extended reporting endorsement or contract and the preceding claims made policy terminates, the reporting entity assumes liability for unreported claims and expense.”

It further states that:

“For coverage for a fixed period, premium shall be earned over the term of the fixed period, the reporting entity shall establish an unearned premium reserve for the unexpired portion of the premium and shall record losses as reported.”

The Company provided the examination with its underwriting and actuarial pricing assumptions, which showed a six-year earnings pattern that earns premiums 90% in the first year, 6% in the second year, and 1% per year in each of the remaining four years. The examination’s consulting actuary reviewed the Company's earning pattern and the examination has accepted the assumptions for examination purposes. This treatment was also found to be consistent with the guidance in SSAP No. 53, paragraph 6, Property and Casualty Contracts. Based on the Company’s assumptions, the recalculated UPR, after taking into account the 75% quota share was \$2,611,083

higher than what the Company had booked on a pooled basis. XLINY's portion of the \$2,611,083 amount was \$78,332.

It is recommended that the Company comply with the SSAP No. 65, paragraph 7 and SSAP No.53, paragraph 6 in the calculation of unearned premium reserve for its "run off" policies.

12. PROVISION FOR REINSURANCE

The examination liability of \$3,907,781 is \$390,427 more than the \$3,517,354 reported by the Company in its 2005 filed annual statement. Reinsurance recoverables for all XL America pool members are reported in XLRA's Schedule F, in accordance with the XL America Group reinsurance pooling agreement. In the case of a voluntary pool, which the Company's affiliate Greenwich Insurance Company is a member, ceded reinsurance contracts for the accounts named Associated Aviation Underwriters or Associated Aerospace Underwriters ("AAU") as the named reinsured. Letters of credit ("LOC") securing losses recoverable due from unauthorized reinsurers of the AAU pool similarly name Associated Aviation Underwriters or Associated Aviation Underwriters, Inc. (pool manager) as the beneficiary.

The Company reported paid loss recoverables due from authorized reinsurers of AAU, totaling \$18,247,000 as of December 31, 2005. These balances were reported as current receivables in XLRA's Schedule F, Part 4. Examination of XLRA's monthly recoverable roll forward reports and AAU account statements, determined that the entire amount was over 90 days old at December 31, 2005.

XLRA reported total reinsurance recoverables for authorized and unauthorized AAU reinsurers of \$121,598,106 in its 2005 annual statement Schedule F, Part 3. No provision for reinsurance for the AAU account was included in its 2005 Annual Statement since it considered all authorized balances to be current and unauthorized balances to be covered by LOC's. Re-calculation of the aging of paid recoverables determined that 100% of the balance was over 90 days old. Taking these factors into account, recalculation of the provision for reinsurance for AAU accounts resulted in an addition to the provision of \$13,014,246. This recalculation included provisions for overdue authorized reinsurance and unsecured unauthorized balances. XLINY's portion of this balance was \$390,427.

13. AGGREGATE WRITE-INS FOR LIABILITIES

The examination liability of \$3,831,692 is \$32,152 more than the \$3,799,540 reported by the Company in its December 31, 2005, filed annual statement.

The Company did not accrue for services rendered by KPMG at December 31, 2005. KPMG was engaged in 2005 to perform audits of claims processing and procedures. KPMG was paid \$1,071,748 for the services in March 2006. The accrual is on a pooled basis, of which XLINY's portion amounted to \$32,152.

14. COMPLIANCE WITH PRIOR REPORT ON EXAMINATION

The prior report on examination contained fifteen recommendations and one comment as follows (page numbers refer to the prior report):

<u>ITEM</u>	<u>PAGE NO.</u>
A. <u>Management</u>	
i. It is recommended that the Company comply with its charter by having at least two regular meetings of the board of directors, in addition to the annual meeting of the stockholders.	5
The Company has complied with this recommendation.	
ii. It is recommended that the Company comply with its charter and by-laws by electing the board members at their annual stockholders' meeting.	6
The Company has complied with this recommendation.	
iii. It is recommended that the Company comply with its charter and only take action via written consent in those situations where time is of the essence and not in lieu of a regularly scheduled meeting.	6
The Company has complied with this recommendation.	
iv. It is recommended that the Company comply with Section 1411(a) of the New York Insurance Law and have all investments approved by its board of directors.	6
The Company has complied with this recommendation.	

<u>ITEM</u>	<u>PAGE NO.</u>
v. It is also recommended that a detailed list of purchases and sales of investments be attached to the minutes.	6
The Company has complied with this recommendation.	
B. <u>Holding Company System</u>	
i. It is recommended that the Company follow the annual statement instructions when completing Schedule Y of the annual statement and include all required affiliates.	9
The Company has complied with this recommendation.	
ii. It is recommended that the Company submit all amendments to the pooling agreement to the Department for approval.	10
The Company has complied with this recommendation.	
C. <u>Accounts and Records</u>	
i. It is recommended that the Company file a revised Section 325(b) plan with the Department setting forth where the Company maintains its records. Subsequent to the examination, in April 2001 the Company submitted a revised Section 325(b) to the Department.	13
The Company has complied with this recommendation.	
ii. It is recommended that the Company institute a disaster recovery plan.	14
The Company has complied with the recommendation.	

15. SUMMARY OF COMMENTS AND RECOMMENDATIONS

<u>ITEM</u>	<u>PAGE NO.</u>
A. <u>Management</u>	
i. It is recommended that board members who are unable or unwilling to attend meetings consistently should resign or be replaced. It is noted that the board member cited above for poor attendance has since been replaced.	6
ii. It is recommended that the Company comply with Section 312(b) of the New York Insurance Law by furnishing each member of the board a copy	7

ITEMPAGE NO.

of the report on examination and retaining a signed statement from each board member that he or she has received and read such report.

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|----------------------------------|---|----|
| iii. | It is recommended that the Company either ensure that at least three of its directors are residents of the State of New York pursuant to the provisions of Article III, Section 3.01 of its by-laws or that it amend its charter and by-laws to require that only two directors be residents of the State of New York as permitted pursuant to Section 1201(a)(5)(B)(vi) of the New York Insurance Law. | 7 |
| iv. | It is recommended that the Company comply with the provisions set forth in Article III, Section 3.14 of its by-laws, which requires the board of directors to elect from the among its members a chairman and one or more vice chairmen. | 7 |
| B <u> Holding Company </u> | | |
| | It is recommended that the Company settle their federal income tax related intercompany balances in accordance with Department Circular Letter No. 33 (1979) and the Company's fifth amended tax sharing and payment agreement. | 13 |
| C. <u> Accounts and Records </u> | | |
| i. | It is recommended that the Company follow NAIC Annual Statement Instructions when completing its annual statements and classify financial statement items into the proper account. | 15 |
| ii. | It is recommended that the Company maintain supporting detailed records and produce same upon examination for any amounts it reports in its financial statements, henceforth. | 15 |
| iii. | It is recommended that the Company file its abandoned property report pursuant to the provisions of Section 1316 of the New York Abandoned Property Law. A similar recommendation was made in the prior report on examination. | 16 |
| iv. | It is recommended that the Company develop and implement a comprehensive process to age and settle inter-company account balances in a timely manner. | 16 |
| v. | It is recommended that the Company properly classify expenses according to the NAIC Property and Casualty Annual Statement Instructions for Uniform Classifications of Expenses of Property and Casualty Insurers. | 16 |

<u>ITEM</u>	<u>PAGE NO.</u>
vi. It is recommended that the Company set up accruals for both written premium and unearned premium reserve that represent the written premium and unearned premium reserve from the cutoff dates to year-end.	17
vii. It is recommended that the Company properly classify claims paid after the early close as reductions to outstanding loss reserves and not as “Remittances and items not allocated”.	17
viii. It is recommended that the Company comply with SSAP No. 53, paragraph 13 when recording advance premiums.	18
ix. It is recommended that the Company ensure that all future contracts entered into with its independent Certified Public Accountants comply with Department Regulation 118 and are properly executed.	18
x. It is recommended that the directors and officers policy covering the Company be brought into compliance with Department Regulation 110 regarding the minimum coinsurance for D&O indemnity coverage as specified in Part 72.4 as regards the New York domiciled insurers.	18
xi. It is recommended that the Company address the weaknesses noted in the IT review in order to strengthen controls and security within its IT environment.	20
D. <u>Uncollected Premiums and Agents’ Balances in the Course of Collection</u>	
It is recommended that the Company ensure that they post all non-admitted premium receivable balances in compliance with SSAP No. 6.	24
E. <u>Accrued Retrospective Premiums</u>	
It is recommended that the Company perform a review each year to determine if any accrued retrospective premiums should be non-admitted per the requirements of SSAP No. 66, paragraph 9 and that the Company retain the necessary documentation to substantiate the recorded balance.	25
F. <u>Funds Held By or Deposited with Reinsured Companies</u>	
It is recommended that the Company take steps to implement controls to ensure future cessions are allocated correctly and ensure that future financial statements are completed correctly in compliance with the NAIC Annual Statement Instructions.	25

<u>ITEM</u>	<u>PAGE NO.</u>
G. <u>Net Deferred Tax Asset</u>	
It is recommended that the Company calculate its Net Deferred Tax Asset in accordance with SSAP No. 10, as modified by Department Regulation 172.	26
H. <u>Aggregate Write-ins for Other than Invested Assets</u>	
It is recommended that the Company comply with SSAP No. 65, paragraph 37 and non-admit uncollateralized recoverables with balances over 90 days past their contractual due date, or billing date if no contractual due date has been established.	26
I. <u>Losses and Loss Adjustment Expenses</u>	
It is recommended that the Company comply with SSAP No. 62, paragraphs 17, 26 and 58 by not taking credit in Schedule F and the loss reserve liability for ceded IBNR recoverables due from insolvent reinsurers.	28
J. <u>Commissions Payable</u>	
It is recommended that the Company establish proper procedures to ensure that it records proper accruals for its obligations and maintain adequate records to support account balances recorded in the general ledger and in financial statements filed with this Department.	28
K. <u>Unearned Premium Reserve</u>	
It is recommended that the Company comply with SSAP No. 65, paragraph 7 and SSAP No. 53, paragraph 6 in the calculation of unearned premium reserve for its “run off” policies.	30

APPENDIX A

	JURISDICTION
XL Capital Ltd	Cayman
EXEL Holdings Limited	Cayman
EXEL Acquisition Ltd.	Cayman
GCR Holdings Limited (<i>in liquidation</i>)	Cayman
Reeve Court Holdings Ltd	Bermuda
X.L. Property Holdings Limited	Bermuda
XL Insurance (Bermuda) Ltd	Bermuda
XL Weather & Energy Ltd (<i>formerly Element Reinsurance Ltd</i>)	Bermuda
XL PP Limited	UK
InQuisCapital Holdings (Bermuda) Limited	Bermuda
InQuisLogic (Bermuda) Limited	Bermuda
RiskConnect Limited	Bermuda
Sovereign Risk Insurance Ltd. (50%)	Bermuda
XL International (Bermuda) Ltd (<i>formerly XL Winterthur International (Bermuda) Ltd</i>) (91%)	Bermuda
XL International Services Ltd (<i>formerly XL Winterthur International Services Ltd</i>)	Bermuda
International Insurance Consulting Services Limited	Bermuda
XL (Brazil) Holdings Ltda (<i>formerly Winterthur Administracao e Participacoes Ltda</i>)	Brazil
XL Insurance (Brazil) Seguradora S/A (<i>formerly Winterthur International Brasil Seguradora S/A</i>)	Brazil
XL Capital Products Ltd	Bermuda
XL Financial Assurance Ltd. (87%)	Bermuda
Reformation Group, Ltd. (<i>In Members' Voluntary Liquidation</i>)	Bermuda
XL Financial Solutions Ltd	Bermuda
XL Services (Bermuda) Ltd	Bermuda
XL Life Ltd	Bermuda
Reeve Court General Partner Limited	Bermuda
Reeve Court 4 Limited Partnership	Bermuda
Reeve Court 6 Limited Partnership	Bermuda
XL Gracechurch Limited	UK
XL Insurance (UK) Holdings Limited (<i>formerly XL Winterthur (UK) Holdings Limited</i>) (42.33%)	UK
XL Financial Holdings (Ireland) Limited	R of Ireland
X.L. Holdings (Barbados) Ltd. (<i>In Liquidation</i>)	Barbados
X.L. America, Inc. (*)	Delaware
XL Capital Investment Partners Inc.	Delaware
XLCA Admin LLC	New York
XLCDS LLC	New York
XL Weather & Energy Advisors Inc. (<i>formerly Element Re Advisors Inc.</i>)	Delaware
XL Weather & Energy Inc. (<i>formerly Element Re Capital Products Inc.</i>)	Delaware
XLA Garrison L.P.	Delaware
Global Credit Analytics, Inc.	Delaware
NAC Re Corporation	Delaware
XL Reinsurance America Inc. *(A-65%) - NY	New York
XL Financial Solutions, LLC	Delaware
Greenwich Insurance Company *(A-12%)	Delaware
Warranty Support Services LLC	Delaware
XL Insurance America, Inc. *(A-10%)(<i>formerly Winterthur International America Insurance Company</i>)	Delaware

XL Select Insurance Company *(A-2%)(formerly <i>Winterthur International America Underwriters Insurance Co.</i>)	Oklahoma
XL Insurance Company of New York, Inc. (A-3%)	New York
Intercargo Corporation	Delaware
XL Specialty Insurance Company *(A-6%)	Delaware
Intercargo Insurance Company H.K. Ltd.	Hong Kong
Indian Harbor Insurance Company *(A-2%)	North Dakota
XL Management Services, LLC	Texas
XL Lloyds Insurance Company	Texas
NAC Re Financial Services, Inc.	Delaware
XL Capital Assurance Inc.	New York
XL Capital Assurance (U.K.) Limited	UK
37 Lambert Road LLC	Delaware
XL Financial Administrative Services, Inc.	Delaware
XL Portfolio Advisors Inc.	Delaware
XL Global, Inc.	Delaware
XL Insurance, Inc.	Delaware
X.L. Global Services, Inc.	Delaware
XL Investment Management (USA) LLC	Delaware
Eagleview Insurance Brokerage Services, LLC	Delaware
XL Life and Annuity Holding Company	Delaware
XL Life Insurance and Annuity Company (<i>formerly Lyndon Life Insurance Company</i>)	Illinois
XL Asset Funding Company I LLC	Delaware
ECS, Inc. (In Liquidation)	Pennsylvania
ECS Child Care Center, Inc.	Pennsylvania
ECS Risk & Insurance Services, Inc.	Barbados
XL Environmental Ltd	UK
XL Investments Ltd	Bermuda
First Cumberland Bank, Inc. (<i>In Liquidation</i>)	Barbados
Garrison Investments Inc. (**)	Barbados
InQuisLogic Ltd.	Barbados
InQuisLogic Inc. (<i>In Liquidation</i>)	Delaware
Kensington Investments Inc.	Barbados
XLB Partners Inc.	Barbados
Cumberland Holdings, Inc.	Delaware
Cumberland California, Inc.	Delaware
Cumberland New York, Inc.	Delaware
RiskConnect Ltd	Barbados
RiskConnect Inc. (<i>In Liquidation</i>)	Delaware
X.L. Investment Private Trustee Ltd.	Bermuda
X.L. Investments (Barbados) Inc.	Barbados
Cybersettle, Inc. (56%)	Delaware
Cybersettle Insurance Brokerage Services LLC	Delaware
Cybersettle Financial Services LLC	Delaware
InsuranceNoodle, Inc.	Delaware
TAM Investment Holdings Inc.	Delaware
ClearWater Opportunity Fund Ltd.	Cayman
XL (LUXEMBOURG) S.a.r.l.	Luxembourg
XL (FINANCE) S.a.r.l.	Luxembourg
XL (INTERNATIONAL) S.a.r.l.	Luxembourg

XL (SERVICES) S.a.r.l.	Luxembourg
XL (SPECIALTY) S.a.r.l.	Luxembourg
XL (WESTERN EUROPE) S.a.r.l.	Luxembourg
XL Re Europe (<i>formerly Le Mans Re</i>)	France
XL Re Europe Services AG (<i>fka Le Mans Re Deutschland AG</i>)	Germany
XL Re Europe Management Company Ltd	Canada
XL Swiss Holdings Ltd	Switzerland
XL Re Latin America Ltd	Switzerland
XL Latin America Investments Ltd	Bermuda
XL Re Latin America (Argentina SA)	Argentina
XL Re Latin America Servicios Ltda	Brazil
XL Insurance Switzerland (<i>fka XL Winterthur International Insurance Switzerland</i>)	Switzerland
Vitodurum Reinsurance Company (<i>fka XL Winterthur International Re</i>)	Switzerland
XL Services Switzerland	Switzerland
XL India Business Services Private Limited	India
XL Insurance Mexico	Mexico
XL Insurance (UK) Holdings Limited (<i>fka XL Winterthur (UK) Holdings Limited</i>) (57.67 %)	UK
XL Insurance Argentina S.A. Compañía de Seguros (<i>fka Winterthur International Argentina SA Compañía de Seguros</i>) (90%)	Argentina
XL Insurance Company Limited (<i>fka XL Winterthur International Insurance Company Limited</i>)	UK
XL Magyarorszag Biztosito Reszvenytarsasag	Hungary
XL Insurance Argentina S.A. Compañía de Seguros (<i>fka Winterthur International Argentina SA Compañía de Seguros</i>) (10%)	Argentina
XL Holdings (Proprietary) Limited (<i>fka XL Winterthur Holdings (Proprietary) Limited</i>)	South Africa
XL Winterthur Properties (Proprietary) Limited	South Africa
XL Insurance Company Limited (<i>fka XL Winterthur International Insurance Company Limited</i>)	South Africa
XL Services UK Limited	UK
XL Trading Partners Ltd	Bermuda
XL Europe Holdings Ltd (<i>formerly X.L. Two Ltd.</i>)	Bermuda
XL Treasury Europe Limited	R of Ireland
XL Europe Ltd	R of Ireland
XL Financial Services (Ireland) Ltd	R of Ireland
Mid Ocean Limited	Cayman
Mid Ocean Holdings Limited	Bermuda
Ridgewood Holdings Limited	Bermuda
XL London Market Group plc	UK
Brockbank Holdings Limited	UK
Baltusrol Holdings Limited	Bermuda
County Down Limited	UK
Dornoch Limited	UK
Stonebridge Underwriting Limited	UK
XL London Market Services Ltd	UK
Brockbank Personal Lines Limited – (<i>Dormant</i>)	UK
Cassidy Brockbank Limited - (<i>Dormant</i>)	UK
Denham Syndicate Management Limited	UK
Denham Direct Underwriters Ltd	UK
Denham Legal and Professional Risks Ltd	UK

Denham Tower Underwriting Agents (PTY) Limited	South Africa
XL London Market Ltd- Syndicates 588/861/990/1209	UK
Brockbank Syndicate Services Limited	UK
XL Capital International Limited	UK
XL Capital Finance (Europe) plc	UK
XL Financial Products Ltd.	UK
XL Re Ltd	Bermuda
ECS Reinsurance Company Inc.	Barbados
Global Capital Underwriting Ltd.	UK
NAC Re International Holdings Ltd	UK
NAC Reinsurance International Limited	UK
XL BCM Limited	UK
XL Mid Ocean Re Limited	UK
XL Investment Management Ltd	Bermuda
XL Capital Partners Corporation	Cayman
XL Capital Partners I, L.P.	Cayman
XL Capital Principal Partners I, L.L.C. (50%)	Delaware
XL Principal Partners I, L.P.	Cayman
XL Capital Principal Partners I, L.L.C. (50%)	Delaware
<i>*A = Company is a member of NAC Reinsurance, Intercargo Pooling Agreement with individual company pooling % noted</i>	
<i>(*) - General Partner of XLA Garrison L.P.</i>	
<i>(**) - Limited Partner of XLA Garrison L.P.</i>	

Appointment No 22430

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:

James Call

as proper person to examine into the affairs of the

XL INSURANCE COMPANY OF NEW YORK INC.

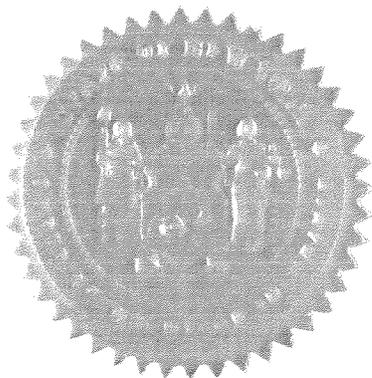
and to make a report to me in writing of the condition of the said

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 28th day of October, 2005



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

HOWARD MILLS
Superintendent of Insurance