REPORT ON EXAMINATION

OF THE

PARAMOUNT INSURANCE COMPANY

AS OF

DECEMBER 31, 1999

DATE OF REPORT	DECEMBER 13, 2000
EXAMINER	KENNETH MERRITT

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

December 13, 2000

Honorable Neil Levin
Superintendent of Insurance
Albany, NY 12257

Sir:

Pursuant to instructions contained in Appointment Number 21653 dated November 17, 2000, I have made an examination into the condition and affairs of the Paramount Insurance Company, as of December 31, 1999, respectfully submit the following report thereon.

Where the designations “Company” or “Paramount” appears herein without qualification, it should be understood to indicate the Paramount Insurance Company.

Where the designation “Magna Carta Companies Inc. ” appears herein without qualification, it should be understood to indicate the Public Service Mutual Insurance Company and its wholly-owned subsidiaries, PSM Holding Corporation, Paramount Insurance Company, Magna Carta Companies, Inc., Western Select Insurance Company and Creative Intermediaries.

1. SCOPE OF EXAMINATION

The prior examination was conducted as of December 31, 1994. This examination covered the five year period beginning January 1, 1995 through December 31, 1999 and was limited in scope to a review or audit of only those balance sheet items considered by this Department to require analysis, verification or description, including: invested assets, inter-company balances, loss and loss adjustment expense reserves and provision for reinsurance. This examination included a review of income, disbursements and Company records deemed necessary to accomplish such verification and, utilized, to the extent considered appropriate, work performed by the Company's independent certified public accountants. 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:

History of Company
Management and control
Corporate records
Fidelity bonds and other insurance
Territory and plan of operation
Market conduct activities
Growth of Company
Business in force by states
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.

A concurrent examination was conducted of the Company's ultimate parent, Public Service Mutual Insurance Company ("PSMIC"), a domestic insurer. Both examinations were conducted at the Company's principal office located at One Park Avenue, New York, New York 10016-5802.

2. DESCRIPTION OF COMPANY

The Company was incorporated under the laws of the State of New York on June 4, 1980 and licensed on July 13, 1981.

Direct control of the Company is held by PSM Holding Corporation ("Holding"), which in turn, is controlled directly by PSMIC, the parent company of the Magna Carta Companies Inc. group. Effective February 11, 1997, the Department approved the Company's proposal of an amendment to its charter to increase its then stated capital of $3 million comprising of three million authorized and issued shares of $1 per share common shares to $4.2 million consisting of 4.2 million shares of $1 per share.

Since January 1992, both Paramount and PSM have pooled premiums, losses and expenses under a reinsurance pooling agreement discussed in item 2C herein.

A. Management

Pursuant to the Company's charter and by-laws, management of the Company shall be vested in a board of directors consisting of a minimum of fifteen members up to a maximum of twenty-four persons serving at any time. As of December 31, 1999, the Company's board was comprised of the following fifteen directors:

Name and Residence	Principle Business Affiliation
Charles Lanham Crouch, III La Canada, California	Partner, Perkins Coies, LLP
Andrew Lawrence Furgatch New York, NY	Chairman of the Board and President, Magna Carta Companies
Julius Gantman White Plains, NY	Attorney, Tellerman, Taticoff & Greenberg
Anita Davis-Goodman Hartsdale, NY	Real Estate Broker, Julia B. Fee, Inc.
John David Hatch Ocala, FL	President, John D. Hatch, P.C.
Donald Henderson Aroma, CA	Consultant, Magna Carta
John Thomas Hill II Trenton, NJ	Chief Financial Officer/Treasurer, Magna Carta Companies
Harold Norman London Malverne, NY	Partner, Freeman, Davis, Furgatch
Stanley Joseph Mastrogiacomo Warwick, NY	Consultant, PSM Insurance Companies
Michael Moody Los Angeles, CA	Senior Vice-President, Magna Carta Companies
Milton Peckman Coconut Creek, FL	Executive Vice-President & Secretary, Magna Carta Companies
Paul Steven Schweitzer Potomac, MD	Senior Directing Manager, Julian J. Studley, Inc.
Leslie W. Seldin, D.D.S. New York, NY	Dental Practice
Lewis James Spellman, Ph.D. Austin, TX	Professor, University of Texas
Irwin Young Manhasset, NY	Chairman of the Board, Du Art Film Labs, Inc.

The Company also has executive, investment and compensation committees comprising of three board members per committee. Designated committee members serve on their committees for one year at a time and are elected annually by votes of the board of directors. A review of the directors and its various committees' minutes revealed that all the meetings were well attended.

The board met four times annually during the examination period as stipulated in the Company's by-laws. All meetings were well attended by the board members, with no exceptions noted.

Several board members have consulting service agreements with the Company. One of these agreements involves a certain director being in-charge with the overall responsibility of establishing and managing the Company's Western United States insurance operations. However, there were at least two directors who did not have such written agreements stipulating their provided services and related compensation.

It is recommended that the Company maintain for each director rendering outside consulting services to the Company individual formal written agreements approved by the board of directors.

The following is a list of officers of the Company as of December 31, 1999:

Name	Title
Andrew L. Furgatch	Chairman of the Board, President and Executive Vice President
John Thomas Hill II	Chief Financial Officer/Treasurer
David Lawless	Vice-President
Gregory Vincent Martino	Senior Vice-President /Underwriting
Louis Masucci	Vive-President
Earl Miller	Senior Vice-President
Michael Moody	Senior Vice President

Name	Title
Milton Peckman	Executive Vice-President/Secretary
Daniel Tagliaferro	Vice-President

B. Territory and Plan of Operation

As of December 31, 1994, the Company was licensed to transact the kinds of insurance as specified in the following paragraphs of Section 1113(a) of the New York Insurance Law:

Paragraph	Line of Business
3(i)	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

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 insurances 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).

As of the examination date, the Company was licensed in the States of New York, Massachusetts, New Jersey and Pennsylvania. Business is produced through independent agents and brokers.

Based upon the lines of business for which the Company is licensed, and pursuant to the requirements of Article 41 of the New York Insurance Law, Paramount Insurance Company is required to maintain a minimum surplus to policyholders in the amount of $2,150,000.

C. Reinsurance

The Company is primarily a direct writer. Substantially all reinsurance assumed represents acquired business from Public Service Mutual Insurance Company under terms of a pooling agreement. The agreement, which was effective January 1, 1992, and approved by the department, provides for the following:

1. PSM assumes 100% of the net writings of the Company. Ten percent of the combined net writings, excluding voluntary assumed reinsurance business, are retroceded to the Company.

2. All losses, claims expenses and underwriting expenses are pooled to PSM and the Company in their pooling percentages, 90% and 10% respectively.

3. All underwriting assets and liabilities are shared in their respective percentages.

The pooling agreement provides that within 45 days after the last day of each month, PSM shall prepare an account showing the apportionment of net underwriting results of the two companies.

The Schedule F data contained in the Company's annual statements filed for the years within the examination period was found to accurately reflect its reinsurance transactions.

The examiner reviewed all ceded reinsurance contracts effected during the examination period. These contracts all contained the required standard clauses including insolvency clauses meeting the requirements of Section 1308 of the New York Insurance Law.

The Company has in effect the following ceded reinsurance contracts at December 31, 1999:

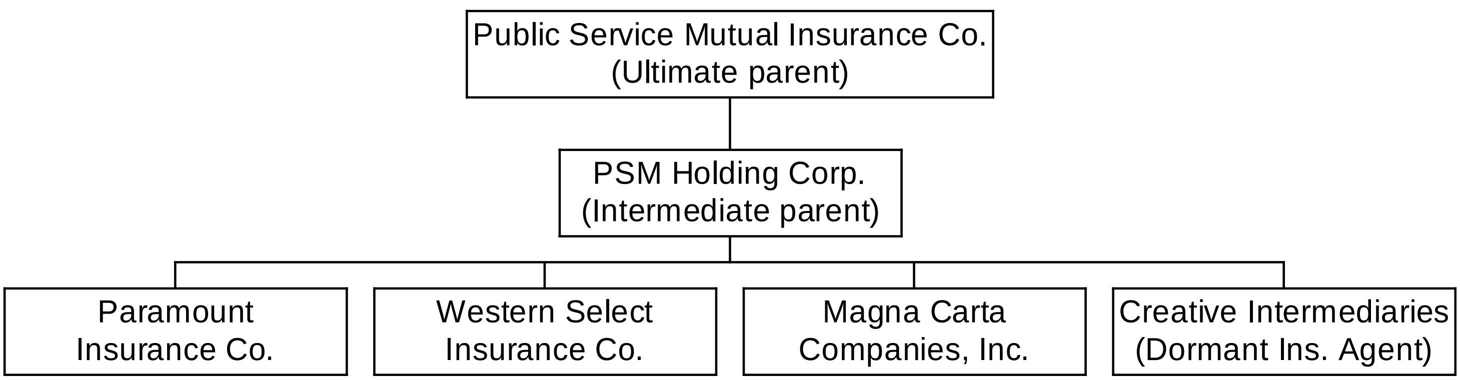
Type of Contract	Cession
Property	
First Surplus-fire, allied lines, commercial multiple peril and inland marine	Up to 5 times the minimum net retention of $250,000 per risk subject to a maximum cession of $12,000,000 per any one risk
Per Risk Excess of Loss (2 layers)-fire, allied lines, homeowners' multiple peril, commercial multiple peril and inland marine	$9,700,000 excess of $300,000 each and every loss occurrence
Catastrophe Excess of Loss-fire (5 layers), Allied lines, homeowners' multiple peril, commercial multiple peril, inland marine, automobile physical damage other than collision and garage keeper's legal liability	95% of $54,000,000 excess $3,000,000 each and every loss occurrence.
Casualty	
Excess of Loss (2 layers)	$10,000,000 ultimate net loss per occurrence excess of $500,000 annual aggregate deductible.
Clash Excess (2 layers)	$50,000,000 each event excess of $5,000,000 each event.
Semi-Automatic Facultative Facility-commercial umbrella	95% share of the Company's net retained insurance liability on each policy under $1,00,000 and 100% of loss under each policy issued in excess of $1,000,000.

The Company's ceded reinsurance program remains basically unchanged since the prior examination, with relatively minor fluctuations in the ratios of business ceded to authorized and unauthorized reinsurers participating.

Approximately 95% of all Company's cessions were transacted with authorized reinsurers. The Company's ceded reinsurance program remains basically unchanged since the prior examination, with relatively minor fluctuations in the ratios of business ceded to authorized and unauthorized reinsurers.

D. Affiliated Companies

Below is an organizational chart showing the Company and its subsidiaries as of December 31, 1999:



PSMIC is the ultimate parent company and is a domestic mutual insurance company. Therefore, it is not subjected to Article 15 of the New York Insurance Law.

On September 11, 1998, the Company, through PSM, formed a legal entity called Magna Carta Companies, Inc. ("MCCI"). This subsidiary was incorporated in the state of Delaware and it is presently dormant in terms of its operations. With respect to MCCI's formation, no formal filing was made with the Department pursuant to Section 1603 of the New York Insurance Law, which states in part the following:

> " No acquisition of a majority of any corporation's outstanding common shares shall be made pursuant to this article unless a notice of intention of such proposed acquisition shall have been filed with the Superintendent not less than ninety days, or such shorter period as may be permitted by the Superintendent, in advance of such proposed acquisition,…"

It is recommended that the Company file the formation of MCCI as a subsidiary with the Department for review pursuant to Section 1603 of the New York Insurance Law. In addition, it is further recommended that the Company comply with Section 1603 of the New York Insurance Law in the future by notifying the Department prior to the formation of a subsidiary.

Pursuant to the Department's April 27, 1999 approval, PSMIC, through PSM, acquired Western Select Insurance Company ("Western Select") by purchasing all 87,000 shares of Western Select's $30 par value per share for a total purchase price of $10,005,000. While Western Select, a California domiciled insurer, was not authorized in the State of New York through the 2000 year-end, management indicated the Company would seek a New York license in the future.

In January 1, 2000, PSMIC and its subsidiaries ceased using the trade name PSM Insurance Companies and commenced marketing under the name, Magna Carta Companies ("MCC").

In addition to the existing inter-company pooling reinsurance agreement between PSMIC and Paramount Insurance Company, the following inter-company agreements in effect as of December 31, 1999 between Paramount and its related parties, were filed with, and approved, by the Department:

1. Consolidated Federal Income Tax Liability Allocation (“ Tax Agreement”).

   Based upon a review of the existing Tax Agreement on file, it has not been amended to reflect the Company’s most recently acquired affiliates, Magna Carta Companies, Inc. and Western Select Insurance Company. In addition, the Tax Agreement also includes various dissolved entities that are no longer affiliates of the Company. Pursuant to the New York Insurance Department’s Circular Letter No. 33 (1979), notification to this Department should be given within thirty days of any amendment to a tax allocation agreement.

   It is recommended that the parent company comply with Circular Letter No. 33 (1979) by filing an amended tax allocation agreement with the Department reflecting Magna Carta Companies Inc. and Western Select Insurance Company as parties therein. In addition, it is recommended that the Company remove those entities no longer affiliated with the Group.

2. Quota Share Reinsurance Agreement effective July 27, 1999 between PSMIC and Western Select Insurance Company

   Under the Quota Share Reinsurance Agreement, PSMIC will assume 90% of Western Select’s gross unexpired liabilities relative to its policies, certificates, binders, agreements and other evidence of insurance issued by the ceding company for all authorized lines of insurance.

3. Inter-company Service and Quota Share Reinsurance Agreements effective July 27, 1999 between PSMIC and WSIC effective July 27, 1999

These agreements state that the State of California has legal governance and enforceability rights.

It is recommended that the Company revise its current inter-company service agreement to refer to the State of New York instead of the State of California, consistent with this State’s public policy for protecting its policyholders.

E. Significant Operating Ratios

The following ratios have been computed as of December 31, 1999, based upon the results of this examination:

Net premiums written to surplus as regards policyholders	.40:1
Liabilities to Liquid assets (cash and invested assets less investment in affiliates)	62.40%
Premiums in course of collection to surplus as regards policyholders	0.00%

The ratios presented above are within the benchmark ranges as prescribed by 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:

	Amounts	Ratios
Losses incurred	$38,206,358	54.27%
Loss adjustment expenses incurred	12,371,405	17.57
Other underwriting expenses incurred	24,572,025	34.90
Net underwriting loss	(4,741,742)	(6.74)
Premiums earned	$70,408,046	100.00%

F. Abandoned Property Law

Section 1316 of the New York State Abandoned Property Law requires certain unclaimed insurance proceeds to be reported to the State of New York, Office of the Comptroller by April 1 of each year. The examination review indicated that the Company has made the required filings on a timely basis.

A review of the Company's records indicated abandoned property filings were submitted as required during the examination period. However, it was noted that in filing years 1997 and 1998, there were a significant number of cases whereby the Company escheated unclaimed funds to the State without providing the claimants' names.

It is recommended that the Company maintain its records adequately to ensure that all claimants' names will be on record during each year in which unclaimed funds are escheated to the State, in accordance with Section 1316 of the New York State Abandoned Property Law.

G. Accounts and Records

The following was noted in conjunction with the review of the accounts and records maintained by the Company:

1. Unavailability of Records

Certain company records namely consulting agreements, lease agreements, agents' records, and Departmental questionnaires etc. were not readily available upon request and were delayed throughout the examination process. This resulted in a delay of completion of the examination. Section 310 of the New York Insurance Law states that the examiners shall be given convenient access to all books, records and files of such insurer.

It is recommended that all Company records be available upon request in a timely manner in order to facilitate future examinations.

2. Bonds Account

Discrepancies were noted in the Company bonds account due to inconsistencies in the securities reported between Schedule D-Part 1 of the Annual Statement and the Company's custodial bank report. Due to immateriality, no financial change was made. In addition, the Company was unable to account for certain broker trade tickets or advices for bond transactions selected for review by the examiners.

It is recommended that the Company prepare routine reconciliations of its bond accounts with the Company's general ledger, Schedule D and its custodial bank statements.

3. FINANCIAL STATEMENTS

A. Balance Sheet

The following shows the assets, liabilities and surplus as regards policyholders as determined by this examination as of December 31, 1999:

Assets	Ledger Assets	Non-ledger Assets	Not-Admitted Assets	Net-Admitted Assets
Bonds	$63,990,482	$	$	$63,990,482
Short-term investments	1,871,442			1,871,442
Agents' balances or uncollected premiums	1,502,420			1,502,420
Reinsurance recoverable on loss payments	139,910			139,910
Interest and dividends due and accrued		740,361		740,361
Equities and deposits in pools and associations	165,061			165,061
Other assets	582,028		49,235	532,793
Total assets	$68,251,343	$740,361	$49,235	$68,942,469

Liabilities

Losses	$26,821,224
Loss adjustment expenses	4,496,491
Contingent commissions	113,000
Other expenses	159,604
Taxes, licenses and fees	761,113
Unearned premiums	6,063,220
Dividends declared and unpaid to policyholders	12,065
Amounts withheld or retained by Company for account of others	(258)
Provision for reinsurance	36,164
Excess of statutory reserves over statement reserves	445,800
Payable to parent, subsidiaries and affiliates	1,967,752
Other liabilities	82,048
Total liabilities	$40,958,223

Surplus and Other Funds

Common capital stock	$4,200,000
Gross paid in and contributed surplus	13,300,000
Unassigned funds	10,484,246
Surplus as regards policyholders	$27,984,246
Total liabilities and surplus	$68,942,469

B. Underwriting and Investment Exhibit

Surplus as regards policyholders increased $6,825,127 during the five-year examination period January 1, 1995 through December 31, 1999, detailed as follows:

Statement of Income

Underwriting Income		
Premiums earned		$70,408,046
Deductions		
Losses incurred	$38,206,358	
Loss adjustment expenses incurred	12,371,405	
Other underwriting expenses incurred	24,509,029	
Aggregate write-in- LAD Program	62,996	
Total underwriting- deductions		75,149,788
Net underwriting loss		$(4,741,742)
Investment Income		
Net investment income earned	$20,447,507	
Net realized capital gains	1,139,639	
Net investment gain		21,587,146
Other Income		
Net (loss) from agents' or premium balances charged off	$(565,798)	
Finance and service charges not included in premiums	90,573	
Deferred compensation	(1,069)	
Miscellaneous	20,237	
Gain from sale of equipment	11,920	
Total other income		(444,137)
Net income before dividends to policyholders and before federal income taxes		$16,401,267
Less: Dividends to policyholders		2,261,827
Net income after dividends to policyholders but before federal income taxes		$14,139,440
Federal income taxes incurred		3,253,919
Net income		$10,885,521

Capital and Surplus Account

Surplus as regards policyholders, per report on examination, December 31, 1994			$19,959,119
	Gains in Surplus	Losses Surplus	
Net income	$10,885,521	$	
Change in not admitted assets	37,901		
Change in provision for reinsurance		11,555	
Change in excess of statutory reserves over statement reserves		136,740	
Capital paid in	1,200,000		
Surplus paid in		1,200,000	
Dividends to stockholders (cash)		2,750,000	
Total gains and losses	$12,123,422	$4,098,295	
Net increase in surplus as regards policyholders			8,025,127
Surplus as regards policyholders, per report on examination, December 31, 1999			$27,984,246

4. LOSSES AND LOSS ADJUSTMENT EXPENSES

The examination liabilities of $26,821,224 and $4,496,491 for the loss and loss adjustment expense reserves respectively, are the same amounts as reported by the Company as of December 31, 1999. Such amounts represent the Company's 10% share of the overall pooled reserves loss and loss adjustment expenses derived under the Company's inter-company reinsurance pooling agreement with its parent, Public Service Mutual Insurance Company.

The examiner conducted a detailed review of historical loss and loss expense data in accordance with generally accepted actuarial principles and practices and were based upon statistical information contained in the Company's internal records and its filed and sworn to annual statements. The reserves as reported by the Company were found to be adequate.

It is recommended that the Company report accurate cumulative claim counts data in Schedule P of the filed annual statement.

5. MARKET CONDUCT ACTIVITIES

In the course of the examination, a review was made of the manner in which the Company conducts its business practices and fulfills its contractual obligations to policyholders and claimants. The review was general in nature and is not to be construed as to encompass the more precise scope of a market conduct examination, 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 major areas:

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

No problems areas were encountered.

6. COMPLIANCE WITH PRIOR REPORT ON EXAMINATION

ITEM		PAGE NO.
A.	It is recommended that the directors elect a person other than the president to the position of executive vice president or that the by-laws be amended accordingly.	5
	The Company has complied with this recommendation.	
B.	It is recommended that the Company comply with the settlement requirements contained in the pooling agreement.	10
	The Company has complied with this recommendation.	
C.	It is recommended that the Company report all leasehold improvements as not admitted assets in future statement filings with this Department.	16
	The Company has complied with this recommendation.	

7. SUMMARY OF COMMENTS AND RECOMMENDATIONS

ITEM		PAGE NO.
A.	Management	
	1. It is recommended that the Company maintain for each director rendering outside consulting services to the Company individual formal written agreements approved by the board of directors.	5
B.	Affiliated companies	
	1. It is recommended that the Company file with the Insurance Department, the formation of the subsidiary, Magna Carta Companies Inc., pursuant to Section 1603 of the New York Insurance Law. In addition, it is recommended that the Company comply with the said statute in the future by notifying the Department prior to the formation of a subsidiary.	10
	2. It is recommended that the parent company comply with Circular Letter No. 33 (1979) by filing with the Insurance Department an amended tax allocation agreement reflecting Magna Carta Companies Inc. and Western Select Insurance Company as parties therein. In addition, it is recommended that the Company remove those entities no longer affiliated with the Group.	11
	3. It is recommended that the Company revise its current inter-company agreement to refer to the State of New York instead of the State of California.	11
C.	Abandoned Property Law	
	1. It is recommended that the Company maintain its records adequately to ensure that all claimants' names will be on record during each year in which unclaimed funds are escheated to the State, in accordance with Section 1316 of the New York State Abandoned Property Law.	13
D.	Account and Records	
	1. It is recommended that all Company records be available upon request in a timely manner in order to facilitate future examination.	13

Respectfully submitted,

Kenneth Merritt

Kenneth Merritt
Senior Insurance Examiner

STATE OF NEW YORK)
)SS.
)
COUNTY OF NEW YORK)

KENNETH MERRITT, being duly sworn, deposes and says that the foregoing report submitted by him is true to the best of his knowledge and belief.

Kenneth Merritt

Kenneth Merritt

Subscribed and sworn to before me

this 28TH day of MARCH 2001.

SAMUEL A. WACHTEL
Notary Public, State of New York
No. 41-4764998
Qualified in Nassau County
Commission Expires April 30, 2002

Appointment No 21653

STATE OF NEW YORK
INSURANCE DEPARTMENT

I, GERGORY V. SERIO, *First Deputy Superintendent of Insurance of the State of New York, pursuant to the provisions of the Insurance Law, do hereby appoint:*

Kenneth Merritt

as proper person to examine into the affairs of the

Paramount Insurance Company

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

Company

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 17th *day of* November

GREGORY V. SERIO
First Deputy Superintendent of Insurance