

Report on Examination
of
NARRAGANSETT BAY INSURANCE COMPANY
Johnston, Rhode Island
as of
December 31, 2018



State of Rhode Island and Providence Plantations
Department of Business Regulation
Insurance Division



**State of Rhode Island and Providence Plantations
DEPARTMENT OF BUSINESS REGULATION
1511 Pontiac Avenue, Bldg. 69-2
Cranston, Rhode Island 02920**

Insurance Division

ADOPTION ORDER

The attached Report of Examination as of December 31, 2018, of the condition and affairs of

NARRAGANSETT BAY INSURANCE COMPANY

was recently completed by duly qualified examiners, pursuant to the provisions of the Rhode Island General Laws.

Due consideration has been given to the comments of the examiners regarding the operation of the Companies and their financial condition, as reflected in the report.

It is therefore ORDERED that said Report be, and it is hereby, adopted and filed and made an official record of this Department as of this date.

Department of Business Regulation

A handwritten signature in black ink, reading 'Elizabeth Kelleher Dwyer', written over a horizontal line.

Dated: April 27, 2020

Elizabeth Kelleher Dwyer
Superintendent of Insurance

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February 14, 2020

Ms. Elizabeth Kelleher Dwyer
Deputy Director and Superintendent of Financial Services
State of Rhode Island and Providence Plantations
Department of Business Regulation
1511 Pontiac Avenue, Bldg. 69-2
Cranston, Rhode Island 02920

Dear Superintendent Dwyer:

In accordance with your instructions and pursuant to Chapters 13.1 and 35 of Title 27 of the General Laws of the State of Rhode Island, an examination has been made as of December 31, 2018, of the financial condition and affairs of

NARRAGANSETT BAY INSURANCE COMPANY

located at 1301 Atwood Avenue, Suite 316E, Johnston, Rhode Island. The report of such examination is herewith submitted.

Narragansett Bay Insurance Company, also referred to within this report as “NBIC,” or “the Company,” was previously examined as of December 31, 2013. Both the current and prior examinations were conducted by Insurance Division of the State of Rhode Island (“Insurance Division”) representing the Northeast Zone of the National Association of Insurance Commissioners.

SCOPE OF EXAMINATION

The current examination covered the five-year period from January 1, 2014 through December 31, 2018 and was performed in compliance with the above-mentioned sections of the General Laws of the State of Rhode Island, as amended. The current examination was conducted in accordance with the National Association of Insurance Commissioners (“NAIC”) *Financial Condition Examiners Handbook* (“Handbook”) risk-focused examination process, performed in conjunction with the 2018 full-scope coordinated multi-state risk-focused examination (“2018 Coordinated Exam”) of Heritage Insurance Holdings, Inc (“HIH”). The Coordinated Exam consisted of four (4) entities within the HIH holding company system. The Florida Department of Insurance served as the Lead State for the Coordinated Exam. In addition to Florida, the states of Rhode Island and Hawaii participated in the Coordinated Exam, which encompassed the following entities:

- Heritage Property & Casualty Insurance Company (FL) – “HPCI”
- Narragansett Bay Insurance Company (RI) – “NBIC”
- Pawtucket Insurance Company (RI) – “PIC”
- Zephyr Insurance Company, Inc. (HI) – “ZIC”

The Handbook requires that we plan and perform the examination to evaluate the financial condition, assess corporate governance, identify current and prospective risks of the Company and evaluate system controls and procedures used to mitigate those risks. An examination also includes identifying and evaluating significant risks that could cause an insurer’s surplus to be materially misstated both currently and prospectively.

All accounts and activities of the Company were considered in accordance with the risk-focused examination process. This may include assessing significant estimates made by management

and evaluating management's compliance with Statutory Accounting Principles. The examination does not attest to the fair presentation of the financial statements included herein. If, during the course of the examination an adjustment is identified, the impact of such adjustment will be documented separately following the Company's financial statements.

COMPANY HISTORY

The Company was established in 1981 by the Rhode Island General Assembly as a wholly owned subsidiary of Pawtucket Mutual Insurance Company ("PMIC") and it commenced business on April 1, 1982. NBIC, in conjunction with PMIC, wrote personal lines of insurance in New England and certain Mid-Atlantic States.

Effective January 1, 2006, the Company commenced writing homeowners and fire policies in Rhode Island, and in early 2007, the Company expanded its direct writings to Massachusetts and in September 2007, to New York. In 2009, the Company received approval to write business in New Jersey and Pennsylvania. In 2018, the Company received approval to write business in Virginia and has applications pending in Maryland and Delaware and to write water-only policies in Florida on an Excess & Surplus lines basis. As of the end of 2018 Pennsylvania is the only state listed above in which the Company is not actively writing.

On November 30, 2017, Heritage Insurance Holdings, Inc., a Delaware insurance holdings company, acquired NBIC Holdings, Inc., the parent company of NBIC. Heritage Insurance Holdings, Inc. acquired NBIC Holdings, Inc. for \$250,000,000. The acquisition was

financed with \$210,000,000 in cash and \$40,000,000 of the Company's common stock.

MANAGEMENT AND CONTROL

Shareholders

The by-laws provide that the annual meeting of the shareholders shall be held at the principal office of the Company or at such other place within the State of Rhode Island and shall be held on the third Tuesday of October in each year, if not a legal holiday, and, if a legal holiday, then on the next succeeding business day not a legal holiday. The annual meeting shall be held for the election of Directors and the transaction of such other business as may come before the meeting.

Special meetings of the shareholders for any purpose may be called by the President, by order of the Board of Directors or by the shareholder or shareholders of record holding at least fifty percent (50%) in voting power of the outstanding shares of the Corporation entitled to vote at such meeting.

At each meeting of the shareholders, a majority of the outstanding shares of the Company entitled to vote, represented in person or by proxy, shall constitute a quorum for the transaction of business.

Board of Directors

The by-laws provide that the property, affairs and business of the Company shall be managed by the Board of Directors, and the Board shall have, and may exercise, all of the

powers of the Company, except such as are conferred by the bylaws upon the shareholders.

The by-laws also stipulate that the number of directors to constitute the Board shall consist of seven (7) as set forth in Section 4 of the Stockholders Agreement of NBIC Holdings, Inc. dated January 23, 2008. Each elected Director shall hold office until the expiration of his or her term and until his or her successor is elected and qualified, or until the death, resignation or removal of such directors. No Director shall be a shareholder.

A majority of the total number of directors at the time in office shall constitute a quorum for the transaction of business at any meeting. In the absence of a quorum, a majority of the Directors present may adjourn any meeting without further notice until a quorum is present.

Regular meetings of the Board of Directors shall be held at such places and at such times as the Board shall from time to time vote to determine; provided however, that the Board of Directors shall meet at least quarterly. The Board shall have the authority to meet in executive session without the attendance by Company management without notice at such place as shall from time to time be determined by the Board of Directors.

Special meetings of the Board of Directors shall be held whenever called by the President or by not less than twenty-five percent (25%) of the members of the Board of Directors.

Any Director may be removed, either with or without cause, at any time, by the affirmative vote of the holders of record of a majority of the issued and outstanding shares entitled to

vote for the election of Directors given at a special meeting of the shareholders called and held for that purpose.

Subject to any provisions of the Articles of Incorporation providing for cumulative voting, any vacancy in the Board of Directors may be filled by a majority vote of the remaining Directors then in office, though less than a quorum, at any regular meeting or special meeting, including the meeting at which any such vacancy may arise, or by the shareholders of the Corporation.

The membership of the Board of Directors, together with the principal business or professional affiliation of each director was as follows at December 31, 2018:

Name	Business Affiliation	Term Expires
Bruce Lucas	Chairman Heritage Insurance Holdings, Inc.	2019
Richard Widdicombe	President Heritage Insurance Holdings, Inc.	2019
Irin Barlas	Principal Megastar Advisors, LLC	2019
James Masiello	Principal Alliance Holdings, Inc.	2019
Shannon Lucas	Principal Securus Risk Management, LLC	2019
Vijay Walvekar	Principal Central Home Health Care, Inc.	2019

On December 16, 2018, the sole shareholder removed Trifon Houvardas from the Board of Directors, as well as the Audit and Compensation Committees, this action created a vacancy at both the board, as well as the Audit and Compensation Committees as of December 31, 2018.

Committees

Pursuant to the bylaws, the Company shall establish an Audit Committee, which shall oversee the financial reporting process of the Company and receive reports directly from the Company's internal auditor. The Audit Committee shall be comprised of three (3) members appointed by the Board of Directors and such members may, but are not required to, consist of members of the Board of Directors. The Audit Committee members shall be financially literate and at least one (1) member shall have knowledge of statutory accounting principles.

The Audit Committee shall have the following responsibilities: (i) oversee the internal audit function of the Company, including reporting and personnel matters; (ii) oversee performance evaluations and compensation of the internal audit director; (iii) oversee the outside auditor including recommending the firm evaluating the auditor's performance and the rotation of senior audit personnel; (iv) review major accounting policies, judgments, and estimates; and (v) oversee the financial reporting process.

At December 31, 2018, the Audit Committee was comprised of the following individuals:

Irimi Barlas, Chairman
Vijay Walvekar

The bylaws also stipulate that the Audit Committee shall meet at least quarterly and shall

maintain minutes of its meetings, which shall be provided to the Board of Directors and reviewed and accepted at the Board of Directors' meeting following an Audit Committee meeting.

In addition to the Audit Committee, the Board of Directors established a Compensation Committee and Investment Committee. At December 31, 2018 the Compensation and Investment Committees were comprised of the following individuals:

Compensation Committee

James Masiello, Chairman
Irimi Barlas

Investment Committee

Bruce Lucas, Chairman
Richard Widdicombe

Officers

The bylaws provide that the officers of the Company shall be a President, a Secretary, a Treasurer, and such other officers as the Board of Directors may appoint, including a Chairman of the Board, one or more Vice Presidents, one or more Assistant Secretaries and one or more Assistant Treasurers. One person may hold the offices and perform the duties of any two or more of said officers, except that one person may not serve as both the President and Secretary. Each officer shall be elected annually by the Board of Directors and shall hold office until a successor is duly elected and qualified, or until the death, resignation or removal of such officer. A vacancy in any office shall be filled for the unexpired portion of the term by the Board of Directors at any regular or special meeting.

The officers serving, and their respective titles at December 31, 2018, are as follows:

Bruce T. Lucas	Chairman and Chief Executive Officer
Timothy M. Moura	President
Kirk H. Lusk	Chief Financial Officer, Secretary and Treasurer

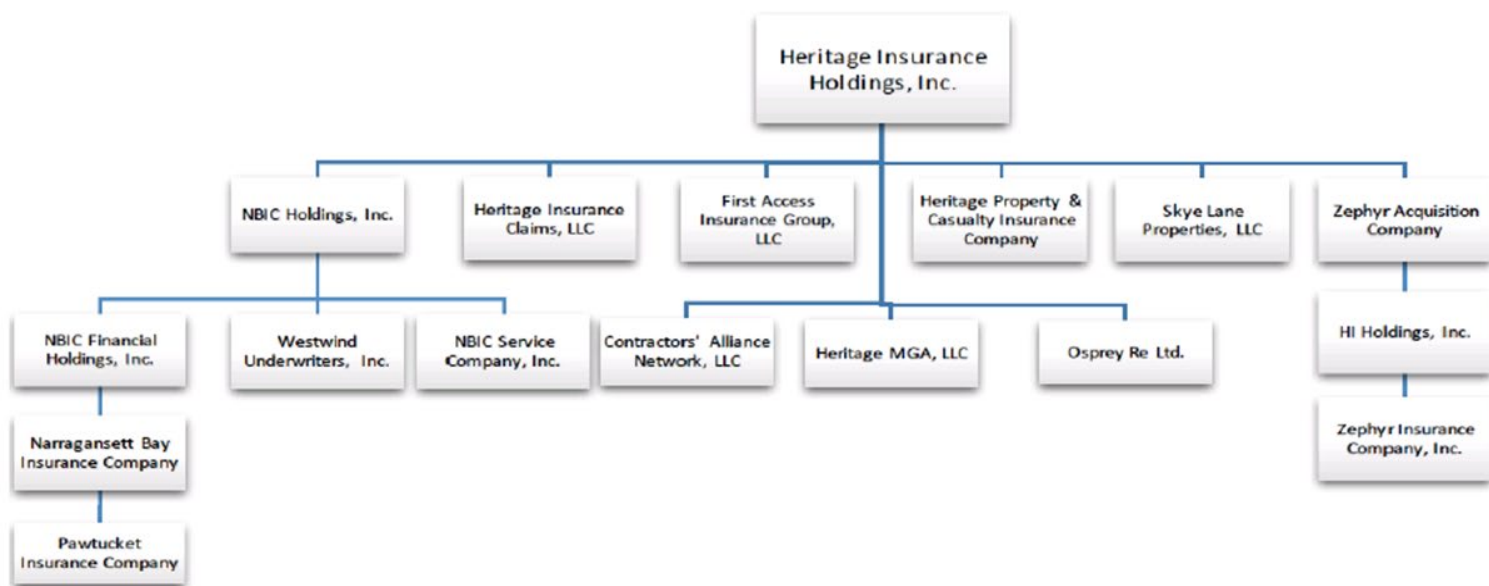
Organizational Structure

Heritage Insurance Holdings, Inc., (“Heritage Insurance”), established in 2012 and incorporated in the state of Delaware in 2014, is a property and casualty insurance holding company that provides personal and commercial residential property insurance. Heritage Insurance is headquartered in Clearwater, Florida and, through its insurance company subsidiaries, Heritage Property & Casualty Insurance Company (“HPCI”), Narragansett Bay Insurance Company (“NBIC”) and Zephyr Insurance Company (“ZIC”), writes personal residential property insurance for single-family homeowners and condominium owners, and rental property insurance in the states of Alabama, Connecticut, Florida, Georgia, Hawaii, Massachusetts, New Jersey, New York, North Carolina, Rhode Island and South Carolina. Heritage Insurance also provides commercial residential insurance for Florida properties and is also licensed in the states of Maryland, Mississippi, Pennsylvania, and Virginia. Heritage Insurance is vertically integrated and controls or manages substantially all aspects of insurance underwriting, customer service, actuarial analysis, distribution and claims processing and adjusting. Heritage Insurance is led by a senior management team with an average of 25 years of insurance industry experience. HPCI, ZIC, and NBIC are the direct insurance risk bearing entities in the group (collectively, the “Insurers”).

In 2017, Heritage Insurance acquired NBIC Holdings Inc., NBIC’s indirect parent company.

NBIC is a wholly owned subsidiary of NBIC Financial Holdings, Inc., a Delaware insurance holding company, which is a wholly owned subsidiary of NBIC Holdings. NBIC owns 100% of Pawtucket Insurance Company ("PIC"). PIC is currently in run off. NBIC Service Company, Inc. ("Service") provides administrative services and human resources according to the terms of their Administrative Services and Employee Leasing Agreement. Westwind Underwriters, Inc. is an inactive subsidiary of NBIC and is reserved for future development.

The following presentation of the holding company system as of December 31, 2018 reflects the identities and interrelationships between the Company and its affiliates:



Intercompany Agreement

Administrative Services and Employee Leasing Agreement

Effective January 1, 2010, NBIC entered into an Administrative Services and Employee Leasing Agreement ("Services and Employee Leasing Agreement") with NBIC Service Company, Inc. ("NBIC Service") whereby NBIC Service agrees to provide certain

administrative services and to make available to NBIC the services of certain of its employees as NBIC may require from time to time. The employees made available by NBIC Service to NBIC shall have such skills and shall devote such portion of their time to the affairs of NBIC as NBIC may reasonably request.

NBIC Service shall be responsible for all employment matters, including payment of wages, distribution of paychecks, withholding of all federal, state and local employment taxes, provision of appropriate workers' compensation coverage, state-mandated disability and unemployment coverage and any other government-mandated benefits, for employees made available to or otherwise providing services to NBIC.

As remuneration for services provided under this agreement, NBIC shall pay to NBIC Service an annual fee based upon a percentage of the Company's Gross Written Premium.

TERRITORY AND PLAN OF OPERATION

A review of the certificates of authority in effect at December 31, 2018, and the Company's compliance with these, we confirmed that NBIC is licensed to transact business in the states of Connecticut, Massachusetts, New Jersey, New York, Virginia and Rhode Island, and that the Company appears to be operating in compliance with its certificates of authority.

The Company is a stock insurer and its charter empowers it to write all lines of insurance except life, annuities, title, mortgage guaranty, workers' compensation and accident & health insurance.

The Company is headquartered in Johnston, Rhode Island and offers specialty insurance

services and products to homeowners along the eastern seaboard, through a network of select independent agents. Its focus is on risk management and loss prevention utilizing ShelterPride, its exclusive risk management and underwriting program. Operations are conducted in the same facilities and managed by the same individuals as its wholly-owned subsidiary, Pawtucket Insurance Company.

REINSURANCE

At December 31, 2018, the Company's ceded reinsurance program consists of the following agreements: Umbrella Facultative Reinsurance Contract, Property Catastrophe Excess of Loss Reinsurance, Reinstatement Premium Protection Covers, Per Risk Excess of Loss, Automatic Facultative, and Quota Share Reinsurance. The following is a brief description of each agreement in place as of December 31, 2018:

Umbrella Facultative Reinsurance Contract

This program, effective January 1, 2018 to December 31, 2018, protects the Company's Umbrella Liability business through a Quota Share structure whereby the Reinsurer provides reinsurance to the Company for 90% of the first \$1,000,000 each occurrence and 100% for \$4,000,000 excess of \$1,000,000.

Property Catastrophe Excess of Loss Reinsurance

This program, effective June 1, 2018 to May 31, 2019, protects the Company of the aggregation of losses in a single occurrence. Reinstatement provisions (one reinstatement at 100% of premium for most layers) provide protection for the Company from multiple catastrophe

events. The program is placed in several layers (with some layers applying to named storms or non-named storms only), the terms and structure of which are summarized below.

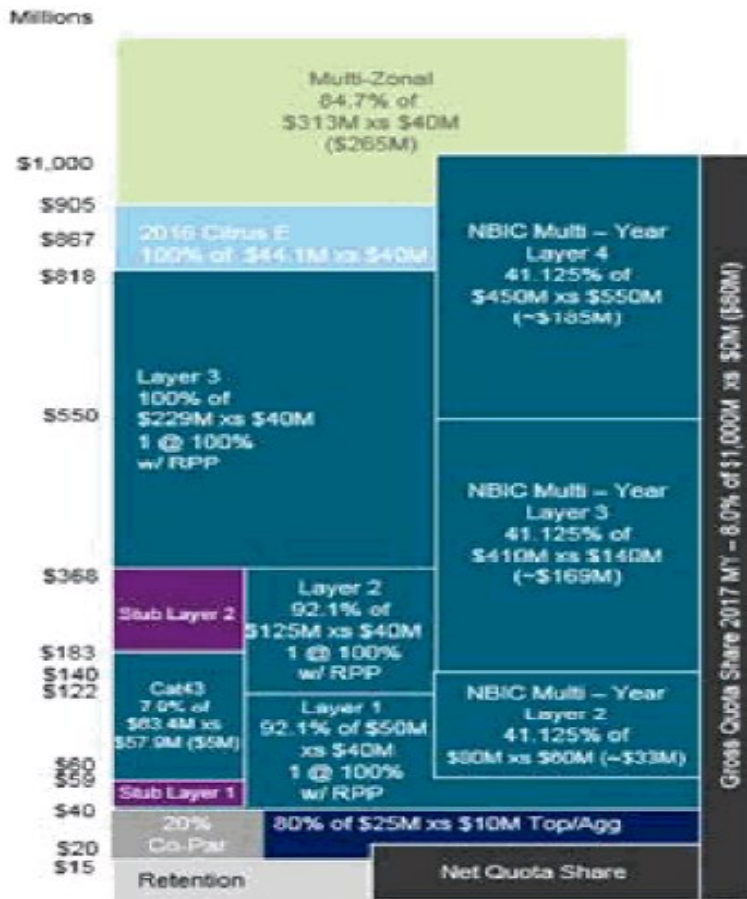
Layer	Limit and Retention	Percent Placed/ Coverage	Storms Covered	Cascading
Top/Aggregate	\$30,000,000 in excess of \$10,000,000 \$5,000,000 Annual Aggregate Deductible	80%	Named Storms only	N
Layer 1	\$50,000,000 in excess of \$40,000,000	100%	All	Y
Layer 2	\$125,000,000 in excess of \$40,000,000	100%	All	Y
Layer 3	\$229,000,000 in excess of \$40,000,000	100%	All	Y
Gap Layer 1	\$17,870,088 in excess of \$40,000,000	7.9%	All	Y
Cat43	\$63,359,849 in excess of \$40,000,000	7.9%	All	Y
Gap Layer 2	\$93,770,063 in excess of \$40,000,000	7.9%	All	Y
NBIC MY Layer 2	\$80,000,000 in excess of \$60,000,000	41.125%	All	N
NBIC MY Layer3	\$410,000,000 in excess of \$140,000,000	41.125%	All	N
NBIC MY Layer 4	\$450,000,000 in excess of \$550,000,000	41.125%	All	N
2016 Citrus E	\$44,147,826 in excess of \$40,000,000	100%	All	Y
Multi-Zonal	\$313,000,000 in excess of \$40,000,000	84.7%	All	Y
NBIC 20x20	\$20,000,000 in excess of \$20,000,000	100%	Non-Named Storms only	N

NBIC AggXOL	\$20,000,000 in excess of \$20,000,000 \$20,000,000 Per Occurrence Limit \$1,000,000 Franchise Deductible	40%	Non- Named Storms only	N
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Due to the acquisition of NBIC by Heritage Insurance Holdings, Inc., the Property Catastrophe Excess of Loss (“XOL”) structure combines layers placed by NBIC on a multi-year (“MY”) basis which inure to newly placed layers (which in lower inure to each other), in order to “fit” the new program around these residual layers and provide cascading coverage in the event of multiple storms.

These new layers are identified with a “Y” in the “Cascading” column in the table above, with \$40,000,000 retentions. These retentions assume all lower insuring layers have been exhausted.

-the effective retention for each layer on a first event basis is \$40,000,000 plus the sum of the limits of all inuring layers. The following diagram is provided to assist with understanding the table above for a Named Storm scenario:



Also noted in the table above, the Company purchased coverage for non-named storm occurrences on both an aggregate and per occurrence basis. On an occurrence basis, coverage for \$20,000,000 in excess of \$20,000,000 was placed at 92% from May 31, 2018 to December 31, 2018. This coverage was renewed at 100% placement effective December 31, 2018 to December 31, 2019.

Aggregate XOL coverage for \$20,000,000 in excess of \$3,000,000 was placed at 42.5% from June 1, 2018 to December 31, 2018 with a franchise deductible of \$1,500,000. Aggregate XOL coverage was also placed at 40%, effective December 31, 2018 to December 31, 2019 for \$20,000,000 in excess of \$20,000,000, subject to a franchise deductible of \$1,000,000.

Reinstatement Premium Protection ("RPP")

This program, effective June 1, 2018 to May 31, 2019, locks in the cost of a potential reinstatement premium charge that would occur should an event trigger the Company's catastrophe reinsurance. Reinstatement Premium Protection is placed for each layer at the percentages shown in the table below:

Layer	RPP Percent Placed / Coverage
Layer 1	95.3%
Layer 2	96.8%
Layer 3	99.7%
NBIC MY Layer 2	41.125%
NBIC MY Layer 3	41.125%
NBIC MY Layer 44	41.125%
Multi-Zonal	84.7%

Per Risk Excess of Loss Reinsurance

This program, effective July 1, 2018 to June 30, 2019, protects the Company from single risk losses, both property and casualty. The casualty coverage provided by this contract also responds on a "Clash" basis, meaning that multiple policies involved in a single loss occurrence can be aggregated into one loss and applied to the reinsurance contract. The following is a summary of the current coverage in place as of December 31, 2018:

Limits and Retention			
Layer	Property	Casualty	Combined Property and Casualty
NBIC Retention	\$300,000 each loss, each risk	\$300,000 each loss, each risk.	\$300,000 each loss, each risk.
First Excess	\$450,000 excess of \$300,000 each risk, each loss, subject to a limit of \$1,350,000 each loss occurrence.	\$450,000 excess of \$300,000 each risk, each loss, subject to a limit of \$450,000 each loss occurrence.	\$300,000 excess of \$300,000 each loss.
Second Excess	\$2,750,000 excess of \$750,000 each risk, each loss, subject to a limit of \$5,500,000 each loss occurrence	\$1,250,000 excess of \$750,000 each risk, each loss, subject to a limit of \$750,000 each loss occurrence	

Automatic Property Facultative Reinsurance

This program, effective July 1, 2018 to June 30, 2019, protects the Company from single risk losses, for property risks with a total insured value excess of \$3,500,000 subject to a limit of \$3,750,000 per risk and \$7,500,000 per occurrence.

Quota Share (Gross)

This coverage, effective June 1, 2017 to May 31, 2019, is for 8.0% of Loss and ALAE subject to the following:

Property coverage subject to each occurrence of \$80,000,000 (8% of \$1,000,000,000); property coverage subject to each loss, each risk limit of \$280,000 (8% of \$3,500,000). The ceding commission is 36.0%.

Quota Share (Net)

This coverage, effective December 31, 2018 to December 31, 2019, is for 52.0% of Loss and Allocated Loss Adjustment Expense ("ALAE ") subject to the following: Property coverage subject to each occurrence of \$10,400,000 (52% of \$20,000,000); property coverage subject to each loss, each risk limit of \$390,000 (52% of \$750,000). The ceding commission details vary by reinsurer, but on a weighted average basis is a provisional 39.5%, sliding scale to a minimum commission of 35.0% at 56.3% loss ratio and maximum of 45.4% at 45.7% loss ratio. General excess of loss and property catastrophe coverage inure to benefit of this quota share coverage, which is the major distinction of this treaty from the *Quota Share (Gross)* treaty described above.

In addition to the coverage above, Quota Share (Net) coverage from contracts expiring December 31, 2018 for 10.0% of Loss & ALAE is applied on a runoff basis, covering losses occurring during 2019 for policies in effect as of December 31, 2018.

The reinsurance contracts were independently reviewed as deemed necessary by Merlinos & Associates, Inc. ("Merlinos"); consulting actuaries for the Rhode Island Insurance Division, for compliance with the risk transfer requirements of SSAP No. 62R of the National Association of Insurance Commissioners "Accounting Practices & Procedures Manual." Merlinos concluded that the reinsurance agreements contain sufficient risk transfer to qualify as reinsurance for statutory reporting purposes.

FINANCIAL STATEMENTS

The following financial statements are based on the statutory financial statements filed by the company with the Rhode Island Insurance Division Department of Business Regulation and present the financial condition of the company for the period ending December 31, 2018. The accompanying comments on the financial statements reflect any examination adjustments to the amounts reported in the annual statements and should be considered an integral part of the financial statements.

Comparative Statement of Assets
December 31, 2018 and December 31, 2013

Comparative Statement of Liabilities, and Capital and Surplus
December 31, 2018 and December 31, 2013

Statement of Income
Year ended December 31, 2018

Reconciliation of Capital and Surplus
December 31, 2013 to December 31, 2018

Analysis of Examination Adjustments
December 31, 2018

NARRAGANSETT BAY INSURANCE COMPANY
Comparative Statement of Assets
December 31, 2018 and 2013

	<u>December 31,</u> <u>2018</u>	<u>December 31,</u> <u>2013</u>	<u>Increase</u> <u>(Decrease)</u>
Bonds	\$90,251,594	\$46,404,062	\$43,847,532
Common stocks	4,105,615	0	4,105,615
Cash, cash equivalents and short-term investments	102,802,125	24,269,014	78,533,111
Investment income due and accrued	611,704	276,703	335,001
Uncollected premiums and agents' balances in the course of collection	6,244,083	4,494,921	1,749,162
Deferred premiums, agents' balances and installments booked but deferred and not yet due	21,128,997	20,176,151	952,846
Amounts receivable from reinsurers	37,293,717	3,207,043	34,086,674
Current federal income tax recoverable	6,913,797	0	6,913,797
Net deferred tax asset	1,810,010	5,525,263	(3,715,253)
Receivable from parent, subsidiaries and affiliates	0	5,002,826	(5,002,826)
Aggregate write-ins for other than invested assets	6,992,459	3,270,267	3,722,192
Total Assets	<u>\$278,154,101</u>	<u>\$112,626,250</u>	<u>\$165,527,851</u>

NARRAGANSETT BAY INSURANCE COMPANY
Comparative Statement of Liabilities, Surplus and Other Funds
December 31, 2018 and 2013

	<u>December 31,</u> <u>2018</u>	<u>December 31,</u> <u>2013</u>	<u>Increase</u> <u>(Decrease)</u>
Losses	\$15,955,290	\$9,085,516	\$6,869,774
Loss adjustment expenses	6,552,281	3,823,218	2,729,063
Commissions payable, contingent commissions and other similar charges	7,812,097	4,638,057	3,174,040
Other expenses	362,578	1,409,502	(1,046,924)
Taxes, licenses and fees	1,516,974	801,693	715,281
Unearned premiums	30,663,681	41,567,168	(10,903,487)
Advance premium	6,079,491	2,290,685	3,788,806
Ceded reinsurance premiums payable (net of ceding commissions)	92,962,799	6,595,593	86,367,206
Funds held by company under reinsurance treaties	15,890	54,468	(38,578)
Provision for reinsurance	9,010,000	454,241	8,555,759
Payable to parent, subsidiaries and affiliates	2,619,814	0	2,619,814
Aggregate write-ins for liabilities	609,472	0	609,472
Total Liabilities	174,160,997	70,720,141	103,440,856
Common capital stock	4,000,000	4,000,000	0
Gross paid in and contributed surplus	83,007,995	83,007,995	0
Unassigned funds (surplus)	16,985,109	(45,101,886)	62,086,995
Surplus as regards policyholders	103,993,104	41,906,109	62,086,995
Total Liabilities, Surplus and Other Funds	\$278,154,101	\$112,626,250	\$165,527,851

NARRAGANSETT BAY INSURANCE COMPANY
Statement of Income
Year ending December 31, 2018

UNDERWRITING INCOME

Premiums earned \$74,489,598

DEDUCTIONS

Losses incurred	\$39,500,396
Loss adjustment expenses incurred	10,793,953
Other underwriting expenses incurred	<u>30,604,760</u>

Total underwriting deductions	<u>80,899,109</u>
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Net underwriting gain or (loss) (6,409,511)

INVESTMENT INCOME

Net investment income earned	3,491,804
Net realized capital gains or (losses) less capital gains tax	<u>(43,405)</u>

Net investment gain or (loss) 3,448,399

OTHER INCOME

Net gain or (loss) from agents' balances or premium balances charged off	(743,926)
Finance and service charges not included in premiums	1,482,963
Aggregate write-ins for miscellaneous income	<u>2,248,608</u>

Total other income	<u>2,987,645</u>
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Net Income before federal income taxes 26,533

Federal and foreign income taxes incurred	<u>3,650,479</u>
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Net Income	<u><u>\$ (3,623,946)</u></u>
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NARRAGANSETT BAY INSURANCE COMPANY
Reconciliation of Capital and Surplus
December 31, 2013 To December 31, 2018

Capital and Surplus, December 31, 2013		\$41,906,109
	<u>Increase</u> <u>(Decrease)</u>	
Net income	\$69,352,387	
Change in net unrealized capital gains or (losses)	4,105,605	
Change in net deferred income tax	(14,363,160)	
Change in nonadmitted assets	10,706,742	
Change in provision for reinsurance	(8,555,759)	
Prior year's tax adjustment	825,181	
Schedule F penalty and other adjustments	16,007	
Rounding	<u>(8)</u>	
Change in capital and surplus for the period		<u>62,086,995</u>
Capital and Surplus, December 31, 2018		<u>\$103,993,104</u>

NARRAGANSETT BAY INSURANCE COMPANY
Analysis of Examination Adjustments
December 31, 2018

The examination of the Company, performed as of December 31, 2018, resulted in an increase in the liability for the “Provision for Reinsurance” as presented below:

Analysis of Change to Surplus			
Surplus at December 31, 2018 per Annual Financial Statement			\$112,993,104
	<u>Increase</u>	<u>Decrease</u>	
Provision for Reinsurance	\$9,000,000		
Net decrease			<u>(\$9,000,000)</u>
Surplus at December 31, 2018 after adjustment			<u>\$103,993,104</u>

ASSETS

Bonds

\$90,251,594

The above amount is the net admitted value of bonds held by the Company and is the same as that reported in its 2018 Annual Statement. All bonds owned at year-end 2018 are held in accordance with a custodial agreement with a third party.

Eighty-nine percent (89.0%) of all bonds in the Company's portfolio at December 31, 2018, were rated as Class 1 based upon evaluation methods established by the National Association of Insurance Commissioners Securities Valuation Office. All other bonds were rated as Class 2. Class 1 and Class 2 securities are considered the "highest" and "high quality" respectively.

The amortized book value of bonds owned at December 31, 2018, represents 32.5% of the Company's total admitted assets. The book/adjusted carrying value, fair value, actual cost and par value of the bond portfolio at December 31, 2018, are as follows:

<u>Book/Adjusted Carrying Value</u>	<u>Fair Value</u>	<u>Actual Cost</u>	<u>Par Value</u>
\$90,251,594	\$88,694,568	\$90,671,018	\$88,357,273

Cash, Cash Equivalents and Short-Term Investments

\$102,802,125

Cash	\$52,213,135
Cash Equivalents	\$48,591,004
Short-Term Investments	\$1,997,986

The above amounts are the net admitted values of the individually listed Annual Statement lines, which in the aggregate, represent 37.0% of the Company's total admitted assets. The amounts shown are the same as that reported in the 2018 Annual Statement.

LIABILITIES

<u>Losses</u>	<u>\$15,955,920</u>
<u>Loss Adjustment Expenses</u>	<u>6,522,281</u>

The significant actuarially determined amounts above are the same as those reported in the Company's 2018 Annual Statement. The reserve calculations prepared by the Company were reviewed by Merlinos & Associates, Inc. ("Merlinos"), consulting actuaries for the State of Rhode Island Insurance Division. Merlinos relied upon the underlying data reported by the Company, and their analyses included a review of the actuarial assumptions and methods used by the Company in determining the reserves, and such tests of actuarial calculations as deemed necessary. Merlinos concluded that the NBIC's appointed actuary's loss and loss adjustment expense reserve analyses and conclusions are reasonable.

In assisting Merlinos with their analysis, the examiners either independently performed or relied upon the procedures performed by the Company's independent accounting firm to verify the integrity of the underlying claims data, including completeness testing. A combination of subjective and statistical sampling techniques was utilized in testing the claims data, as deemed appropriate.

Merlinos also assisted in the review of the Company's key underwriting policies, pricing of insurance policies, and reinsurance risk transfer and reinsurance structure (discussed further in the "Reinsurance" section). The results of their review did not produce any recommendations.

Provision for Reinsurance

\$9,010,000

The amount reported above is \$9,000,000 greater than the amount reported by the Company in its 2018 Annual Statement, and is the result of the examiners estimating an increase in the Provision for Reinsurance (“Provision”) liability for overdue reinsurance recoverables as explained below.

During the course of the examination, we determined that the Company does not properly age its reinsurance recoverables. Based on the records available and provided, the examination team estimated an increase in the Provision by determining collections received during the first three months of 2019 and netting that amount against related year end receivable balances. The examination team performed this calculation on approximately 89% of the year-end 2018 balance. Although this approach does not represent an entirely accurate calculation, the examination team feels this provides a reasonable, conservative estimate of the additional provision given the limited records available.

The Company, subsequent to the date of this examination, has begun to age its reinsurance recoverables and is implementing procedures to correctly calculate and age its recoverables in the Annual Statement and underlying schedules and exhibits.

Recommendation #1

It is recommended that in all future Annual Statement filings, the Company properly age its reinsurance recoverables and calculate its Provision for Reinsurance , in accordance with SSAP 62R.

SUBSEQUENT EVENTS

A review of financial information, Company records, and the minutes to the Board of Directors' meetings and its various committees for the period subsequent to the examination period was performed to ascertain whether any subsequent events have occurred which would have a material impact on the Company's operations or financial statements. In addition, an inquiry was made of the Company's management regarding subsequent events. Based upon our review, there were no significant events that occurred subsequent to December 31, 2018.

SUMMARY OF RECOMMENDATIONS

No.	Recommendation	Page No.
1	It is recommended that in all future Annual Statement filings, the Company properly age its reinsurance recoverables and record its Provision for Reinsurance in accordance with SSAP 62R.	27

CONCLUSION

We have applied verification procedures to the data and information contained in this report using sampling techniques and other examination procedures as deemed appropriate. While sampling and other examination procedures do not give complete assurance that all errors and irregularities will be detected, had any been detected during this examination, such errors and/or irregularities would have been disclosed in this report. Other than what has been noted in the body of this report, we were not informed of, and did not become aware of any errors or irregularities that could have a material effect on the financial condition of the Company as presented in this report.

Participating in the examination with the undersigned were various staff insurance examiners from the Rhode Island Insurance Division. In addition, acknowledgment is made of INS Regulatory Insurance Services, Inc for the services rendered to assist with the examination by providing a consulting financial examiner.

Respectfully submitted,

Louis A. Gabriele Jr, CPA, CFE

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Rhode Island Insurance Division