

Report on Examination
of
PAWTUCKET 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

PAWTUCKET 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

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

PAWTUCKET INSURANCE COMPANY

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

Pawtucket Insurance Company, also referred to within this report as “PIC” or “the Company,” was previously examined as of December 31, 2013. Both the current and prior examinations were conducted by the 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 (“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 companies:

- 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.

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

COMPANY HISTORY

Pawtucket Mutual Insurance Company ('PMIC') was originally chartered by Act of the Rhode Island General Assembly of 1848 (the 'Charter') and commenced business on February 10, 1849. The Charter was subsequently amended by acts of the General Assembly in 1870, 1881, 1905, 1913, 1936, and 1952.

On December 7, 2005, Narragansett Bay Insurance Company ("NBIC"), and its parent PMIC were purchased by Blackstone Financial Group, Inc. ("BFG"), a Delaware domiciled holding company. PMIC amended, restated and converted its Charter to a capital stock form of organization and changed its name to Pawtucket Insurance Company ('PIC').

On December 28, 2011, the Company issued a surplus note to its affiliate NBIC Service Company, Inc. in the amount of \$650,000. Interest on the surplus note shall be paid at the rate equal to LIBOR. The principal amount of the surplus note shall be payable upon the

earlier of, 1) the Company being reimbursed for net operating losses utilized by NBIC Holdings, Inc.'s consolidated tax return, or, 2) December 31, 2016. On December 28, 2016, the Company attached an allonge to the surplus note extending the payable date (item 2) from December 31, 2016 to December 31, 2017. The Company received approval from the Department of Business Regulation ("DBR") and settled the note plus interest at December 31, 2017.

On December 28, 2012, the Company issued a surplus note to its affiliate NBIC Service Company, Inc. in the amount of \$500,000. Interest on the surplus note shall be paid at the rate equal to LIBOR. The principal amount of the surplus note shall be payable upon the earlier of, 1) the Company being reimbursed for net operating losses utilized by NBIC Holdings, Inc.'s consolidated tax return, or, 2) December 31, 2017. The Company received DBR approval and settled the note plus interest at December 31, 2017.

On November 12, 2015, the Company received an additional capital contribution from NBIC in the form of cash in the amount of \$1,500,000. The proceeds of this capital contribution were used to fund the Company's pension plan.

On November 30, 2017, Heritage Insurance Holdings, Inc., a Delaware insurance holding company, acquired NBIC Holdings Inc., the parent company of PIC. 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.

During 2018, the Company's defined benefit plan was terminated and there are neither assets

nor estimated future payments due the pension plan. As of December 31, 2018, there was one remaining claim left outstanding, which was settled in February 2019.

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 by-laws 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.	2020
Richard Widdicombe	President Heritage Insurance Holdings, Inc.	2020
Irini Barlas	Principal Megastar Advisors, LLC	2020
James Masiello	Principal Alliance Holdings, Inc.	2020
Shannon Lucas	Principal Securus Risk Management, LLC	2020
Vijay Walvekar	Principal Central Home Health Care, Inc.	2020

On November 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; and (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:

Irini 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
Irina 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
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Organizational Structure

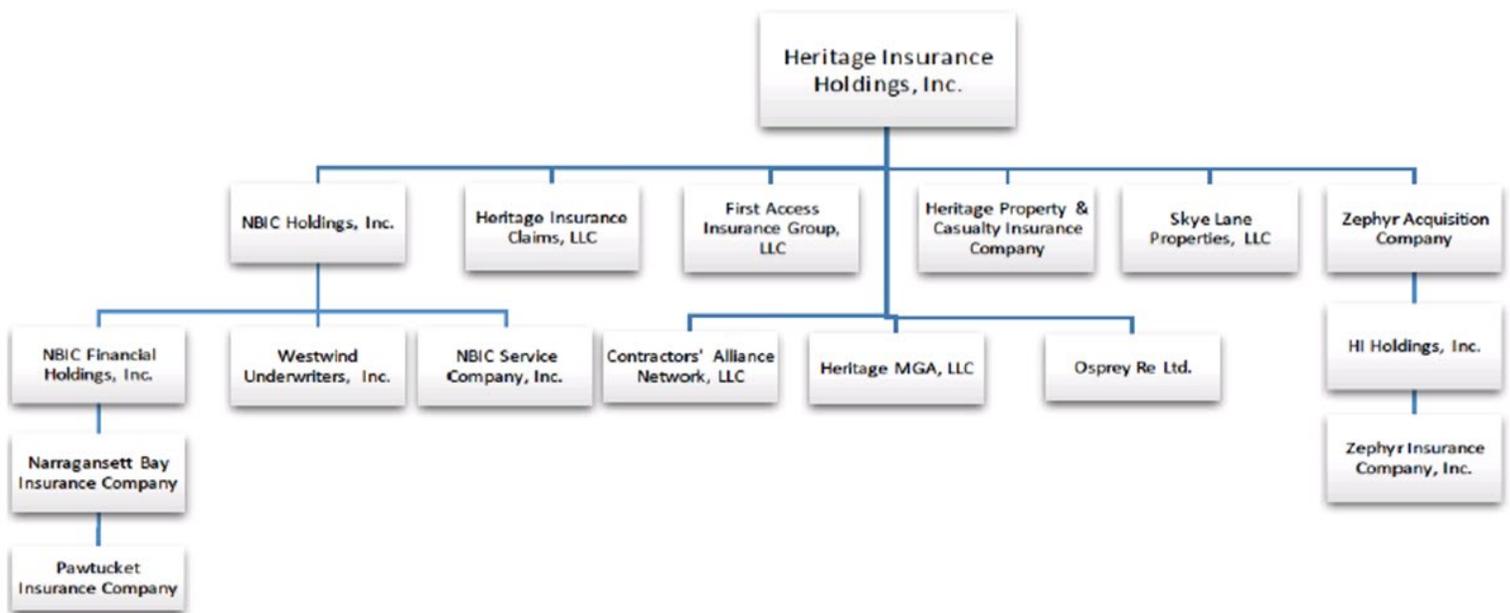
Heritage Insurance Holdings, Inc., (“Heritage Insurance”), established in 2012 and incorporated in the state of Delaware in 2014, is a property and casualty insurance holding company that provides personal and commercial residential property insurance. Heritage Insurance is headquartered in Clearwater, 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, PIC’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 PIC which 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 Holdings, Inc. and is reserved for future development.

The following presentation of the holding company system as of December 31, 2013 reflects the identities and interrelationships between the Company and its affiliates:



Intercompany Agreements

Administrative Services Agreement

Effective January 1, 2010, PIC entered into an Administrative Services Agreement (“Services Agreement”) with NBIC Service Company, Inc. ("NBIC Service") whereby NBIC Service agrees to provide certain services and facilities to PIC required by PIC in the ordinary course of business of PIC, including: office space, claims department management services, policy services, financial, financial reporting and financial management services, preparation of

quarterly financial statements, perform bookkeeping, data processing, and other services as needed.

TERRITORY AND PLAN OF OPERATION

The Company is headquartered in Johnston, Rhode Island and operations are conducted in the same facilities and managed by the same individuals as its parent, Narragansett Bay Insurance Company.

The Company has not written any business since 2004 and there are no plans to write new business in the foreseeable future. At December 31, 2018, Company activities are limited to the servicing of claims that were incurred prior to 2004. Its focus consists of two objectives: (a) timely and aggressive claims settlement, and (b) management and control of allocated loss adjustment expenses. As of December 31, 2018, there was one remaining claim outstanding which was settled in February 2019.

Although the Company is no longer actively writing business, a review of the certificates of authority in effect at year-end 2018, confirmed that it remains licensed to transact business in the following three (3) jurisdictions:

New Jersey
New York
Rhode Island

In addition to the above, at December 31, 2018, the Company's certificate of authority is restricted to servicing existing business in New Hampshire. The Company voluntarily withdrew its licenses in Delaware, Massachusetts, Maryland, Maine, Vermont, Connecticut

and Pennsylvania.

During 2018, the Company's defined benefit plan was terminated and there are neither assets nor estimated future payments due the pension plan.

FINANCIAL STATEMENTS

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

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

Comparative Statements 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

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

	<u>December 31,</u> <u>2018</u>	<u>December 31,</u> <u>2013</u>	<u>Increase</u> <u>(Decrease)</u>
Bonds	\$0	\$7,747	(\$7,747)
Real estate: Properties held for the production of income	0	1,897,500	(1,897,500)
Cash, cash equivalents and short-term investments	1,694,139	2,037,473	(343,344)
Investment income due and accrued	0	38	(38)
Amounts recoverable from reinsurers	0	563,991	(563,991)
Current federal and foreign tax recoverables	2,848,245	0	2,848,245
Receivable from parent, subsidiaries and affiliates	0	109,460	(109,460)
Aggregate write-ins for other than invested assets	170,170	18,367	151,803
Total Assets	<u>\$4,712,554</u>	<u>\$4,634,576</u>	<u>\$77,978</u>

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

	<u>December 31,</u> <u>2018</u>	<u>December 31,</u> <u>2013</u>	<u>Increase</u> <u>(Decrease)</u>
Losses	\$215,000	\$406,933	(\$191,933)
Loss adjustment expenses	44,281	315,729	(271,448)
Other expenses	467	3,202,266	(3,201,799)
Taxes, licenses and fees	0	117,322	(117,322)
Net deferred tax liability	307,656	0	307,656
Provision for reinsurance	0	152,878	(152,878)
Aggregate write-in for liability	39,535	0	39,535
Total Liabilities	606,939	4,195,128	(3,588,189)
Common capital stock	1,000,000	1,000,000	0
Surplus notes	0	1,150,000	(1,150,000)
Gross paid in and contributed surplus	2,000,000	500,000	1,500,000
Unassigned funds (surplus)	1,105,615	(2,210,522)	3,316,167
Surplus as regards policyholders	4,105,615	439,448	3,666,167
Total Liabilities, Surplus and Other Funds	\$4,712,554	\$4,634,576	\$77,978

PAWTUCKET INSURANCE COMPANY
Statement of Income
Year Ended December 31, 2018

UNDERWRITING INCOME

Premiums Earned \$0

DEDUCTIONS

Losses incurred	(\$25,506)
Loss adjustment expenses incurred	(81,914)
Other underwriting expenses incurred	<u>(126,256)</u>

Total underwriting deductions (233,676)

Net underwriting gain or (loss) 233,676

INVESTMENT INCOME

Net investment income earned	24,167
Net realized capital gains or (losses) less capital gains tax	<u>0</u>

Net investment gain or (loss) 24,167

Net income before federal income taxes 257,843

Federal income taxes (1,488,038)

Net income \$1,745,881

PAWTUCKET INSURANCE COMPANY
Reconciliation of Capital and Surplus
December 31, 2013 to December 31, 2018

Capital and Surplus, December 31, 2013		\$439,448
	<u>Increase</u> <u>(Decrease)</u>	
Net income	\$3,168,304	
Change in net deferred income tax	(4,535,361)	
Change in nonadmitted assets	7,842,483	
Change in provision for reinsurance	152,877	
Change in surplus notes	(1,150,000)	
Change in gross paid in capital	1,500,000	
Prior year tax adjustment	1,194,894	
Pension termination	(4,507,025)	
Rounding	<u>(5)</u>	
Net change in capital and surplus		<u>3,666,167</u>
Capital and Surplus, December 31, 2018		<u><u>\$4,105,615</u></u>

PAWTUCKET INSURANCE COMPANY
Analysis of Examination Adjustments
December 31, 2018

The examination of the Company, performed as of December 31, 2018, did not disclose any material misstatements to the financial statements contained in its 2018 Annual Statement filing. Accordingly, the amounts reported by the Company have been accepted for purposes of this report.

ASSETS

Cash and Cash Equivalents

\$1,694,139

Cash	\$968,056
Cash Equivalents	\$726,083

The above amount is the net admitted value of cash and cash equivalents, held by the Company and is the same as that reported in its 2018 Annual Statement. Included in the cash equivalents is an amount of \$378,761 held as a special deposit for the State of Rhode Island.

LIABILITIES

<u>Losses</u>	<u>\$215,000</u>
<u>Loss Adjustment Expenses</u>	<u>44,281</u>

The reserve consists of a single reported claim as of December 31, 2018, and the loss adjustment expense required to settle the claim subsequent to December 31, 2018. Due to the immateriality of the loss and loss adjustment expense reserves, no independent actuarial analysis was performed.

SUBSEQUENT EVENTS

In the first quarter of 2019, PIC settled its one remaining reported claim for \$214,317, which includes the associated loss adjustment expense.

A review of the minutes to the Board of Directors' meetings 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 which occurred subsequent to the period covered by this examination requiring disclosure.

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 the course of 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., CFE, CPA*

Louis A Gabriele Jr, CPA, CFE
Insurance Examiner-In-Charge
Rhode Island Insurance Division