

REPORT OF EXAMINATION
OF THE
WILLIAMSBURG NATIONAL INSURANCE COMPANY
AS OF
DECEMBER 31, 2003

Participating State
and Zone:

California

Filed June 27, 2005

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Los Angeles, California
April 19, 2005

Honorable Alfred W. Gross
Chairman of the NAIC Financial
Condition Subcommittee
Commissioner of Insurance
Virginia Bureau of Insurance
Richmond, Virginia

Honorable John Morrison
Secretary, Zone IV-Western
Commissioner of Insurance and Securities
Montana Department of Insurance
Helena, Montana

Honorable John Garamendi
Insurance Commissioner
California Department of Insurance
Sacramento, California

Dear Chairman and Commissioners:

Pursuant to your instructions, an examination was made of the

WILLIAMSBURG NATIONAL INSURANCE COMPANY

(hereinafter also referred to as the Company) at its statutory home office and the primary location of its books and records, 12641 East 166th Street, Cerritos, California 90703

SCOPE OF EXAMINATION

The previous examination of the Company was made as of December 31, 2000. This examination covers the period from January 1, 2001 through December 31, 2003. The examination was made pursuant to the National Association of Insurance Commissioners' (NAIC) plan of examination. The examination included a review of the Company's practices and procedures, an examination of management records, tests and analyses of detailed transactions within the examination period, and an evaluation of the assets and a determination of liabilities as of December 31, 2003, as deemed necessary under the circumstances.

In addition to those items specifically commented upon in this report, other phases of the Company's operations were reviewed including the following areas that require no further comment: corporate records; fidelity bonds and other insurance; officers', employees' and agents' welfare and pension plans; growth of company; business in force by states; accounts and records; and sales and advertising.

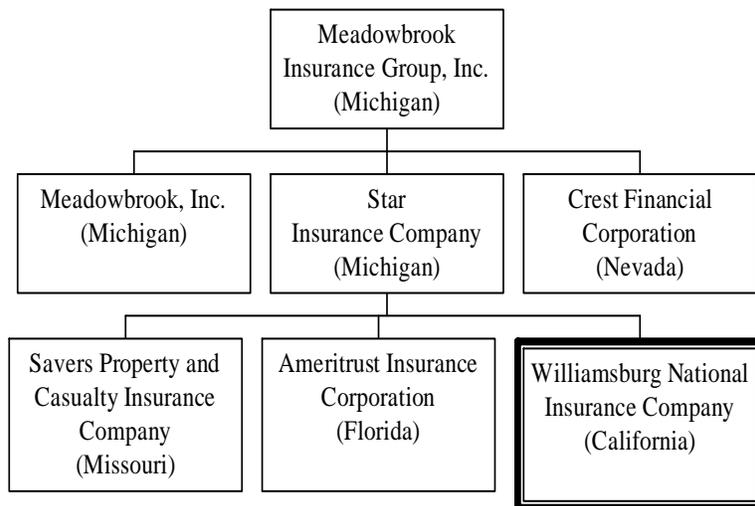
COMPANY HISTORY

The Company was incorporated under the laws of the State of California on September 18, 1986 and commenced business on December 30, 1986. On December 31, 1999, Star Insurance Company (Star), a Michigan corporation, acquired all of the outstanding stock of the Company. Star is a wholly-owned subsidiary of Meadowbrook Insurance Group, Inc., a publicly traded insurance holding company incorporated in Michigan.

The Company's immediate parent, Star Insurance Company, contributed \$857,734 in cash to the Company in 2002.

MANAGEMENT AND CONTROL

The following abridged organizational chart, which is limited to the Company's ultimate parent along with its subsidiary insurance companies and other affiliates maintaining written agreements with the Company, depicts the Company's relationship within the holding company system (all ownership is 100%):



Management of the Company is vested in a seven-member board of directors elected annually. A listing of the members of the board and principal officers serving on December 31, 2003 follows:

Directors

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Robert Samuel Cubbin Birmingham, Michigan	President and Chief Executive Officer Meadowbrook Insurance Group, Inc.
Kenn Rene Allen South Lyon, Michigan	President Meadowbrook Agency Operations
Karl Wyatt Koch (*) Shawnee Mission, Kansas	President Savers Property and Casualty Insurance Company
Archie Stephen McIntyre Shelby Township, Michigan	Senior Vice President – Business Development Meadowbrook, Inc.
Merton Joseph Segal Bloomfield Hills, Michigan	Chairman of the Board Meadowbrook Insurance Group, Inc.
Karen Marwell Spaun Farmington Hills, Michigan	Senior Vice President, Chief Financial Officer Meadowbrook Insurance Group, Inc.
Gregory Lee Wilde Troy, Michigan	Executive Vice President Meadowbrook Insurance Group, Inc.

(*) resigned November 12, 2004, replaced by Arthur Carl Pletz

Principal Officers

<u>Name</u>	<u>Title</u>
Robert S. Cubbin	Chairman of the Board of Directors and Chief Executive Officer
Gregory L. Wilde	President
Michael G. Costello	Senior Vice President, General Counsel and Secretary
Karen M. Spaun	Treasurer and Vice President
Josephine D. Duco	Assistant Vice President and Assistant Treasurer
Michael E. O’Shea	Assistant Vice President and

<u>Name</u>	<u>Title</u>
Douglas Young (**)	Assistant Secretary Assistant Vice President and Assistant Secretary

(**) resigned August 12, 2004.

Management Agreements

Management Services Agreement: Effective January 1, 2003, Meadowbrook Insurance Group, Inc. (MIGI), the Company, and Meadowbrook, Inc. (MIG) entered into a Management Service Agreement. Pursuant to the Management Services Agreement, MIG provides all accounting services; collects all funds due the Company; deposits premiums daily; pays accounts payable; provides underwriting services; arranges for appropriate reinsurance; pays all expenses; and administers all claims (pays allocated loss expenses, establishes claim files, and arranges for loss prevention services). MIG charges the Company based on projected amounts for management fees, loss control and claims expenses for specific programs. The fees shall be no greater than actual costs the Company would incur in providing the same services itself. For 2000, 2001, 2002 and 2003, the Company paid \$1,286,096, \$954,817, \$757,175 and \$1,117,785 respectively, in fees to MIG.

Tax Allocation Agreement: The Company and its affiliates are included in the consolidated federal income tax return of its ultimate parent, MIGI, pursuant to a Tax Allocation Agreement dated December 31, 1985 and subsequently amended. Each affiliate of MIGI will compute its separate tax liability as though it filed a separate tax return. All settlements are made within 30 days of filing the consolidated federal corporate income tax return. If a refund is due the Company, MIGI may defer payment to the Company for up to 30 days of receipt of refund. The Company will retain the rights to any refund or reduction in tax liability arising from unused loss or tax credit.

The above affiliated agreements have been approved by the California Department of Insurance (CDI).

Loan Agreement: The Company and its affiliates are included in the Intercompany Loan Agreement dated April 30, 2001 with MIG. The Intercompany Loan Agreement allows MIG to advance monies from one affiliate to another as intercompany loans. These loans are settled on a monthly basis and are not to exceed the threshold for prior notice set by California Insurance Code (CIC) Section 1215.5(b)(2). Subsequent to the examination date, effective September 1, 2004, this agreement was amended to allow for receipt of funds from third parties and single payments to vendors on behalf of all the companies. The Company stated that the amended agreement was submitted to and approved by the CDI.

TERRITORY AND PLAN OF OPERATION

As of December 31, 2003, the Company was licensed to transact multiple lines of property and casualty insurance in 36 states plus the District of Columbia. The Company operates on a surplus lines basis in Missouri. The following is a listing of the states in which the Company is licensed:

Alabama	Illinois	Nevada	South Dakota
Alaska	Indiana	New Mexico	Tennessee
Arizona	Iowa	New York	Texas
Arkansas	Kansas	North Dakota	Utah
California	Kentucky	Ohio	Virginia
Delaware	Maryland	Oklahoma	Washington
Florida	Michigan	Oregon	West Virginia
Georgia	Montana	Pennsylvania	Wisconsin
Idaho	Nebraska	South Carolina	Wyoming

In 2003, direct premium written was \$39.8 million. Of the direct premium written, \$30.2 million (75.9%) was written in California, \$4.2 million (10.5%) was written in Tennessee, and \$3.6 million (9.0%) was written in Nevada.

The Company originally wrote auto liability and related lines for the trucking industry. Workers' compensation became the Company's dominant line of business from 2000 through 2002. This line was reduced in 2003 when the Company opted to discontinue its unprofitable programs to improve operating performance. In 2003, 64.6% of the business written was commercial auto insurance, and 26.3% was workers' compensation.

The Company has operations in Cerritos, California and Southfield, Michigan. The Cerritos office manages the commercial multiple peril, inland marine, auto liability and auto physical damage lines, while the Southfield office maintains the commercial package policy, umbrella liability, and workers' compensation lines. In addition, there are 16 field offices operated by Meadowbrook Insurance Group, Inc.

The Company writes business utilizing agents, general agents, and third party administrators. Marketing distribution is through agents with a focus on business by program. Programs include the truckers' program (auto liability, auto physical damage and inland marine), the agricultural business program (property and liability for working farms), several workers' compensation programs, plus several others.

LOSS EXPERIENCE

The Company reported operating and/or net losses in the three years under examination as follows:

Year	Net Underwriting Gain or (Loss)	Net Income Or (Loss)
2000	\$ 57,349	\$ 580,684
2001	(211,488)	317,749
2002	(1,503,998)	(1,029,539)
2003	3,867,591	2,689,054

Although the Company received a capital contribution of \$857,734 in 2002, its surplus has remained fairly stable over the examination period. Reduction of unprofitable programs, particularly in workers' compensation, caused net income and surplus to improve in 2003.

REINSURANCE

Assumed

Other than certain mandatory reinsurance pools, the Company has no reinsurance assumed.

Ceded

The Company cedes most of its premiums written to its immediate parent, Star Insurance Company. Of the Company's \$39.8 million in direct premiums written, \$5 million were retained. The following is a summary of the principal ceded reinsurance treaties inforce as of December 31, 2003:

<u>Type of Contract</u>	<u>Reinsurer's Name</u>	<u>Company's Retention</u>	<u>Reinsurer's Maximum Limits</u>
Multi –Line Quota Share	Star Insurance Company – 100%	10% of each net loss occurrence after excess	90% each net loss occurrence after excess
1 st Excess of Loss – Workers' Compensation & Employer Liability	Employers Reinsurance Corporation – 100%	\$300,000 each loss occurrence	\$700,000 each loss occurrence
2 nd Excess of Loss – Workers' Compensation & Employer Liability	Employers Reinsurance Corporation – 100%	\$1 million each loss occurrence	\$1 million each loss occurrence
3 rd Excess of Loss – Workers' Compensation & Employer Liability	Employers Reinsurance Corporation – 100%	\$2 million each loss occurrence	\$3 million each loss occurrence
4 th Excess of Loss – Workers' Compensation & Employer Liability	Omitted after restructuring, April 2003, but higher layers retained their layer titles.		
5 th Excess of Loss – Workers' Compensation & Employer Liability	American National Insurance Co. – 30% Lloyds and London Companies – 40%	\$5 million each loss occurrence	\$5 million each loss occurrence
5 th Excess of Loss – Workers' Compensation, Terrorism Only	Axis Specialty Reinsurance – 100%	\$5 million each loss occurrence	\$5 million each loss occurrence
6 th Excess of Loss – Workers' Compensation & Employer Liability	American National Insurance Co. – 45% PMA Capital Insurance Co. – 15% (*) Lloyds and London Companies – 40%	\$10 million each loss occurrence	\$10 million each loss occurrence

<u>Type of Contract</u>	<u>Reinsurer's Name</u>	<u>Company's Retention</u>	<u>Reinsurer's Maximum Limits</u>
7 th Excess of Loss – Workers' Compensation & Employer Liability	American National Insurance Co. – 25% PMA Reinsurance – 15% (*) Folksamerica Reinsurance – 15% Aspen Insurance UK Limited – 2.40% Lloyds and London Companies – 42.60%	\$20 million each loss occurrence	\$30 million each loss occurrence
1 st Excess of Loss – Core Casualty	Employers Reinsurance Corp. – 75% Lloyds and London Companies – 25%	\$350,000 each loss occurrence	\$650,000 each loss occurrence
2 nd Excess of Loss – Core Casualty	Employers Reinsurance Corp. – 75% Lloyds and London Companies – 25%	\$1,000,000 each loss occurrence	\$1,000,000 each loss occurrence
3 rd Excess of Loss (clash) – Core Casualty	Employers Reinsurance Corp. – 75% Lloyds and London Companies – 25%	\$2,000,000 each loss occurrence	\$3,000,000 each loss occurrence
1 st Excess of Loss – Crest Trucking	Motors Insurance Corporation – 100%	\$350,000 each risk attaching	\$650,000 each risk attaching
2 nd Excess of Loss (clash) – Crest Trucking	Motors Insurance Corporation – 100%	\$1,000,000 each risk attaching	\$1,000,000 each risk attaching

(*) replaced by Endurance Reinsurance Co., 1/1/2004

The Company reported in its 2003 Annual Statement reinsurance recoverables and ceded reserve credits totaling \$41.2 million, which represents 301% of the Company's reported policyholder surplus as of December 31, 2003. Of the total reinsurance recoverables and ceded reserve credits, \$35.1 million is attributable to reinsurance with the Company's immediate parent, Star Insurance Company.

Subsequent to the examination date, the Company executed an Inter-Company Reinsurance Agreement, effective January 1, 2005, with several affiliates by which it cedes 100% of its premiums, losses and loss adjustment expenses, net of ceded reinsurance to nonaffiliates, to Star Insurance Company (Star), the Company's immediate parent, and then reassumes 13% of the resulting pooled amounts. Any change to the pooling percentages must be pre-approved by the California Department of Insurance.

FINANCIAL STATEMENTS

The financial statements prepared for this examination report include:

Statement of Financial Condition as of December 31, 2003

Underwriting and Investment Exhibit for the Year Ended December 31, 2003

Reconciliation of Surplus as Regards Policyholders
from December 31, 2000 through December 31, 2003

Statement of Financial Condition
as of December 31, 2003

<u>Assets</u>	<u>Ledger and Nonledger Assets</u>	<u>Assets Not Admitted</u>	<u>Net Admitted Assets</u>	<u>Notes</u>
Bonds	\$ 10,928,688	\$	\$ 10,928,688	
Cash and short-term investments	4,533,203		4,533,203	
Investment income due and accrued	134,606		134,606	
Premiums and considerations:				
Uncollected premiums and agents' balances in course of collection	2,712,604	390,070	2,322,534	
Deferred premiums, agents' balances and installments booked but deferred and not yet due	3,600,657	47,161	3,553,496	
Reinsurance:				
Amounts recoverable from reinsurers	300,088		300,088	
Net deferred tax asset	979,781	131,689	848,092	
Receivable from parent, subsidiaries and affiliates	5,253		5,253	
Health care and other amounts receivable	9,996	9,996		
Aggregate write-ins for other than invested assets	<u>370,191</u>	<u>504,463</u>	<u>(134,272)</u>	
Total assets	<u>\$ 23,575,067</u>	<u>\$ 1,083,379</u>	<u>\$ 22,491,689</u>	
 <u>Liabilities, Surplus and Other Funds</u>				
Losses			\$ 853,261	(1)
Loss adjustment expenses			1,163,718	(1)
Commissions payable, contingent commissions and other similar charges			435,176	
Other expenses			317,106	
Taxes, licenses and fees			864,093	(2)
Current federal and foreign income taxes			1,181,804	
Unearned premiums			1,803,649	
Ceded reinsurance premiums payable			2,099,872	
Amounts withheld or retained by company			4,000	
Provision for reinsurance			0	(3)
Payable to parent, subsidiaries and affiliates			44,365	
Aggregate write-ins for liabilities			<u>3,985</u>	
Total liabilities			8,771,027	
Common capital stock		\$ 2,600,000		
Gross paid-in and contributed surplus		6,157,734		
Unassigned funds (surplus)		<u>4,962,927</u>		
Surplus as regards policyholders			<u>13,720,661</u>	
Total liabilities, surplus and other funds			<u>\$ 22,491,689</u>	

Underwriting and Investment Exhibit
for the Year Ended December 31, 2003

Statement of Income

Underwriting Income

Premiums earned		\$ 3,568,571
Deductions:		
Losses incurred	\$ 344,888	
Loss expense incurred	1,177,904	
Other underwriting expenses incurred	<u>(1,821,812)</u>	
Total underwriting deductions		<u>(299,020)</u>
Net underwriting gain		3,867,591

Investment Income

Net investment income earned	\$ 483,330	
Net realized capital gains	<u>6,370</u>	
Net investment gain		489,700

Other Income

Net loss from agents' or premium balances charged off	\$ (68,165)	
Finance and service charges not included in premiums	28,950	
Aggregate write-ins for miscellaneous income	<u>1,300</u>	
Total other income		<u>(37,915)</u>
Net income before federal income taxes		4,319,376
Federal income taxes incurred		<u>1,630,322</u>
Net income		<u>\$ 2,689,054</u>

Capital and Surplus Account

Surplus as regards policyholders, December 31, 2002		\$ 11,227,899
Net income	\$ 2,689,054	
Change in net deferred income tax	383,149	
Change in nonadmitted assets	<u>(579,441)</u>	
Change in surplus as regards policyholders		<u>2,492,762</u>
Surplus as regards policyholders, December 31, 2003		<u>\$ 13,720,661</u>

Reconciliation of Surplus as Regards Policyholders
from December 31, 2000 through December 31, 2003

Surplus as regards policyholders, December 31, 2000, per Examination			\$ 11,021,897
	<u>Gain in Surplus</u>	<u>Loss in Surplus</u>	
Net income	\$ 1,977,262	\$	
Change in net deferred income tax	934,252		
Change in nonadmitted assets		1,033,293	
Cumulative effect of changes in accounting principles		37,191	
Surplus adjustments: Paid-in	<u>857,734</u>	<u> </u>	
Totals	<u>\$ 3,769,248</u>	<u>\$ 1,070,484</u>	
Net increase in surplus as regards policyholders			<u>2,698,764</u>
Surplus as regards policyholders, December 31, 2003, per Examination			<u>\$ 13,720,661</u>

COMMENTS ON FINANCIAL STATEMENT ITEMS

(1) Losses and Loss Adjustment Expenses

A Casualty Actuary from the California Department of Insurance reviewed the Company's loss and loss adjustment expense reserves. Based on the analysis, the Company's loss and loss adjustment expense reserves as of year-end 2003 were determined to be reasonably stated and have been accepted for purposes of this report.

It was noted, however, that loss and loss adjustment expense reserves for commercial auto liability were deficient by \$40,503 according to California Insurance Code (CIC) Section 11558. Due to the immateriality of the amount, no examination adjustment was made. It is recommended that the Company maintain reserves for losses and loss adjustment expenses in accordance with CIC Section 11558.

(2) Taxes, Licenses and Fees

CIC Sections 1872.8(a), 1872.81(a) and 1874.8(a) state, in part, that each insurer doing business in the State of California must pay an annual Vehicle Fraud Assessment Fee for each vehicle insured under an insurance policy it issues in California. The fee provides funding for the increased investigation and prosecution of fraudulent automobile insurance claims and automobile theft in the State of California. During the course of this examination, it was noted that the Company inadvertently failed to remit the Vehicle Fraud Assessment Fee on its policies issued under its Trucking program as required by the above CIC Sections. The total amount due is \$13,057 plus additional late charges assessed based on CIC Section 12995 and is summarized by quarter as follows:

Quarter	Fee/Vehicle	Vehicle Count	Amount Due
1/1/01 – 3/31/01	\$0.45	2,538	\$1,142
4/1/01 – 6/30/01	\$0.45	2,448	\$1,102
7/1/01 - 9/30/01	\$0.45	2,217	\$998
10/1/01 – 12/31/01	\$0.45	2,089	\$940
1/1/02 – 3/31/02	\$0.45	1,902	\$856
4/1/02 – 6/30/02	\$0.45	1,774	\$798
7/1/02 - 9/30/02	\$0.45	1,492	\$671
10/1/02 – 12/31/02	\$0.45	1,242	\$559
1/1/03 – 3/31/03	\$0.45	1,602	\$721
4/1/03 – 6/30/03	\$0.45	2,677	\$1,205
7/1/03 – 9/30/03	\$0.45	3,810	\$1,715
10/1/03 – 12/31/03	\$0.45	5,222	\$2,350
	Total	29,013	\$13,057

It is recommended that the Company remit the amount due to the California Department of Insurance (CDI) and implement procedures to insure future compliance. The Company and the CDI are in the process of settling the assessment fee and the additional late charges. Since the amount was deemed not material, no adjustment was made to the Company's financial statements. The Company stated that it has implemented procedures to assure future compliance with the requirement of CIC Sections 1872.8(a), 1872.81(a) and 1874.8(a).

(3) Provision for Reinsurance

It was noted that several assuming reinsurers listed as authorized to conduct business in California on the Company's Schedule F – Part 3 were not actually authorized. As a result, the provision for unauthorized reinsurance was increased by \$206,000. Due to the immateriality of the amount, no examination adjustment was made.

SUMMARY OF COMMENTS AND RECOMMENDATIONS

Current Report of Examination

Comments on Financial Statement Items - Losses and Loss Adjustment Expenses (Page13): It is recommended that the Company maintain reserves for losses and loss adjustment expenses in accordance with California Insurance Code (CIC) Section 11558

Comments on Financial Statement Items - Taxes, Licenses and Fees (Page 13): It is recommended that the Company remit amounts due pursuant to the Vehicle Fraud Assessment program and implement procedures to insure future compliance.

Previous Report of Examination

Management and Control – Intercompany Agreements (Page 5): It was recommended that the Company’s Management Service Agreement with Meadowbrook, Inc. be amended to reflect the Company as a party to the agreement. A new agreement was executed in 2003 which includes the Company as a party to the agreement.

Accounts and Records (Page 9): It was recommended that the Company automate its workers’ compensation information systems and make appropriate changes to strengthen internal controls. In addition, it was recommended that the Company separately itemize fidelity/forgery and burglary/theft business within its Annual Statement The Company has automated its information systems for workers’ compensation and made appropriate changes to strengthen internal controls. In 2003, the Company was no longer writing either fidelity/forgery or burglary/theft business.

ACKNOWLEDGEMENT

The courtesy and cooperation extended by the Company's officers and affiliate's employees during the course of this examination are hereby acknowledged.

Respectfully submitted,

_____/S/_____
David Gilman, CFE
Examiner-In-Charge
Associate Insurance Examiner
Department of Insurance
State of California