

# STATE OF CONNECTICUT

## INSURANCE DEPARTMENT

### ORDER ADOPTING REPORT OF EXAMINATION

I, Anne Melissa Dowling, Deputy Insurance Commissioner of the State of Connecticut, having fully considered and reviewed the Examination Report (the "Report") of the Sentinel Insurance Company, Ltd. ("the Company") as of December 31, 2012, do hereby adopt the findings and recommendations contained therein based on the following findings and conclusions,

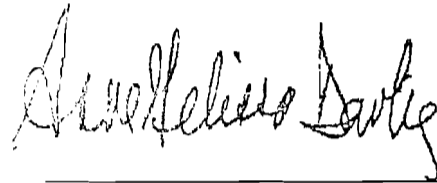
**TO WIT:**

1. I, Anne Melissa Dowling, Deputy Insurance Commissioner of the State of Connecticut, and as such is charged with the duty of administering and enforcing the provisions of Title 38a of the Connecticut General Statutes ("CGS").
2. The Company is a domestic insurer authorized to transact the business of insurance in the State of Connecticut.
3. On January 13, 2014, the verified Report of the Company was filed with the Connecticut Insurance Department (the "Department").
4. In accordance with CGS §38a-14(e) (3), the Company was afforded a period of thirty (30) days within which to submit to the Connecticut Insurance Department a written submission or rebuttal with respect to any matters contained in the Report.
5. On February 12, 2014, the Company notified the Department of certain responses and comments relating to matters contained in the Report.
6. Following a review of the Report, it was deemed necessary and appropriate to modify the Report. A copy of the Report is attached hereto and incorporated herein as Exhibit A.

**NOW, THEREFORE,** it is ordered as follows:

1. That the Report of the Company hereby is adopted as filed with the Department.
2. That the Company shall comply with all of the recommendations set forth in the Report, and that the failure of the Company to so comply shall result in sanctions or administrative action as provided by Title 38a of the CGS.

Dated at Hartford, Connecticut this 18th day of February, 2014



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Anne Melissa Dowling  
Deputy Insurance Commissioner

EXHIBIT A

EXAMINATION REPORT

OF THE

SENTINEL INSURANCE COMPANY, LTD.

AS OF

DECEMBER 31, 2012

BY THE

CONNECTICUT INSURANCE DEPARTMENT

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January 13, 2014

The Honorable Thomas B. Leonardi  
Commissioner of Insurance  
State of Connecticut Insurance Department  
153 Market Street  
Hartford, Connecticut 06103

Dear Commissioner Leonardi:

In compliance with your instructions and pursuant to the requirements of Section 38a-14 of the General Statutes of the State of Connecticut (CGS), the undersigned has made a financial examination of the condition and affairs of the

**SENTINEL INSURANCE COMPANY, LTD.**

(hereinafter referred to as the Company or Sentinel), a corporation with capital stock, incorporated under the laws of the State of Connecticut and having its statutory home office and its main administrative office located at One Hartford Plaza, Hartford, Connecticut 06155. The report on such examination is respectfully submitted.

SCOPE OF EXAMINATION

The previous examination of the Company was conducted as of December 31, 2007. The current examination which covers the subsequent five-year period was conducted at the statutory home office of the Company.

As part of the examination planning procedures, the Financial Regulation Division of the Connecticut Insurance Department (the Department) reviewed the following materials submitted by the Company:

- Board of Director (Board) minutes from 2008 through the latest 2013 meeting;
- statutory audit reports from 2008 through 2012, completed by the Company's independent certified public accountants, Deloitte & Touche, LLP (D&T);
- Management's Discussion and Analysis from 2008 through 2012;
- Statements of Actuarial Opinion from 2008 through 2012;
- documentation supporting Section 404 of the Sarbanes-Oxley Act of 2002;
- Annual Statements filed with the Department; and
- reports of the Company's Internal Audit Department from 2008 through 2012.

A comprehensive review was made of the financial analysis files and documents submitted to the Financial Analysis Unit of the Department, reports from the National Association of Insurance Commissioners (NAIC) database, as well as the independent audit reports which indicated no material concerns with respect to financial condition or regulatory compliance issues.

SENTINEL INSURANCE COMPANY, LTD.

Workpapers prepared by D&T in connection with its annual statutory audit were reviewed and relied upon to the extent deemed appropriate.

Jennan Enterprises, LLC (Jennan) was engaged by the Department to conduct an evaluation of the Information Technology (IT) controls.

Invotex Group (Invotex) was engaged by the Department to conduct an evaluation of the Company's investment holdings and provided staff accounting services.

Oliver Wyman Actuarial Consulting, Inc. (Oliver Wyman) was engaged by the Department to conduct an evaluation of the Company's reserving and underwriting processes.

The State of Indiana contracted with Noble Consulting Services, Inc. (Noble) for the examination of the Indiana domestic insurance companies. The State of Illinois contracted with INS Regulatory Insurance Services, Inc. (INS) for the examination of the Illinois domestic insurance company.

The examination was conducted on a full scope, comprehensive basis in accordance with the procedures outlined in the NAIC Financial Condition Examiners Handbook (the Handbook). The Handbook requires that we plan and perform the examination to evaluate the financial condition and identify prospective risks of the Company by obtaining information about the Company, including corporate governance, identifying inherent risks within the Company, and evaluating system controls and procedures used to mitigate those risks. An examination also includes assessing the principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation, management compliance with the NAIC Accounting Practices & Procedures Manual (Manual) and the NAIC Property and Casualty Annual Statement Instructions.

Concurrent examinations were made of the following Connecticut and non-Connecticut domestic property and casualty companies within The Hartford Financial Services Group, Inc. (the Group or HFSG), collectively referred to as the Hartford Fire Pool (HFP):

- Nutmeg Insurance Company (CT)
- Hartford Accident and Indemnity Company (CT)
- Hartford Insurance Company of Illinois (IL)
- Hartford Casualty Insurance Company (IN)
- Hartford Underwriters Insurance Company (CT)
- Pacific Insurance Company, Limited (CT)
- Twin City Fire Insurance Company (IN)
- Hartford Fire Insurance Company (CT)
- Hartford Insurance Company of the Midwest (IN)
- Trumbull Insurance Company (CT)
- Property and Casualty Insurance Company of Hartford (IN)
- Hartford Lloyd's Insurance Company (TX)
- Hartford Insurance Company of the Southeast (CT)

SENTINEL INSURANCE COMPANY, LTD.

The Department also performed concurrent financial examinations of three Connecticut domestic affiliates which are currently in run-off:

First State Insurance Company (FSIC)  
New England Insurance Company (NEIC)  
New England Reinsurance Corporation (NERC)

These companies are collectively referred to as the First State Insurance Group (FSIG).

The Department also performed an examination of the following Connecticut domestic life insurance affiliates:

Hartford Life Insurance Company  
Hartford Life and Accident Insurance Company (HLAIC)  
Hartford Life and Annuity Insurance Company  
Hartford International Life Reassurance Corporation  
American Maturity Life Insurance Company

All accounts and activities of the Company were considered in accordance with the risk focused examination process.

Comments in this report are generally limited to exceptions noted or to items considered to be of a material nature.

Failure of items in this report to add to totals or for totals to agree with captioned amounts is due to rounding.

HISTORY

Sentinel Insurance Company (Sentinel – HI) was originally incorporated on November 30, 1955, under the laws of the Territory of Hawaii. Sentinel-HI commenced business immediately, writing all lines of insurance under its Certificate of Authority.

In 1963, Hartford Fire Insurance Company (Hartford Fire) acquired Pacific Insurance Company, Limited (Pacific) and its subsidiary Sentinel – HI.

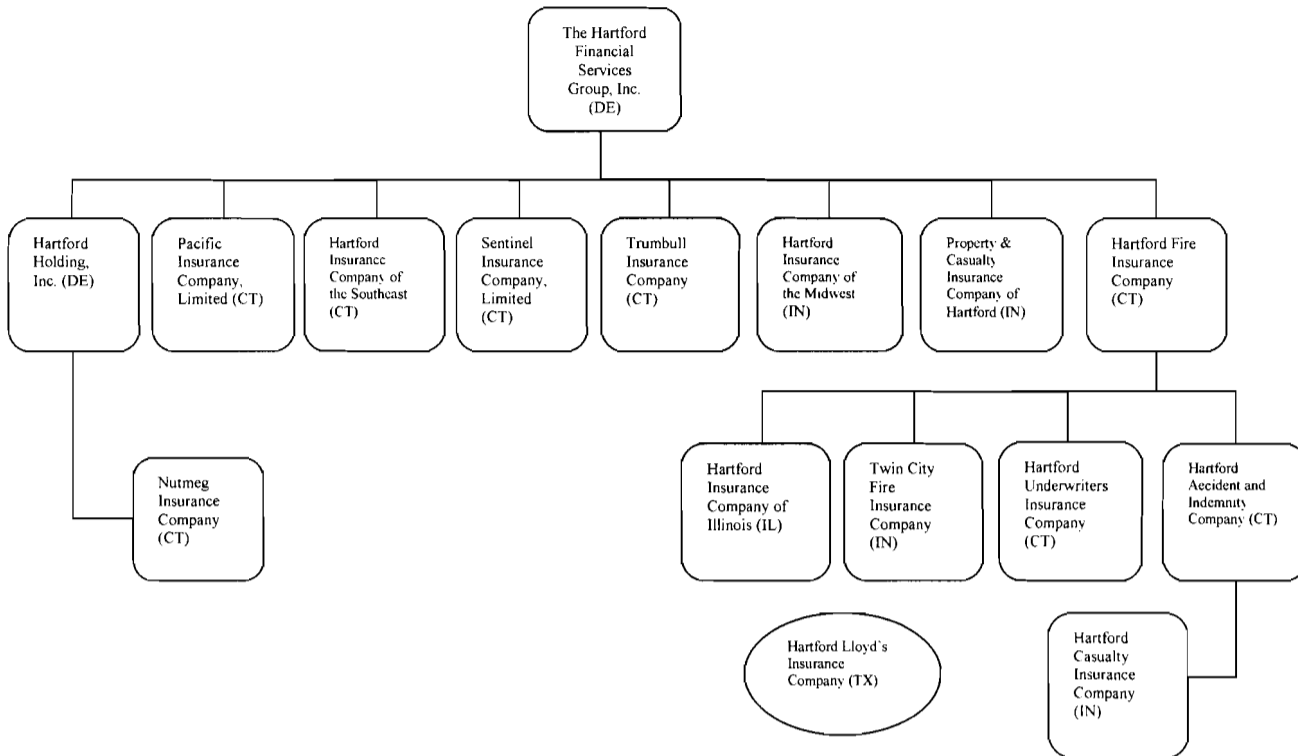
Sentinel Insurance Company of Connecticut (Sentinel-CT) was incorporated in Connecticut on July 6, 1999, for the purposes of re-domesticating Sentinel - HI from Hawaii to Connecticut. Effective October 14, 1999, Sentinel – HI merged with and into Sentinel – CT, with Sentinel – CT remaining as the surviving corporation. Simultaneous with the merger, Sentinel – CT changed its name to Sentinel Insurance Company, Ltd. As part of the merger, ownership of the Company changed from Pacific to Hart Re Group, LLC (Hart Re) a wholly owned subsidiary of Nutmeg Insurance Company. The Company is a member of the HFP.

In June 2003, Hart Re transferred ownership of Sentinel to HFSG.

SENTINEL INSURANCE COMPANY, LTD.

ORGANIZATIONAL CHART

The following is an organizational chart of the Company and its parent, subsidiaries and affiliated companies within the Group as of December 31, 2012:



Notes to Organizational Chart

The Texas domestic, Hartford Lloyd’s Insurance Company, is part of the HFP. The Group also owns one hundred percent of Heritage Holdings, Inc., the parent company of FSIC. FSIC is the parent company of NEIC and NERC.

MANAGEMENT AND CONTROL

Annual Shareholders Meetings

The bylaws state that the annual meeting of the stockholders shall be held at the office of the Company, in the City of Hartford, Connecticut, on such day and at such hour in the months of January, February or March of each year as the Board may appoint for the election of Directors and such other business as may properly come before said meeting.

Special meetings of the stockholders may be called at any time by the chairman of the Board (Chairman), or the president or, in the absence of both, by any vice-president and shall be so called upon the written request of a majority of the Directors.

Written notice of every meeting of the stockholders and the time and place thereof shall be given by an executive officer of the Company at least seven days prior to the time appointed for such meeting.



SENTINEL INSURANCE COMPANY, LTD.

Board of Directors

The management of the property and affairs of the Company shall be vested in the Board subject to provisions of the charter of the Company, the acts amendatory thereof and the bylaws. The number of directors shall not be fewer than three. Regular and special meetings of the Board shall be held in the city of Hartford or such other place as may be designated by the Board and at such times and on such dates as may be determined by the Board. A majority of the members of the Board, present at a regular or special meeting, shall constitute a quorum for the transaction of business.

Directors serving the Company as of December 31, 2012, were:

<u>Name</u>	<u>Title and Principal Business Affiliation</u>
Andre A. Napoli	Chief Executive Officer and President Hartford Fire Insurance Company
Douglas G. Elliot	President, Commercial Markets The Hartford Financial Services Group, Inc.
Mark J. Niland	Head of Portfolio Management The Hartford Financial Services Group, Inc.
Robert W. Paiano	Senior Vice President and Treasurer Hartford Fire Insurance Company

Officers

The president, a vice president, a secretary, and a treasurer shall be elected by the Board. The Board may also elect one of its members to serve as Chairman, and if there is a finance committee, the Board shall elect one of its members to serve as Chairman of such committee. The president, or an officer appointed by him, shall have authority to appoint all other officers, except as stated herein, including one or more vice presidents and assistant vice presidents, one or more associate or assistant treasurers, one or more secretaries and assistant secretaries, and such other officers as the president may from time to time designate. All officers of the Company shall hold office at the pleasure of the Board.

Senior officers of the Company as of December 31, 2012, were:

<u>Name</u>	<u>Title</u>
Andre A. Napoli	President and Chief Executive Officer
Jonathan R. Bennett	Executive Vice President and Chief Financial Officer
Michael R. Hazel	Vice President and Controller

SENTINEL INSURANCE COMPANY, LTD.

Thomas Moran	Senior Vice President and Director of Taxes
Robert W. Paiano	Senior Vice President and Treasurer
Michael W. Kooken	Senior Vice President and Chief Actuary
Terence D. Shields	Assistant Vice President and Corporate Secretary

RELATED PARTY AGREEMENTS

Investment Management and Administration Agreement

The Company is party to an investment management and administration agreement with Hartford Investment Management Company (HIMCO). Pursuant to the terms of the agreement, HIMCO provides a broad spectrum of investment services, including but not limited to providing advice to the Company concerning the development of investment strategies and objectives, the development of investment policies and guidelines, the investment and management of assets, the measurement and evaluation of investment performance, investment accounting, cash management, the management of banking relationships, the management of a custodial relationship, and administrative support.

Investment Pooling Agreement

The Company participates in a Second Amended and Restated Investment Pooling Agreement between Hartford Investment Services, Inc. (Hartford Investment) and HIMCO. Hartford Investment acts as the investment manager to invest certain cash balances available to the participants in the investment pool known as "Hartford Short-Term Investment Pool". Hartford Investment is compensated at least quarterly for all incurred direct and indirect costs related to the services provided to the Company.

Tax Allocation Agreement (TAA)

The Company is party to a TAA with HFSG and its subsidiaries. The TAA governs the tax return filing, payment and allocation of federal, state and local income tax liability between HFSG and its subsidiaries. Each member will calculate its separate tax liability, and the consolidated federal regular income tax liability will be apportioned among the members in accordance with the ratio which is consistent with the taxable income. Payment to the parent will be made by the due date of the payment to the Internal Revenue Service.

Intercompany Pooling Agreement

The Company is party to an intercompany reinsurance and pooling agreement whereby all property and casualty business written by these companies is ceded to Hartford Fire, the lead participant. The total pool of business is then redistributed to the various participants, including the Company, based on their pre-determined percentage. Each participant in the pool agrees to cede to the Hartford Fire, and Hartford Fire accepts, assumes, and reinsures 100% of each other participant's underwriting liabilities. Hartford

## SENTINEL INSURANCE COMPANY, LTD.

Fire then cedes to each participant, and each participant accepts, assumes and reinsures its proportionate share.

### Cost Allocation Agreements

The Company is party to a number of service and cost sharing agreements with several of its affiliates including HFSG. Such services include, but shall not be limited to: employee costs such as salaries, benefit and taxes; fixed assets including furniture and personal computers; miscellaneous accounts payable including rent, travel and entertainment, insurance, advertising, taxes, license and fees, etc.; and costs related to corporate services.

Hartford Fire is incurring and paying certain expenses on behalf of other legal entities and acting as the banker for these entities without a signed written agreement. Statements of Statutory Accounting Principles (SSAP) No. 25 states, in part, that “transactions between related parties must be in the form of a written agreement”. It is recommended that the Company prepare a cost allocation agreement to comply with SSAP No. 25 and submit it to the Department for approval. On November 25, 2013, the Company filed a new services and cost allocation agreement with the Department.

### INSURANCE COVERAGE

The Company is insured under a fidelity policy issued by five insurers (St. Paul Fire and Marine Insurance Company, Federal Insurance Company, Fidelity and Deposit Company of Maryland, ACE American Insurance Company, and Continental Casualty Insurance Company). HFSG and its affiliates are listed as named insureds. Coverages include, but are not limited to business automobile liability, directors and officers liability, errors and omissions liability, employment practices liability, computer crime, fiduciary, general liability, commercial property, and workers’ compensation. The coverages also include an aggregate liability of \$200 million, a single loss limit of liability of \$100 million and a single loss deductible of \$10 million. These limits exceed the suggested minimum as outlined in the Handbook.

### TERRITORY AND PLAN OF OPERATION

The Company is licensed to write multiple lines of property and casualty insurance in all fifty states and the District of Columbia.

The HFP provides: (1) workers’ compensation, property, automobile, marine, livestock, liability, and umbrella coverage to commercial accounts primarily throughout the United States; (2) a variety of customized insurance products and risk management services including professional liability, fidelity, surety, and specialty casualty coverage to commercial accounts; (3) standard automobile, homeowners and home-based business coverage to individuals across the United States, including a special program designed exclusively for members of AARP. It also operates a member contact center for health insurance products offered through the AARP Health program.

SENTINEL INSURANCE COMPANY, LTD.

REINSURANCE

The property and casualty companies listed below participate in the Pooling Agreement, an intercompany reinsurance and pooling agreement whereby all property and casualty business written by these companies is ceded to Hartford Fire, the lead participant. The total pool of business is then redistributed to the various participants, including the Company, based on pre-determined percentages.

Each participant in the HFP agrees to cede to Hartford Fire and Hartford Fire accepts, assumes, and reinsures 100% of each participant's underwriting liabilities. Hartford Fire then cedes to each participant and each participant accepts and assumes its proportionate share as identified below. The participants share to the extent of their pooling percentages: (a) all premiums written by the HFP; (b) all amounts paid or incurred during such period for losses and loss adjustment expenses (LAE); other underwriting expenses and other specific losses arising out of their underwriting operations; (c) all claims and settlements involving business covered by the agreement; and (d) all resulting net underwriting income or loss. All participants settle their accounts monthly, within thirty days of closing.

The following are the member company participation percentages in effect at December 31, 2012:

	<u>Pooling Percentages</u>
Hartford Fire Insurance Company	41.50
Hartford Accident and Indemnity Company	32.69
Hartford Insurance Company of Illinois	10.10
Hartford Casualty Insurance Company	5.50
Hartford Underwriters Insurance Company	4.00
Pacific Insurance Company, Limited.	1.70
Twin City Fire Insurance Company	1.50
Nutmeg Insurance Company	0.70
Trumbull Insurance Company	0.50
Hartford Insurance Company of the Midwest	0.50
Property and Casualty Insurance Company of Hartford	0.50
Hartford Insurance Company of the Southeast	0.50
Sentinel Insurance Company, Ltd.	0.30
Hartford Lloyd's Insurance Company	<u>0.01</u>
Pool Total	<u>100.0%</u>

All accident and health business written by the Company and its United States affiliates is 100% reinsured with HLAIC.

Reinsurance Accounting Systems

The Company uses various sub-systems, the most significant being the ProCede application, to process and report reinsurance. ProCede identifies direct written risks to which reinsurance applies and calculates ceded premiums and losses. ProCede processes reinsurance accounting entries to the Basic Loss Control (BLC) system and to the New

## SENTINEL INSURANCE COMPANY, LTD.

Premium Processing System (NPPS) which both feed the general ledger. Cash disbursements, receipts, transfers, and miscellaneous adjustments against receivable and payable balances are fed from ProCede to the general ledger via ReCess, the reinsurance operations workstation. Receivable and payable balances at a reinsurer and contract level are maintained in the reporting database in ReCess. Business assumed from pools and ceding companies is processed through the Strategic HartRe Automated Reinsurance Process (SHARP) system. SHARP feeds NPPS, BLC and Cores (an actuarial reporting system) which in turn feeds the general ledger.

### Assumed Reinsurance

All reinsurance assumed from external companies is booked by Hartford Fire. In April 2003, the Company made a strategic decision to exit the assumed reinsurance business and place its assumed reinsurance operations into run-off. With the exception of primarily mandatory participations in a limited number of reinsurance pools and associations, the Company no longer engages directly in the assumed reinsurance business. The only remaining significantly assumed premium income relates to business written in Texas using a "front company" (i.e. Republic Underwriters) to achieve an alternative rating vehicle for certain personal lines business and premium income resulting from participation in the National Council on Compensation Insurance, Inc., National Workers' Compensation pool.

### Ceded Reinsurance

The Company maintains various reinsurance treaties including a property per-risk excess of loss and a property catastrophe reinsurance program intended to limit group-level exposures to pre-determined levels of risk. These corporate excess of loss and catastrophe reinsurance programs cover the Company and its pool affiliates. The Company places 100% of the first \$90 million in per-risk loss exposure above a loss retention of \$10 million per covered risk with a group of reinsurers. Coverage is provided by four individual layers, each fully subscribed by various external reinsurers.

Property catastrophe exposures are reinsured through three layers providing approximately \$675 million (90%) of the first \$750 million in coverage for aggregate catastrophe related losses above an initial retention of \$350 million per insured event. In addition to the reinsurance protection provided by the Company's traditional property catastrophe reinsurance program, the Company has fully collateralized reinsurance coverage from Foundation Re III for losses sustained from qualifying hurricane loss events.

The Workers' Compensation Catastrophe Excess of Loss Reinsurance program, which became effective July 1, 2012, is a multi-layer program that covers industrial accident perils, natural perils and terrorism perils on an excess of loss basis with a limit of \$350 million excess of \$100 million retention and is 95% placed. In addition, the program includes a non-catastrophe, industrial accident layer for 80% of \$30 million limit excess of a \$20 million retention.

The Company also cedes business covering specified business units to external reinsurers on both a facultative and treaty basis. Facultative reinsurance is purchased covering

## SENTINEL INSURANCE COMPANY, LTD.

specified individual risks depending on need. The reinsurance treaties cover specified property and casualty business segments and consist of working layers, umbrella layers and catastrophe layers. The Company's retention will vary based upon business unit and corporate risk appetite.

### INFORMATION TECHNOLOGY CONTROLS

Jennan performed a risk-focused assessment and review of the Company's IT general controls in accordance with NAIC requirements as outlined in the Handbook. The guidance and direction used to perform the review of the Company's IT general controls was derived from Exhibit C Part 1 – Information Technology Planning Questionnaire (ITPQ) and Exhibit C Part 2 – Information Technology Work Program (collectively, Exhibit C). The Company's responses to the ITPQ were evaluated, and certain controls within the IT control environment were tested to assess whether the selected controls were designed effectively and were functioning properly.

Jennan's objectives were to determine that Information Systems resources align with the Company's objectives and ensure that significant risks (strategic, operational, reporting, and compliance) arising out of its IT environment were appropriately mitigated by strategies and controls as outlined in the Handbook's Exhibit C Part 2 – Evaluation of Controls in Information Technology Work Program.

The objectives above were achieved through a combination of reviewing the Company's policies and procedures, testing in key areas related to Exhibit C, interviewing the Company's IT senior management, reviewing IT risk assessment processes, and leveraging the risk assessment procedures performed by the Company's internal and external auditors.

As a result of this review, findings were noted in controls over operations, logical security, physical security, application changes, and corporate governance. These findings were presented to the Company along with recommendations that the Company establish and implement appropriate control policies and procedures to strengthen its IT controls. The Company's remediation is well underway, with efforts expected to be complete by year end 2013. It is recommended that the Company continue these remediation efforts. In 2014, the Department will conduct a limited IT review to assess the Company's remediation policies and procedures.

### ACCOUNTS AND RECORDS

The Company reports all financial accounting transactions in Horizon, a Peoplesoft, Inc. system, the official book of record for all HFSG financial accounting operations.

The majority of accounting transactions within Horizon originate from monthly feeds that flow through a process called the interface manager which is responsible for summarizing, converting and extracting the financial data from each feeding system in order to populate the Horizon database. These feeds represent the detail monthly activity of the various administrative systems including premiums, losses, expenses, investments, and cashbook. Horizon also receives direct journal entries and spreadsheet uploads for other miscellaneous information such as tax settlements and foreign financial statements.

SENTINEL INSURANCE COMPANY, LTD.

The Booke Seminars' software package, "The Complete Package for Windows" (TCP) is used to create the annual statement. TCP is updated manually using data from multiple sources, including Horizon for creation of the balance sheet and income statement. TCP is also updated manually using data from the Statutory Reporting Automation Project (SRAP) system, which is a client server system written in Oracle that produces the Underwriting and Investment Exhibits and Schedule T of the annual statement. SRAP receives direct feeds from NPPS and BLC.

The year-end trial balance for 2012 was reconciled to the annual statement.

SENTINEL INSURANCE COMPANY, LTD.

FINANCIAL STATEMENTS

The following statements represent the Company's financial position, as filed by the Company, as of December 31, 2012.

ASSETS

	Assets	Nonadmitted Assets	Net Admitted Assets
Bonds	\$188,721,913		\$188,721,913
Cash, cash equivalents and short-term investments	1,408,089		1,408,089
Other invested assets	1,168,357		1,168,357
Receivables for securities	30,000		30,000
Investment income due and accrued	1,868,648		1,868,648
Premiums and considerations:			
Uncollected premiums	1,582,340		1,582,340
Accrued retrospective premiums	41,607	\$4,161	37,446
Current federal and foreign income tax recoverable and interest thereon	1,235,954		1,235,954
Net deferred tax asset	3,130,764	694,764	2,436,000
Guaranty funds receivable or on deposit	18,485		18,485
Receivable from parent, subsidiaries and affiliates	3,111,648		3,111,648
Total assets	<u>\$202,317,807</u>	<u>\$698,925</u>	<u>\$201,618,882</u>

LIABILITIES, SURPLUS AND OTHER FUNDS

Losses	\$43,986,063
Reinsurance payable on paid losses and loss adjustment expenses	1,824,955
Loss adjustment expenses	9,179,950
Commissions payable, contingent commissions and other similar charges	253,176
Other expenses (excluding taxes, licenses and fees)	479,492
Taxes, licenses and fees (excluding federal and foreign income taxes)	478,083
Unearned premiums	14,082,406
Dividends declared and unpaid – policyholders	59,748
Remittances and items not allocated	30,587
Total liabilities	<u>70,374,461</u>
Common capital stock	4,200,000
Gross paid in and contributed surplus	15,787,500
Unassigned funds (surplus)	111,256,920
Surplus as regards policyholders	131,244,420
Totals	<u>\$201,618,882</u>



SENTINEL INSURANCE COMPANY, LTD.

STATEMENT OF INCOME

<b>UNDERWRITING INCOME</b>	
Premiums earned	\$29,670,152
<b>DEDUCTIONS</b>	
Losses incurred	17,918,825
Loss expenses incurred	3,638,216
Other underwriting expenses incurred	8,587,526
Total underwriting deductions	<u>30,144,568</u>
Net underwriting gain (loss)	(474,416)
<b>INVESTMENT INCOME</b>	
Net investment income earned	8,529,548
Net realized capital gains (losses)	582,410
Net investment gain (loss)	<u>9,111,958</u>
<b>OTHER INCOME</b>	
Finance and service charges not included in premiums	11,806,688
Total other income	<u>11,806,688</u>
Net income before dividends to policyholders, after capital gains tax and before all other federal and foreign income taxes	20,444,230
Dividends to policyholders	50,270
Net income, after dividends to policyholders, after capital gains tax and before all other federal and foreign income taxes	20,393,961
Federal and foreign income taxes incurred	5,990,465
Net income	<u><u>14,403,495</u></u>
<b>CAPITAL AND SURPLUS ACCOUNT</b>	
Surplus as regards policyholders, December 31 prior year	128,555,024
Net income	14,403,495
Change in net unrealized capital gains or (losses)	375,815
Change in net deferred income tax	932,534
Change in nonadmitted assets	(15,796)
Cumulative effect of changes in accounting principles	246,000
Dividends to stockholders	(13,000,000)
Aggregate write-ins for gains and losses in surplus	(252,653)
Change in surplus as regards policyholders for the year	<u>2,689,396</u>
Surplus as regards policyholders, December 31 current year	<u><u>\$131,244,420</u></u>

INVESTMENTS

Invotex was engaged to assist in an evaluation of investment risk management practices and procedures of HFSG as of December 31, 2012.

The scope of Invotex's review included, but was not limited to:

- an assessment of the Company's corporate governance structure, including its enterprise risk management (ERM) related to investment risks;
- a review and evaluation of the Company's general risk management practices and processes related to investment risks, including asset-liability management, credit, market, liquidity, and hedging risks;
- an assessment of the Company's risk management programs used to identify current and emerging risks with regard to invested assets;
- a review and evaluation of the Company's investment policies and guidelines; and
- an assessment of the Company's use of derivatives and its related hedging programs including its determination of hedge effectiveness.

Investments of HFSG and all its insurance subsidiaries are managed by HIMCO. The largest components of the investment portfolio are investment grade corporate bonds and tax exempt municipal bonds.

ERM functions such as asset liability management, market risk and credit risk are centralized in a corporate level ERM group. The Board exercises its investment related oversight function through its Finance, Investment and Risk Management Committee. The Company maintains a formal and extensive framework of senior management risk committees that manage and oversee the ERM program and various investment related risks such as credit, market, liquidity, and hedging risks. The Company maintains formal and well documented policy documents, including investment strategy policies, asset liability management processes and procedures, various risk management policies, and hedge strategy policies. Compliance with investment guidelines, policies and limits is monitored on a regular basis and formally reported to the appropriate committee.

The Company conducted stress testing surrounding market risk sensitivity, interest rate sensitivity, liquidity requirements, and exposure to credit risk. The estimates of potential losses that resulted from such stress testing were compared to established statutory surplus loss limits. The limits appeared reasonable and based on the review of various internal management reports, the Company was in compliance with its stress testing limits. Hedging strategies and limits were well documented in formal policy statements.

Overall, the Company's investment related risk management practices, including the corporate governance framework, ERM processes, documented policies, risk limits, hedging strategies, and compliance monitoring adequately addressed investment risks.

SENTINEL INSURANCE COMPANY, LTD.

LOSSES AND LOSS ADJUSTMENT EXPENSES

\$53,166,013

The following items are included in the captioned account:

Losses	\$43,986,063
LAE	<u>9,179,950</u>
	<u>\$53,166,013</u>

Oliver Wyman conducted a comprehensive actuarial review of the loss and LAE reserves of the Company as of December 31, 2012. The actuarial review was conducted in accordance with generally accepted actuarial reserving standards and principles. Oliver Wyman based its review on the following information provided by the Company:

- the Actuarial Report as of December 31, 2012 (including detailed calculations supporting the actuarial data to Schedule P - Part 1 – Summary of the Annual Statement);
- the 2012 Statements of Actuarial Opinion and Actuarial Opinion Summaries;
- D&T actuarial work papers;
- the Complex Claims Group's claim handling protocols and sampled asbestos and environment accounts; and
- the 2008-2012 Annual Statements and other information requested and obtained during the course of the review through emails, discussions and meetings with key personnel of the Company which included but was not limited to:
  - loss reserve analysis;
  - multivariate pricing model and results;
  - monitoring of underwriting and pricing; and
  - catastrophe models and results.

A review by the Department of the Company's underlying data integrity concluded that there were no indications of any significant inaccuracies or inconsistencies in the underlying data.

The scope of Oliver Wyman's actuarial review included:

- An assessment of reserve risk including but not limited to:
  - a review of the prior and current statutory financial statements, other exhibits and actuarial documentation;
  - participation in the interviews with Company officers responsible for establishing the carried actuarial liabilities and direction on actuarial risk areas;
  - meetings with appropriate claims personnel, reserve actuaries and/or other officers of the Company to assess the appropriateness of methodologies and the quality of assumptions used;
  - a review of samples of claims/account files to evaluate the consistency of practices with the corresponding policies in place;

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- a review of the processes and controls in place that are intended to mitigate the key areas of reserve risk and the process for reporting actuarial indications to management;
  - a review of the Company's claim handling procedures and processes used to estimate loss and LAE liabilities for asbestos, environmental, mass tort, and other segment exposures; and
  - a review of the Company's reserve segments that may increase the risk that actual losses or other contractual payments reflected in the corresponding reserves will be greater than the carried liabilities.
- An assessment of pricing and underwriting risk including but not limited to:
    - meetings with appropriate actuaries and other officers of the Company to assess the appropriateness of methodologies and the quality of assumptions;
    - meetings with officers responsible for establishing pricing and underwriting practices and policies;
    - a high level evaluation of the actuarial process for the development of price indications and monitoring price changes; and
    - a review of the pricing and underwriting risks and the controls in place to mitigate those associated risks.
  - An assessment of liquidity risk including but not limited to:
    - evaluation of the Company's processes and controls for managing exposure due to catastrophic loss and risk concentration, including but not limited to claims for property, workers' compensation and liability exposure; and
    - a review of the frequency of and the processes and controls for reporting considerations to management.

### Reserve Risk

Management has appropriate supervision over the reserving risks facing the Company and has adequately tracked and compiled the data necessary to correctly quantify losses and LAE reserves. The Company has proper procedures in place to ensure extensive communication between the actuaries, management and applicable departments (e.g., legal, claims, pricing, etc.). The business segmentation of the data used by the Company in its reserve analyses was complete and sound. The Company used appropriate methods and reasonable assumptions to estimate its reserves for losses and LAE.

Oliver Wyman specifically addressed the reserve risk exposure for the asbestos and environmental liabilities, workers' compensation and director and officers liability lines of business and found that the Company's methodologies for assessing and monitoring reserve risk were appropriate.

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Pricing and Underwriting Risk

The Company has taken a reasonable approach to establishing and implementing the processes used for pricing risks, has adequately documented its pricing processes and has accurately performed peer reviews of its actuarial selections and calculations. Furthermore, the Company's pricing processes in place and the methodologies used are both sound and consistent with actuarial standards and principles.

Liquidity Risk

The Company demonstrated that it closely monitors its business on a regular basis to ensure that its exposure to potentially natural and man-made catastrophic events remains within its prescribed limits. The enterprise risk related activities are supervised by committees staffed with the highest levels of management within the organization.

Conclusion

Based upon the risk-based assessment and review, no material findings were noted which affected the Company's ability to manage its reserving, pricing and underwriting, or liquidity risk.

SPECIAL SURPLUS FUNDS

Effective January 1, 2012, the Company adopted SSAP No. 101. During the first quarter of 2012, the Company reclassified an amount between special surplus funds and unassigned surplus representing the additional admitted deferred tax assets that had been calculated under the provision of SSAP No. 10R. The value is no longer required to be presented as special surplus funds on the balance sheet. The following exhibit reflects the balance of this account during the five-year period under review:

2012	-
2011	\$246,000
2010	\$150,000
2009	\$224,000
2008	-

COMMON CAPITAL STOCK

\$4,200,000

The Company is authorized to issue 2,000 shares of common capital stock. As of the date of the examination there were 500 shares issued and outstanding with a par value of \$8,400.00 per share. All shares are owned by the Group. There were no changes in common capital stock during the period under examination.

GROSS PAID IN AND CONTRIBUTED SURPLUS

\$15,787,500

In December of 2009, the Company paid an \$8,000,000 ordinary cash dividend to the Hartford that was recorded as return of capital. Additionally, on June 30, 2011, the

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Company paid a \$4,000,000 ordinary cash dividend to the Hartford, of which \$2,000,000 was recorded as a return of capital and \$2,000,000 was an ordinary cash dividend.

2012	\$15,787,500
2011	\$15,787,500
2010	\$17,787,500
2009	\$17,787,500
2008	\$25,787,500

UNASSIGNED FUNDS (SURPLUS) \$111,256,920

The following is a reconciliation of unassigned funds (surplus) during the period under examination:

(in millions)	
Unassigned Funds (Surplus) as of December 31, 2007	\$92.7
Net Income	59.9
Change in Net Unrealized Capital Gains or (Losses)	0.1
Change in Net Deferred Income Tax	(0.2)
Change in Nonadmitted Assets	0.3
Cumulative Effect of Changes in Accounting Principles	(0.6)
Dividends to Stockholders	(41.0)
Aggregate Write-Ins for Gains and Losses in Surplus	<u>(0.1)</u>
Unassigned Funds (Surplus) as of December 31, 2012	<u>\$111.2</u>

RECOMMENDATIONS

Page

7 COST ALLOCATION AGREEMENT

It is recommended that the Company prepare a cost allocation agreement to comply with SSAP No. 25 and submit it to the Department for approval.

10 INFORMATION TECHNOLOGY CONTROLS

It is recommended that the Company continue these remediation efforts.

CONCLUSION

The results of this examination disclosed that as of December 31, 2012, the Company had admitted assets of \$201,618,882 liabilities of \$70,374,461, and surplus as regards policyholders of \$131,244,420. During the period under examination, admitted assets decreased \$168,383,123, liabilities increased \$3,373,100, and surplus as regards policyholders decreased \$171,456,224.

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SIGNATURE

In addition to the undersigned, the following members of the Department participated in the examination: Grace Jiang, CFE; Edna Bosley; Mark Murphy, CFE; Richard Marcks, FCAS, MAAA; Susan Gozzo-Andrews, FCAS, MAAA, RPLU +; Kenneth Roulier, AFE, CISA, AES; Michael Shanahan; Philip Barrett; and the professional services firms of Invotex, Jennan, Oliver Wyman, INS, and Noble.

I, Wayne Shepherd, CFE, do solemnly swear that the foregoing report on examination is hereby represented to be a full and true statement of the condition and affairs of the subject insurer as of December 31, 2012, to the best of my information, knowledge and belief.

Respectfully submitted,

Wayne Shepherd  
Wayne Shepherd, CFE  
Examiner-In-Charge  
State of Connecticut  
Insurance Department

State of Connecticut ss.

County of Hartford

Subscribed and sworn to before me, Patricia Butler  
Notary Public on this 13<sup>th</sup> day of January, 2014.

Patricia Butler  
Notary Public  
My Commission Exp. Sep. 30, 2018