STATE OF MISSOURI

DEPARTMENT OF INSURANCE, FINANCIAL INSTITUTIONS AND PROFESSIONAL REGISTRATION

P.O. Box 690, Jefferson City, Mo. 65102-0690

RE: Examination Report of Cornerstone National Insurance Company for the period ended December 31, 2013

ORDER

After full consideration and review of the report of the financial examination of Cornerstone National Insurance Company for the period ended December 31, 2013, together with any written submissions or rebuttals and any relevant portions of the examiner's workpapers, I, John M. Huff, Director, Missouri Department of Insurance, Financial Institutions and Professional Registration pursuant to section 374.205.3(3)(a), RSMo., adopt such examination report. After my consideration and review of such report, workpapers, and written submissions or rebuttals, I hereby incorporate by reference and deem the following parts of such report to be my findings and conclusions to accompany this order pursuant to section 374.205.3(4), RSMo: summary of significant findings, subsequent events, company history, corporate records, management and control, fidelity bond and other insurance, pension, stock ownership and insurance plans, territory and plan of operations, growth of the company and loss experience, reinsurance, accounts and records, statutory deposits, financial statements, comments on financial statement items, and examination changes.

Based on such findings and conclusions, I hereby ORDER, that the report of the Financial Examination of Cornerstone National Insurance Company as of December 31, 2013 be and is hereby ADOPTED as filed and for Cornerstone National Insurance Company to take the following action or actions, which I consider necessary to cure any violation of law, regulation or prior order of the Director revealed by such report: (1) implement, and verify compliance with each item, if any, mentioned in the Comments on Financial Statement Items and/or Summary of Recommendations section of such report; (2) account for its financial condition and affairs in a manner consistent with the Director's findings and conclusions.

So ordered, signed and official seal affixed this 1st day of June, 2015.

John M. Huff, Director
Department of Insurance, Financial Institutions and Professional Registration

REPORT OF THE

FINANCIAL EXAMINATION OF

CORNERSTONE NATIONAL INSURANCE COMPANY

AS OF

DECEMBER 31, 2013

STATE OF MISSOURI

DEPARTMENT OF INSURANCE, FINANCIAL INSTITUTIONS AND PROFESSIONAL REGISTRATION

JEFFERSON CITY, MISSOURI

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Columbia, Missouri
March 3, 2015

Honorable John M. Huff, Director
Missouri Department of Insurance, Financial Institutions
and Professional Registration
301 West High Street, Room 530
Jefferson City, Missouri 65101

Director Huff:

In accordance with your financial examination warrant, a full scope financial examination has been made of the records, affairs and financial condition of

Cornerstone National Insurance Company

hereinafter referred to as such, CNIC, or as the Company. Its administrative office is located at 3100 Falling Leaf Court, Suite 200, Columbia, Missouri, 65201, telephone number (573) 817-2481. This examination began on March 3, 2014, and concluded on the above date.

SCOPE OF EXAMINATION

Period Covered

We have performed a multi-state examination of CNIC. The last examination was completed as of December 31, 2010. This examination covers the period of January 1, 2011, through December 31, 2013. This examination also included the material transactions or events occurring subsequent to December 31, 2013.

Procedures

This examination was conducted in accordance with the NAIC Financial Condition Examiners Handbook (Handbook), except where practices, procedures and applicable regulations of the Missouri Department of Insurance, Financial Institutions and Professional Registration (DIFP) and statutes of the State of Missouri prevailed. 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 corporate governance, identifying and assessing inherent risks, and evaluating the Company's 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's compliance with Statutory Accounting Principles and annual statement instructions.

All accounts and activities of the Company were considered in accordance with the risk-focused examination process. The key activities identified in our examination of CNIC were as follows:

- Investments
- Premiums
- Underwriting
- Claims Handling
- Reserving
- Taxes
- Related Party Transactions
- Reinsurance

The examiners relied upon information supplied by the Company's independent auditor, Williams Keepers, LLP, of Columbia, Missouri, for its audit covering the period from January 1, 2013 through December 31, 2013. Areas in which the testing and results from the CPA workpapers were relied upon in our examination included internal controls, bank confirmations, paid claims data, premiums receivable, unearned premiums, attorney representation letters, fraud assessment, and subsequent events review.

SUMMARY OF SIGNIFICANT FINDINGS

The Company has a material asset for net deferred tax assets (DTAs), which represented 9.4% of capital and surplus, as of December 31, 2013, and 10.6% of capital and surplus, as of September 30, 2014. There is significant negative evidence that indicates a valuation allowance may be necessary to non-admit a portion or all of the net DTAs, pursuant to guidance in statutory accounting principles. Management's termination of an unprofitable business segment provides offsetting positive evidence that a valuation allowance may not be needed.

SUBSEQUENT EVENTS

The Company hired a new Chief Executive Officer (CEO), William J. Wheeler, effective August 11, 2014. Mr. Wheeler was also elected to the Company's Board of Directors. The former CEO, James C. French, remained at the Company in a different capacity. Mr. French also continues to serve as a member of the Board of Directors.

A bad faith claim settlement lawsuit for damages of $14 million was filed by a policyholder against the Company on April 8, 2014. The lawsuit involved a claim in which the CNIC policyholder was the at-fault driver in an fatal accident that occurred on July 4, 2011. The Company paid the full policy limits of $25,000 to the claimant on July 6, 2012. However, the claimant subsequently filed a wrongful death lawsuit against the Company's policyholder and and received a $14 million judgment in December 2012. The policyholder then filed the bad faith claim lawsuit against CNIC alledging a failure to obtain a release from the claimant and a failure to provide legal representation to the policyholder in the claimant's lawsuit. The bad faith claim lawsuit was settled in September 2014 for a total of $6.75 million. The Company paid $1.75 million of the settlement, while insurance coverage under the Company's liability policies covered the remaining $5 million of the costs. A portion of the settlement cost was also ceded under the Company's reinsurance agreements. The net cost to CNIC was $720,000.

COMPANY HISTORY

General

The Company was incorporated on March 6, 1997 and commenced business on March 19, 1997. The Company operates as a stock property and casualty insurer under the insurance laws of Chapter 379 RSMo (Insurance Other Than Life).

Dividends and Capital Contributions

CNIC paid $200,000 to its sole shareholder, Cornerstone Management Partners, Inc. (CMP), in 2011 that was recorded as a "return of capital" distribution instead of a dividend payment. The Company did not pay any dividends to CMP in 2012 or 2013.

Mergers and Acquisitions

There were no mergers or acquisitions involving the Company or the holding company system of the parent, CMP, during the examination period.

CORPORATE RECORDS

The Company's Articles of Incorporation and Bylaws were reviewed. The Articles of Incorporation were amended in January 2011 to update the section listing the Company's principle place of business. The Bylaws were amended in March 2011 to prohibit the same officer from simultaneously holding the offices of President and Secretary.

The minutes of the Board of Directors' meetings and the written consents of the sole shareholder (in lieu of meeting) were reviewed for proper approval of corporate transactions. In general, the minutes and written consents appear to properly reflect and approve the Company's major transactions and events for the period under examination.

MANAGEMENT AND CONTROL

Corporate Governance

The management of the Company is vested in a Board of Directors, which is appointed by the sole shareholder. The Company's Bylaws specify that the Board of Directors shall consist of fourteen (14) members, but the Board has the power to change the number of members. The Board approved a resolution to increase the number of directors to fifteen (15), effective May 29, 2009. The Board of Directors appointed and serving, as of December 31, 2013, were as follows:

Name	Address	Principal Occupation and Business Affiliation
Michael G. Burnam	Columbia, MO	Chief Exec. Officer, Storage Mart Partners, LP
D. Scott Forrest	Columbia, MO	Vice President and General Counsel, CMP
James C. French	Columbia, MO	President and Chief Executive Officer, CMP
James E. Godfrey, Jr.	St. Louis, MO	Attorney, Evans & Dixon, LLC
Brian G. Harrison	Columbia, MO	Owner, Harrison Agency, Inc.
R. Alan Hedrick	Dexter, MO	Owner, Country Wide Insurance Agency
Earl P. Holland [1]	Fort Myers, FL	Retired / Investor
Lewis E. Melahn	Mexico, MO	Attorney, Private Practice
Stephen M. Palmer	Frontenac, MO	Physician, Private Practice
Robert A. Rowles	Tipton, MO	President, Insurance Associates America, Inc.
Kirk W. Schmidt	Jefferson City, MO	Vice President and Chief Financial Officer, CMP
Roger W. Thomas [2]	Naples, FL	Retired
Roger D. Walker	Columbia, MO	Senior VP and Chief Operating Officer, CMP

[1] Resigned, effective May 12, 2014, and replaced by David N. Ridgely
[2] Resigned, effective June 9, 2014, and replaced by William J. Wheeler

Committees

The Articles of Incorporation and Bylaws do not require any committees, but the Bylaws do allow for the creation of committees, if authorized by a resolution of the Board of Directors. The Company did not have any appointed committees, as of December 31, 2013. However, the parent company, CMP, had committees established throughout the exam period that regularly address and take actions on the business affairs of CNIC. The CMP committees appointed and serving, as of March 2014, were as follows: Audit Committee, Executive Compensation Committee, Governance Committee, Marketing and Agency Relations Committee, and Technology Committee.

Officers

The officers elected by the Board of Directors and serving as of December 31, 2013, were as follows:

Officer	Position
James C. French [3]	Chief Executive Officer
Kirk W. Schmidt	President, Chief Financial Officer, Treasurer
Roger D. Walker	Senior Vice President, Chief Operating Officer, Secretary
D. Scott Forrest	Vice President – Claims, General Counsel, Asst. Secretary
Don Ellis	Vice President – Agency Relations

[3] Replaced by William J. Wheeler, effective August 11, 2014

Holding Company, Subsidiaries and Affiliates

The Company is a member of an Insurance Holding Company System as defined by Section 382.010, RSMo (Definitions). An Insurance Holding Company System Registration Statement was filed by CNIC for each year of the examination period.

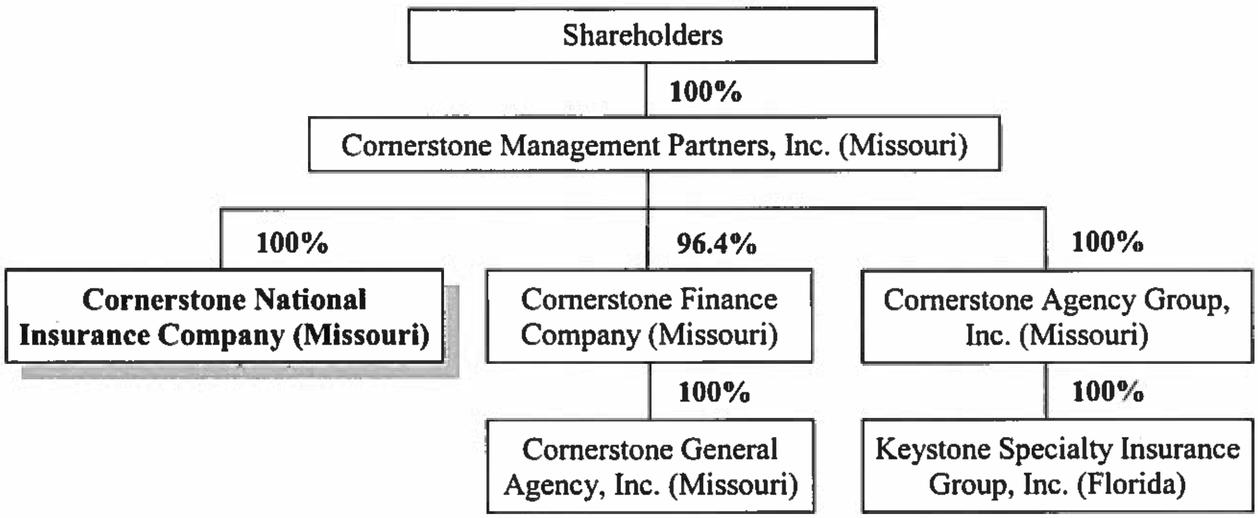
The Company is directly owned 100% by Cornerstone Management Partners, Inc., a holding company. CMP is a privately held stock company with approximately 350 common and preferred shareholders. The largest shareholder of CMP is James French, a director. Mr. French owned 13% of the outstanding common stock of CMP, as of December 31, 2013. Collectively, officers and directors of CNIC own 30% of CMP common stock. The 30 largest stockholders of CMP own 62% of CMP common stock.

CMP has other subsidiaries, which have business operations in or related to the insurance industry. CMP and its subsidiaries are collectively referred to as the Cornerstone Group. CNIC is by far the largest entity in the Cornerstone Group. A description of the business operations of CMP and its subsidiaries are as follows:

- Cornerstone Management Partners, Inc. – Holding company with a primary purpose to manage and support the business operations of CNIC. Employees of CMP perform the day-to-day operational functions of CNIC and its other subsidiaries.
- Cornerstone Finance Company – A commercial lender that issues loans to businesses for the purpose of financing insurance premiums on commercial policies.
- Cornerstone General Agency, Inc. (CGA) – An agency that is responsible for managing the network of independent agents that produce business for CNIC. CGA also produces business for unaffiliated insurers for any risks, such as homeowners insurance and life products, that are not written by CNIC.
- Cornerstone Agency Group, Inc. – A holding company with no operations.
- Keystone Specialty Insurance Group, Inc. (Keystone) – Formerly a managing general agent that marketed and serviced the Company's non-standard auto policies in Florida and Texas. Keystone ceased operations at the end of April 2008 and remains a shell company, as of December 31, 2013.

Organizational Chart

Below is the organizational chart of the Company and its affiliates, as of December 31, 2013.



Intercompany Agreements

The Company's active agreements with related parties that were in effect, as of December 31, 2013 are outlined below.

1. **Type:** Tax Allocation Agreement

   Affiliates: Cornerstone Management Partners, Inc., Cornerstone Finance Company, and Keystone Specialty Insurance Group, Inc.

   Effective: October 4, 2006

   Terms: All of the parties to the Agreement will annually file a consolidated federal income tax return commencing with the 2000 tax year. Each entity's share of the consolidated tax liability or refund shall be calculated as the amount that would have been incurred if each entity would have filed a tax return on a stand-alone basis. The settlements of tax payments due to CMP are to be paid within 30 days of the date that each filing is due to the Internal Revenue Service (IRS). Any tax refunds receivable from CMP are due within 30 days of CMP's receipt of the funds from the IRS.

2. **Type:** Cost Allocation Agreement

   Affiliate: Cornerstone Management Partners

   Effective: March 1, 2009

   Terms: CMP will provide various management and administrative services for CNIC, which includes claims processing, underwriting, policyholder services, marketing, accounting, tax reporting, premium rating, legal, human resources, investments, billing and collection, financial reporting, regulatory compliance, strategic planning, data processing, computer support, and office space. CMP will allocate the direct costs for salary and benefits of its employees that provide services to CNIC, based upon a mutually agreed upon methodology. Various other general and administrative expenses incurred by CMP to provide services to CNIC will be allocated with the same percentage used for the allocation of salary and benefits. CNIC will reimburse CMP for the depreciation of its computer hardware and software costs used to provide data processing services. CMP will invoice CNIC on a monthly basis for all direct and allocated costs under the agreement.

3. **Type:** General Agency Agreement

   Affiliate: Cornerstone General Agency, Inc.

   Effective: May 1, 2010; amended effective June 1, 2012

   Terms: CGA will serve as the general agent to supervise and conduct the writing of CNIC's private passenger automobile business. CGA shall have the authority to appoint local agents and solicit applications for insurance in the states of Missouri, Arkansas, Oklahoma, Kansas and Texas. CGA must follow the underwriting guidelines of CNIC. CGA does not have the responsibility to collect premiums and will not process claims. CNIC will pay CGA a monthly fee equal to CGA's direct costs of providing services under the agreement.

   A separate Assignment and Assumption Agreement was executed simultaneous with the General Agency Agreement to transfer the rights and obligations under CNIC's existing agent contracts to CGA, effective May 1, 2010.

Intercompany Payments

The following table summarizes the payments made during the examination period, between CNIC and its affiliates, pursuant to intercompany agreements and other transactions.

Affiliate	Agreement / Transaction	Net Paid / (Received) 2011	2012	2013
CMP	Cost Allocation	$4,728,537	$4,780,215	$4,468,745
CMP	Tax Allocation	(a)	(a)	(a)
CGA	General Agency	5,227,894	4,968,893	4,588,518
TOTAL		$9,956,431	$9,749,108	$9,057,263

(a) No cash settlements with CMP occurred during the examination period. However, CNIC incurred the following tax benefits (due to taxable losses), pursuant to the Tax Allocation Agreement: 2011 - $758,444, 2012 - $297,107, 2013 - $163,188.

FIDELITY BOND AND OTHER INSURANCE

The Company's parent, CMP, has a financial institution bond to cover losses resulting from fraudulent or dishonest acts of an employee. The bond insures all subsidiaries of CMP, including CNIC. The bond has a liability limit of $1,000,000 with a $10,000 deductible, which meets the minimum coverage that is recommended by the NAIC.

The Company is also covered by several other insurance policies of the parent, CMP. These policies include the following: property, general liability, commercial excess and umbrella liability, employment liability, directors' and officers' liability, insurance services professional liability, and cyber security. Although CNIC is not a named insured on most of these policies, the terms of the policies extend coverage to the subsidiaries of the named insured, CMP.

PENSION, STOCK OWNERSHIP AND INSURANCE PLANS

CNIC does not have any direct employees and thus, does not directly incur or accrue any expenses for employee benefits. The employees of the parent, Cornerstone Management Partners, Inc., perform all of the operational and administrative functions of the Company. Most of the CMP employees are located in the Columbia, Missouri home office. At the end of 2013, CMP had 48 total employees. An allocated portion of the payroll and benefit costs of CMP employees are paid by CNIC pursuant to a Cost Allocation Agreement, which is described in the Intercompany Agreements section of this report.

TERRITORY AND PLAN OF OPERATION

Cornerstone National Insurance Company is licensed as a property and casualty insurer by the Missouri DIFP under Chapter 379 RSMo (Insurance Other than Life). The Company is licensed in nineteen (19) states, but only wrote business in nine states during 2013. The states with the largest written premiums were as follows:

State	2013 Direct Written Premiums	% of Total
Missouri	$15,951,267	36.3%
Oklahoma	9,684,570	22.1%
Arkansas	6,783,256	15.5%
California	6,486,404	14.8%
All Other	4,987,008	11.4%
Total	$43,892,505	100.0%

The Company's two main lines of business are Private Passenger Auto Liability and Auto Physical Damage, which accounted for 58% and 42% of net written premiums in 2013, respectively. The Company divides its personal auto business into "Core" and "Program" segments.

The Company insures standard auto risks in its Core states of Arkansas, Kansas, Missouri, Oklahoma, and Texas. Core business is produced entirely by a network of independent agents. Cornerstone stopped writing new business in Texas, effective October 1, 2013. The exit from the Texas market was due to above average loss ratios, an inability to grow the premium volume, and the retirement of the Vice President responsible for Texas operations at the end of 2013.

The Program business was produced by three managing general agents (MGAs) and one general agent that wrote non-standard auto business in Arizona, California, Colorado, Georgia, Louisiana and Utah that was mostly ceded. The Program business in Georgia began experiencing lawsuits for bad faith claims settlement allegations in late 2011. The MGA in Georgia performed the claims handling for the claims involved in litigation. Several large losses occurred from bad faith claims litigation that led to the termination of the Program business in 2012. Direct premium volume for the Program segment has decreased from $47.9 million in 2010 to $7.9 million in 2013. Run-off of the Program business is expected to be mostly completed by the end of 2015.

GROWTH OF COMPANY

The table below shows the Company's premium writings and writing ratios for the most recent four years, which includes the current examination period.

Year	Direct Premiums Written	Net Premiums Written	Change in Net Premiums	Capital and Surplus	Ratio of Net Premiums to Surplus
2010	$79,550,476	$33,145,930	na	$14,335,016	2.31
2011	66,434,365	34,132,148	3.0%	11,151,459	3.06
2012	56,179,624	35,610,828	4.3%	9,548,095	3.73
2013	43,892,505	36,291,991	1.9%	10,739,069	3.38

The large decrease in direct premiums in 2011 were attributable to the exit from crop insurance and a lower volume from the Program business. Management terminated the Program business beginning in 2012, which resulted in large premium decreases in 2012 and 2013 from the run-off of policies from this segment. Net written premiums increased slightly each year due to growth in the Core segment. The increase in the net premium to surplus ratio during the examination period was due to the decrease in surplus from large losses in the Program business. As explained previously, the Company had large losses from bad faith claims settlement litigation in 2011 and 2012. In addition, significant receivables of approximately $2.5 million from one MGA were written off in the exam period.

LOSS EXPERIENCE

The table below shows the Company's incurred losses and loss ratios for the most recent four years, which includes the current examination period.

Year	Net Premiums Earned	Net Losses and Loss Adjustment Expenses Incurred	Loss Ratio
2010	$33,084,831	$23,703,156	71.6%
2011	33,725,168	27,928,828	82.8%
2012	35,332,476	27,711,293	78.4%
2013	36,268,213	26,014,051	71.7%

The loss ratios in 2011 and 2012 were higher than normal due to the losses from bad faith claims settlement litigation for the Program business segment.

REINSURANCE

General

The Company's premium activity on a direct written, assumed and ceded basis, for the period under examination, is detailed below:

	2011	2012	2013
Direct Business	$ 66,434,365	$ 56,179,624	$ 43,892,505
Reinsurance Assumed	-	-	-
Reinsurance Ceded:			
Affiliates	-	-	-
Non-affiliates	(32,302,217)	(20,568,796)	(7,600,514)
Net Premiums Written	$ 34,132,148	$ 35,610,828	$ 36,291,991

Assumed

CNIC did not assume any premiums during the exam period and there are no plans to assume business in the future.

Ceded

The Company's reinsurance program for the Core business involves separate agreements for property and casualty risks. As of December 31, 2013, the Company had a casualty excess of loss agreement to cede 100% of liability losses in excess of a $500,000 retention, subject to a reinsurer limit of $5,000,000 per occurrence. Property business is reinsured on a catastrophe basis only, due to the low insured values of personal autos. The property catastrophe agreement in effect at year-end 2013 ceded 95% of losses in excess of a $500,000 retention, subject to a reinsurer limit of $1,300,000 per occurrence. There were no changes in the Core reinsurance program for new agreements effective in 2014.

The Company has separate quota share reinsurance coverage for each MGA / general agent participating in the Program business. As of December 31, 2013, the ceding percentages for property and liability risks under each Program were as follows: Freedom National Insurance Services, Inc. – 90%, THI General Agency, Inc. – 70%, Lane and Associates, Inc. – 95%, and Sun Coast General Agency, Inc. (Sun Coast) – 87.5%. All of the reinsurance agreements for the Program business have no limit of reinsurer liability, except for the reinsurance agreement for the Sun Coast Program, which provides no coverage for losses in excess of a 125% loss ratio.

All liability risks in the Program business are also covered by the casualty excess of loss agreement that is described above for the Core business. There is no property catastrophe coverage for the Program business. Management has not deemed catastrophe coverage necessary since a high percentage of the risk in the Program business is already ceded under the quota share agreements.

Below is a summary of the major external reinsurers, based upon 2013 ceded premiums and net reinsurance recoverables, as of December 31, 2013:

Name of Reinsurer	2013 Premiums Ceded	Percent of Ceded Premiums	Net Reins. Recoverable 12/31/2013	Percent of Net Recov.
NGM Insurance Company	5,342,000	70.30%	6,852,000	57.40%
Dorinco Reinsurance Company	995,000	13.10%	3,414,000	28.60%
FEMA (National Flood Program)	695,000	9.10%	0	0.00%
All Others	569,000	7.50%	1,661,000	13.90%
Total Ceded	$7,601,000	100.00%	$11,927,000	100.00%

The top two reinsurers in the table above pertain to the Program business. There were no significant ceded premiums in 2013 or reinsurance recoverables, as of December 31, 2013, associated with the Core business.

The Company is contingently liable for all reinsurance losses ceded to others. This contingent liability would become an actual liability in the event that an assuming reinsurer fails to perform its obligations under the reinsurance agreement.

ACCOUNTS AND RECORDS

The Company uses the SurePower Innovation system for policy management, premium billing, claims management, and case reserving. The Innovation system was purchased in 2012 and was implemented gradually on a state-by-state basis to phase out the same functions performed previously by the old Policy Tracking System (PTS) from Information Distribution & Marketing, Inc. Portfolio Manager software from Accurate Business Systems is used for investment management and reporting. QuickBooks Enterprise 15 software from Intuit, Inc. is used for financial reporting. All software applications are hosted on a Dell PowerEdge server located at an underground facility in Columbia, Missouri. The server, server applications, and data are accessed remotely to the Company's office via an Ethernet connection.

The CPA firm, Williams Keepers, LLC, of Columbia, Missouri issued audited statutory financial statements of the Company for all years in the examination period.

The actuarial opinion regarding the Company's reserves for losses and loss adjustment expenses was issued by Mark A. Doepke, FCAS, MAAA, of Actuarial Advisors, Inc. in Minneapolis, Minnesota, for all years of the examination period.

STATUTORY DEPOSITS

Deposits with the State of Missouri

The funds on deposit with the Missouri DIFP as of December 31, 2013, as reflected below, were sufficient to meet the capital deposit requirements for the State of Missouri in accordance with Section 379.098 RSMo (Securities to be Deposited). The funds on deposit were as follows:

Type of Security	Par Value	Fair Value	Book Value
State and Municipal Bonds	$2,060,000	$2,120,098	$2,063,407

Deposits with Other States

The Company also has funds on deposit with other states. Those funds on deposit, as of December 31, 2013, were as follows:

State	Type of Security	Par Value	Fair Value	Book Value
Arkansas	Municipal Bonds	$150,000	$150,327	$149,311
Georgia	Municipal Bonds	35,000	35,076	34,839
Oklahoma	Municipal Bonds	375,000	409,685	381,209
Virginia	Municipal Bonds	220,000	222,377	219,912
Total		$780,000	$817,465	$785,271

FINANCIAL STATEMENTS

The following financial statements, with supporting exhibits, present the financial condition of Cornerstone National Insurance Company for the period ending December 31, 2013. Any examination adjustments to the amounts reported in the financial statements and/or comments regarding such are made in the "Comments on Financial Statement Items." The failure of any column of numbers to add to its respective total is due to rounding or truncation.

There may have been additional differences found in the course of this examination, which are not shown in the "Comments on Financial Statement Items." These differences were determined to be immaterial concerning their effect on the financial statements, and therefore, were only communicated to the Company and noted in the workpapers for each individual Annual Statement item.

ASSETS
as of December 31, 2013

	Assets	Non-Admitted Assets	Net Admitted Assets
Bonds	$ 28,980,505	$ -	$ 28,980,505
Common Stocks	1,113,644	-	1,113,644
Cash, Cash Equivalents and Short-Term Investments	1,150,045	-	1,150,045
Investment Income Due and Accrued	357,093	-	357,093
Uncollected Premiums and Agents' Balances	6,156,573	1,126,534	5,030,039
Amounts Recoverable from Reinsurers	2,102,049	-	2,102,049
Other Reinsurance Amounts Receivable	(8,269)	-	(8,269)
Federal Income Tax Recoverable	2,330,303	2,330,303	-
Net Deferred Tax Asset (**Note 1**)	1,070,711	57,902	1,012,809
EDP Equipment and Software	806,003	806,003	-
Aggregate Write-In Assets	325,510	325,510	-
TOTAL ASSETS	**$ 44,384,167**	**$ 4,646,252**	**$ 39,737,915**

LIABILITIES, SURPLUS AND OTHER FUNDS
as of December 31, 2013

Losses	$11,390,416
Loss Adjustment Expenses	5,063,826
Commissions Payable	0
Other Expenses	254,128
Taxes, Licenses and Fees	28,907
Unearned Premium	9,421,819
Advance Premium	335,078
Ceded Reinsurance Premiums Payable	2,070,607
Funds Held Under Reinsurance Treaties	58,992
Payable to Parent, Subsidiaries and Affiliates	375,073
TOTAL LIABILITIES	**$28,998,846**
Common Capital Stock	2,350,000
Surplus Notes	5,028,371
Gross Paid-In and Contributed Surplus	12,624,342
Unassigned Funds (Surplus)	(9,263,644)
Capital and Surplus	**$10,739,069**
TOTAL LIABILITIES AND SURPLUS	**$39,737,915**

STATEMENT OF INCOME
For the Year Ended December 31, 2013

Premium Earned	$36,268,213
DEDUCTIONS:	
Losses Incurred	21,628,926
Loss Adjustment Expenses Incurred	4,385,125
Other Underwriting Expenses Incurred	11,094,136
Total Underwriting Deductions	$37,108,187
Net Underwriting Loss	$ (839,974)
Net Investment Income Earned	1,058,154
Net Realized Capital Losses	(51,673)
Net Investment Gain	$ 1,006,481
Other Income	530,505
Dividends to Policyholders	0
Federal Income Taxes Incurred	(163,188)
Net Income	**$ 860,200**
CAPITAL AND SURPLUS ACCOUNT:	
Surplus as Regards Policyholders, December 31, 2012	$ 9,548,095
Net Income	860,200
Change in Net Unrealized Capital Gains or (Losses)	234,986
Change in Net Deferred Income Tax	(405,102)
Change in Non-Admitted Assets	500,890
Change in Surplus Notes	(443)
Aggregate Write-In for Gains and Losses in Surplus	443
Surplus as Regards Policyholders, December 31, 2013	**$10,739,069**

COMMENTS ON FINANCIAL STATEMENT ITEMS

Note 1 – Net Deferred Tax Asset **$1,012,809**

Statement of Statutory Accounting Principle (SSAP) No. 101, Income Taxes, provides guidance for deferred tax assets. Paragraph 7.e. of SSAP No. 101 states that a statutory valuation allowance adjustment shall be made to reduce gross DTAs that are more than likely not to be realized. SSAP No. 101 further states that the statutory valuation allowance is to be determined in accordance with paragraphs 20-25 of Statement of Financial Accounting Standard (FAS) No. 109.

Paragraph 23 of FAS 109 states – "Forming a conclusion that a valuation allowance is not needed is difficult when there is negative evidence such as cumulative losses in recent years." FAS 109 does not define a time period for "recent years". However, accounting guidance from national "Big 4" CPA firms have interpreted cumulative losses in recent years as pre-tax results for the most recent three years. CNIC has a pre-tax loss of approximately $2.5 million for the three year period from 2011 to 2013. This factor supports a conclusion that a valuation allowance is needed.

Paragraph 24 of FAS 109 provides examples of positive evidence that may offset the negative evidence of cumulative losses in recent years, which could eliminate the need for a valuation allowance. One example given states – "A strong earnings history exclusive of the loss that created the future deductible amount coupled with evidence indicating that the loss is an aberration rather than a continuing condition." The Company's losses in 2011 to 2013 can be attributed to the Program business that is currently in run-off status. CNIC would not have a cumulative loss during 2011-2013 if the results from the Program segment are excluded. The Company's elimination of the impact of the Program business on future results could be viewed as positive evidence to support a conclusion that a valuation allowance for DTAs is not necessary.

However, negative financial impacts from the Program business continue to occur in 2014, based upon information available as of September 30. Write-offs of receivables (impacting taxable income only) of over $1 million from the Program business appear likely to occur during 2014 and 2015, which is another example of negative evidence in the evaluation of the DTAs. Management is hopeful that no further losses from the Program business will occur, but uncertainty remains over extent of losses that will result in 2014 and future years.

EXAMINATION CHANGES

None.

GENERAL COMMENTS AND/OR RECOMMENDATIONS

Net Deferred Tax Assets (page 17)

There is both negative evidence and positive evidence in the consideration of a valuation allowance for the net DTAs. Management should continually evaluate the need for a valuation allowance for DTAs in consultation with its CPA firm and consideration of guidance available from other accounting firms. Financial results from 2014 should strongly influence the decision of whether a valuation allowance is necessary at year-end 2014. If there are cumulative losses for the period from 2012 to 2014, it appears that an valuation allowance may be necessary, as of December 31, 2014, in accordance with statutory accounting guidelines.

ACKNOWLEDGMENT

The assistance and cooperation extended by the officers and the employees of Cornerstone National Insurance Company during the course of this examination is hereby acknowledged and appreciated. In addition to the undersigned, Marc Peterson, CFE, Kim Dobbs, CFE, AES, examiners for the Missouri DIFP, participated in this examination. Jon Michelson, FCAS, MAAA, of Expert Actuarial Services, LLC, also participated as a consulting actuary.

VERIFICATION

State of Missouri)
)
County of)

I, Tim L. Tunks, on my oath swear that to the best of my knowledge and belief the above examination report is true and accurate and is comprised of only facts appearing upon the books, records or other documents of Cornerstone National Insurance Company its agents or other persons examined or as ascertained from the testimony of its officers or agents or other persons examined concerning its affairs and such conclusions and recommendations as the examiners find reasonably warranted from the facts.

Tim L. Tunks

Tim L. Tunks, CPA, CFE
Examiner-In-Charge
Missouri DIFP

Sworn to and subscribed before me this 18th day of February, 2015.

My commission expires: 10/2/2016 Susan M. Greenfield
Notary Public

SUSAN M. GREENFIELD
Notary Public - Notary Seal
State of Missouri, County of Boone
Commission # 12479801
My Commission Expires Oct. 2, 2016

SUPERVISION

The examination process has been monitored and supervised by the undersigned. The examination report and supporting workpapers have been reviewed and approved. Compliance with NAIC procedures and guidelines as contained in the Financial Condition Examiners Handbook has been confirmed.

Mark A. Nance, CPA, CFE
Audit Manager
Missouri DIFP

CORNERSTONE
NATIONAL INSURANCE COMPANY
Our Foundation is You

May 6, 2015

Leslie Nehring, CPA, CFE
Chief Financial Examiner
Department of Insurance, Financial Institutions, and Professional Registration
301 W. High Street, Room 530
Jefferson City, MO 65109

Ms. Nehring:

We have received the copy of our December 31, 2013 financial examination. We appreciate the Department's review and evaluation of our Deferred Tax Asset, and we have further evaluated it as a result of the examination and report.

As of December 31, 2014 we have a three year cumulative pre-tax loss of $(40,404). Included in this loss are losses of $(3,520,938) from our discontinued program business and other discontinued lines of business. This leaves a three year profit of $3,480,534 on our continuing business segments.

We agree with the evaluation of taking both negative and positive evidence into consideration; however, on a prospective basis we believe it is more likely than not that we will achieve sufficient taxable income to realize a substantial portion of the current deferred tax assets over the next three years. This conclusion was arrived at by taking our budgeted profit numbers for 2015 and then adding a substantial margin for conservatism. We believe it is much more likely than not that we can achieve these numbers and therefore realize all the deferred tax assets that are currently carried in our financial filings.

We will continue to evaluate these numbers in the future in conjunction with our independent auditors, who currently seem comfortable with the deferred tax assets we are currently carrying in our financial statements. We will fully consider what the Department has suggested and will make any adjustments necessary in future financial statements.

Thanks for the cooperation and effort put forth in this examination. We would ask that this **response be included in the final report.**

Sincerely,

Kirk Schmidt

Kirk W. Schmidt, CPA, CFE
President and CFO
Cornerstone National Insurance Co.

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