

STATE OF MISSOURI



DEPARTMENT OF INSURANCE, FINANCIAL INSTITUTIONS AND PROFESSIONAL REGISTRATION

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

RE: Examination Report of Safety National Casualty Corporation as of December 31, 2008

ORDER

After full consideration and review of the report of the financial examination of Safety National Casualty Corporation for the period ended December 31, 2008, 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 report. After my consideration and review of such report, workpapers, and written submissions or rebuttals, the findings and conclusions of the examination report are incorporated by reference and deemed to be my findings and conclusions to accompany this order pursuant to section 374.205.3(4), RSMo.

Based on such findings and conclusions, I hereby ORDER Safety National Casualty Corporation, 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 mentioned in the General Comments and/or 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 November 3, 2009.




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

REPORT OF
FINANCIAL EXAMINATION

**SAFETY NATIONAL CASUALTY
CORPORATION**

As of:
DECEMBER 31, 2008

FILED
NOV 13 2009
DIRECTOR OF INSURANCE
FINANCIAL INSTITUTIONS &
PROFESSIONAL REGISTRATION



STATE OF MISSOURI
DEPARTMENT OF INSURANCE, FINANCIAL INSTITUTIONS
AND PROFESSIONAL REGISTRATION
JEFFERSON CITY, MISSOURI

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September 23, 2009

Honorable Alfred W. Gross, Commissioner
Bureau of Insurance
Virginia State Corporate Commission
Chairman, Financial Condition (E) Committee, NAIC

Honorable Merle D. Scheiber, Director
Division of Insurance
State of South Dakota
Secretary, Midwestern Zone, NAIC

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

Dear Sirs:

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

SAFETY NATIONAL CASUALTY CORPORATION

hereinafter referred to as "Safety National", "SNCC", or as the "Company". The Company's office is located at 1832 Schuetz Road, St. Louis, Missouri 63146-4235; telephone number (314) 995-5300. Examination fieldwork began on February 18, 2009, and concluded on the above date.

SCOPE OF EXAMINATION

Period Covered

The last full scope association financial examination of Safety National was made as of December 31, 2005, by examiners from the state of Missouri representing the Midwestern Zone of the National Association of Insurance Commissioners (NAIC) with no other zones participating.

The current full scope financial examination covers the period from January 1, 2006, through December 31, 2008, and was conducted by examiners from the state of Missouri representing the Midwestern Zone of the NAIC with no other zones participating. This examination also included material transactions or events occurring subsequent to December 31, 2008.

Procedures

This examination was conducted using guidelines set forth in the Financial Condition Examiners Handbook of the NAIC, except where practices, procedures and applicable regulations of the Department of Insurance, Financial Institutions and Professional Registration ("DIFP") or 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 the Company including corporate governance, identifying and assessing inherent risks within the Company, and evaluating systems 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 when applicable to domestic state regulations.

All accounts and activities of the Company were considered in accordance with the risk-focused examination process. The following key activities were identified: Management and Control, Investments, Treasury, Premiums and Underwriting, Claims and Actuarially Determined Liabilities, Reinsurance, Debt and Surplus, Taxes and Affiliated Parties.

The examiners relied upon information and workpapers provided by the Company's independent auditor, Ernest and Young, LLP, of Clayton, Missouri, for its audit covering the period from January 1, 2008, through December 31, 2008. Such reliance included fraud risk analysis, internal control narratives and tests of internal controls.

SUMMARY OF SIGNIFICANT FINDINGS

Safety National is a property and casualty company that specializes in excess workers' compensation policies for self-insured employers. It is one of the oldest continuous writers of excess workers' compensation insurance and is currently the largest writer of this line of business in the United States. The Company has operated profitably for several years and reported net incomes between \$42 million and \$54 million each year of the current examination period. These earnings, along with an additional \$55 million capital contribution from its parent, allowed Safety National to avoid a surplus decline in 2008 even though it sustained \$49 million in unrealized capital losses because of the collapse in the financial markets in the last quarter of 2008. As a result the Company has a strong capital position, with surplus increasing from \$359 million at the end of the prior examination period to \$531 million at the end of the current examination period. The ratio of the Company's surplus relative to the Authorized Control Level of risk-based capital has been stable during the examination period, hovering around 330%.

The Company has, however, experienced significant adverse loss development in recent years. Reserves were materially understated for the years 2000 to 2004 (based on actual runoff development through December of 2008). The magnitude of the deficiency was such that the Company's surplus relative to its required risk-based capital may have triggered regulatory action if the correct reserves had been recorded in those years and if

the Company had not taken the steps necessary to strengthen its capital position. The Company explained that it has strengthened its IBNR and carried reserves over the last several years, which has had the result of appearing as adverse development when compared to prior carried reserves. The Company also noted that reserves reported in the 2008 Annual Statement were redundant by over \$30 million compared to the estimate of the Company's outside actuaries, PricewaterhouseCoopers (PwC). DIFP's consulting actuary for this examination confirmed that the carried reserves at year-end 2008 were approximately \$31 million higher than PwC's point estimate, that the analysis performed by PwC was completed in accordance with actuarial standards and principles, and that he believes the reserve estimation by PwC is reasonable.

As a result of the reserve strengthening in 2003, 2004 and 2005, the adverse development since 2005 has not been as high as in prior years, but has still been substantial. The 2008 Annual Statement reported one-year adverse development on net loss and LAE reserves of at least 5% for the years 2004 through 2008. Significantly higher, double-digit percentage two-year adverse developments were also reported for that same time period, ranging from \$91 million to \$154 million for the past four calendar years.

Due to the Company's recent adverse loss development history its reserves will continue to be a concern until the trend of material one-year and two-year deficiencies is broken. This should occur in the near future if reported reserves are sufficient and further reserve strengthening is no longer necessary.

Comments Previous Examination

Comment:

The prior examination report noted that the Company had not fully complied with a management letter recommendation from the 2002 examination. The management letter noted that the Company's custodial agreement was missing three requirements listed in the Financial Condition Examiners Handbook. The comment in the last examination indicated that the requirement for the custodian to notify the DIFP within three days of the custodial account being closed or of the withdrawal of all the assets, was still excluded from the agreement.

Company Response:

The Company stated that the custodian indicated that it was unable to comply with this requirement because of computer system limitations, but that an agreement with the DIFP was reached to have the custodian send monthly statements directly to the DIFP showing the daily balances in the custodial account.

Current Findings:

The custodian sent monthly statements of the custodial account to the DIFP from September 2007 through November 2008. The Company discontinued using this account in December 2008 and now sends an email to the DIFP each month stating that the account balance is zero. The Company intends to close this account at the end of 2009.

SUBSEQUENT EVENTS

None

COMPANY HISTORY

General

Safety Mutual Casualty Corporation was incorporated in the state of Missouri on November 28, 1942, and commenced business on December 28, 1942, as a mutual property and casualty insurer operating under Chapter 379 RSMo (Insurance Other than Life).

Safety Mutual Casualty Corporation was originally organized to provide excess workers' compensation coverage to self-insured employers. Insurers Service Corporation managed the operations of Safety Mutual Casualty Corporation until 1982, when the two shareholders of Insurers Service Corporation sold their interests to Frank B. Hall & Company. The management agreement between Safety Mutual Casualty Corporation and Insurers Service Corporation was terminated in 1988 under a settlement that required the Company to pay Insurers Service Corporation 6% of direct and assumed premiums until December 31, 1989, and 7% from January 1, 1990, to December 31, 2002.

Safety Mutual Casualty Corporation was converted to a stock company on September 30, 1991, and the name was changed to Safety National Casualty Corporation. SIG Holdings, Inc., a Missouri corporation, became the sole shareholder of the Company.

On March 5, 1996, SIG Holdings Inc., a Delaware corporation and subsidiary of Delphi Financial Group, Inc., purchased SIG Holdings Inc. of Missouri and merged it into SIG Holdings Inc. of Delaware.

Capital Stock and Paid-In Surplus

The Company is authorized to issue 5,000 shares of common stock with a par value of \$1,000 per share. The Company is also authorized to issue 1,000,000 shares of preferred stock with a par value of \$100 per share. At December 31, 2008, the Company had 5,000 shares of common stock and 250,000 shares of preferred stock issued and outstanding, resulting in total capital stock of \$30 million.

In December 2008 the Company received capital contributions from Delphi Financial Group of \$54,799,338, resulting in total paid-in and contributed surplus of \$106,649,399. The 2008 capital contribution was non-disapproved by the DIFP on April 8, 2009.

Dividends

Dividends paid from inception through 2005 totaled \$76,000,000. Dividends paid during the current examination period were \$1,000,000 in 2006, \$2,000,000 in 2007 and \$2,000,000 in 2008.

Acquisitions, Mergers and Major Corporate Events

None.

Surplus Debentures

The Company issued a \$40,000,000 surplus note to Delphi Financial Group in exchange for cash on December 24, 2008. The effective interest rate for the note is 7.0% per annum paid semiannually. The maturity date is January 15, 2029. The surplus note was approved by the DIFP on December 19, 2008.

CORPORATE RECORDS

A review was performed of the Company's articles of incorporation and by-laws. The by-laws were amended in June 2007 to include three new corporate positions: Chief Operating Officer, Chief Financial Officer, and Chief Underwriting Officer. The articles of incorporation were not amended during the examination period but were amended in April 2009 to reflect the Company's new registered office address. The by-laws were also amended in April 2009 to correct grammatical errors.

The minutes of the shareholder, board of directors and committee meetings were reviewed and appear to properly support and approve the corporate transactions and events for the period under examination. The minutes reflect that the Board reviewed and approved the prior examination report on April 22, 2008.

MANAGEMENT AND CONTROL

Board of Directors

The management of the Company is vested in a board of directors consisting of not less than nine or more than twenty-five members. Directors serving at December 31, 2008 were as follows:

<u>Name and Address</u>	<u>Principal Occupation and Business Affiliation</u>
Harold F. Ilg St. Louis, MO	Chairman Emeritus Safety National Casualty Corp.
Terrence T. Schoeninger St. Louis, MO	Chairman of Board and Chief Executive Officer Safety National Casualty Corp.
Mark A. Wilhelm St. Louis, MO	President and Chief Underwriting Officer Safety National Casualty Corp.
Duane A. Hercules St. Louis, MO	Chief Financial Officer and Treasurer Safety National Casualty Corp.

Gerald R. Scott St. Louis, MO	Executive Vice President & Chief Operating Officer Safety National Casualty Corp.
Jeffrey W. Otto St. Louis, MO	Senior Vice President, Secretary and General Counsel Safety National Casualty Corp.
C. Donald Ainsworth St. Louis, MO	Senior Vice President Government Relations Safety National Casualty Corp.
Robert Rosenkranz New York, NY	Chairman and Chief Executive Officer Delphi Financial Group
Donald A. Sherman New York, NY	President and Chief Operating Officer Delphi Financial Group
Robert M. Smith, Jr. New York, NY	Executive Vice President Delphi Financial Group

Officers

The officers of the Company serving at December 31, 2008 were as follows:

<u>Name</u>	<u>Position</u>
Harold F. Ilg	Chairman Emeritus
Terrence T. Schoeninger	Chairman of Board and Chief Executive Officer
Mark A. Wilhelm	President and Chief Underwriting Officer
Duane A. Hercules	Chief Financial Officer, Treasurer and Executive Vice President, Mergers & Acquisitions
Gerald R. Scott	Executive Vice President & Chief Operating Officer
Jeffrey W. Otto	Senior Vice President, Secretary and General Council
Steven E. Luebbert	Senior Vice President of Business Development
John P. Csik	Senior Vice President of Finance & Assistant Treasurer
Eugene R. Maier	Senior Vice President, Underwriting
Carleton S. Reynolds, III	Senior Vice President, Workers' Compensation Claims

Committees

The Company's bylaws authorize an Executive and Investment Committee and any other committees that may be needed. Committees as of December 31, 2008, were as follows:

Executive and Investment Committee

Terrence T. Schoeninger
Donald A. Sherman
Robert M. Smith, Jr.
Robert Rosenkranz
Mark A. Wilhelm

Derivative Use Plan Compliance Committee

Duane A. Hercules
Gerald R. Scott
Mark A. Wilhelm

The Company has a policy requiring officers and directors to complete conflict of interest disclosure statements annually. The board of directors reviews the statements at its annual meeting. The conflict of interest disclosure statements for the years under examination were reviewed. No significant conflicts were noted.

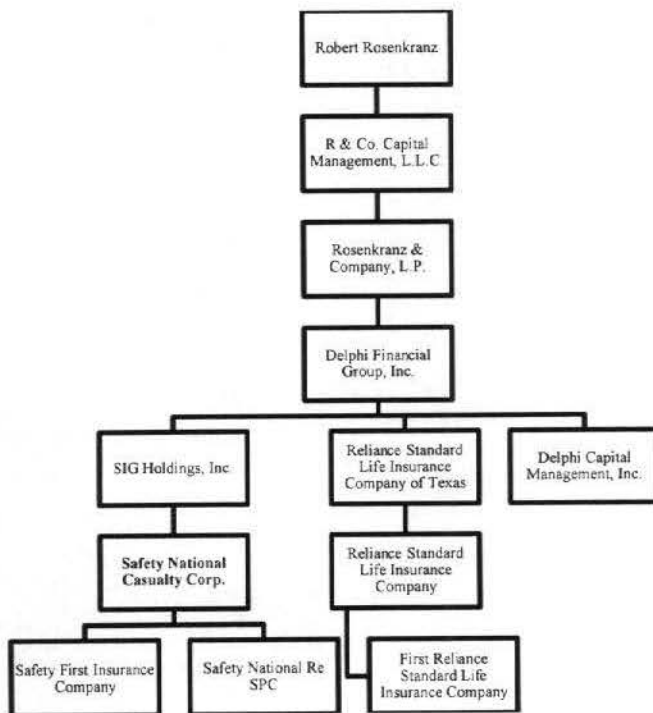
Holding Company, Subsidiaries and Affiliates

The Company is a member of an Insurance Holding Company System as defined by Section 382.010 RSMo (Definitions).

Robert Rosenkranz, as beneficial owner of the sole general partner of Rosenkranz & Company, a New York limited partnership, is the ultimate controlling person within the holding company system. Rosenkranz & Company owns 49.1% voting control of subsidiary Delphi Financial Group, Inc. All outstanding shares of Safety National Casualty Corporation are owned by SIG Holdings, Inc. (SIG), an insurance holding company domiciled in the state of Delaware. SIG is a wholly owned subsidiary of Delphi Financial Group, Inc.

The following organizational chart depicts the holding company system at December 31, 2008. All subsidiaries are wholly owned, except the ownership interest in Delphi Financial Group, Inc. noted in the preceding paragraph. Only entities that have direct and indirect ownership of, and entities that have transactions with Safety National are listed.

Organization Chart



Affiliated Transactions

The Company has entered into the following agreements with affiliates, each of which has been submitted to and not disapproved by DIFP:

Tax Allocation Agreement

Effective January 1, 2001, the Company became a party to a tax allocation agreement with Delphi Financial Group, Inc. Under this agreement, Delphi Financial Group, Inc. files a consolidated federal income tax return annually with eligible entities within the holding company system. The tax liability is apportioned to the companies of the group according to the ratio that each company's separate taxable income bears to the consolidated taxable income. An additional amount is allocated to each company equal to the excess, if any, of the separate return tax liability of such company for the taxable year over the tax liability allocated as outlined above. The Company incurred \$17,547,130 in federal income taxes in 2008 under the tax allocation agreement.

Cost Sharing Agreement (Investments)

Effective January 1, 1997, the Company entered into a cost sharing agreement with Delphi Capital Management, Inc. (DCM) under which DCM provides the Company with investment advisory and administrative services. The services include but are not limited to advice and assistance in determining investment policy, strategic investment planning and selecting the parties to perform custodial and investment management services and investment portfolio accounting. The charges paid by the Company for these services are intended to represent the actual cost incurred by DCM so that DCM receives no profit and suffers no loss. The Company paid \$4,109,387 in investment fees in 2008 under this agreement.

Cost Sharing Agreement (Marketing)

Effective December 1997, the Company entered into cost sharing agreements with Reliance Standard Life Insurance Company and its subsidiary, First Reliance Standard Life Insurance Company (Life Companies), under which the parties agree to share office space and other administrative costs related to the Company's marketing personnel operating out of the regional marketing offices of the Life Companies. The Company paid Marketing costs of \$101,937 to the Life Companies in 2008.

Cost Sharing Agreement (Software)

Effective August 6, 1998, the Company entered into a cost sharing agreement with Reliance Standard Life Insurance Company (RSL) under which RSL agrees to allow SNCC to use software licensed to RSL by SQL Financials International Inc. (SQL) in accordance with the terms of RSL's license agreement with SQL. This software is used for the purpose of performing various accounting, financial and internal audit functions. Under this agreement, RSL also agrees to provide the services of its Internal Audit Department employees to SNCC. The charges paid by the Company for these services are intended to represent the actual cost incurred by RSL, so that no profit or loss is suffered. No fees were paid to RSL in 2008 under this agreement.

Intercompany Service Agreement

Effective July 1, 2001, the Company became party to an intercompany service agreement with its subsidiary Safety First Insurance Company. Under the terms of this agreement, Safety National Casualty Corporation provides Safety First Insurance Company with administrative staff and employees necessary to administer and service Safety First Insurance Company's workers' compensation insurance business. The Company received fees totaling \$170,846 in 2008 for providing this service.

FIDELITY BOND AND OTHER INSURANCE

The Company is a named insured on a financial institution bond with its parent that provides coverage with a single loss limit of \$15,000,000 and a \$100,000 deductible. This coverage complies with the suggested minimum amount of fidelity insurance according to the National Association of Insurance Commissioners guidelines. The Company is also insured on policies that provide the following coverages: commercial property and liability; commercial excess liability; professional liability; employer practices liability; workers' compensation; umbrella liability; and, extortion coverage. The Company's insurance coverage appears to be adequate.

PENSIONS, STOCK OWNERSHIP AND INSURANCE PLANS

Prior to 2008 the Company sponsored two retirement plans for its employees, a defined contribution pension plan and a 401(k) savings plan. These two plans were merged on January 1, 2008, at which time the assets of the defined contribution plan were merged into a new 401(k) plan. The new plan includes both a savings and a profit sharing component. Under the savings component employees who have three months of service may contribute up to the lesser of \$46,000 or 100% of their compensation and the Company matches employee contributions up to 4% of the salary. The Company's 2008 contribution under the savings component of the plan was approximately \$1,387,000. The profit sharing component of the plan provides for a discretionary profit sharing contribution by the Company for eligible employees. The Company did not make a contribution for 2008 under the profit sharing component of the plan.

The Company also has a profit-sharing bonus plan under which eligible employees may receive semi-annual bonuses. The bonus amount is based on statutory net income, length of service, base salary and managerial evaluation. There are no minimum payment guarantees. For 2008, the profit-sharing bonus expense was approximately \$5,277,000.

Safety National participates in a stock purchase plan offered by its upstream affiliate, Delphi Financial Group, Inc. This plan is available to all employees working more than twenty hours per week with a minimum of one year service. Employees may contribute up to 10% of their salary on an after-tax basis. Shares are purchased semi-annually at a discounted price (the lesser of 85% of fair market value on either the first or last day of the offering period).

The Company also provides its employees with benefits typical of the industry: medical, dental and vision coverage; life and disability insurance; paid sick, personal, vacation and holiday leave; dependent care assistance; and, educational assistance.

TERRITORY AND PLAN OF OPERATION

The Company is licensed in Missouri under Chapter 379 RSMo (Insurance Laws Other than Life) to write property, liability, fidelity and surety, accident and health and miscellaneous insurance. The Company is also licensed in the remaining 49 states, the District of Columbia and Canada.

The Company specializes in writing aggregate and specific excess workers' compensation insurance for self-insured employers, targeting medium-sized companies and associations. Coverage applies to losses in excess of applicable self-insured retentions. The Company also underwrites large deductible workers' compensation, primary workers' compensation, workers' compensation loss portfolio transfers, excess unemployment compensation, Texas non-subscriber occupations injury programs, excess workers' compensation self-insurance bonds and bail bonds, and assumed workers' compensation reinsurance. The Company expects to begin writing commercial auto liability and commercial general liability insurance sometime in 2009.

Business is developed through a network of independent agents and brokers. The Company also uses licensed third party administrators, which provide loss control and claims settlement functions.

The DIFP has a separate market conduct staff that performs a review of policy forms, underwriting and treatment of policyholders. The market conduct staff reports its findings in a market conduct report. The most recent market conduct examination was performed on the Company covering the period January 1, 2001, through December 31, 2004. The market conduct examination report was issued March 29, 2006. The report contained no adverse findings.

GROWTH OF COMPANY

The Company continues to grow in terms of admitted assets and surplus. Premium writings have been stable over the examination period, however the Company's admitted assets increased from \$1.32 billion as of the previous examination to \$1.90 billion at December 31, 2008. Capital and surplus also increased from \$359 million to \$531 million during the same time period. This was attributable mainly to strong net operating income.

LOSS EXPERIENCE

The Company has experienced significant adverse loss development in recent years. Reserves were materially understated for the years 2000 to 2004 (based on actual runoff development through December of 2008). The magnitude of the deficiency was such that the Company's surplus relative to its required risk-based capital may have triggered regulatory action if the correct reserves had been recorded in those years and had the Company not taken the steps necessary to strengthen its capital position. The Company explained that it has strengthened its IBNR and carried reserves over the last several years, which has had the result of appearing as adverse development when compared to prior carried reserves.

As a result of the reserve strengthening in 2003, 2004 and 2005, the adverse development since 2005 has not been as high as in prior years, but has still been substantial. The 2008 Annual Statement reported one-year adverse development on net loss and LAE reserves of at least 5% for the years 2004 through 2008. Significantly higher, double-digit percentage two-year adverse developments were also reported for that same time period, ranging from \$91 million to \$154 million for the past four calendar years.

Due to the Company's recent adverse loss development history its reserves will continue to be a concern until the trend of material one-year and two-year deficiencies is broken. This should occur in the near future if reported reserves are sufficient and further reserve strengthening is no longer necessary.

REINSURANCE

General

Premiums written by the Company during the examination period were as follows:

	<u>2006</u>	<u>2007</u>	<u>2008</u>
Direct Written	\$297,309,708	\$292,155,935	\$287,987,344
Reinsurance Assumed:			
Affiliates	2,092,734	2,191,834	2,524,133
Non-Affiliates	41,992,191	37,286,599	36,341,713
Reinsurance Ceded:			
Affiliates	0	0	0
Non-Affiliates	(30,366,956)	(27,756,159)	(24,818,999)
Net Premiums	<u>\$311,027,677</u>	<u>\$303,878,209</u>	<u>\$302,034,191</u>

Assumed

Safety National provides coverage for losses in excess of a specified amount, subject to specified maximums. On workers' compensation business, the Company's attachment points range from \$1 million to \$100 million. Exposure on any one workers' compensation treaty is generally limited to the range of \$1 million to \$2 million. The

highest net exposure on a workers' compensation treaty is \$5 million. Coverage for losses as a result of terrorism is typically excluded from these reinsurance treaties. The Company currently has no assumed loss portfolio transfers on reinsurance contracts.

Ceded

The Company cedes business to its reinsurers principally to reduce net liability on individual risks and to protect against catastrophic losses. Safety National currently maintains treaty reinsurance coverage in the amount of \$190,000,000 excess of \$10,000,000 per occurrence on its Specific Excess Workers' Compensation, Large Deductible Workers' Compensation and Primary Workers' Compensation lines of business. All such treaty reinsurance agreements are written for a one-year term and are renegotiated annually. Reinsurance intermediaries utilized by the Company include Towers Perrin, Arthur J. Gallagher (UK) Ltd., Guy Carpenter & Company, Inc., Aon Re, Inc., JLT Re (North America), Inc., Benfield, Inc. and Access Reinsurance Ltd.

Safety National maintains treaty reinsurance on Primary Workers' Compensation business, which includes a Captive or Rent-A-Captive facility. The Company cedes the liability that the insured would have retained under a self-insured retention. Safety National's excess reinsurance coverage assumes the exposure above the Captive or Rent-A-Captive limit. The Company is no longer actively marketing its Primary Workers' Compensation line of business which includes Captive or Rent-A-Captive facilities.

Safety National maintains treaty reinsurance coverage in the amount of \$8,000,000 excess of \$2,000,000 per occurrence on its Texas Non-Subscriber business. This reinsurance agreement is originally written for an eighteen-month term.

Safety National maintains catastrophe treaty reinsurance coverage in the amount of \$10,000,000 excess of original market loss of \$10,000,000,000 for Earthquake, Fire and Tsunami Industry Loss Warranty business. The \$10 billion attachment point is based on industry-wide losses, not losses specific to Safety National only. The primary purpose of this reinsurance is to cover employee concentration exposures under the Company's assumed reinsurance book of business, specifically due to California earthquake exposures. This agreement is written for a one-year term and is renegotiated annually.

Safety National does not currently maintain reinsurance for Aggregate and Specific Excess Unemployment Compensation business, Aggregate Excess Workers' Compensation business, or Workers' Compensation Self-Insurance Bonds. The Company attempts to limit its exposure on these coverages through its policy terms and strict underwriting practices.

ACCOUNTS AND RECORDS

General

The Company's financial statements are prepared on statutory accounting principles. Accounting entries are recorded on the PeopleSoft general ledger system software.

Independent Auditor

The Company's financial statements are audited annually by the accounting firm Ernst & Young LLP. The workpapers and reports of the most recent independent audit were reviewed for this examination. These workpapers and reports were used in the course of this examination as deemed appropriate.

Independent Actuaries

Loss reserves, loss adjustment expense reserves and related actuarial accounts reported in the financial statements were opined on and certified by Christopher Walker, FCAS, MAAA, of the accounting firm PricewaterhouseCoopers LLP. His review concluded the Company's net reserves were within a reasonable range of acceptable actuarial estimates.

Pursuant to a contract with the DIFP, Glenn A. Tobleman, FCAS, FSA, MAAA and Gregory S. Wilson, FCAS, MAAA of the consulting actuarial firm Lewis & Ellis, Inc. reviewed the adequacy of the Company's loss and loss adjustment expense reserves. Their Statement of Actuarial Opinion of the Company's reserves concluded the gross and net reserves carried were adequate.

Information Systems

In conjunction with this examination, Andrew Balas, AES, Information Systems Financial Examiner with the DIFP, conducted a review of the Company's information systems. His evaluation did not identify any significant weaknesses.

STATUTORY DEPOSITS

Deposits with the State of Missouri

The funds on deposit with the DIFP as of December 31, 2008, as reflected below, were sufficient in par and market value to meet the deposit requirement for the state of Missouri in accordance with Section 379.098 RSMo (Securities to be deposited by all companies, kind and amount).

<u>Type of Security</u>	<u>Par Value</u>	<u>Market Value</u>	<u>Statement Value</u>
St. Charles (MO) Public Water Bond	<u>\$ 2,750,000</u>	<u>\$ 2,290,998</u>	<u>\$ 2,626,994</u>

Deposits with Other States

The Company also has funds on deposit with other states and Canada to satisfy their statutory deposit requirements. Those funds on deposit as of December 31, 2008, were as follows:

<u>State</u>	<u>Type of Security</u>	<u>Par Value</u>	<u>Market Value</u>	<u>Statement Value</u>
Arizona	IL Municipal Bond	\$ 10,850,000	\$ 10,691,032	\$ 10,952,039
California	Municipal Bonds	81,410,000	83,393,551	83,166,717
Delaware	IL Midway Bond	100,000	73,092	97,822
Florida	IL Revenue Bond	1,300,000	1,318,564	1,307,570
Georgia	IL Bond and Money Market	125,000	98,092	122,822
Idaho	US Treasury Note	300,000	323,647	316,013
Indiana	IN Cash Bail Bond	75,000	75,000	75,000
Louisiana	LA Municipal Bond	150,000	155,271	151,903
Maine	IL Midway Bond	750,000	565,585	737,421
Massachusetts	IL Municipal Bond	1,150,000	840,558	1,124,951
Montana	US Treasury Note	25,000	26,971	26,334
Nevada	IL Municipal Bond	100,000	101,428	100,582
New Hampshire	IL Municipal Bond	1,600,000	1,169,472	1,565,149
New Jersey	NJ Municipal Bond	200,000	204,322	200,437
New Mexico	IL Municipal Bond	350,000	255,822	342,376
North Carolina	US Treasury Obligations	1,811,362	1,828,362	1,828,362
Oklahoma	IL Revenue Bond	4,000,000	4,057,120	4,023,294
Oregon	IL Municipal Bond	1,050,000	887,023	1,043,588
South Carolina	IL Revenue Bond	175,000	177,499	176,019
Texas	Certificates of Deposit	3,397,159	3,397,159	3,397,159
Virginia	IL Municipal Bond	300,000	219,276	293,465
Canada	Municipal Bonds	12,600,000	13,203,057	12,719,865
Totals		<u>\$ 121,818,521</u>	<u>\$ 123,061,903</u>	<u>\$ 123,768,888</u>

FINANCIAL STATEMENTS

The following financial statements, with supporting exhibits, present the financial condition of the Company as of December 31, 2008, and the results of operations for the year then ended. Any examination adjustments to the amounts reported in the financial statements and/or comments regarding such are made in the "Comments On Financial Statements," which follow the financial statements.

There may have been additional differences found in the course of this examination, which are not shown in the "Comments On Financial Statements." These differences were determined to be immaterial in relation to 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, 2008

	<u>Assets</u>	Nonadmitted <u>Assets</u>	Net Admitted <u>Assets</u>
Bonds	\$ 1,451,573,038	\$ -	\$ 1,451,573,038
Preferred stocks	54,888,405	-	54,888,405
Common stocks	102,729,478	-	102,729,478
First liens - mortgage loans on real estate	8,889,399	267,491	8,621,908
Other than first liens - mortgage loans on real estate	1,638,879	-	1,638,879
Properties occupied by the company	22,737,576	-	22,737,576
Properties held for sale	10,027,606	278,699	9,748,907
Cash, cash equivalents and short-term investments	92,899,439	-	92,899,439
Other invested assets	43,801,234	-	43,801,234
Receivables for securities	17,203,386	-	17,203,386
Investment income due and accrued	22,711,433	118,747	22,592,686
Uncollected premiums	24,043,724	3,587,485	20,456,239
Deferred premiums	30,700,766	-	30,700,766
Amounts recoverable from reinsurers	6,445,590	-	6,445,590
Funds held by or deposited with reinsured companies	479,056	-	479,056
Current federal income tax recoverable	2,741,314	-	2,741,314
Net deferred tax asset	56,193,913	45,822,753	10,371,160
Guaranty funds receivable or on deposit	691,290	-	691,290
Electronic data processing equipment and software	2,305,067	1,762,743	542,324
Furniture and equipment	2,576,501	2,576,501	-
Net adjustment in assets due to foreign exchange rates	53	-	53
Receivables from parent, subsidiaries and affiliates	555,497	-	555,497
Cash surrender value of officer's life insurance	2,383,025	-	2,383,025
Total Assets	<u>\$ 1,958,215,669</u>	<u>\$ 54,414,419</u>	<u>\$ 1,903,801,250</u>

LIABILITIES
As of December 31, 2008

	<u>Current Year</u>
Losses	\$ 1,183,845,004
Loss adjustment expenses	31,142,609
Other expenses	13,340,438
Taxes, licenses and fees	4,648,149
Unearned premiums	108,026,014
Ceded reinsurance premiums payable	6,262,064
Funds held by company under reinsurance treaties	1,990,718
Amounts withheld or retained by company for account of others	13,765,257
Remittances and items not allocated	2,674,397
Provision for reinsurance	4,504,200
Payable for securities	<u>2,695,814</u>
Total liabilities	\$ 1,372,894,664
Common capital stock	\$ 5,000,000
Preferred capital stock	25,000,000
Surplus notes	40,000,000
Gross paid in and contributed surplus	106,649,399
Unassigned funds (surplus)	<u>354,257,187</u>
Surplus as regards policyholders	\$ 530,906,586
Total Liabilities, Surplus and Other Funds	<u>\$ 1,903,801,250</u>

INCOME STATEMENT
For Year Ending December 31, 2008

	<u>Current Year</u>
Premiums earned	\$ 296,358,007
Losses incurred	216,454,964
Loss expenses incurred	5,754,359
Other underwriting expenses incurred	<u>82,125,031</u>
Total underwriting deductions	304,334,354
Net underwriting gain	(7,976,347)
Net investment income earned	83,706,429
Net realized capital gains	<u>(21,337,143)</u>
Net investment gain	62,369,286
Net loss from premium balances charged off	<u>(108,308)</u>
Total other income	(108,308)
Net income before federal and foreign income taxes	<u>54,284,631</u>
Federal income taxes incurred	<u>8,185,761</u>
Net income	<u>\$ 46,098,870</u>

CAPITAL AND SURPLUS
Changes for 2008

	<u>Current Year</u>
Surplus as regards policyholders; December 31 prior year	\$ 462,951,494
Net income	46,098,870
Change in net unrealized capital gains	(49,177,934)
Change in net unrealized foreign exchange capital gain	(2,745,864)
Change in net deferred income tax	19,300,260
Change in nonadmitted assets	(39,875,578)
Change in provision for reinsurance	1,556,000
Capital surplus notes	40,000,000
Surplus adjustments paid in	54,799,338
Dividends to stockholders	<u>(2,000,000)</u>
Change in surplus as regards policyholders for the year	<u>\$ 67,955,092</u>
Surplus as regards policyholders; December 31 current year	<u>\$ 530,906,586</u>

COMMENTS ON FINANCIAL STATEMENTS

There are no comments on the Company's financial statements.

GENERAL COMMENTS OR RECOMMENDATIONS

Loss Experience, page 11

Due to the Company's recent adverse loss development history its reserves will be a concern until the trend of material one-year and two-year deficiencies is broken. This should occur in the near future if reported reserves are sufficient and further reserve strengthening is no longer necessary.

ACKNOWLEDGEMENT

The assistance and cooperation extended by the officers and employees of Safety National Casualty Corporation during the course of this examination is hereby acknowledged and appreciated. In addition to the undersigned, Wyatt Sample, CFE, CPA, John Boczkiewicz, CFE, CPA, Richard Stamper, CFE, Vasco Stoyhoff and Andy Balas, CFE, CPA, examiners for the Missouri Department of Insurance, Financial Institutions and Professional Registration, participated in this examination.

VERIFICATION

State of Missouri)
) ss
County of St. Louis)

I, Richard Hayes, 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 the 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.

Richard Hayes
Richard Hayes, CFE
Examiner-in-Charge
Missouri Department of Insurance, Financial
Institutions and Professional Registration

Sworn to and subscribed before me this 13 day of August 2009
My commission expires: 1/21/12

Becky Bryant
Notary Public
Becky Bryant
Notary Public-Notary Seal
STATE OF MISSOURI
St. Louis County
My Commission Expires: Jan. 21, 2012
Commission # 08475706

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.

Michael K. Shadowens
Michael Shadowens, CFE
Audit Manager, St. Louis
Missouri Department of Insurance, Financial
Institutions and Professional Registration



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St. Louis, MO 63146-3540
Telephone (314) 995-5300
Fax (314) 995-3843

October 30, 2009

Mr. Frederick G. Heese, CFE, CPA
Chief Financial Examiner & Division Director
State of Missouri
Department of Insurance
P.O. Box 690
Jefferson City, MO 65102-0690

RE: Examination Report

Dear Mr. Heese,

I am writing in response to your letter to Terrence T. Schoeninger dated October 19, 2009. Safety National has the following response to the comment in the Examination Report.

Loss Experience

Comment: Due to the Company's recent adverse loss development history its reserves will be a concern until the trend of material one-year and two-year deficiencies is broken. This should occur in the near future if reported reserves are sufficient and further reserve strengthening is no longer necessary.

Company Response to Examiner's Observation: As reflected in the Examination Report, the Company has strengthened loss reserves and its capital position. The total reserves carried by the Company at December 31, 2009 are in excess, or redundant, by approximately \$31 million compared to the estimate made by the Company's independent actuaries, PricewaterhouseCoopers.

We would like to have this response included in the Examination Report. If you require additional information, please do not hesitate to contact me.

Very truly yours,

John Csik
Sr. Vice President, Finance

a **DELPHI** company