REPORT ON EXAMINATION

OF THE

AMERICAN SAFETY CASUALTY INSURANCE COMPANY

AS OF

DECEMBER 31, 2004

State of Delaware

Department of Insurance

Dover, Delaware

I, Matthew Denn, Insurance Commissioner of the State of Delaware, do hereby certify that the attached REPORT ON EXAMINATION, made as of December 31, 2004 of the

AMERICAN SAFETY CASUALTY INSURANCE COMPANY

is a true and correct copy of the document filed with this Department.

ATTEST BY: Antoinette Handy

DATE: 17 JANUARY 2006

INSURANCE COMMISSIONER • STATE OF DELAWARE •

In Witness Whereof, I HAVE HEREUNTO SET MY HAND AND AFFIXED THE OFFICIAL SEAL OF THIS DEPARTMENT AT THE CITY OF DOVER, THIS 17TH DAY OF JANUARY 2006 .

Matthew Denn

Insurance Commissioner

Deputy Insurance Commissioner

REPORT ON EXAMINATION

OF THE

AMERICAN SAFETY CASUALTY INSURANCE COMPANY

AS OF

December 31, 2004

The above captioned Report was completed by examiners of the Delaware Insurance Department.

Consideration has duly been given to the comments, conclusions, and recommendations of the examiners regarding the status of the Company as reflected in the Report.

This Report is hereby accepted, adopted, and filed as an official record of this Department.

Matthew Denn

MATTHEW DENN
INSURANCE COMMISSIONER

DATED this 17th day of JANUARY 2006.

TABLE OF CONTENTS

August 17, 2005

Honorable Alfred W. Gross
Secretary, Southeastern Zone
State Corporation Commission
Bureau of Insurance
Commonwealth of Virginia
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Richmond, Virginia 23218

Honorable Susan F. Cogswell
Secretary, Northeastern Zone
State of Connecticut
Insurance Department
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Hartford, CT 06142-0816

Honorable Merwin Stewart
Secretary, Western Zone
Department of Insurance
State of Utah
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Honorable Sally McCarty
Secretary, Midwestern Zone
Indiana Department of Insurance
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Indianapolis, IN 46204-2787

Honorable Alfred W. Gross
Chairman, NAIC Financial
Condition Committee
2301 McGee, Suite 800
Kansas City, Missouri 64108-2604

Honorable Matthew Denn
Insurance Commissioner
Delaware Department of Insurance
841 Silver Lake Boulevard
Dover, Delaware 19904

Dear Commissioners:

In compliance with instructions and pursuant to statutory provisions contained in Certificate of Authority No. 05-002, dated March 15, 2005 an Association examination has been made of the affairs, financial condition and management of the

AMERICAN SAFETY CASUALTY INSURANCE COMPANY

hereinafter referred to as "Company," incorporated under the laws of the State of Delaware as a stock company with its home office located at 2333 Westville Road, Marydel, Delaware. Until 2003 the home office was located at 3 South American Avenue, Dover, Delaware. The examination was conducted at the principal office of the Company, located at 1845 The Exchange, Atlanta, Georgia.

The Report of such examination is submitted herewith.

SCOPE OF EXAMINATION

The last examination was conducted as of December 31, 2001. This examination covered the period from January 1, 2002 through December 31, 2004, and consisted of a general survey of the Company's business policies and practices, management, any corporate matters incident thereto, a verification and evaluation of assets and a determination of liabilities. Transactions subsequent to the latter date were reviewed where deemed necessary.

This Report is presented on an exception basis. It is designed to set forth the facts with regard to any material adverse findings disclosed during the examination. The text will explain changes wherever made. If necessary, comments and recommendations have been made in those areas in need of correction or improvement. In such cases, these matters were thoroughly discussed with responsible Company officials during the course of the examination.

The general procedures of the examination followed the rules established by the Committee on Financial Condition Examiners Handbook of the National Association of Insurance Commissioners (NAIC) and generally accepted statutory insurance examination standards consistent with the Insurance Laws and Regulations of the State of Delaware. In accordance with the aforementioned Handbook, a limited information systems review was performed by the consulting firm of INS Services, Inc.

The 2001 examination was conducted by the Delaware Insurance Department in accordance with the Association Plan of Examination guidelines established by the NAIC.

HISTORY

The Company was incorporated on June 8, 1981 under the laws of Georgia as TICOR Indemnity Company and commenced business July 1, 1981. On July 26, 1991, the name was changed to TIC Indemnity Company. Effective April 2, 1993, the Company was sold by the

California Department of Insurance, as liquidator of the parent company. Simultaneously with the sale, the new name was adopted and the Company was redomesticated from Georgia to Delaware.

On April 2, 1993, 92% of the Company was purchased by American Safety Insurance Group, Ltd. (now known as American Safety Insurance Holdings, Ltd.), a Bermuda based captive insurance company, and 8% by Lloyd A. Fox, then president of the Company. While Lloyd Fox initially owned 8% of the stock of the Company, that stock position was converted to ASIG stock on December 29, 1995, and ASIG then owned 100% of the Company.

On August 31, 1999, ASIG transferred its ownership of the entire 100,000 issued and outstanding shares of the Company to American Safety Holdings Corporation (ASHC), a Georgia corporation. That transfer was approved by the Delaware Department of Insurance on August 26, 1999. ASHC is in turn owned by American Safety Insurance Holdings, Ltd. (formerly American Safety Insurance Group, Ltd.), a Bermuda corporation and ultimate parent of the Company.

The Company's Certificate of Incorporation was restated on September 13, 2000, to change the registered agent to GCL Services, LLC, and also to give the Company authority to issue 500,000 shares of capital stock, increasing the par value from $25 per share to $35 per share.

CAPITALIZATION

Common Capital Stock

As of December 31, 2004, the Company's common capital stock is represented by 500,000 shares authorized, with 100,000 shares issued and outstanding at $35 par value, for total common capital stock of $3,500,000. ASHC, a Georgia corporation, owns 100% of the outstanding stock.

Gross Paid In and Contributed Surplus

At the prior examination as of December 31, 2001, gross paid in and contributed surplus amounted to $17,478,199. Originally, the Company had issued 100,000 shares of stock at $25 per share. On April 2, 1993, the Company purchased from Lloyd Fox, President of the Company, all of the outstanding common stock of Synergy Insurance Services, Inc. (formerly Environmental Management Insurance Services, Inc.) in exchange for 8% of the outstanding common stock of the Company. The transaction was recorded as a contribution to surplus in the amount of $45,255, the statutory valuation of Synergy Insurance Services, Inc. at the date of ownership transfer. Synergy Insurance Services is now known as American Safety Insurance Services, Inc.

On September 13, 2000, to comply with revised regulatory standards, the Company restated its Certificate of Incorporation, changing the per share par value of its capital stock from $25 to $35. To effect the change, $1,000,000 was transferred from unassigned surplus to capital in the form of a stock dividend.

On September 29, 2000, 100% of the capital stock of American Safety Indemnity Company, an Oklahoma insurance company, was transferred from ASHC to the Company. The Company recorded the value of this asset of $15,932,944 as a contribution to surplus.

As a result of the above transactions, at December 31, 2001 the gross paid in and contributed surplus amounted to $17,478,199.

During this examination period, the Company received an additional $12,000,000 in capital contributions. The infusion was the result of a transfer of $3,000,000 cash from

American Safety Holdings Corporation, the parent company. This was recorded as a receivable of $3,000,000 at December 31, 2002, and the cash received by the Company on March 31, 2003.

In 2003, the Company increased its Gross Paid In and Contributed Surplus by an additional $6,000,000 by setting up a receivable at December 31, 2003. That contribution consisting of $3,882,251 in cash, and securities with a market value of $2,117,749, was received on February 27, 2004.

As a result of the above transactions, at December 31, 2004, the Gross Paid In and Contributed Surplus amounted to $29,478,199.

Surplus Notes

On September 1, 1999, the Company issued a surplus note to ASIG (now known as American Safety Insurance Holdings, Ltd.) for $2,500,000. This transaction was approved by the Delaware Department of Insurance on August 26, 1999. The total amount due under this note has remained at $2,500,000, with interest on the unpaid principal at an annual rate of 6%.

The terms of the surplus note require that the principal and interest on this note shall be paid only to the extent that, after any such payment, the Company has remaining at least $10,000,000 of free surplus. Also, under the terms of the surplus note, no principal or interest will be paid unless approved in advance by the Delaware Department of Insurance and payments on the surplus note will be subordinated to payments due policyholders and claimants, as well as debts owed to all other classes of creditors in the event of liquidation, insolvency, bankruptcy or reorganization.

The Company's submittal was approved with an exemption from Delaware Insurance Statutes, Section 5003. In compliance with Paragraph 12, of SSAP #41, the surplus note was properly disclosed in the Notes to Financial Statements of the Annual Statement for each of the three years under examination.

Stock Ledger

During the prior examination, the Company was unable to locate its original stock certificates and transfer book. During the course of this examination, the Company presented an Affidavit of Lost Stock Certificates, and an original stock transfer ledger (share register) that appears to correctly reflect the chronology of certificates issued, certificates surrendered, and the name of the current stockholder. The Company appears to be in compliance with the provisions of Delaware General Corporation Law Title 8, Chapter 1, Sections 220 and 224.

MANAGEMENT AND CONTROL

Directors

A review of the minutes of the sole shareholder of the Company for the three year period of examination reflects that the Board of Directors was duly elected for each of the respective years. Names of directors were compared to the respective Annual Statement jurat pages without exception. Those directors serving at December 31, 2004 were as follows:

Cody W. Birdwell
David V. Brueggen
Stephen R. Crim
Thomas W. Mueller

Officers

Corporate minutes were obtained and reviewed for each of the three years of examination. Names of officers were compared to the respective Annual Statement jurat pages. Those officers serving at December 31, 2004 were as follows:

Stephen R. Crim	President
Joseph D. Scollo, Jr.	Executive Vice President
J. Jeffrey Hood	Senior Vice President – Technical Services
Steven B. Mathis	Treasurer, Vice President – Finance, and Assistant Secretary
Fred J. Pinckney*	Secretary and General Counsel

*Subsequent to the date of examination, Fred J. Pinckney retired effective March 31, 2005. By Unanimous Written Consent of the Board of Directors of American Safety Casualty Insurance Company in Lieu of an Annual Meeting dated March 10, 2005, Dorothy J. Giglio was named Secretary.

Conflict of Interest

The Company appears to have an adequate policy and statement concerning conflict of interest, and the conflict of interest statements are signed each year by directors, officers and key employees. These statements were reviewed for the three year period of examination with no exceptions noted.

HOLDING COMPANY SYSTEM

The Company is a member of an Insurance Holding Company System. The ultimate parent of the system is American Safety Insurance Holdings, Ltd. (formerly American Safety Insurance Group, Ltd.), a stock company domiciled in Bermuda. The following is an organizational chart that reflects the identities and interrelationships between the Company, parent, all affiliated insurers, and other members of the system as of December 31, 2004, as presented in Schedule Y:

American Safety Insurance Holdings, Ltd.

- American Safety Reinsurance, Ltd.
- American Safety Assurance, Ltd.
- American Safety Holdings Corporation
  - **American Safety Casualty Insurance Company**
    - American Safety Indemnity Company
  - Ponce Lighthouse Properties, Inc.
    - Harbour Village Realty Corporation
  - Rivermar Contracting Company
  - American Safety Insurance Services, Inc.
    - Environmental Claims Services, Inc.
    - American Safety Purchasing Group, Inc.
    - Sureco Bond Services, Inc.
    - American Safety Financial Corporation
      - American Safety Mortgage Corporation
  - American Safety Capital Trust, Inc.
  - American Safety Capital Trust II, Inc.
  - WHE Corporation
    - Winston at Harbour Village, LLC

Other related and controlled entities include American Safety Risk Retention Group, Inc. and 1845 RE, LLC.

Copies of the Form B Holding Registration Statements filed with the Delaware Department of Insurance during the period under examination were reviewed in conjunction with the review of the management, service, and tax agreements in place during the period of examination. This review indicated that the Company complied with the provisions of Regulation 13 of the Delaware Insurance Statutes.

The agreements were submitted and subsequently approved by the Delaware Department of Insurance. The agreements were filed in compliance with requirements of Delaware Insurance Statutes, Chapter 50 (Insurance Holding Company System Registration Act) and Delaware Insurance Regulation 13 (Holding Company System Forms and Instructions).

MANAGEMENT AND SERVICE AGREEMENTS

Agreements with Affiliates

Program Management Agreement

An agreement signed April 2, 1993, between American Safety Insurance Services, Inc. and the Company provides for cost allocation to account for shared costs between affiliated entities. The agreement was amended March 31, 2002, to allocate expenses based on direct costs and on the basis of direct written premiums.

Reinsurance Agreements

Several reinsurance agreements with affiliates are described in the Reinsurance section of this Report.

Tax Sharing Agreement

Under the Tax Sharing Agreement, the tax charge to the Company shall not be more than the Company would have paid if it had filed on a separate return basis.

The Tax Sharing Agreement in effect calls for settlement to take place between the parties on or before the due date of the consolidated federal income tax return. Section 2.3 of the Tax Sharing Agreement states that in the event the parent company owes the subsidiary company, settlement is to take place on or before the tax return due date including extensions.

Agreements with Non-Affiliates

Investment Advisory Agreement

On March 7, 2003, the Company entered into an Investment Management Agreement with an asset management company incorporated in Missouri, to act as investment advisor. The investment advisor is to act with respect to the assets of the Company only with the prior approval of the Company, except where specific investment parameters are agreed to in advance.

It was noted that the Board of Directors approved the investments in bonds and stocks during the examination period as required by Section 1304 of the Delaware Insurance Statutes.

Custodial Agreement

The Company has a "Master Custody Agreement" with a trust company (The Bank) dated December 14, 1999, and amended January 15, 2003, with respect to the custody and management of its investments. A review of this agreement disclosed that the Company complied with the recommendation from the prior examination concerning the replacement of loss custodial securities, for which "The Bank" is obligated to indemnify the Company and that the securities so deposited shall at all times be kept separate and apart. The Custodial Agreement did not clearly state the following:

- That confirmation of all transfers should be provided to the insurance company in hard-copy or in electronic format.
- That in the event that the custodian gains entry in a clearing corporation through an agent, there should be a written agreement between the custodian and the agent that the agent shall be subjected to the same liability for loss of securities as the custodian.
- That if the custodial agreement has been terminated or if 100% of the account assets in any one custody account have been withdrawn, the custodian shall provide written notification, within three business days of termination or withdrawal, to the insurer's domiciliary commissioner.
- That upon reasonable notice, an officer or employee of the insurance company or a representative of an appropriate regulatory body shall be entitled to examine its records relating to securities.

- That the custodian and its agents, upon reasonable request, shall be required to send all reports from clearing corporation or the Federal Reserve book-entry to the insurance company on their respective system of internal control.
- That the custodian agrees to maintain records sufficient to determine and verify information in preparation of the Company's Annual Statement.
- That custodian shall provide, upon written request, the appropriate affidavits with respect to the insurance company's securities held by the custodian.
- That the custodian shall secure and maintain insurance protection in an adequate amount.

Therefore,

> **It is recommended that the Company take the necessary steps to correct the custodian agreement to comply with requirements set forth in the *NAIC Financial Condition Examiners Handbook*, Part 1, Section IV, Paragraph J.**

TERRITORY AND PLAN OF OPERATION

Territory

During the examination, the Company's certificates of authority were reviewed without exception. As of December 31, 2004, the Company was licensed in the following jurisdictions:

Alabama	Louisiana	Oklahoma
Alaska	Maine	Oregon
Arizona	Maryland	Pennsylvania
Arkansas	Massachusetts	Rhode Island
California	Michigan	South Carolina
Colorado	Minnesota	South Dakota
Delaware	Mississippi	Tennessee
District of Columbia	Missouri	Texas
Florida	Montana	Utah
Georgia	Nebraska	Vermont
Hawaii	Nevada	Virginia
Idaho	New Jersey	Washington
Illinois	New Mexico	West Virginia
Indiana	New York	Wisconsin
Iowa	North Carolina	Wyoming

Kansas	North Dakota
Kentucky	Ohio

In addition, the Company has a certificate of authority qualifying as an acceptable surety for federal bonds and a certificate of surplus line insurer eligibility from Puerto Rico.

Plan of Operation

The Company underwrites, manages and markets primary property and casualty insurance, reinsurance programs, and insurance program business in the alternative insurance market for environmental remediation risks and other specialty risks. During the year ended December 31, 2004, the core business was the underwriting of general liability for environmental coverage, workers' compensation, surety and commercial lines.

The Company markets its products through approximately 637 independent insurance agencies and insurance brokerage firms. The Company does not have any full service branch offices. The Company has one affiliated agency, Sureco Bond Services, Inc., a Georgia surety agency wholly-owned by American Safety Insurance Services, Inc. The Company does not directly own any agencies.

The 2004 Annual Statement indicates that direct business written was as follows:

Workers' compensation	$ 1,401,169
Other liability – occurrence	18,541,970
Other liability – claims made	14,016,939
Private passenger auto liability	56,140
Commercial auto liability	3,315,023
Auto physical damage	338,517
Surety	2,045,879
Total	$39,715,637

Fronting Arrangements

During the examination period, products were also marketed under approximately eleven different program (fronting) agreements.

Third-Party Administrators

During this examination period, claims were handled by approximately twelve different third-party administrators (TPAs).

Reinsurance Intermediary-Brokers

During the examination period, the Company worked with approximately six different reinsurance intermediary-brokers as defined in Delaware Insurance Statutes, Section 1602 (f), as follows:

Aon Re, Inc.
Ballantyne, McKean & Sullivan, Inc.
Benfield Blanch, Inc.
Guy Carpenter & Company, Inc.
John P. Woods Company, Inc.
Willis Re, Inc.

Managing General Agents

During the examination period, the Company was a participant in an agreement which met the definition of Managing General Agent under Title 18, Chapter 18, Section 1804, of the Delaware Insurance Code. Only one program manager met the qualifications of an MGA at December 31, 2004, as defined by Title 18, Chapter 18, Section 1802, of the Delaware Insurance Code by underwriting premiums in excess of 5% of the policyholder surplus at the prior year end. Following is a description of that agreement which appears to meet the requirements of Delaware Insurance Code.

The Company is a participant in a Program Management and Underwriting Agreement for Lawyers Professional Liability Insurance with Professional Coverage Managers, Inc. (PCM). PCM is an insurance program manager and underwriter operating in regional offices through licensed insurance brokers and agents to solicit applications for and provide Lawyers Professional Liability insurance. PCM also provides the administrative, marketing, underwriting, and claims handling functions. The maximum limits of insurance are $3,000,000 per claim/per policy aggregate.

GROWTH OF COMPANY

The following information was obtained from the Company's filed Annual Statements:

Year	Admitted Assets	Surplus	Premiums Earned	Net Income
2004	$141,584,918	$46,465,796	$28,306,024	$(9,745,645)
2003	122,365,626	39,769,857	30,095,801	(2,756,413)
2002	96,002,545	29,525,318	20,157,798	297,608
2001	108,631,328	24,600,583	42,932,611	(1,760,468)

The preceding schedule reflects changes in the Company's premium writings and net income during the three-year examination period. The net written premiums decreased 42% in 2002, 2% in 2003 and 14% in 2004. The decrease in 2004 reflected the Company's shift in its focus in 2003 back to its core lines of business. The majority of the core programs were written for bail bonds, pest control operators, lawyer legal liability, and the Hawaii taxi cabs.

Of the $19 million increase in admitted assets in 2004 over 2003, $16 million is the result of an increase in the book value of the Company's 100% owned affiliate, American Safety Indemnity Company, an increase of 95% of the original cost.

REINSURANCE

The Company both ceded and assumed reinsurance during the period under examination. Following is a summary of the reinsurance program in place as of December 31, 2004:

Direct business written	$39,715,637
Assumed from affiliates	34,186,093
Assumed from non-affiliates	(157,868)
Ceded to affiliates	(24,523,658)
Ceded to non-affiliates	(25,472,453)
Net premiums written	$23,747,751

Assumed

During 2004, the Company discontinued all assumed contracts except pooling contracts with affiliates. The Company entered into an inter-company pooling arrangement on January 1, 2002, which pooled the environmental business written by the Company, its subsidiary American Safety Indemnity Company, and two affiliates, American Safety Reinsurance, Ltd. and American Safety Risk Retention Group. This agreement was approved by the Delaware Department of Insurance. The Company is the manager in the pool and it retrocedes the business back with each participant receiving 25% of the pool. The pooling agreement covers all environmental insurance which includes contractors' and consultants' general liability, contractors' pollution liability, environmental consultants' professional liability, property transfer pollution liability, commercial real estate pollution liability, and fixed site environmental liability. Policies are written up to $10 million of coverage.

There was no non-affiliated assumed business in effect as of December 31, 2004.

Ceded

The Company's reinsurance program for general, pollution and professional liability, and excess and surplus lines risks operates on an excess of loss and quota share basis. A description of the ceded reinsurance program follows:

- Casualty business is covered under several excess of loss and quota share treaties with various reinsurers.
- The Company has catastrophe coverage up to $5 million on its liability business with retention of $500,000.
- The attorney's professional liability is ceded under a 75% quota share contract and an excess of loss contract which cedes $2 million in excess of $1 million.
- The Company cedes 50% of surety business through a quota share contract.
- The Company cedes the environmental business through four layers of excess of loss contracts with the Company retaining $500,000 with coverage up to $11,000,000.

FIDELITY BONDS AND OTHER INSURANCE

The Company is covered under a standard financial institution bond covering the American Safety Insurance Group, Ltd. Fidelity coverage under that bond met the minimum amount of fidelity insurance suggested by the NAIC. The Company is also the named insured on other policies that include:

- Professional liability
- Directors and officers liability and company indemnification
- Commercial auto policy
- Workers compensation and employers liability policy
- Commercial excess liability policy

- Commercial umbrella
- Financial institutions policy

ACCOUNTS AND RECORDS

The accounts and records reviewed included an evaluation of the Company's operational and organizational controls. The areas evaluated included computer systems, accounting systems, organizational structure, and the processing structure.

During the examination the Company's books and records were reviewed and compared to reported items and values in the Annual Statements. A trial balance for the final year under review was obtained and traced to the Company's Annual Statement.

The main applications used by the Company are Microsoft Windows 2000/2003 Server; Microsoft Windows NT Server 4; Microsoft Windows XP Pro; Citrix Presentation Server 3.0, Microsoft Access 2000 and Microsoft Office 2000 Groupware Suite; the Platinum Accounting v5.2 package and FRX v6.5 reporting module; Microsoft Exchange Server 2000, Microsoft SQL Server v2000 and v7; Q & A v4 Database; and ADP Payroll (outsourced service). In addition, the Company is in the process of implementing the Genius System from REBUS, which is an enterprise-wide system to handle both premiums and claims.

The <u>NAIC Annual Statement Instructions for Property and Casualty Companies</u> requires that the total management and service fees incurred attributable to affiliates and non-affiliates be reported in the footnote to the Underwriting and Investment Exhibit of the Annual Statement. The prior examination report contained a recommendation that the Company disclose the total management and service fees incurred in the footnote to the Underwriting and Investment Exhibit of the Annual Statement. The Company did not include that disclosure in the Annual Statement.

Therefore:

> **It is again recommended that the Company comply with the <u>NAIC Annual Statement Instructions for Property and Casualty Companies</u> and disclose the total management and service fees incurred attributable to affiliates and non affiliates and report them in the footnote to the Underwriting and Investment Exhibit of the Annual Statement.**

During the testing of premiums written, it was noted that for various programs the Company does not maintain policy level detail within its premiums system which would permit the reporting and aging of agents' balances on a policy level. This is not in compliance with SSAP 6, Paragraph 9c of the *NAIC Accounting Practices and Procedures Manual*, which requires policy level reporting and aging of agents' balances.

Therefore:

> **It is recommended that in the future the Company report and age agents' balances on a policy level basis in compliance with SSAP 6, Paragraph 9c of the *NAIC Accounting Practices and Procedures Manual.***

<u>NAIC FINANCIAL RATIOS</u>

The Company's 2004 NAIC Financial Ratios from the Insurance Regulatory Information System (IRIS Ratios) were reviewed and it was noted that the Company had unusual values for five of the ratios: two-year overall operating ratio, investment yield, liabilities to liquid assets, one-year reserve development to surplus, and two-year reserve development to surplus.

The unusual operating ratio is primarily the result of high costs related to the surety, workers' compensation and commercial lines, all of which were de-emphasized during 2002. Those units still incurred costs in 2003, yet did not contribute significantly to net earned premiums. In 2004, those costs were reduced.

The investment yield is outside of the normal range because total cash and invested assets includes an investment in common stock of an affiliate, American Safety Indemnity Company, of $38,538,339, which paid no dividends in 2004.

The liabilities to liquid assets ratio is outside the normal range, but has improved over the past three years. At December 31, 2001, the ratio was 159%; at December 31, 2004, the ratio was 116%. The Company asserted that improvement will continue as assets classified as non-liquid are collected and invested. In addition, the investment in the insurance subsidiary is classified as non-liquid in the ratio's formula.

The one and two-year reserve development to surplus ratios were unusual because the Company experienced $16 million of adverse loss development in 2004 as follows:

Environmental products	$ 500,000
Excess and surplus lines products	10,300,000
Program business	1,600,000
Other lines	3,600,000
Total	$ 16,000,000

The development in the Excess and Surplus lines segment is attributable to certain New York contractor risks written in 2001. Exposure to New York contractor risks was significantly reduced during 2002 and 2003. The Other lines segment development is primarily due to $1.5 million on workers' compensation business and $1.7 million on the assumed liability program business. Both programs are currently in run-off.

FINANCIAL STATEMENTS

The following statements show the assets, liabilities, surplus and other funds of the Company, as determined by this examination, as of December 31, 2004.

Asset
Liabilities, Surplus and Other Funds
Statement of Income
Capital and Surplus Account

Assets

December 31, 2004

	Assets	Nonadmitted Assets	Net Admitted Assets
Bonds	$ 71,130,629	$ 0	$ 71,130,629
Common stocks	41,297,506		41,297,506
Cash and short-term investments	4,340,173		4,340,173
Investment income due and accrued	943,077		943,077
Premiums and agents' balances in course of collection	5,810,384		5,810,384
Premiums, agents' balances and installments booked but deferred and not yet due	3,270,102		3,270,102
Amounts recoverable from reinsurers	6,294,986		6,294,986
Funds held by or deposited with reinsured companies	298,000		298,000
Other amounts receivable under reinsurance contracts	824,000		824,000
Current federal and foreign income tax recoverable and interest thereon	3,916,726		3,916,726
Net deferred tax asset	4,452,696	3,119,238	1,333,458
Receivables from parent, subsidiaries, and affiliates	568,075		568,075
Funds on deposit with third party claims administrators	1,557,802		1,557,802
Total Assets	$144,704,156	$ 3,119,238	$141,584,918

Liabilities, Surplus and Other Funds

December 31, 2004

Losses	$ 44,724,641
Reinsurance payable on paid loss and loss adjustment expenses	8,141,838
Loss adjustment expenses	14,771,716
Commissions payable, contingent commissions and other similar charges	300,360
Other expenses	325,001
Taxes, licenses and fees	1,890,351
Unearned premiums	12,583,812
Ceded reinsurance premiums payable	7,239,215
Funds held by Company under reinsurance treaties	1,113,569
Amounts withheld or retained by Company for account of others	1,740,428
Provision for reinsurance	255,000
Payable to parent, subsidiaries and affiliates	1,942,876
Funds owed to third party administrators	90,315
Total Liabilities	$ 95,119,112
Common capital stock	3,500,000
Surplus notes	2,500,000
Gross paid in and contributed surplus	29,478,194
Unassigned funds (surplus)	10,987,602
Surplus as regards policyholders	$ 46,465,796
Total Liabilities and Surplus	$141,584,918

Statement of Income

December 31, 2004

Underwriting Income	
Premiums earned	$28,306,024
Deductions	
Losses incurred	23,864,717
Loss expenses incurred	9,576,430
Other underwriting expenses incurred	10,922,732
Net underwriting loss	$(16,057,855)
Investment Income	
Net investment income	2,579,097
Net realized capital gains	31,747
Net investment gain	$2,610,844
Other Income	
Net loss from agents' or premium balances charged off	(500,721)
Net income before federal taxes	$(13,947,732)
Federal taxes incurred	(4,202,087)
Net Loss	$ (9,745,645)

Capital and Surplus Account

December 31, 2003 to December 31, 2004

Surplus as Regards Policyholders, December 31, 2003		$ 39,769,857
Net Loss	$(9,745,645)	
Net unrealized capital gains	16,200,887	
Change in net deferred income tax	319,977	
Change in nonadmitted assets and related items	(364,280)	
Change in provision for reinsurance	285,000	
Net change in capital and surplus for the year		6,695,939
Surplus as Regards Policyholders, December 31, 2004		$ 46,465,796

EXAMINATION FINANCIAL CHANGES

No financial changes were made as a result of this examination.

NOTES TO THE FINANCIAL STATEMENTS

Note 1. Losses	**$ 44,724,641**
Loss Adjustment Expenses	**$ 14,771,716**

The amount per examination is the same as the Company reported in the 2004 Annual Statement.

INS Consultants, Inc. (INS) was retained by the Delaware Department of Insurance as consulting actuary to conduct a review of the Company's reserving methodologies and adequacy. The Company provided the consulting actuary with their statement of actuarial opinion and the supporting actuarial data and documents. Additional data, as requested by INS, was also provided by the Company.

INS performed an independent analysis of the Company's gross and net loss and loss adjustment expense reserves as of December 31, 2004. The analysis was performed, gross and net of reinsurance, for eight major sources of business: Excess & Surplus Lines General Liability, Professional & General Liability excluding E&S Lines, Surety, Commercial Lines Property & Liability, Workers Compensation – ISA, Vision Non-Standard Private Passenger Auto & Other Lines, Workers Compensation – ASCIC, and AS Resources - ASCIC.

The Company's carried gross reserve of $132.556 million is lower than INS' estimate by $1.974 million, or 1.5% of the carried reserve. American Safety Casualty's carried net reserve of $59.496 million is lower than INS' estimate by $0.937 million, or 1.6% of the carried reserve.

Samples of randomly selected policies from the Company's material blocks of direct written business were used to test the validity of valuation data. The policy sample tests indicated a general absence of errors in the underlying data used for valuation. In addition, based on completeness testing, it appears that the valuation extract files are complete.

The balance sheet items enumerated in the examination appear fairly stated, and were calculated using valuation parameters free of material error. Valuation extract files appear to be complete. Therefore, the balance sheet items covered by this examination have been accepted, as stated by the Company, for the purpose of this report.

COMPLIANCE WITH PRIOR EXAMINATION RECOMMENDATIONS

There were 29 recommendations made in the prior examination report. The Company's compliance with prior examination recommendations was reviewed during the current examination.

It has been determined in the current examination that the Company has complied with prior examination recommendations except as follows.

- The prior examination report recommended that the Company comply with the NAIC Annual Statement Instructions for Property and Casualty Companies and disclose the total management and service fees incurred attributable to affiliates and non affiliates in the footnote to the Underwriting and Investment Exhibit of the Annual Statement. The Company did not comply with that recommendation.

SUMMARY OF RECOMMENDATIONS

Management and Service Agreements

- It is recommended that the Company take the necessary steps to correct the custodian agreement to comply with requirements set forth in the *NAIC Financial Condition Examiners Handbook*, Part 1, Section IV, Paragraph J. (Page 11)

Accounts and Records

- It is again recommended that the Company comply with the NAIC Annual Statement Instructions for Property and Casualty Companies and disclose the total management and service fees incurred attributable to affiliates and non affiliates and report them in the footnote to the Underwriting and Investment Exhibit of the Annual Statement. (Page 18)
- It is recommended that in the future the Company report and age agents' balances on a policy level basis in compliance with SSAP 6, Paragraph 9c of the *NAIC Accounting Practices and Procedures Manual.* (Page 18)

CONCLUSION

The following schedule shows the results of this examination and the results of the prior examination with changes between the examination periods:

Description	December 31, 2004	December 31, 2001	Increase or Decrease
Assets	$141,584,918	$107,404,020	$34,180,898
Liabilities	$95,119,122	$83,753,195	$11,365,927
Capital and Surplus	$46,465,796	$23,650,825	$22,814,971

The assistance of Delaware's consulting actuarial firm, INS Consultants, Inc. is acknowledged.

Respectfully submitted,

____
Jerry H. Smith, CFE
Examiner-In-Charge
State of Delaware
Northeastern Zone, NAIC

SUBSEQUENT EVENTS

The Company reported that in March, 2005, the underwriting and claims processing for the environmental business was converted to a new processing system.