

REPORT ON EXAMINATION OF
MAPFRE REINSURANCE CORPORATION
FLORHAM PARK, NEW JERSEY 07932
AS AT
DECEMBER 31, 2005
N.A.I.C. COMPANY CODE 23876



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Honorable Steven M. Goldman
Commissioner of Banking and Insurance
20 West State Street
Trenton, New Jersey 08625

April 12, 2007

Dear Commissioner:

In accordance with the authority vested in you, a financial condition examination has been made of the assets and liabilities, method of conducting business and other affairs of the

MAPFRE REINSURANCE CORPORATION

FLORHAM PARK, NEW JERSEY

NAIC COMPANY CODE 23876

hereinafter referred to as, "Company" or "MRC."

SCOPE OF THE EXAMINATION

This examination of Mapfre Reinsurance Corporation "MRC" covers the period from January 1, 2003 to December 31, 2005. The examination was conducted under Section 17:23-22 of the New Jersey Statutes Annotated (N.J.S.A.) Revised Statutes. During this period under examination, the Company's assets increased from \$173,168,902 to \$247,160,213. Liabilities increased from \$63,227,497 to \$99,901,094 and surplus as regards to policyholders increased from \$109,941,405 to \$147,259,119.

In determining the emphasis placed on each item reported herein, consideration was given to the Company's accounting methods and internal controls, information systems controls, audits performed by certified public accountants for the period under review, financial analysis performed by the Financial Analysis Unit of the New Jersey Department of Banking and Insurance ("NJDOBI"), and procedures specified by the National Association of Insurance Commissioners.

No accounts were determined to require special emphasis. Standard emphasis, as defined in the New Jersey Financial Condition Examiners Handbook, was used in several instances. Accounts requiring standard emphasis were:

- Losses
- Reinsurance and the related accounts
- Premium in course of collection
- Unearned premiums
- Bonds
- Cash

All other accounts were determined to require reduced emphasis. Additional areas reviewed during this examination were as follows:

- History and Kind of Business
- Management and Control
- Territory and Plan of Operation
- Policy on Conflict of Interest
- Intercompany Agreements
- Accounts and Records
- Fidelity Bond and Other Insurance Coverage

The examination report, contained herein, will address significant balance sheet accounts and, if necessary, comments on those accounts which involve departures from laws, regulations or rules, or which are deemed to require special explanation or description.

Work papers prepared by the Company's external accounting firm, Ernst & Young LLP ("E&Y"), New York, New York, in connection with the annual audit, were reviewed and relied upon to the extent possible.

COMPLIANCE WITH PRIOR REPORT ON EXAMINATION RECOMMENDATIONS

There was one recommendation from the prior examination report. It was recommended that a formal report be prepared by the Corporate Secretary indicating annual compliance with the Company's conflict of interest questionnaires and any conflicts if there are any to the Board of Directors. The Company complied with the recommendation.

HISTORY AND KIND OF BUSINESS

The Company was incorporated under the laws of the State of California on February 21, 1985 as The New Zealand Reinsurance Company of America to serve as the corporate vehicle for the domestication of the United States Branch of The New Zealand Insurance Company Ltd. and commenced operations on March 6, 1986.

On April 18, 1991, Chatham Holdings Inc., a Delaware general business corporation, purchased all of the issued and outstanding capital stock of the Company. The Company's name was changed on May 15, 1991 to English & American Insurance Corporation and on June 25, 1993 to Chatham Reinsurance Corporation.

On June 7, 2000 the Company was sold to Mapfre Mutualidad De Seguros Y Reaseguros A Prima Fija of Spain ("Mapfre Re" or "Parent") a subsidiary of Mapfre Group, the leading insurance entity in Spain. Following the transaction the company was renamed to its present name and was capitalized with \$100 million from the Parent. By written consent of the sole shareholder on November 21, 2001 and by resolution of the Board of Directors September 11, 2002, the Corporation was authorized to re-domesticate (for the purpose of administrative and operational efficiency) from the State of California to the State of New Jersey.

A transfer of \$700,000 was authorized on September 11, 2002 to be made from the paid in and contributed surplus account to the common capital stock account. The transfer was made to meet State of New Jersey minimum capital requirements of \$4.2 million per N.J.S.A. 17:17-6.

In December 2003, the Company filed an application with the Office of Superintendent of Financial Institutions (OSFI) to open a Canadian Branch. On November 15, 2004 the Company's application was approved and a license limited to the business of reinsurance was granted by the OSFI.

The Company received capital contributions from its Parent of \$15,000,000 on February 24, 2003 and \$20,000,000 on April 27, 2004.

As of December 31, 2005, the Company had common capital stock of \$4,200,000 (420 outstanding shares with a \$10,000 par value per share), paid in surplus of \$135,077,577, and unassigned surplus of \$7,981,542.

No dividends were paid to stockholders during the examination period.

The Company's Certificate of Authority authorizes the Company to write the types of insurance specified in paragraphs "a", "b", "e", "f", "g", "i", "j", "k", "l", "m", "n", and "o" of N.J.S.A. 17:17-1 and health insurance as defined in N.J.S.A. 17B:17-4.

The principal and main administrative office of the Company is located at 100 Campus Drive, Florham Park, New Jersey 07054. The registered agent upon whom process may be served is John Lynch, Senior Vice President, CFO and Treasurer.

The Company is a member of an insurance holding company system as defined in N.J.S.A. 17:27A-1.

TERRITORY AND PLAN OF OPERATION

The Company is a New Jersey domestic property and casualty reinsurance company. The ultimate Parent is a worldwide insurance holding company, which through its insurance subsidiaries writes a broad range of life and property and casualty insurance products.

The Company no longer writes any direct business. The Company underwrites traditional and specialty lines of business through the brokerage market on risks located in the United States and Canada. The Company is not producer controlled and most business is obtained through intermediaries. The Company is licensed in thirty one states and the District of Columbia.

On November 15, 2004, the Company was granted a license limited to the business of reinsurance by the Office of Superintendent of Financial Institutions (“OSFI”). In addition on December 14, 2004, the Company was granted a license by the Province of Ontario.

CORPORATE RECORDS

The minutes from the Board of Directors and the Shareholders were reviewed from 2003 through 2006 for any subsequent events. The Board of Directors approves the investment transactions, elects officers and generally is proactive in the Company. The Shareholder minutes documents the elections of the Board of Directors. The Board members attended meetings on a regular basis.

The Board of Directors maintains two committees an executive committee and an investment committee as of December 31, 2005. The Board of Directors of the Company’s ultimate parent, has (13) members out of (22) that are outside directors in addition the ultimate parent has established a compliance committee composed of only external directors (5) and therefore the Company complies with N.J.S.A. 17:27:4 (d).

REINSURANCE

The Company enters into reinsurance agreements in the normal course of business to reduce overall risk and to minimize its exposure to significant losses. The Company has a catastrophe excess of loss program in place with the Parent. In the event of a catastrophe, the Company’s maximum loss is limited to its retention of \$12,000,000 in both 2004 and 2005. Additionally, the Company is reinsured by its Parent under an aggregate excess of loss contract to protect the Company from multiple events which, when combined exceed \$6,000,000 but individually are less than the \$12,000,000 retention of the catastrophe excess of loss program, this cover can additionally absorb the catastrophe retention on second events.

In connection with the sale of the Company in 2000 to Mapfre Re, the Company purchased a reinsurance contract from National Indemnity Company under which unpaid losses and loss adjustment expense reserves and unearned premium reserves as of January 1, 2000 up to \$17,000,000, ultimately the Company collected \$14,000,000 and wrote off the remaining \$3,000,000 in 2007. The contract was prospective in nature and the Company received the approval of regulatory agencies for the transaction.

The Company has the following ceding treaties that are effective as of December 31, 2005:

Adverse Loss Development Cover with National Indemnity Insurance Company - This treaty covers all the old business for the 1999 and prior underwriting years. The limit is up to \$56,560,000 after the Company retains \$17,500,000. The contract was terminated in 2007 through arbitration.

Whole Account Quota Share – This treaty covers all business written by the Company. The Company cedes 15% of the gross assumed liability on all policies to its Parent.

Catastrophe Excess of Loss – This treaty with the Parent covers the Company for \$113,000,000 in excess of \$12,000,000 on all property business written and retained by the Company.

Reinstatement Premium Cover – This treaty with the Parent covers reinstatement premiums incurred on the Catastrophe Excess of Loss cover mentioned above, the limit is \$20,800,000 excess of \$3,500,000.

Facultative Excess of Loss Cover with the Parent covers all facultative property business written prior to September 2004 in run-off with limits of \$4,250,000 excess \$1,000,000.

Aggregate Excess of Loss Cover with the Parent covers all property business written and retained by the Company with limits of \$18,000,000 excess of \$12,000,000.

MANAGEMENT AND CONTROL

The Company a subsidiary of Mapfre Re. was assigned an A.M. Best rating of A (Excellent) in 2005 based on the financial strength of the Company and the Mapfre Group. The Company has its own Board of Directors which numbered seven at the date of the examination. The Company has fourteen employees at its home office. The Company utilizes the services of certain affiliated companies for data center systems.

Directors

The by-laws of the Company specify that the Board will not have less than seven (7) nor more than nine (9) directors with each director elected by the shareholders at their annual meeting. The elected directors shall hold office for one year and until their successors have been duly elected and qualified. The annual meeting of the Board will be held on the third Tuesday of March. Special meetings of the Board of Directors shall be held whenever called by the President, or by the Board of Directors. Notice of Special meetings shall be given to members of the Board either personally, or by mail, at least ten days prior to the time designated for the convening of such Special meeting. At all meetings of the Board of Directors, a majority of the members of the Board of Directors shall constitute a quorum for the transaction of business.

A listing of the Directors serving at December 31, 2005 and their principal occupation follows:

<u>Name</u>	<u>Principal Occupation</u>
Robert E. Giddings	Director Retired
Javier Jose Fernandez-Cid	President, Chief Executive Officer Mapfre Reinsurance Corporation
James J. Folger	Senior Vice President Shelter Reinsurance Insurance Company
Andres Jimenez	Chairman of the Board Mapfre Reinsurance Corporation
William G. Shearn	Senior Vice President, Chief Financial Officer Ecclesiastical Insurance
Marc M. Tract	Attorney Katten Muchen Zavis Rosenman LLP

Jeremy R. Wallis

Consultant
Mapfre Reinsurance Corporation

The Board has an investment committee, which consists of the following:

Javier Jose Fernandez-Cid	President and Chief Executive Officer
John J. Lynch	Sr. Vice President, Chief Financial Officer and Treasurer
Pedro Lopez	Chief Financial Officer of the parent Mapfre Re

The Board also has an executive committee, which consists of the following:

Marc M. Tract	Secretary
Javier Jose Fernandez-Cid	President and Chief Executive Officer
Andres Jimenez	Chairman of the Board

Officers

The officers of the Company who were elected and serving at December 31, 2005 were as follows:

Javier Jose Fernandez-Cid	President and Chief Executive Officer
Marc Mitchell Tract	Secretary
John Joseph Lynch	Senior Vice President, Chief Financial Officer and Treasurer
Javier San Basillo	Senior Vice President - Corporate Development
Carlos J. Sanzo	Senior Vice President - Chief Underwriting Officer
Mariam George	Vice President and Controller

The business and affairs of the Company are managed by the President and his delegated officers under the guidance of the Board of Directors.

The President of the Company, subject to the direction of the Board, shall be the chief executive officer of the Company, shall have general charge and supervision of the responsibility for the business and affairs of the Company, shall have the direction of all other officers and employees and may assign such duties to the other officers of the Company as he deems appropriate. He shall have the general powers and duties of management usually vested in the office of the president of a company.

CONFLICT OF INTEREST

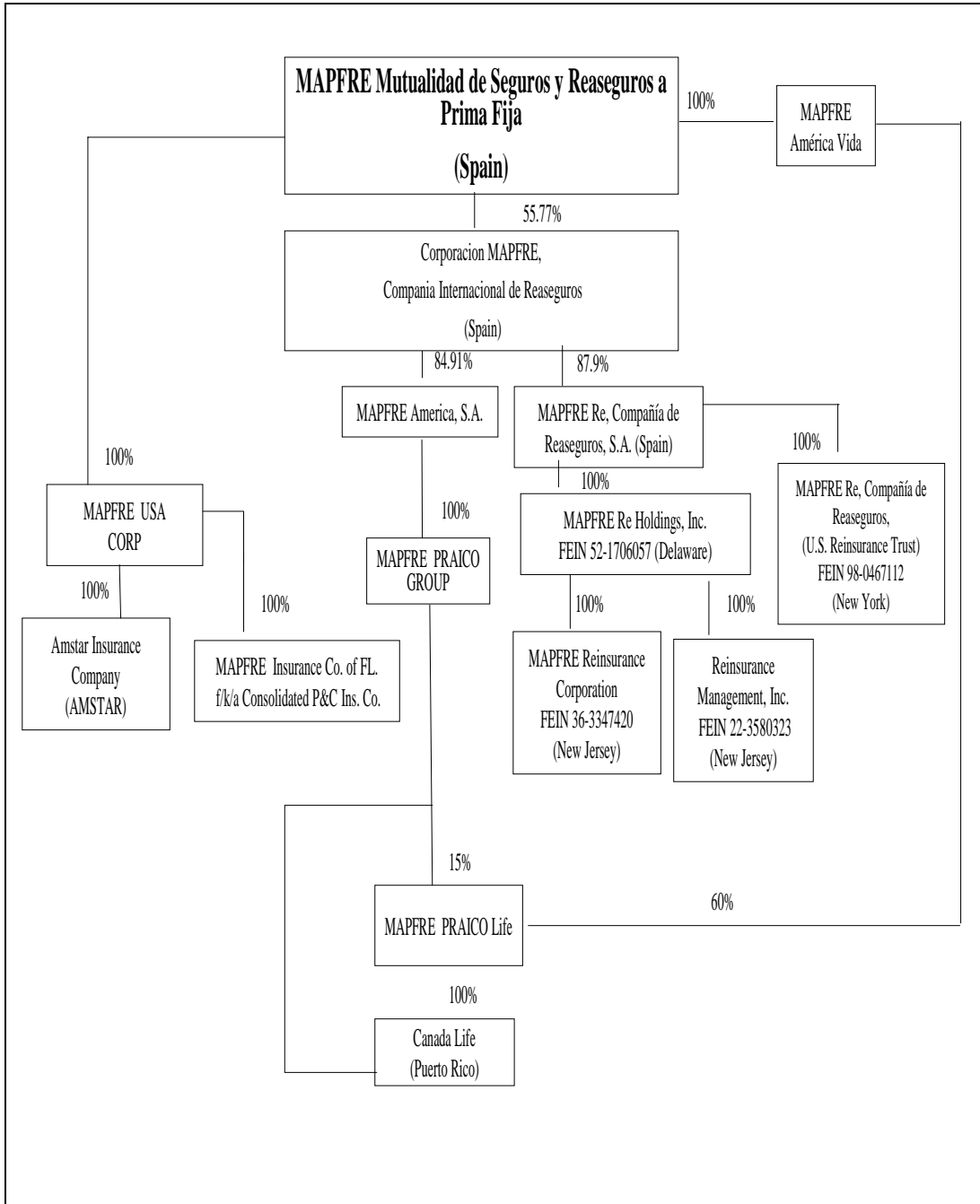
The Company completes conflict of interest questionnaires annually. A formal report is prepared by the Corporate Secretary indicating annual compliance with the Company's conflict of interest questionnaires and reports any conflicts to the Board of Directors.

PARENT, SUBSIDIARIES AND AFFILIATES

The Company is a member of an insurance holding company system as defined in N.J.S.A. 17:27A-1 and is wholly owned by Mapfre Re Holdings, Inc ("MHC") a Delaware Corporation.

Under New Jersey law, the Company files a holding company registration statement with the NJDOBI. Examination review of the holding company registration statement filed with the NJDOBI supports the representations contained in that document. In addition, the CPA work papers were reviewed to determine if they evaluated related party transactions, the risk of unusual transactions, and unrecorded transactions.

An organization chart follows which reflects the Company and its parent.



INTERCOMPANY AGREEMENTS

The Company participates in a federal income tax allocation agreement dated December 31, 2003, along with MHC and Reinsurance Management, Inc. a wholly owned subsidiary of MHC. The agreement was filed and approved by the NJDOBI. The Company and affiliates constitutes an affiliated group within section 1504(a) of the Internal Revenue Code of 1986 of which is Mapfre Holdings Inc., is the common parent and, therefore, are eligible to file a consolidated United States federal income tax return and pay federal income taxes on a consolidated basis if necessary. Federal income tax expense and benefits are allocated in the ratio that the Company's separate tax return liability or benefit bears to the sum of the separate return tax liabilities and benefits of the Mapfre Group. Estimated payments are made between members during the year.

FIDELITY BOND AND OTHER INSURANCE COVERAGES

The Company has a \$3 million Fidelity Bond, which provides fidelity coverage for all officers and employees of the Company and which is more than adequate to meet the minimum requirement of coverage as suggested by the NAIC.

The Company also has the following policies in force at December 31, 2005 to protect itself against the various perils/hazards to which it may become exposed. These policies include an automobile liability policy; a comprehensive all risk property policy designed to safeguard its building and the contents held within; a workers compensation and employers liability policy; a directors and officers liability policy to protect the Company's officers and directors from possible risks/perils, which could arise during the course of the Company's business; an umbrella policy and a travel accident policy.

ACCOUNTS AND RECORDS

The Company uses the Freedom software package to prepare the general ledger and to complete the annual statement. The general ledger system was tested and reconciled to the annual statement. Financial information needed in conjunction with the verification of assets and the determination of liabilities was made available in detail and summary form. The Company's accounting books and records are maintained at its main administrative office located at 100 Campus Drive in Florham Park, New Jersey.

The Company maintains two systems for reporting business. The RSG system maintains the old run-off business from Chatham Reinsurance Company, the system generates both premium and loss reports. The CONDOR system is where all other business is recorded; the system also generates reports which feed the general ledger and exhibits for the filed Annual Statements. The CONDOR system is administered in Spain and the Company has direct access to CONDOR through the internet.

FINANCIAL STATEMENTS AND OTHER EXHIBITS

The financial statements and other exhibits contained in this report are listed below:

- Exhibit A Balance Sheet as of December 31, 2005
- Exhibit B Summary of Operations for the Three-Year Period Ending December 31, 2005
- Exhibit C Capital and Surplus Account for the Three-Year Period Ending December 31, 2005

EXHIBIT A

MAPFRE REINSURANCE CORPORATION
BALANCE SHEET AS OF DECEMBER 31, 2005 AND DECEMBER 31, 2002

	Examination at 12/31/05	Annual Statement at 12/31/02	Increase (Decrease)
<u>Assets</u>			
Bonds	\$162,504,579	\$120,618,449	\$41,886,130
Cash and Short-Term Investments	24,938,861	8,367,444	16,571,417
Investment Income Due and Accrued	2,115,664	1,832,437	283,227
Agents' Balances or Uncollected Premiums:			
Uncollected premiums and agents' balances in the course of collection	23,151,010	15,017,704	8,133,306
Deferred premiums, agent's balances and installments booked but deferred and not yet due	4,271,828	2,824,369	1,447,459
Reinsurance			
Amounts recoverable from reinsurers	22,767,957	20,233,456	2,534,501
Funds held by or deposited with reinsured companies	1,974,309	2,449,948	(475,639)
Current federal and foreign income tax recoverable and interest thereon	1,500,000	1,670,016	(170,016)
Net deferred tax asset	3,581,091	0	3,581,091
Electronic data processing equipment and software	25,543	9,780	15,763
Aggregate Write-ins for Other than Invested Assets	329,371	145,300	184,071
Total Admitted Assets	<u>\$247,160,213</u>	<u>\$173,168,902</u>	<u>\$73,991,310</u>
<u>Liabilities</u>			
Losses	\$36,824,694	\$9,908,291	\$21,309,403
Reinsurance payable on paid losses and loss adjustment expenses	21,980,447	24,086,960	(\$2,106,513)
Loss adjustment expenses	8,929,170	2,674,626	6,254,544
Commissions payable, contingent commissions and other similar charges	132,901	183,544	(50,643)
Other Expenses (excluding taxes, licenses, and fees)	377,268	227,502	149,766
Taxes, Licenses and Fees	381,498	77,773	303,725
Unearned Premiums	14,053,342	6,912,302	7,141,040
Ceded Reinsurance Premiums Payable	15,875,708	13,009,678	2,866,030
Funds held by company under reinsurance treaties	279,266	4,953,162	(4,673,896)
Amounts withheld or retained by company for account of others	29,962	(1,249)	31,211
Provision for reinsurance	1,036,838	1,194,906	(158,068)
Total Liabilities	<u>\$99,901,094</u>	<u>\$63,227,497</u>	<u>\$31,066,599</u>
<u>Surplus and Other Funds</u>			
Common Capital Stock	\$4,200,000	\$4,200,000	0
Gross Paid in and Contributed Surplus	135,077,577	100,077,577	0
Unassigned Funds (Surplus)	7,981,542	5,663,828	42,924,711
Surplus as Regards Policyholders	<u>\$147,259,119</u>	<u>\$109,941,405</u>	<u>\$42,924,711</u>
Total Liabilities, Surplus and Other Funds	<u>\$247,160,213</u>	<u>\$173,168,902</u>	<u>\$73,991,310</u>

EXHIBIT B

MAPRE REINSURANCE CORPORATION
SUMMARY OF OPERATION FOR THE THREE YEAR PERIOD ENDING DECEMBER 31, 2005

	<u>2003</u>	<u>2004</u>	<u>2005</u>
<u>UNDERWRITING INCOME</u>			
Premiums Earned	<u>\$51,531,314</u>	<u>\$70,407,110</u>	<u>\$61,181,689</u>
Deductions:			
Losses Incurred	\$33,251,918	\$50,680,885	\$43,720,578
Loss Expenses Incurred	3,155,643	4,132,132	10,691,896
Other Underwriting Expenses Incurred	<u>14,019,775</u>	<u>22,257,100</u>	<u>20,715,758</u>
Total Deductions	<u>\$50,427,336</u>	<u>\$77,070,117</u>	<u>\$75,128,232</u>
Net Underwriting gain or (Loss)	<u>\$1,103,978</u>	<u>(\$6,663,007)</u>	<u>(\$13,946,543)</u>
<u>INVESTMENT INCOME</u>			
Net Investment Income Earned	\$4,955,553	\$5,875,651	\$7,072,257
Net Realized Capital Gains or (-) Losses	<u>2,414,727</u>	<u>45,789</u>	<u>(158,061)</u>
Net Investment Gain	<u>\$7,370,279</u>	<u>\$5,921,440</u>	<u>\$6,914,196</u>
<u>OTHER INCOME</u>			
Aggregate write-in for miscellaneous income	\$140,161	(\$224,273)	\$152,679
Net Income Before Federal and Foreign Income Taxes	\$8,614,418	(\$965,840)	(\$6,879,668)
Dividends to policyholders	\$0	\$0	\$0
Federal and Foreign Income Taxes Incurred	<u>2,550,477</u>	<u>0</u>	<u>(409,769)</u>
Net Income	<u>\$6,063,941</u>	<u>(\$965,840)</u>	<u>(\$6,469,899)</u>

EXHIBIT C

MAPFRE REINSURANCE CORPORATION
CAPITAL AND SURPLUS ACCOUNT FOR THE THREE YEAR PERIOD
ENDED DECEMBER 31, 2005

	<u>2003</u>	<u>2004</u>	<u>2005</u>
Net Income	\$6,063,941	(\$965,840)	(\$6,469,899)
<u>OTHER SURPLUS GAINS OR (LOSSES)</u>			
Change in net unrealized capital gains or (losses)	(303,115)	0	0
Change in net realized foreign exchange capital gains (losses)	99,394	1,243,833	549,629
Change in Net Deferred Income Tax	(516,996)	315,910	3,747,485
Change in Non Admitted Assets	397,923	439,605	(2,442,226)
Change in Provision for Reinsurance	(144,738)	(292,644)	595,450
Paid in surplus	<u>15,000,000</u>	<u>20,000,000</u>	<u>0</u>
Total Other Surplus Gains or (-) Losses	14,835,583	21,706,704	2,450,338
Change In Surplus as Regards Policyholders for the Year	<u>\$20,596,409</u>	<u>\$20,740,864</u>	<u>(\$4,019,560)</u>
Surplus as Regards Policyholders			
December 31, Previous Year	<u>\$109,941,406</u>	<u>\$130,537,815</u>	<u>\$151,278,679</u>
Surplus as Regards Policyholders			
December 31, Current Year	<u>\$130,537,815</u>	<u>\$151,278,679</u>	<u>\$147,259,119</u>

NOTES TO THE FINANCIAL STATEMENTS

Note 1

Losses and loss adjustment expenses

\$36,824,694

The NJDOBI completed a comprehensive review of the Company's loss and loss adjustment expense reserves and determined that the Company's gross reserves were deficient by \$16.2 million which were within the reasonable range of estimates. The deficiency is mostly due to hurricane Katrina losses. The Company reported net reserves were found to be \$9.5 million redundant and were also within the range of estimates.

The materiality established for this examination was \$7.5 million. The business produced by the Company produces a much wider range of reasonable estimates, through discussion with the NJDOBI actuaries it was agreed both the gross and net reserves booked by the Company would be acceptable for examination purposes, therefore no examination adjustment was reflected in this examination report.

As part of the review of the above mentioned reserves, the examination verified the data concerning case reserves and losses paid to Company actuarial reports and to Schedule P by line of business and by accident year. A haphazard sample of claims were selected and traced/agreed to actual claim files to verify underlying claim attributes. The test work performed yielded no material exceptions or problems.

SUBSEQUENT EVENTS

On June 30, 2006 the Company entered into an Assumption and Assignment Reinsurance Agreement with its Parent, Mapfre Re. Under this agreement the Company's loss and premium reserves on all US business, for the 2000 through 2005 underwriting years were transferred to the Parent. The NJDOBI approved this transaction on July 12, 2006.

On September 1, 2006 the Company filed a Form D with the NJDOBI to permit the Company to make an extraordinary distribution of capital in the amount of \$111,965,715 to its Parent. The NJDOBI approved the transaction on September 27, 2006.

Additionally on December 31, 2006 the Company entered into a second Assumption and Assignment Reinsurance Agreement with its Parent, whereby the Company's loss and premium reserves on all Canadian business, for the 2000 through 2005 underwriting years were also transferred to the Parent. On December 28, 2006 the Office of the Superintendent of Financial Institutions (OSFI) approved the transaction.

Therefore as of December 31, 2006 the only reserves remaining on the Company's books are the run-off reserves of the predecessor company Chatham Reinsurance Corporation.

On March 26, 2007 the Company filed a business plan with NJDOBI as a precursor to a Form D filing with the following points of emphasis noted:

- 1) Further reduce capital and surplus to \$25 million from filed 2006 Annual Statement amount of \$47 million, a request to transfer \$22 million back to its Parent.
- 2) The Mapfre Group has reconsidered its earlier decision to license the Company in Florida as a direct insurer and re-domesticate the Company to Florida and will retain the Company's status as a New Jersey insurer.
- 3) Transfer the ownership of the Company to Mapfre USA Corp. in 2007.

