STATE OF NEW JERSEY
DEPARTMENT OF BANKING AND INSURANCE

IN THE MATTER OF THE ACQUISITION OF CONTROL OF 21ST CENTURY AUTO INSURANCE COMPANY OF NEW JERSEY, BY AMBAC FINANCIAL GROUP, INC. AND EVERSPAN INSURANCE COMPANY	)))))	HEARING OFFICER'S REPORT

Procedural History

In accordance with N.J.S.A. 17:27A-2, by a filing dated June 4, 2021 and by an amended filing dated December 10, 2021, Ambac Financial Group, Inc. ("AFG") and Everspan Insurance Company ("EIC") (Collectively, "the Applicants"), filed with the Department of Banking and Insurance ("the Department") an application to acquire control ("the Form A filing") of 21st Century Auto Insurance Company of New Jersey ("the Company" or "21st Century Auto"). EIC is an Arizona stock insurance company. EIC is a direct, wholly-owned subsidiary of Everspan Indemnity Insurance Company ("EIIC"), which is a direct, wholly-owned subsidiary of Everspan Holdings, LLC ("Holdings"), which is a direct, wholly-owned subsidiary of AFG, the ultimate controlling person of the EIC. AFG is a publicly traded financial services holding company incorporated in the State of Delaware and headquartered in New York City.

This transaction is part of an agreement whereby EIC will acquire all the issued and outstanding common stock of 21st Century Auto.

Pursuant to N.J.S.A. 17:27A-2(d), a public hearing was held on the Form A filing on December 27, 2021. Pursuant to N.J.A.C. 11:1-35.6(g), the public hearing was conducted based on the documents filed. The hearing panel and Department staff determined that the documents filed in connection with the proposed acquisition satisfied the requirements of N.J.S.A. 17:27A-2(b). Public comments were allowed to be submitted through the close of business on December

27, 2021. No comments were received. No other documents were required, and the record was closed on December 27, 2021.

Findings of Fact

The Company was incorporated on December 12, 1994 and commenced business in New Jersey on January 23, 1995. 21st Century Auto is a wholly owned subsidiary of 21st Century Centennial Insurance Company ("21st Centennial"), which is wholly owned by Mid-Century Insurance Company. Mid-Century Insurance Company is 80% owned by Farmers Insurance Exchange, 10% owned by Fire Insurance Exchange, and 10% owned by Truck Insurance Exchange. The focus of the Company will be to write a diversified, casualty-focused underwriting portfolio, accessed through a program business model utilizing managing general agents and third-party administrators for claims adjustment and processing. 21st Century Auto has not written any direct written premiums over the past five years.

EIC is an admitted carrier domiciled in Arizona and is a wholly-owned subsidiary of EIIC, which is a wholly-owned subsidiary of Holdings which is in turn a direct, wholly-owned subsidiary of AFG, and together with EIC, EIIC and Holdings, (the "Everspan Group"). AFG is a publicly traded financial services holding company (NYSE: AMBC) incorporated in the State of Delaware and headquartered in New York City.

EIC proposes to acquire control of 21st Century Auto pursuant to a Stock Purchase Agreement, dated April 23, 2021, by and between 21st Centennial and EIC (the "Stock Purchase Agreement"). Under the Stock Purchase Agreement, EIC will acquire all the issued and outstanding common stock of 21st Century Auto. Upon approval of the transaction, 21st Century Auto will be renamed Heartwood Insurance Company.

As of December 31, 2020, BlackRock, Inc. ("BlackRock") owned 6,306,239 shares of common stock of AFG, or approximately 13.8% of all outstanding shares of common stock of AFG.[1]

As of May 12, 2021, The Vanguard Group ("Vanguard") owned 4,660,194 shares of common stock of AFG, or approximately 10.1% of all outstanding shares of common stock of AFG.[2]

As consideration for the purchase of the shares of 21st Century Auto, EIC will pay to 21st Centennial an aggregate amount equal to the capital and surplus of 21st Century Auto as of the closing date, plus $112,000 per license of 21st Century Auto. The total consideration of approximately $6.7 million will be contributed by AFG as a surplus contribution to Holdings which will in turn make a surplus contribution to EIC to pay cash to 21st Centennial for the purchase price. No part of the consideration used to acquire control has been borrowed.

Following the acquisition of control, EIC will elect a new slate of directors to the board of 21st Century Auto, who will in turn elect executive officers to manage day-to-day business operations.

21st Century Auto will join the following intercompany agreements: (1) certain Tax Sharing Agreement under which 21st Century Auto will be included in AFG's consolidated Federal income tax return; (2) certain Expense Sharing and Cost Allocation Agreement under which 21st Century Auto will participate in the allocation of costs and expenses of AFG and its

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[1] On July 26, 2021, Blackrock requested a Disclaimer of Affiliation ("Disclaimer") in relation to Ambac Financial Group Inc. and 21st Century Auto Insurance Company of New Jersey pursuant to N.J.S.A. 17:27A-3(j) and N.J.A.C. 11:1-35.9. The Disclaimer was conditionally granted and will be effective upon an Order approving the proposed acquisition.

[2] On July 20, 2021, Vanguard requested a Disclaimer of Affiliation ("Disclaimer") in relation to Ambac Financial Group Inc. and 21st Century Auto Insurance Company of New Jersey pursuant to N.J.S.A. 17:27A-3(j) and N.J.A.C. 11:1-35.9. The Disclaimer was conditionally granted and will be effective upon an Order approving the proposed acquisition.

other subsidiaries; and (3) certain Reinsurance Pooling Agreement under which 21st Century Auto will join a pool of other entities affiliated with EIC for the purpose of insuring and reinsuring all business written by or on behalf of each of them.

Pursuant to Section 6.9 of the Stock Purchase Agreement, EIC is required to change the name of 21st Century Auto following the closing of the transaction. The Applicants have reserved and intend to change the Company's name to Heartwood Insurance Company following the closing of the Stock Purchase Agreement.

EIC will acquire 42,000 shares of the common stock of 21st Century Auto, which amounts to all the issued and outstanding common stock of 21st Century Auto.

The Applicants stated that this acquisition will complement AFG's efforts to build a presence in the specialty property and casualty market to transform what has historically been known as a bond insurer into a financial services holding company.

EIC has purchased two other insurers within the 21st Century group. The pricing terms have been the same for each transaction with a consideration of $112,000 per license held by the domestic insurer and its surplus at the time of closing.

AFG had total assets of approximately $13.22 billion in 2020; $13.32 billion in 2019 and $14.6 billion in 2018. AFG had stockholder equity of approximately $1.14 billion in 2020; $1.54 billion in 2019 and $1.63 billion in 2018. AFG had a negative net income of approximately $437 million in 2020; a negative net income of $216 million in 2019; and a positive net income of $186 million in 2018.

Analysis

N.J.S.A. 17:27A-2(d)(1) provides that the Commissioner shall approve an acquisition of control of a domestic insurer unless he or she finds that one or more of the seven disqualifying factors set forth therein exist. The statute provides in pertinent part:

> (1) The Commissioner shall approve any merger or other acquisition of control … unless, after a public departmental hearing thereon, he [or she] finds that:
>
> (i) After the change of control the domestic insurer … would not be able to satisfy the requirements for the issuance of a license to write the line or lines of insurance for which it is presently licensed;
>
> (ii) The effect of the merger or other acquisition of control would be substantially to lessen competition in insurance in this State or tend to create a monopoly therein … [applying the competitive standard as set forth in the statute];
>
> (iii) The financial condition of any acquiring party is such as might jeopardize the financial stability of the insurer, or prejudice the interest of its policyholders;
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> (iv) The financial condition of any acquiring party is such that (a) the acquiring party has not been financially solvent on a generally accepted accounting principles basis, or if an insurer, on a statutory accounting basis, for the most recent three fiscal years immediately prior to the date of the proposed acquisition (or for the whole of such lesser period as such acquiring party and any predecessors thereof shall have been in existence); (b) the acquiring party has not generated net before-tax profits from its normal business operations for the latest two fiscal years immediately prior to the date of acquisition (or for the whole of such lesser period as such acquiring party and any predecessors thereof shall have been in existence); or (c) the acquisition debt of the acquiring party exceeds 50% of the purchase price of the insurer;
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> (v) The plans or proposals which the acquiring party has to liquidate the insurer, sell its assets or consolidate or merge it with any person, or to make any other material change in its business or corporate structure or management, are unfair and unreasonable to policyholders of the insurer and not in the public interest;
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> (vi) The competence, experience and integrity of those persons who would control the operation of the insurer are such that it would not be in the interest of policyholders of the insurer and of the public to permit the merger or other acquisition of control; or

(vii) The acquisition is likely to be hazardous or prejudicial to the insurance buying public.

Upon a thorough review of the documents submitted into evidence, the hearing panel and Department staff have determined that none of the seven disqualifying factors set forth above should result if the proposed acquisition is effectuated. Each of these conditions is discussed below.

First, after the acquisition, 21st Century Auto will continue to meet the requirements to transact the business for which it is presently licensed pursuant to Title 17 of the New Jersey Statutes. It was incorporated on December 12, 1994, commenced business in New Jersey on January 23, 1995, and is currently licensed in good standing. There is nothing in the record to indicate that after the proposed transaction, the Company would not be able to continue to satisfy the requirements to transact the business for which they are presently licensed.

Second, it does not appear that the proposed transaction will substantially lessen competition in the New Jersey insurance market or tend to create a monopoly therein. N.J.S.A. 17:27A-2(d)(1)(ii) provides that in applying this competitive standard, the standard set forth in N.J.S.A. 17:27A-4.1(d) shall apply. That statute utilizes a complex formula based on the market shares of the insurers involved in the transaction. The statute by its terms does not apply if, as an immediate result of the acquisition, there would be no increase in the overall market share of the involved insurers after the acquisition. In all lines of business, the transaction meets these exemption standards because EIC and the Company do not compete in any lines of business. Accordingly, the proposed transaction will not violate the competitive standard set forth in N.J.S.A. 17:27A-4.1 because it does not substantially lessen competition in New Jersey or tend to create a monopoly therein.

Third, it does not appear that the financial condition of the Applicants will jeopardize the financial condition of the New Jersey domestic insurer. For the last three years, EIC has had positive net income. AFG has not experienced positive net income over the past three years preceding the proposed transaction. AFG has had substantial shareholder's equity for the three-year period immediately preceding the proposed acquisition. Further, no part of the consideration used to acquire control has been borrowed.

Fourth, it appears that the financial condition of EIC is such that it has been solvent on a basis of generally accepted accounting principles ("GAAP") for the three-year period immediately prior to the date of the proposed acquisition as it reported substantial shareholders equity for that period. Additionally, EIC reported a net income, after taxes, of $9.2 million in 2020, $6.7 million in 2019, and $4.6 million in 2018. EIC reported a surplus of $10.8 million in 2020, $245.7 million in 2019, an $239.1 million in 2018. EIC reported a surplus of $51.6 million as of September 30, 2021, which is more than adequate to cover 100% of the total consideration of $6.7 million. As such, the transaction will satisfy the requirements of N.J.S.A. 17:27A-2(d)(1)(iv)(c). It should be noted that AFG has not experienced positive net income over the three years preceding the proposed transaction. The Applicants have stated that on a consolidated GAAP basis, AFG produced net losses in both 2019 and 2020. However, on an operating basis, measured by Adjusted earnings (a non-GAAP measure), AFG incurred a loss only in 2020. The 2020 operating loss was driven by a number of factors, including (i) higher incurred losses related to an affiliate's exposure to Puerto Rico, (ii) lower interest/discount rates, which increased the present value of loss reserves, (iii) volatility in investment results as a fall out from the impact of COVID on the capital markets, (iv) incremental loss reserves and credit adjustments on COVID exposed credits and counterparties and (iv) the impact of lower interest rates on interest rate hedge positions. However, EIC has experienced positive net income over that period.

Fifth, the Applicants do not propose to declare an extraordinary dividend, liquidate the Company, or sell its assets. As set forth above, the Applicants do not intend to change the business operations, corporate structure, or general plan of operations other than may arise in the ordinary course of business. The Applicants stated that following the acquisition of control, EIC will elect a new slate of Directors to the Board of the Domestic Insurer. In addition, as noted above, the Applicants stated that they intend to change the name of the Company after the closing of the transaction.

Sixth, there is nothing in the record from which it may be concluded that the competence, experience, and integrity of the persons who will control the operations of the Company are such that it would not be in the interest of the policyholders and of the public to permit the acquisition of control. Following the transaction, the Applicants will attain ultimate control of the Company. Following the transaction, the Applicants intend to maintain the Company's business operations and corporate structure.

Seventh, there is nothing in the record from which it may be concluded that the proposed transaction is likely to be hazardous or prejudicial to the insurance buying public for the reasons set forth above.

Recommendation

Based on the foregoing analysis, the hearing panel and Department staff recommend that the proposed acquisition of 21st Century Auto by the Applicants be approved.

Upon a thorough review of the foregoing, I concur with the findings, analysis and recommendations of the hearing panel and Department staff. I therefore recommend that the proposed acquisition be approved.

12/28/2021 Date

/s/ Michelle Mire
Michelle Mire
Hearing Officer

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Exhibits List

In the Matter of the Acquisition of Control of 21st Century Auto Insurance Company of New Jersey ("Domestic Insurer") by Everspan Insurance Company and Ambac Financial Group, Inc. ("Applicants").

Exhibit 1 – Form A Statement dated June 4, 2021

Exhibit 2 – Amended Exhibit III received on November 9, 2021

Exhibit 3 – Amended Form A Statement and related filings received on December 10, 2021

Exhibit 4 – Waiver of 20–day notice of hearing submitted Victoria L. McCarthy, Head of Regulatory Strategy & Analytics, Farmers Insurance for the Domestic Insurer.

Exhibit 5 – Waiver of 20–day notice of hearing submitted by Nicholas Scott, Esq. for the Applicants.

Exhibit 6 – Affidavit of Publication of Notice of Hearing in The Record, reflecting publication on December 17, 2021

Exhibit 7 – Affidavit of Publication of Notice of Hearing in Courier Post, reflecting publication on December 17, 2021

Exhibit 8 – Affidavit of Publication of Notice of Hearing in Star Ledger, reflecting publication on December 17, 2021