

CASTLEPOINT NATIONAL INSURANCE COMPANY, in liquidation

**Selected Financial Information and Analysis
September 30, 2018**

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(Unaudited)

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Overview

CastlePoint National Insurance Company (CNIC or the Company) is the surviving entity from a merger with Tower Insurance Company of New York, CastlePoint Insurance Company, Hermitage Insurance Company, Massachusetts Homeland Insurance Company, North East Insurance Company, Preserver Insurance Company, Tower National Insurance Company, York Insurance Company of Maine and CastlePoint Florida Insurance Company (pre-merger affiliates). The merger agreement was structured so that CNIC will have responsibility for all of Tower's direct insurance business. CNIC and the pre-merger affiliates (except for CastlePoint Florida Insurance Company) were members of Tower's US Pool. Subsequent to the completion of the merger, on July 28, 2016, CNIC was placed into conservation by the Superior Court of the State of California and subject to the oversight of the California Insurance Commissioner. The Company is owned by Tower Group, Inc., which in turn is owned by Tower Group International Ltd. (Tower). Tower was acquired by ACP Re, Ltd. (ACPRE) on September 15, 2014 and was contributed to a special purpose trust formed in Bermuda in September 2016 as more fully described below.

Pursuant to the July 28, 2016 Order Appointing Insurance Commissioner as Conservator and Restraining Orders (the Conservation Order), the California Insurance Commissioner was appointed as the statutory Conservator of the Company. The Commissioner also filed a Conservation and Liquidation Plan for the Company which was approved September 13, 2016. As part of the Conservation and Liquidation Plan, ACP Re commuted its aggregate stop loss reinsurance retrocession agreement with two affiliated companies who in turn provided aggregate stop loss reinsurance protection to CastlePoint Reinsurance Company (CPre), (a Bermuda reinsurance company that was an affiliate of CNIC) and those companies' aggregate stop loss to CPre were also cancelled, terminated and commuted. Concurrent with the execution of these agreements, CPre commuted all of its reinsurance agreements with CNIC and the pre-merged companies, with consideration to CNIC being all of net tangible assets of CPre, such that after the commutation CPre has no further obligation to CNIC. Finally, CNIC received a cash payment of \$200 million from the owners of ACPRe in exchange for their agreement to the commutation agreements. CNIC used these funds to pay losses and other expenses of the estate while in conservation. Finally, pursuant to the Conservation and Liquidation Plan, ACP Re transferred its ownership interest in the stock of all of the remaining Tower companies to a purpose trust formed in Bermuda and as of September 2016 has no control over CNIC or ownership of any other of the Tower companies.

In accordance with the Conservation and Liquidation Plan, two Administrative Services Agreements were executed with AmTrust Financial Services Inc. and with National General Holdings Company for the continuity of claims servicing and payment processing for a period of 24 months. Such agreements were modified and extended to terminate on June 30, 2019.

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On March 30, 2017, the Superior Court of the State of California issued a Liquidation Order (the Order), effective April 1, 2017, for the Company. The Order directs the Liquidator to liquidate and wind up the business of CastlePoint and to act in all ways and exercise all powers necessary for the purpose of carrying out this Order and the Liquidation provision of the California Insurance Co, Insurance Sections 1010 et seq. On April 1, 2017 all direct claims of CastlePoint (and the merged entities) that arose under policies of insurance that are protected by State Guaranty Funds were transferred to the State Guaranty Funds that have jurisdiction over the claims. All claims issued under direct policies of insurance that are not protected by State Guaranty Funds were transferred back to the insured's under the policies, and such insured's are eligible to file a proof of claim with the Liquidator. Such proofs of claim forms were mailed to insured's and all other potential creditors in the second quarter of 2017, with a final claims bar date of December 31, 2017. Proofs of claim filed by those direct insured's without Guaranty Fund protection and approved by the Liquidator will receive the same creditor classification as those claims filed by the State Guaranty Funds.

Other creditors, including claims that arose from policies of reinsurance issued by the Company are subordinated to the claims of the Guaranty Funds and the direct claims of insured's not protected by Guaranty Funds.

The accompanying balance sheets are presented as of September 30, 2018 and December 31, 2017. The statement of operations and statement of cash flows are presented for the nine-month period ended September 30, 2018 and 2017.

The Liquidator continues to investigate the account balances contained within this statement and will adjust the balances as more information becomes available.

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Statutory Balance Sheets
(Unaudited)

(\$ in thousands)	September 30, 2018	December 31, 2017	Increase (Decrease)
Admitted Assets			
Cash and invested assets			
Unrestricted assets	\$ 160,736	\$ 143,181	\$ 17,555
Restricted assets			
Pledged to states	96,241	97,747	(1,506)
Pledged for reinsurance	69,910	78,052	(8,142)
Funds at Lloyds and other invested assets	1,355	1,538	(183)
Total restricted assets	167,506	177,337	(9,831)
Total cash and invested assets	328,242	320,518	7,724
Investment income due and accrued	1,895	2,108	(213)
Amounts recoverable from reinsurers	5,765	4,450	1,315
Funds held by or deposited with reinsured companies	14	772	(758)
Advances to Insurance Guarantee Associations	230,620	227,576	3,044
Miscellaneous assets	15,682	29,351	(13,669)
Total admitted assets	\$ 582,218	\$ 584,775	\$ (2,557)
Liabilities, capital and surplus			
Liabilities			
Reserve for losses and loss adjustment expenses	\$ 745,514	\$ 811,287	\$ (65,773)
Reinsurance payable on paid losses and LAE	13,409	9,131	4,278
Ceded reinsurance premiums payable	(476)	(358)	(118)
Funds held by company under reinsurance treaties	16,604	18,434	(1,830)
Payable to Guaranty Funds	75,495	6,112	69,383
Miscellaneous liabilities	20,494	24,069	(3,575)
Total liabilities	871,040	868,675	2,365
Capital and surplus			
Common capital stock	4,200	4,200	-
Gross paid in and contributed surplus	524,741	524,742	(1)
Unassigned deficit	(817,763)	(813,153)	(4,610)
Special surplus funds from retroactive reinsurance	-	311	(311)
Total capital and surplus	(288,822)	(283,900)	(4,922)
Total liabilities, capital and surplus	\$ 582,218	\$ 584,775	\$ (2,557)

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Notes to Statutory Balance Sheets

Assets

Total cash and invested assets were \$328.2 million at September 30, 2018 compared to \$320.5 million at December 31, 2017. All investment amounts are carried at market, which the Liquidator believes represents realizable value. The increase in cash and invested assets is due to the sale of CPRe in 2018 for \$7.9 million (see more information on this in the discussion on other assets, below) and to collections of reinsurance and investment income that have outpaced the cash expenses incurred in managing the liquidation for the nine-month period ended September 30, 2018.

Investment income due and accrued decreased by \$0.2 million, to \$1.9 million at September 30, 2018 as compared to \$2.1 million at December 31, 2017.

Reinsurance recoverable was \$5.8 million at September 30, 2018, compared to \$4.5 million at December 31, 2017. None of these balances are currently in dispute, but one reinsurer is not current with their payments. Reinsurance contracts do not relieve CNIC from its obligations to policyholders. Failure of reinsurers to honor their obligations could result in losses to CNIC.

Funds held by or deposited with reinsured companies were \$0.01 million at September 30, 2018 and \$0.8 million at December 31, 2017.

Advances to Insurance Guarantee Associations represent funds transferred by the Company to certain of the state insurance guarantee associations in accordance with the laws of such states. Such amounts are considered early access distributions.

Miscellaneous Assets (Unaudited)

(\$ in thousands)	September 30, 2018	December 31, 2017	Increase (Decrease)
Tangible value of CPRe due to Estate	\$ -	\$ 8,400	\$ (8,400)
Involuntary fair plan assumed	9,719	9,719	-
Workers' compensation fund assessment	2,203	5,741	(3,538)
Receivable from residual market pools	1,122	3,209	(2,087)
Other	2,638	2,282	356
Total	\$ 15,682	\$ 29,351	\$ (13,669)

Miscellaneous assets were \$15.7 million at September 30, 2018 compared to \$29.4 million at December 31, 2017. The amounts receivable from CPRe represent CPRe's net tangible assets due to CNIC under the terms of the commutation agreement with CPRe. CNIC sold its rights to receive the tangible value of CPRe to a third party, and this sale closed during the third quarter 2018 with CNIC receiving \$7.9 million in proceeds. Involuntary fair plan assumed assets represent balances that may be returned to CNIC from

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various state involuntary pools. CNIC is no longer an active participant in the pools. Workers' compensation fund assessments represent amounts due from funds, it is expected that the company will receive a portion of these funds in 2018 and the remainder of these funds in 2019. Included in other assets are \$2.2 million at September 30, 2018 and December 31, 2017 representing funds held for the benefit of CNIC by State National Insurance Company under an old reinsurance agreement.

Liabilities

The Company's net loss and LAE reserves were \$745.5 million at September 30, 2018 compared to \$811.3 million at December 31, 2017. The balances represent the net reserves transferred to the State Insurance Guarantee Associations for all claims valued as of March 31, 2017, the date the Company went into liquidation, reduced by payment data reported by the insurance guarantee associations and payments made by the Liquidator, primarily for LAE and for certain workers' comp indemnity benefits. The Company received March 2018 data from the guarantee funds in the third quarter of 2018. The Company expects to receive information from all of the guarantee associations on a lagged basis and will disclose in its financial statements the period for which it has received guarantee fund payment information. Further, the Company will also receive additional information on claims that are not covered by Guarantee Associations, and such amounts will likely increase the Company's ultimate obligation to policyholders.

Reinsurance payable on paid losses and LAE were \$13.4 million at September 30, 2018 and \$9.1 million at December 31, 2017. Under the Conservation and Liquidation Plan, the Company is no longer making payments on assumed business and is only permitting its cedants to draw down any available collateral against their balances.

Ceded reinsurance premiums payable were (\$0.5) million at September 30, 2018 and (\$0.3) million at December 31, 2017.

Funds held by the Company were \$16.6 million at September 30, 2018 and \$18.4 million at December 31, 2017. The decrease of \$1.8 million is primarily due to losses paid on a quota share treaty. Such payments were made from ceding companies drawing down available collateral against their balances.

The Company had no balances payable to parent and affiliates at September 30, 2018 and at December 31, 2017.

Payable to Guaranty funds of \$75.5 million at September 30, 2018 and \$6.1 million at December 31, 2017 represents claim payments made by various state insurance guaranty funds to claimants under policies issued by CastlePoint. The Company has recorded losses paid through March 2018 by the state insurance guaranty funds at September 30, 2018.

Miscellaneous liabilities were \$20.5 million at September 30, 2018 and \$24.1 million at December 31, 2017. Included in this balance are outstanding checks of \$15.6 million at September 30, 2018 and \$16.9 million December 31, 2017.

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Notes to Statutory Balance Sheets, continued

Capital and Surplus Accounts

The following table sets forth the changes in policyholders' surplus for the nine months ended September 30, 2018 and 2017:

**Changes in Policyholders' Surplus
(Unaudited)**

(\$ in thousands)	Nine months ended September 30, 2018	Nine months ended September 30, 2017
Policyholders' surplus, beginning period	\$ (283,900)	\$ (281,909)
Net income (loss)	(1,066)	4,701
Change in net unrealized capital gains	(5,382)	1,425
Change in non-admitted assets	-	(391)
Change in provision for reinsurance	1,526	-
Aggregate write-ins for gains and losses in surplus	-	471
Policyholders' surplus, ending period	\$ (288,822)	\$ (275,703)

Surplus decreased by \$4.9 million from year end 2017 as bond market values have decreased due to rising interest rates. The Company had a loss through the nine months ended September 30, 2018, largely due to realized capital losses associated with writing down a private placement bond to realizable value (\$3.3 million).

**Changes in Non-Admitted Assets
(Unaudited)**

(\$ in thousands)	Nine months ended September 30, 2018	Nine months ended September 30, 2017
Premium receivable	\$ -	\$ (850)
Other assets	-	459
Total change in non-admitted assets	\$ -	\$ (391)

Since the Company was placed into liquidation, there has been an elimination of the remaining agent balances. In the first quarter of 2017, the Company reversed the TPA advance allowance, as such advances were returned upon transfer of the claims to state guarantee associations.

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Statements of Operations

(Unaudited)

(\$ in thousands)	Nine months ended September 30, 2018	Nine months ended September 30, 2017
Premium earned	\$ -	\$ (168)
Losses incurred and loss adjustment expenses incurred	-	430
Other underwriting expenses incurred	4,398	6,210
Net underwriting loss	(4,398)	(6,808)
Net investment income earned	9,544	8,452
Net realized capital gain (loss)	(5,972)	2,774
Net investment gain	3,572	11,226
Other income (loss)	(240)	283
Net income (loss)	\$ (1,066)	\$ 4,701

Notes to Statements of Operations

Other underwriting expenses

Other underwriting expenses for the nine months ended September 30, 2018 and 2017 were \$4.4 million and \$6.2 million respectively. The expenses incurred in the first quarter 2017 were prior to the Company being placed into liquidation. The table below details charges by components.

Other Underwriting Expenses

(Unaudited)

(\$ in thousands)	Nine months ended September 30, 2018	Nine months ended September 30, 2017
Commission and BB&A	\$ -	\$ 1,578
Salaries and employee benefits	1,376	2,358
Rent & depreciation	121	15
Professional services	2,866	3,450
Other expense (income)	35	(1,191)
Total	\$ 4,398	\$ 6,210

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Notes to Statements of Operations, continued

Since the Company has been in liquidation, no further commissions or BB&T are being incurred. The charge for the first quarter 2017 was primarily associated with \$2.0 million of sliding scale ceded commission for the Company's reinsurance covers recorded during the three months ended March 31, 2017. The decrease in salaries and employee benefits since liquidation were due to the reduction in the employee head count. Professional services were lower in 2018, as the Company was incurring fees to prepare for the liquidation in the first quarter 2017. Other (income) expense in 2017 was comprised of various state premium tax refunds and returns of assessments which were not accrued when the Company was placed into conservation.

Net investment income and net realized capital gains (losses)

Net investment income earned was \$9.5 million and \$8.5 million for the nine months ended September 30, 2018 and 2017, respectively. Investment income includes amounts recorded from assets advanced to Insurance Guarantee Associations, and such income increases the amount advanced to the Insurance Guarantee Associations.

Net realized capital losses were \$6.0 million for the nine months ended September 30, 2018 as compared to net realized capital gain of \$2.8 million for the nine months ended September 30, 2017. Capital losses in the first quarter 2018 included a write down of a private placement bond to realizable value (\$3.3 million) and a \$0.5 million charge to reduce the value of the net tangible equity of CPRe.

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Statutory Statements of Cash Flow

(Unaudited)

(\$ in thousands)	Nine months ended September 30, 2018	Nine months ended September 30, 2017
Cash from Operations		
Benefit and loss related payments	\$ 3,880	\$ (79,401)
Commission and other expenses paid	(5,078)	(16,868)
Premiums collected net of reinsurance	340	(2,973)
Net investment income	10,206	11,362
Miscellaneous income (expense)	313	(160)
Net cash provided by (used in) operations	9,661	(88,040)
Net cash provided by (used in) investments	(50,754)	(5,830)
Net cash provided by miscellaneous sources	12,910	23,919
Net change in cash and cash equivalents	(28,183)	(69,951)
Cash and cash equivalents Beginning of year	78,804	179,444
Cash and cash equivalents, end of period	\$ 50,621	\$ 109,493

Notes to Statutory Statements of Cash Flows

CNIC used cash of \$28.2 million and \$70.0 million for the nine months ended September 30, 2018 and 2017, respectively. In 2018, CNIC increased invested assets from year-end 2017, which was the most significant use of cash flow. Cash balances decreased in 2017 due to transfers of cash for early advances of indemnity benefits and the reinvestment of cash balances that were on deposit at certain states. The Company has been in liquidation effective April 1, 2017, and as such expects its future cash outflows will be limited to operating expenses and to distributions to State Guarantee Associations. The decrease in cash used in the nine months ended September 30, 2018, compared to the same period in 2017 is due to the Company paying its own claim liabilities in the first quarter 2017, prior to liquidation.

The investment assets of \$328.2 million at September 30, 2018 ties to the amount that would be included in the Company's statutory presentation of assets. A reconciliation to the accompanying balance sheet is presented below (\$000):

Bonds	\$ 276,266
Cash	50,621
Other Invested assets	1,355
Total	<u>\$ 328,242</u>