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15 SUPERIOR COURT OF THE STATE OF CALIFORNIA
16 CITY AND COUNTY OF SAN FRANCISCO – UNLIMITED JURISDICTION

17 **INSURANCE COMMISSIONER OF THE**
18 **STATE OF CALIFORNIA,**

19 Applicant,

20 v.

21 **MAJESTIC INSURANCE COMPANY, A**
22 **CALIFORNIA CORPORATION,**

23 Respondent.

Case No.

CPF-11-511261

**VERIFIED APPLICATION FOR EX
PARTE ORDER APPOINTING
CONSERVATOR [INSURANCE CODE
SECTION 1011]; MEMORANDUM OF
POINTS AND AUTHORITIES IN
SUPPORT THEREOF**

Date: April 21, 2011

Time: 11:00 a.m.

Dept.: 301

24 Applicant Insurance Commissioner of the State of California ("Commissioner"),
25 respectfully alleges the following facts:

26 1. The Commissioner is the duly elected Insurance Commissioner of the State of
27 California.

28 2. Respondent Majestic Insurance Company ("Majestic") is now and at all times
mentioned herein has been a corporation duly organized and existing under and by virtue of the
laws of the State of California, with its principal office in San Francisco, California.

3. Majestic's statutory office is located at 101 California Street, 22d Floor, San
Francisco, California 94111.

1 4. Majestic is a wholly owned subsidiary of Embarcadero Insurance Holdings, Inc.,
2 which is in turn an indirect wholly owned subsidiary of Majestic's ultimate parent, Majestic
3 Capital, Ltd., a Bermuda exempt company (formerly known as CRM Holdings, Ltd.).

4 5. At all times relevant hereto, Majestic was authorized to transact the business of
5 property and casualty insurance in California under the authority of a Certificate of Authority
6 issued by the Commissioner.

7 6. Majestic requires a Certificate of Authority from the Commissioner for the
8 transaction of its insurance business and is subject to examination by the Commissioner under the
9 provisions of Article 4, Chapter 1, Part 2, Division 1, of the Insurance Code (sections 730-738),
10 and for these reasons is one of the "persons" subject to Article 14, Chapter 1, Part 2, Division 1 of
11 the Insurance Code (sections 1010-1062).

12 7. By virtue of Insurance Code section 730, the Commissioner conducted a financial
13 examination of Majestic in accordance with the National Association of Insurance
14 Commissioner's Financial Condition Examiner's Handbook covering the period from January 1,
15 2005 through December 31, 2010.

16 8. Upon completion of the Commissioner's financial examination of Majestic for the
17 period ending December 31, 2010, it was determined that (a) Majestic's loss and loss adjustment
18 expense reserves were deficient by approximately \$40.9 million and due to the increase in
19 reserves, a premium deficiency reserve was required in the amount of \$5.5 million;
20 (b) Majestic's surplus is declining at a rate of approximately \$1.5 million per month due to
21 continued underwriting losses; (c) Majestic's net cash from operations was **negative** \$37.5
22 million for 2010, compared to **negative** \$18.7 million for 2009; (d) Majestic had unencumbered
23 invested assets of approximately \$37.2 million at December 31, 2010; (e) Majestic's expense
24 ratio was 60% of premiums earned for 2010, compared to 38% for 2009; (f) the New York State
25 Workers' Compensation Board (NY WCB) filed a lawsuit against the Company and its holding
26 company, including individual officers, for damages in excess of \$400 million. Any proposed
27 settlement with the NY WCB could negatively affect the financial condition of the Majestic; (g)
28 there are three pending lawsuits in California against Majestic and its holding company, including

1 individual officers, for damages in excess of \$34 million that could negatively affect the financial
2 condition of Majestic; and (h) Majestic's in-force premium has dropped from \$150 million at
3 December 31, 2009 to approximately \$84 million at December 31, 2010.

4 9. Based upon the foregoing financial examination and the examination adjustments
5 made to Majestic's financial statements, Majestic's Risk-Base Capital (RBC) is \$11,527,233
6 which is less than the minimum required amount for Majestic of \$18,842,438. As a result,
7 Majestic's RBC ratio causes it to fall within the Mandatory Control Level RBC per Insurance
8 Code section 739.6(b)(2), and the Commissioner finds Majestic to be in such condition that
9 pursuant to Insurance Code section 1011(d) its further transaction of business outside of
10 conservation will be hazardous to its policyholders, or its creditors, or the public and is grounds
11 for conservation under Insurance Code section 1011.

12 10. In accordance with Insurance Code section 1011, the Commissioner files this ex
13 parte application for an order appointing him as conservator of Majestic. Majestic has reached a
14 state in its business where a formal conservation is necessary and appropriate. The Commissioner
15 has made the following determinations: that Majestic is in such condition that the further
16 transaction of business by it will be, and is, hazardous to its policyholders, creditors and the
17 public, and such condition is a ground for conservation under Insurance Code section 1011(d).

18 **WHEREFORE**, the Commissioner prays that this Court issue the following orders:

19 1. Appointing the Commissioner as Conservator (hereinafter "Conservator") of
20 Majestic and directing him to conduct the business of Majestic or so much thereof as he may
21 deem appropriate; and authorizing the Conservator, in his discretion, to pay or defer payment of
22 some or all proper claims, expenses, liabilities and obligations of Majestic, in whole or in part,
23 accruing prior or subsequent to his appointment as Conservator;

24 2. Authorizing the Conservator to assume or reject, or to modify, any executory
25 contract, including without limitation, any lease, rental or utilization contract or agreement
26 (including any schedule to any such contract or agreement), and any license or other arrangement
27 for the use of computer software of business information systems, to which Majestic is a party or
28 as to which Majestic agrees to accept an assignment of such contract; directing the Conservator to

1 effect any such assumption or rejection or modification of any executory contract not later than
2 120 days of the date of the Order Appointing Conservator, unless such date is extended by
3 application to and further order of this Court; ordering that all executory contracts that are not
4 expressly assumed by the Conservator shall be deemed rejected;

5 3. Authorizing the Conservator to take possession of all of the assets of Majestic,
6 including books, records and property, both real and personal, accounts, safe deposit boxes, rights
7 of action, and all such assets as may be in the name of Majestic, wheresoever situated;

8 4. Vesting title to all property and assets of Majestic, including deposits, securities,
9 contracts, rights of actions, books, records and other assets of every type and nature, and
10 including both those presently in Majestic's possession and those which may be discovered
11 hereafter, wheresoever situated, in the Conservator or his successor in office, in his official
12 capacity as Conservator, authorizing the Conservator to deal with the same in his own name as
13 Conservator or in the name of Majestic, and enjoining all persons from interfering with
14 Conservator's possession and title thereto;

15 5. Granting the Conservator all the powers of the directors, officers and managers of
16 Majestic, whose authorities are suspended except as such powers may be redelegated by the
17 Conservator;

18 6. Authorizing the Conservator to terminate compensation and benefits arrangements
19 with employees, to enter into new compensation arrangements with employees, including
20 arrangements containing retention incentives, and authorizing the Conservator to hire employees
21 on such terms and conditions as he deems reasonable;

22 7. Except upon the express authorization of the Conservator, enjoining Majestic, its
23 officers, directors, agents and employees from transacting any of the business of Majestic,
24 whether in the State of California or elsewhere, or from disposing of, using, transferring, selling,
25 assigning, canceling, alienating, hypothecating or concealing in any manner or any way, or
26 assisting any person in any of the foregoing, of the property or assets of Majestic or property or
27 assets in the possession of Majestic, of any nature or kind, including claims or causes of action,
28 until further order of this Court and further, enjoining such persons from obstructing or interfering

1 with the Conservator's conduct of his or her duties as Conservator;

2 8. Enjoining all persons from instituting or prosecuting or maintaining any action at
3 law or suit in equity, including but not limited to actions or proceedings to compel discovery or
4 production of documents or testimony and matters in arbitration, except in matters before either
5 the California Workers Compensation Appeals Board or equivalent administrative boards or
6 organizations performing such functions in other States in which Majestic issued workers
7 compensation policies, against Majestic or against Conservator, and from attaching, executing
8 upon, redeeming of or taking any other legal proceedings against any of the property of Majestic,
9 and from doing any act interfering with the conduct of said business by the Conservator, except
10 after an order from this Court obtained after reasonable notice to the Conservator;

11 9. Directing Majestic and all officers, directors, agents and employees of Majestic to
12 deliver to, and immediately make available to, the Conservator all assets, books, records,
13 accounts, records, information, computers, tapes, discs, writings, other recordings of information,
14 equipment and other property of Majestic, wheresoever situated, in said persons custody or
15 control and further, directing the aforesaid to disclose verbally, or in writing if requested by the
16 Conservator, the exact whereabouts of the foregoing items if such items are not in the possession
17 custody or control of said persons;

18 10. Directing that all officers, directors, trustees, employees or agents of Majestic, or
19 any other person, firm, association, partnership, corporate parent, holding company, affiliate or
20 other entity in charge of any aspect of Majestic's affairs, either in whole or in part, and including
21 but not limited to banks, savings and loan associations, financial or lending institutions, brokers,
22 stock or mutual associations, or any parent, holding company, subsidiary or affiliated corporation
23 or any other representative acting in concert with Majestic, shall cooperate with the Conservator
24 in the performance of his or her duties;

25 11. Authorizing the Conservator to pay all reasonable costs of taking possession of
26 and conserving Majestic (including but not limited to Commissioner's pre-conservation costs in
27 examining Majestic's financial condition, and preparing to take possession and conserve
28 Majestic) out of the funds and assets of the Majestic;

1 12. Authorizing the Conservator to pay all reasonable costs of operating Majestic as
2 Conservator (including direct and allocated direct costs, direct and allocated general and
3 administrative costs and overhead, and all other allocated costs) out of any and all funds and
4 assets of Majestic; and if there are insufficient funds, to pay for the costs out of the Insurance
5 Fund pursuant to Insurance Code section 1035;

6 13. Directing that all funds and assets, including certificates of deposit, bank accounts,
7 and mutual fund shares of Majestic, in various financial depository institutions, including banks,
8 savings and loan associations, industrial loan companies, mutual funds or stock brokerages,
9 wheresoever situated, be vested in the Conservator and subject to withdrawal upon his order only;

10 14. Ordering all persons who maintain records for Majestic, pursuant to written
11 contract or any other agreement, to maintain such records and to deliver to the Conservator such
12 records upon his request;

13 15. Directing all agents of Majestic, and all brokers who have done business with
14 Majestic, to make all remittances of all funds collected by them or in their hands directly to the
15 Conservator;

16 16. Ordering all persons having possession of any lists of policyholders or escrow
17 holders of Majestic to deliver such lists to the Conservator; and that all persons are enjoined from
18 using any such lists or any information contained therein without the consent of the Conservator;

19 17. Authorizing the Conservator to initiate such equitable or legal actions or
20 proceedings in this or other States as may appear to him necessary to carry out his functions as
21 Conservator;

22 18. Authorizing the Conservator to appoint and employ special deputies, estate
23 officers and managers, other professionals, clerks and assistants and to give each of them such
24 power and authority as may be deemed necessary by him, and authorizing the Conservator to
25 compensate these persons from the assets of Majestic as he shall deem appropriate;

26 19. Authorizing the Conservator to divert, take possession of and secure all mail of
27 Majestic, in order to screen such mail, and to effect a change in the rights to use any and all post
28 office boxes and other mail collection facilities used by Majestic;

1 20. Directing that Majestic and its officers, directors, agents, servants, employees,
2 successors, assigns, affiliates, and other persons or entities under their control and all persons or
3 entities in concert or participation with Majestic, and each of them, shall turn over to Conservator
4 all records, documentation, charts and/or descriptive materials of all funds, assets, property
5 (owned beneficially or otherwise), and all other assets of Majestic wherever situated, and all
6 books and records of accounts, title documents and other documents in their possession or under
7 their control, which relate, directly or indirectly to assets or property owned or held by Majestic
8 or to the business or operations of Majestic;

9 21. Except with leave of court issued after a hearing in which the Conservator has
10 received reasonable notice, enjoining all persons from obtaining preferences, judgments,
11 attachments or other liens, or making any levy against Majestic or its assets or property, and from
12 executing or issuing or causing the execution or issuance of any court attachment, subpoena,
13 replevin, execution or other process for the purpose of impounding or taking possession of or
14 interfering with or creating or enforcing a lien upon any property or assets owned or in the
15 possession of Majestic or Conservator, wheresoever situated, and from doing any act interfering
16 with the conduct of said business by the Conservator;

17 22. Except with leave of court issued after a hearing in which the Conservator has
18 received reasonable notice, enjoining all persons from accelerating the due date of any obligation
19 or claimed obligation; exercising any right of set-off; taking, retaining, retaking or attempting to
20 retake possession of any real or personal property; withholding or diverting any rent or other
21 obligation; doing any act or other thing whatsoever to interfere with the possession of or
22 management by the Conservator of the property and assets, owned or controlled by Majestic or in
23 the possession of Majestic or in any way interfering with the Conservator or interfering in any
24 manner during the pendency of this proceeding with the exclusive jurisdiction of this Court over
25 Majestic;

26 23. Ordering that any and all provisions of any agreement entered into by and between
27 any third party and Majestic, including by way of illustration, but not limited to, the following
28 types of agreements (as well as any amendments, assignments, or modifications thereto);

1 financial guarantee bonds, promissory notes, loan agreements, security agreements, deeds of trust,
2 mortgages, indemnification agreements, subrogation agreements, subordination agreements,
3 pledge agreements, assignments of rents or other collateral, financial statements, letters of credit,
4 leases, insurance policies, guaranties, escrow agreements, management agreements, real estate
5 brokerage and rental agreements, servicing agreements, attorney agreements, consulting
6 agreements, easement agreements, license agreements, franchise agreements, or employment
7 contracts that provide in any manner that selection, appointment or retention of a conservator,
8 receiver or trustee by any court, or entry of any order such as hereby made, shall be deemed to be,
9 or otherwise operate as, a breach, violation, event of default, termination, event of dissolution,
10 event of acceleration, insolvency, bankruptcy, or liquidation shall be stayed, and the assertion of
11 any and all rights and remedies relating thereto shall also be stayed and barred, except as
12 otherwise ordered by this Court, and this Court shall retain jurisdiction over any cause of action
13 that has arisen or may otherwise arise under any such provision;

14 24. Authorizing the Conservator to invest Majestic's assets and funds in such a
15 manner as to him may seem suitable for the best interest of Majestic's creditors, which funds are
16 not immediately distributable to Majestic's creditors. However, no investment or reinvestment
17 shall be made exceeding the sum of \$100,000 without first obtaining permission of this Court,
18 except the Conservator may make investments or reinvestments in excess of \$100,000, but not
19 exceeding \$5,000,000 per investment or reinvestment, without prior approval if such investments
20 or reinvestments are made pursuant to the investment guidelines of the Conservator's
21 Conservation & Liquidation Office, a true and correct copy of which is attached hereto as Exhibit
22 A and incorporated herein by this reference. The Conservator shall file quarterly reports of such
23 investments or reinvestments in excess of \$100,000 with the Court, with notice to all persons on
24 the service list, such reports to be filed within 60 days of the end of each quarter;

25 25. Authorizing the Conservator to pay for his costs and fees in bringing and
26 maintaining this action, and such other actions as are necessary to carry out his functions as
27 Conservator, out of the funds and assets of Majestic;

28 26. Enjoining all persons from the waste of the assets of Majestic; and

27. For such other and further relief as may be proper or necessary.

Dated: April 18, 2011

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KRISTIAN D. WHITTEN
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1 MEMORANDUM OF POINTS AND AUTHORITIES

2

3 **AN IMMEDIATE CONSERVATION ORDER IS REQUIRED**

4 The Insurance Commissioner of the State of California is authorized by Insurance Code
5 section 1011¹ to obtain an *ex parte* order appointing him Conservator of entities regulated by him.
6 Section 1011 states in part:

7 “The superior court of the county in which the principal office of a person
8 described in Section 1010 is located shall, upon the filing by the commissioner of
9 the verified application showing any of the following conditions hereinafter
10 enumerated to exist, issue its order vesting title to all of the assets of that person,
11 wheresoever situated, in the commissioner or his or her successor in office, in his
12 official capacity as such, and direct the commissioner forthwith to take possession
13 of all of its books, records, property, real and personal, and assets, and to conduct,
14 as conservator, the business of said person, or so much thereof as to the
15 commissioner may seem appropriate, and enjoining said person and its officers,
16 directors, agents, servants, and employees from the transaction of its business or
17 disposition of its property until the further order of said court:

18 . . .

19 (d) That such person is found, after an examination, to be in such condition that its
20 further transaction of business will be hazardous to its policyholders, or creditors,
21 or to the public....”

22

23 Section 1010, *et seq.*, which authorize, *inter alia*, conservation and liquidation, provides
24 that its provisions “apply to all persons subject to examination by the commissioner or purporting
25 to do insurance business in this state . . . or from whom the commissioner’s certificate of
26 authority is required for the transaction of business . . .” (§ 1010.) The Commissioner is

27 ¹ Unless otherwise indicated, all code references shall be to the Insurance Code.

1 authorized by Section 1011 to obtain an *ex parte* order appointing him Conservator of the entities
2 which he is mandated by law to regulate. (*Garamendi v. Golden Eagle Ins. Co.* (2005) 128 Cal.
3 App. 4th 452, 463-464.) As an officer of this State, the Commissioner, as Conservator, exercises
4 the State's police power to promote the public interest and protect policyholders and creditors of
5 the insolvent insurer. (*Quackenbush v. Mission Ins. Co.* (1996) 46 Cal.App.4th 458, 465-466; *In*
6 *re Executive Life Ins. Co.* (1995) 32 Cal.App.4th 344, 356.)

7 In obtaining an *ex parte* order pursuant to Section 1011, the Commissioner need only
8 show that he has determined and found that one of the conditions enumerated exists. (*Financial*
9 *Indemnity Co. v. Superior Court* (1955) 45 Cal.2d 395, 402; *Rhode Island Ins. Co. v. Downey*
10 (1949) 95 Cal.App.2d 220, 230-231.) Under the insolvency and delinquency provisions of the
11 Insurance Code, the issuance of an order under Section 1011 is mandatory. (*Financial Indemnity*
12 *Co. v. Superior Court, supra*, 45 Cal.2d at p. 402.) The seized company may apply for and have a
13 full hearing pursuant to Section 1012 after an *ex parte* order pursuant to Section 1011 has been
14 obtained. (*Rhode Island Ins. Co. v. Downey, supra*, 95 Cal.App.2d at pp. 235-36.)

15 Section 1020 of the Insurance Code provides that the Court shall issue orders as may be
16 necessary to, among other things, prevent waste of assets, obtaining of preferences, and
17 interference with the Commissioner of the conservatorship proceeding.

18 Here, after adjusting Majestic' loss and loss adjustment expense reserve deficiencies of
19 \$40.9 million and premium reserve deficiency of \$5.5 million, Majestic Insurance Company's
20 ("Majestic") Risk-Based Capital (RBC) falls within the Mandatory Control level RBC per
21 Insurance Code section 739.6(b)(2), and taking into account Majestic's continuing negative cash
22 from operations and pending lawsuits that could further negatively affect Majestic's financial
23 condition, Majestic has been found to be in such condition that its further transaction of business
24 will be hazardous to its policyholders, its creditors and the public within the meaning of Insurance
25 Code section 1011(d). The Commissioner's findings are presumed to be correct. (*Caminetti v.*
26 *Guarantee Union Life Ins. Co.* (1942) 52 Cal. App. 2d 330, 337.)

27 Under these circumstances, the issuance of a conservation order in this state is plainly
28 required in order to protect the company's policyholders, creditors and the public.

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Dated: April 18, 2011

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13

Application for Ex parte Order Appointing the Ins. Commissioner as Conservator

INSURANCE COMMISSIONER of the
STATE of CALIFORNIA
CONSERVATION & LIQUIDATION OFFICE
INVESTMENT GUIDELINES

Objectives

To maintain safety of principal and to maximize available yield while assuming a minimum of risk through a balance of quality and diversification within the investment portfolio.

A. Safety

Quality

None of the Portfolio will be invested in fixed income securities rated below investment grade quality by Standard & Poor's, Moody's or by another nationally recognized statistical rating organization. Unrated securities may not be held. The minimum average market value weighted credit quality of securities in the Portfolio will be AA- by Standard & Poor's and Aa3 by Moody's or their equivalent.

Commercial Paper will be rated no less than A1 by Standard & Poor's or P1 by Moody's.

Sectors

Permitted investments for the Portfolio shall include:

1. Fixed income securities and other fixed income obligations of any type which may be issued or guaranteed by (i) the U.S. and the agencies, instrumentalities, and political sub-divisions of the U.S., and (ii) U.S. corporations, trusts and special purpose entities. Such securities must be traded on exchanges or in over the counter markets in the U.S. No emerging markets' securities are allowed.
2. Repurchase agreements.

Restrictions on permitted investments

None of the Portfolio may be invested in foreign securities and in securities not denominated in U.S. dollars. Manager may not elect to hedge currency and/or interest rate exposure. No speculative currency positions are permitted.

All repurchase agreements will be transacted with counterparties approved by the Manager in accordance with its policies and procedures and terms and conditions set forth in the applicable Investment Management Agreement and any applicable Master Repurchase Agreement(s).

No investment in interest only ("IO"), principal only ("PO"), or inverse floater CMOs are permitted. The manager should only accept reasonable prepayment risk, consistent with the stated objectives of their respective funds.

Derivatives, or financial investments containing derivatives, are not permitted, defined as options, forwards, futures and swaps.

Investment transactions (i) which result in leverage or short sales and/or (ii) with affiliates of the Manager, are not permitted.

Diversification

No more than 5 % of the Portfolio will be invested in the securities of any one issuer, other than those securities issued or guaranteed by the U.S. government, its agencies, and instrumentalities and refunded municipal issues (all of which may be held without limit). For the purposes of this guideline, asset backed and mortgage-related securities (not issued by the U.S. Government, its agencies or instrumentalities), issued by trusts and other special purpose entities, will be limited to no more than 5 percent per issue, in addition to a common originator limit of no more than 20 percent.

B. Maturity

Portfolio duration will be maintained within a range of (+/-) twelve months of Barclays Capital US Government/Credit 1-3 Yr ex Baa (the Index) under normal market conditions. There will be no restriction on the duration of any single security. Duration will be calculated adjusting for any optionality in

securities as well as adjusting for the expected prepayment level of mortgage-backed security pools.

C. Calculation of Returns

Returns will be calculated in compliance with the Association for Investment Management and Research standards.

D. General

All percentage restrictions on Portfolio holdings will initially be evaluated at the time of purchase. At any time thereafter, concentrations in eligible portfolio investments will not exceed the prescribed limit by more than one percent.

Notwithstanding any provision to the contrary, Manager will not be required to sell any particular holding because a rating of a security is downgraded subsequent to purchase. However, Manager is required to notify the client in the event of a downgrade below investment grade. In the event a security is split rated, the lower rating will apply with respect to all portfolio percentage and quality restrictions.

Investment personnel who will have input into or control over any investment decision on behalf of the Commissioner are required, if they have a beneficial interest in that security, to disclose in writing their beneficial interest and receive written authority from the Commissioner before an investment decision is made.

E. Benchmark

The benchmark for the Portfolio will be the Barclays Capital US Government/Credit 1-3 Yr ex Baa or better, (the "Index"). The objective of the Portfolio will be to maintain safety of principal and maximize available yield while assuming a minimum of risk through a balance of quality and diversification within the portfolio.