REPORT ON EXAMINATION

OF THE

ARCHITECTS & ENGINEERS INSURANCE COMPANY
(A RISK RETENTION GROUP)

AS OF

DECEMBER 31, 2007

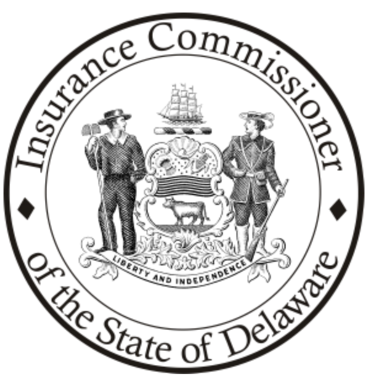
I, **Matthew Denn**, Insurance Commissioner of the State of Delaware, do hereby certify that the attached **Report On Examination**, made as of **December 31, 2007**, of the

Architects & Engineers Insurance Company (A Risk Retention Group)

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

Attest By: __________________

Date: 12 August 2008



In Witness Whereof, I HAVE HEREUNTO SET MY HAND AND AFFIXED THE OFFICIAL SEAL OF THIS DEPARTMENT AT THE CITY OF DOVER, THIS 12TH DAY OF AUGUST, 2008.

Matthew Denn
Insurance Commissioner

REPORT ON EXAMINATION

OF THE

ARCHITECTS & ENGINEERS INSURANCE COMPANY
(A RISK RETENTION GROUP)

AS OF

DECEMBER 31, 2007

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
INSURANCE COMMISSIONER

DATED this 12TH day of August, 2008.

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SALUTATION

March 31, 2008

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

Dear Commissioner:

In compliance with your instructions and pursuant to statutory provisions contained in Certificate of Authority letter 08.101, dated January 4, 2008, an examination has been made of the affairs, financial condition and management of the

ARCHITECTS & ENGINEERS INSURANCE COMPANY
(A Risk Retention Group)

Hereinafter referred to as AEIC or "Company", incorporated under the laws of the State of Delaware as a stock company with its home office located at 1209 Orange Street, Wilmington, Delaware 19807. The examination was conducted at the Company's main administrative office located at 2056 Westings Avenue, Suite 150, Naperville, Illinois 60563. The report of examination thereon is respectfully submitted.

SCOPE OF EXAMINATION

The last examination was conducted as of December 31, 2003. This examination covered the period January 1, 2004, through December 31, 2007, 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 and events occurring subsequent to the latter date were reviewed and have been commented upon to the extent deemed necessary.

The format of this report is designed to explain the procedures employed on the examination and 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 personnel and/or officials during the course of the examination.

The general procedure of the examination followed rules established by the National Association of Insurance Commissioners (NAIC) Committee on Financial Condition Examiners Handbook as adopted by the Delaware Insurance Department and generally accepted statutory insurance examination standards.

In addition to noted items in this report, the following topics were reviewed and are included in the workpapers of this examination. No exceptions or errors were noted during our review of these items:

Corporate Records
Legal Actions
All Asset and Liability Items not Mentioned in this Report
Subsequent Events

HISTORY

The Company was organized and incorporated as a stock insurance company under the captive insurance laws of the State of Delaware 18 Del. C. Section 6902 with a designation as a "Risk Retention Group" as described under the insurance laws of the State of Delaware 18 Del. C. Section 80; and under the Federal Risk Retention Act of 1986. The Certificate of Incorporation was filed on July 8, 1987. The Certificate of Authority issued January 4, 1988, authorizes the Company to transact the business of liability insurance as a risk retention group. It commenced business on April 29, 1988.

The Company's registered and home offices are located at 1209 Orange Street, Wilmington, Delaware 19807. The main administrative offices are currently located at 2056 Westings Ave. Suite 150, Naperville, Illinois 60563.

CAPITALIZATION

The Company is required to maintain a minimum capital and surplus of $1,000,000, which is the minimum amount required of a risk retention group under the insurance laws of the State of Delaware 18 Del. C. 6905(a). These Code sections indicate that such capital and surplus may be in the form of cash or promissory notes backed by an irrevocable letter of credit issued by a Delaware bank or any other bank, which is a member of the Federal Reserve System and approved by the Commissioner.

The amended Certificate of Incorporation currently authorizes the issuance of 500,000 shares of common stock with a par value of $5.00 per share. The stock originally was issued by the Company for $100.00 per share. The issue price was increased to $120.00 per share in 1990, and increased again in 1992 to the current $140.00 per share. The Company was initially capitalized via the purchase of common stock. This common stock was issued in exchange for cash and promissory notes, which were backed by irrevocable letters of credit.

STOCKHOLDER PARTICIPATION

Chapter 65, 15 USCS Section 3901(4) (E) of the Federal Statutes indicate that a “Risk Retention Group” must have “as its owners only persons who comprise the membership of the risk retention group and who are provided insurance by such group.” Therefore, ownership is necessary to obtain liability coverage from the Company. Ownership is obtained through the purchase of the Company’s capital stock by those firms seeking liability coverage. The Company enters into a shareholders’ agreement with each policyholder they insure.

Investment Requirements

Prior to 1998, the shareholders’ subscription agreement required a minimum capital investment equal to 3.0% of gross revenues for the year in which the stock purchase plan was selected. The minimum investment varied depending upon which stock purchase plan was selected. Effective in 1998, the Company required that new shareholders/policyholders purchase only one (1) share of common stock at a total cost of $140.00.

Redemption of Stock

The aforementioned Federal Statues also indicate that if a member decides to leave the Risk Retention Group, it cannot continue to be an owner of the Group. The shares of the member therefore become subject to immediate redemption. In the event of redemption the shareholder is entitled to receive the lesser of:

(1) The book value for the shares or
(2) The subscription price actually paid for such shares less any amount as is necessary to satisfy estimated outstanding obligations to the Company. The redemption price may be paid only when the Company has attained certain minimum levels of capitalization and has achieved appropriate ratios of capital and surplus to gross premiums. The redemption amount may be paid over a period not to exceed five years, unless such payment would impair or otherwise jeopardize the financial condition of the Company.

According to the requirements of the Delaware Insurance Department, payment of the redemption value for a terminated shareholder's interest may not be made until the Company achieves and maintains $10 million in capital and surplus (surplus as regards policyholders).

As of December 31, 2007, the Company segregated an amount of $2,206,048 in special surplus funds to reflect a provision for stock awaiting redemption.

MANAGEMENT AND CONTROL

The Company's amended bylaws, stipulate that the property and daily business affairs of the Company are to be managed by the Board of Directors, the number of which may vary between three (3) and seven (7) persons. One (1) Director is to be designated as a representative of the firm of Architects & Engineers Loss Control (AELC), currently under contract to manage the Company.

Board of Directors:

The Directors are divided into three (3) staggered classes. A Board member's term is three (3) years and directors are elected at the annual shareholders' meeting, which takes place in the month of June. As of the December 31, 2007, six (6) individuals were serving as Directors of the Company. They are:

Director & Residence	Principal Business Affiliation	Term Expires
Harold A. Dombeck Duluth, GA	Chairman Dombeck Associates	2009
George X. Cannon Fishers, IN	Chief Executive Officer The Upchurch Group	2008
Alan Christopherson Anchorage, AK	Senior Vice President Peratrovich, Nottingham & Drage	2009
Robert Pratzel St. Louis, MO	Chief Financial Officer Hellmuth, Obata & Kassabaum, Inc.	2008
Pradeep Patel Philadelphia, PA	Senior Vice President Ewing Cole Cherry Brott	2008
Jason Peterson Hockessin, DE	Vice President Architects & Engineers Loss Control	2008

Committees:

The bylaws indicate the Board of Directors can create Committees and appoint two (2) or more individuals to serve on them. Recent amendments to the bylaws indicate that Committee members need not be members of the Board of Directors. To date, only an Executive Committee has been created. Those individuals appointed by the Board to serve on the Executive Committee as of year-end 2007 are as follows:

Harold A. Dombeck (Chairman)
George X. Cannon
Pradeep Patel
Mitch Sellett

Officers:

The Company's officers are elected by the Board of Directors for one (1) year terms at the annual board meeting. Those persons serving as officers at year-end 2007 are:

Name	Title
Harold A. Dombeck	Chairman of the Board
Mitchell A. Sellett	President and Chief Executive Officer
George X. Cannon	Treasurer and Vice President
Jason Peterson	Secretary

INSURANCE HOLDING COMPANY SYSTEM

The Company is not currently a member of an Insurance Holding Company System. As a Risk Retention Group, the Company is owned by its policyholders.

MANAGEMENT AND SERVICE AGREEMENTS

The Company has no employees of its own. It contracts with other firms to provide the necessary resources to perform the services required for its daily business operations. The Company was involved in the following types of arrangements throughout the current examination period:

Management Agreement

The Company has a management agreement in effect with Architects and Engineers Loss Control (AELC) effective January 1, 2007. It authorizes AELC to handle all management, operational and administrative services for the Company with the exception of claims and investments. AELC receives a fee equal to 15.0% of gross written premiums on a quarterly basis for services provided. The contract is continuous unless terminated for cause. The terms of the agreement are reviewed every 3 years. AELC is owned in varying percentages by C. Roy Vince, Mitch Sellett, and Jason Peterson, all of whom are significantly involved with the Company's management. Mr. Sellett has controlling interest in AELC. The Company paid $1,076,245 to AELC in 2007.

Claims Administration Agreement

The Company maintains a claims administration agreement with C.R. Vince & Associates Inc. The agreement, effective January 1, 1998, stipulates that C.R. Vince & Associates Inc. provides claim management services to the Company in connection with losses incurred under insurance policies the Company issues. It also requires C.R. Vince & Associates Inc. to provide the Company monthly loss reports. Hourly fees that C.R. Vince & Associates Inc. can charge range from $55 per hour to $175 per hour depending upon the individual doing the claim processing. In 2007 the Company paid $25,261 to C.R. Vince & Associates Inc. for services provided. Mr. Vince owns 100% of C.R. Vince & Associates Inc. and is significantly involved with the management of the Company.

Investment Advisory Agreement

Since 1991, the Company has maintained an agreement with Alpha Advisors Inc., an Illinois firm that acts as investment managers for the Company. Per the agreement, Alpha Advisors Inc. is authorized to buy and sell the Company's investments on its behalf subject to strict investment guidelines. The Board of Directors must approve deviations from these guidelines. The fees paid to Alpha Advisors Inc. are based upon a percentage of the value of the portfolio being managed and are payable quarterly. Fees paid to Alpha Investors Inc. totaled $18,370 during 2007.

Consulting Agreement

Since 1995, the Company has had a consulting agreement with Dombeck Associates Inc. The agreement compensates Harold A. Dombeck for performance of his duties as the Company's Chairman of the Board. Mr. Dombeck received $39,500 in 2007 for his services.

TERRITORY AND PLAN OF OPERATION

Territory

As of December 31, 2007, the Company was licensed to transact business in the State of Delaware, and registered as a "Foreign Risk Retention Group" in an additional thirty-nine (39) states and the District of Columbia.

Plan of Operation

The Company is authorized to transact the business of liability insurance as a Risk Retention Group. As such it provides professional, directors & officers, employment practices, and benefit trust liability coverage, on a claims-made basis, to firms who are members of the Risk Retention Group. The Architect & Engineers Practice and Project policies are issued to member firms and provide up to $10,000,000 of liability coverage per claim and in the aggregate. The firms have a choice of either a one-year or a three-year policy term. The Company has 106 member insureds, with the average insured carrying roughly $1.5 million in coverage. Premiums are assessed based upon the annual gross revenues of the member firm. Each policy is subject to certain specified deductibles as well as various terms, conditions and endorsements as set out in the policy form. Coverage is available to any firm that meets the Company's underwriting standards and agrees to be bound by the terms and conditions of the shareholders' agreement.

Beginning January 1, 1998, the Company issues policies on a direct basis. Presently, independent brokers and the internet are used to market the Company's products.

GROWTH OF THE COMPANY

The Company's growth and activities during the period under examination are depicted in the following chart:

Year	Admitted Assets	Policyholders Surplus	Net Premiums Written	Net Income
2007	$18,663,192	$8,547,176	$ 445,502	$412,299
2006	19,415,924	8,134,595	594,067	710,711
2005	15,225,065	7,413,544	302,752	182,516
2004	15,395,474	7,223,101	790,356	72,991
2003	11,786,576	6,361,981	1,583,141	74,548

As indicated above, the Company experienced 5 positive business years. The significant decrease in net written premiums from 2003 to 2004 was due to the Company retaining less risk for issued coverage during this period from 31.75% to 10% as discussed on the section titled "Retention and Reinsurance".

RETENTION AND REINSURANCE

The Company protects itself from risk over-exposure through the use of reinsurance. The following is a description of the Company's reinsurance activity for the current period under review.

Assumed Reinsurance

The Company did not have any assumed business.

Ceded Reinsurance

As of December 31, 2007, the Company had in place two separate cession reinsurance agreements. The first agreement ceded, on a quota share basis, 90% of the first $1,000,000 of risk on each policy issued. The Company received ceding commissions of 28% in 2004 and 2005, 29% in 2006, and 29.5% in 2007.

The second agreement was an excess of cessions contract whereby the Company ceded 100% of the next $9,000,000 of risk on each policy issued. The Company received a 15% commission on business it ceded during the years 2004 and 2005, and a 25% commission on business ceded in 2006 and 2007.

The Company's net maximum retention was $100,000 per insured risk.

COMMITMENTS AND CONTINGENCIES

The State of California currently requires the Company to maintain a letter of credit pertaining to business it assumed from Firemen's Fund prior to 1/1/1999. At 12/31/07, the Letter of credit was $23,500 and covers the reserves regarding the one open claim for this business.

ACCOUNTS AND RECORDS

The Company's closing balance sheet and other documents were reviewed for the purposes of this examination. A review of the adjusted trial balance as of December 31, 2007 indicated that the balances supported the financial data of the Company's 2007 Annual Statement.

Based on the examination review of Annual Statement classifications and subsequent discussions with management, the accounting system and procedures conformed to insurance accounting standard practices and requirements.

The Company is audited by Strohm Ballweg, LLP and Pinnacle Actuarial Resources provided the Company's actuarial certification. The 2007 CPA audit of the Company was not completed prior to the conclusion of this examination. As a result, the CPA workpapers were not available for review.

FINANCIAL STATEMENTS

The following financial statements as determined by this examination are presented herein:

Analysis of Assets
Liabilities, Surplus and Other Funds
Underwriting and Investment Exhibit – Statement of Income
Capital and Surplus Account
Analysis of Examination Changes

It should be noted that the various schedules and exhibits may not add to the totals shown due to rounding.

Analysis of Assets
As of December 31, 2007

	Ledger Assets	Non-Admitted Assets	Net Admitted Assets	Notes
Bonds	$ 5,786,445		$ 5,786,445	1
Cash, cash equivalents, and short-term investments	616,205		616,205	
Investment income due and accrued	77,232		77,232	
Uncollected premiums and agents balances in the course of collection	2,987,802		2,987,802	
Deferred premiums, agents' balances and installments booked but deferred and not yet due	5,166,454		5,166,454	
Amounts recoverable from reinsurers	676,943		676,943	
Current federal and foreign income tax recoverable	17,703		17,703	
Net deferred tax asset	179,261	115,467	63,794	
Notes receivable	3,209,796		3,209,796	2
Prepaid expenses	28,620	28,620	0	
State premium tax receivable	72,943		72,943	
Total Assets	$ 18,819,404	$ 144,087	$ 18,675,317	

Statement of Liabilities, Surplus and Other Funds
December 31, 2007

			Notes
Losses	$	2,551,047	
Loss adjustment expenses		85,063	
Commissions payable		106,262	
Other expenses		108,530	
Taxes, licenses and fees		14,650	
Unearned premiums		879,405	
Ceded reinsurance balances payable		6,079,009	
Amounts withheld or retained by Company for account of others		250,316	
Total Liabilities	$	10,074,282	
Common capital stock	$	315,622	
Provision for redeemable capital stock		2,206,048	3
Gross paid-in and contributed surplus		4,661,142	
Unassigned funds (surplus)		1,418,223	
Surplus as regards policyholders	$	8,601,035	
Total Liabilities and Surplus	$	18,675,317	

Underwriting and Investment Exhibit

Statement of Income
December 31, 2007

UNDERWRITING INCOME		
Premiums earned	$	592,544
DEDUCTIONS		
Losses incurred	$	490,627
Loss expenses incurred		54,514
Other underwriting expenses incurred		(285,837)
Total underwriting deductions	$	259,304
Net underwriting gain or (loss)	$	333,240
INVESTMENT INCOME		
Net investment income earned	$	290,170
Net realized capital gains or (losses)		(2,770)
Net investment gain or (loss)	$	287,400
OTHER INCOME		
Net income before dividends to policyholders and before federal income taxes	$	620,640
Dividends to policyholders		0
Net income after dividends to policyholder but before federal income taxes	$	620,640
Federal and foreign income taxes incurred		149,613
Net income	$	471,027

Capital and Surplus Account
December 31, 2006 through December 31, 2007

Surplus as regards policyholders, December 31, 2006	$	8,134,595
Net income	$	471,027
Change in net deferred income tax		(19,724)
Change in non-admitted assets		14,017
Capital changes:		
Paid in		(7,922)
Surplus adjustments:		
Paid in		9,042
Change in surplus as regards policyholders for the year	$	466,440
Surplus as regards policyholder, December 31, 2007	$	8,601,035

Analysis of Examination Changes
December 31, 2007

There were no examination adjustments made to the Company's financial statements.

NOTES TO FINANCIAL STATEMENTS

Note 1 - Bonds **$5,786,445**

Procedures were performed to confirm the existence and ownership of the bond investments reported in Schedule D, part 1 of the 2007 Annual Statement. These procedures were performed without exception. The Company's bond portfolio comprised 31% of total admitted assets as of December 31, 2007. All of the Company's bonds were rated class 2 or better by the NAIC Securities Valuation Office.

Note 2 – Notes Receivable **$3,209,796**

The Company properly segregates the balances which represent the capital contributions of the firms which have left the program. As noted previously, when a firm discontinues insurance coverage, it also must relinquish ownership. However, even though the applicable common stock is redeemed and retired, the Company is not allowed to refund capital until a minimum of $10 million in Policyholders Surplus is attained and appropriate ratios of capital and surplus to gross premiums are achieved.

Note 3 – Provisions for Redeemable Capital Stock **$2,206,048**

The Company segregates the balances which represent the capital contributions of the firms which have left the program. As noted previously, when a firm discontinues insurance coverage, it also must relinquish ownership. However, even though the applicable common stock is redeemed and retired, the Company is not allowed to refund capital until a minimum of $10 million in Policyholders Surplus is attained and appropriate ratios of capital and surplus to gross premiums are achieved.

COMPLIANCE WITH PRIOR EXAMINATION RECOMMENDATIONS

The Company's compliance with prior examination recommendations was reviewed for each account in the current examination for which there was a prior exam recommendation. All prior examination recommendations were either directly or indirectly addressed subsequent to the previous examination.

SUMMARY OF RECOMMENDATIONS

There were no recommendations made in this examination report.

CONCLUSION

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

Description	12/31/2007 Current Examination	12/31/2003 Prior Examination
Assets	$ 18,675,317	$ 11,786,575
Liabilities	$ 10,074,282	$ 5,424,595
Common capital stock	$ 315,622	$217,301
Provision for redeemable capital stock	2,206,048	1,902,292
Gross paid in and contributed surplus	4,661,142	4,305,800
Unassigned funds (surplus)	1,418,223	(63,413)
Total Capital and Surplus	$ 8,601,035	$ 6,361,980
Totals	$ 18,675,317	$ 11,786,575

Since the last examination as of December 31, 2003, Assets have increased $6,888,742. Liabilities have increased $4,649,687, and Capital and Surplus has increased $2,239,055.

The assistance on the analysis of the Company's loss reserves and loss adjustment expense reserves by Mr. Michael Morro, ACAS, MAAA from the consulting actuarial firm, INS Consultants, Inc., Philadelphia, Pennsylvania is hereby acknowledged.

Respectfully submitted,

Dwight Ward

Dwight W. Ward, CFE
Examiner-in-Charge
State of Delaware