

REPORT ON EXAMINATION
OF
ESSEX INSURANCE COMPANY
AS OF
DECEMBER 31, 2007

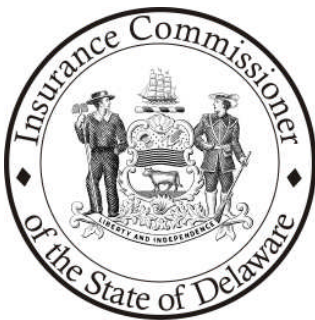
I, Karen Weldin Stewart, Insurance Commissioner of the State of Delaware, do hereby certify that the attached REPORT ON EXAMINATION, made as of December 31, 2007 of the

ESSEX INSURANCE COMPANY

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

Attest By: *Sonia C. Harris*

Date: 29 June 2009



In witness whereof, I have hereunto set my hand and affixed the official seal of this Department at the City of Dover, this 29th day of June 2009. .

[Handwritten signature]

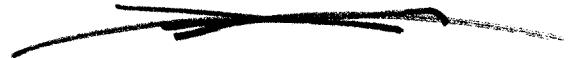
Karen Weldin Stewart, CIR-ML
Insurance Commissioner

REPORT ON EXAMINATION
OF THE
ESSEX INSURANCE COMPANY
AS OF
DECEMBER 31, 2007

The above-captioned Report was completed by examiners of the Delaware Department of Insurance.

Consideration has been duly 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.



Karen Weldin Stewart, CIR-ML
Insurance Commissioner

Dated this 29th day of June, 2009

Essex Insurance Company
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MAY 8, 2009

Honorable Alfred W. Gross
Chairman, Financial Condition (E)
Committee, NAIC
Bureau of Insurance
PO Box 1157
Richmond, VA 23218

Honorable Karen Weldin Stewart, CIR-ML
Commissioner of Insurance
State of Delaware
841 Silver Lake Boulevard
Dover, Delaware 19904

Commissioners:

In compliance with instructions and pursuant to statutory provisions contained in Certificate of Authority No. 08-026, dated May 20, 2008, an examination has been made of the affairs, financial condition and management of the:

ESSEX INSURANCE COMPANY

hereinafter referred to as "Company", incorporated under the laws of the State of Delaware as a stock company with its home office located at 4521 Highwoods Parkway, Glen Allen, Virginia.

The report of such examination is submitted herewith.

SCOPE OF EXAMINATION

The last examination was conducted as of December 31, 2004. This examination covered the three year period from January 1, 2005 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 subsequent to the latter date were reviewed where deemed necessary.

This report is presented on the exception basis. It is designed to set forth the facts with regard to any material adverse findings disclosed during the examination. 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 discussed with responsible company officials during the course of the examination.

The general procedures of the examination followed the rules established by the Committee on Financial Condition Examiners Handbook of the National Association of Insurance Commissioners (NAIC) and generally accepted statutory insurance examination standards consistent with the Insurance Laws and Regulations of the State of Delaware. In accordance with the aforementioned Handbook, an information systems review was performed by the consulting firm of INS Services, Inc.

HISTORY

The Company was incorporated on February 29, 1980, under the laws of the State of Delaware. It began business on October 22, 1980, in Minnesota, as a stock insurance company licensed to transact health, credit health, property, marine transportation and casualty insurance.

Essex Insurance Company

The Company was brought to Richmond, VA in December 1985, and expanded its writings from property coverages to general liability, light to medium products, miscellaneous errors and omissions/professional liability, excess and umbrella. In addition, the Company also writes unusual or large property risks, cargo and inland marine and truck physical damage. On June 16, 1983, the Company amended its Certificate of Authority to include surety.

The Company is a diversified specialty insurance underwriting organization. Operations of the Company are conducted under management agreements with Underwriting Management Incorporated (UMI), a wholly owned subsidiary of Markel Corporation. UMI provides underwriting, management, claims handling, accounting and administrative services to the Company. The Company has an agreement with Markel-Gayner Asset Management Corp. (Markel-Gayner) whereby Markel-Gayner provides investment advisory services with respect to the investment portfolio. The Company has no employees.

On December 31, 1991, the Company purchased National Specialty Insurance Company (NSIC) from the affiliated Evanston Insurance Company, for consideration equal to the statutory capital and surplus of NSIC (\$4,670,432). The Company immediately contributed another \$350,000 in capital to NSIC, bringing the total investment to \$5,020,432. In connection with the reorganization, NSIC was re-domesticated from Colorado to Illinois and was renamed Richmond Insurance Company (RIC) on February 27, 1992. Effective September 30, 1994, RIC was merged with and into the Company, with the Company being the survivor.

In connection with the sale of the Company's former affiliate, Investors Insurance Company of America (now known as Specialty Surplus Insurance Company), to an unaffiliated

Essex Insurance Company

company, Lumbermen's Mutual Casualty Company (Lumbermen's), effective January 1, 2000, the ownership interest in L.Z.L. Corporation, a California subsidiary corporation of Investors Insurance Company of America, was transferred to the Company.

On March 24, 2000, Markel Corporation (Markel), an insurance holding company domiciled in the Commonwealth of Virginia, completed its acquisition of Terra Nova (Bermuda) Holdings, Ltd (Terra Nova), a Bermuda based insurance holding company whose insurance subsidiaries are based in Bermuda and the United Kingdom. Markel formed a new holding company, Markel Holdings Inc., which, in turn, formed a new subsidiary to enter into the merger with and into the existing Markel Corporation. In the merger, Markel shareholders received an identical number of shares in Markel Holdings. Markel Holdings also issued cash and securities to Terra Nova shareholders in exchange for their Terra Nova shares. Upon completion of the transaction, Markel, then known as Markel North America, Inc., and Terra Nova became wholly owned subsidiaries of Markel Holdings, and Markel Holdings changed its name to Markel Corporation.

Effective March 31, 2001, Markel North America, Inc., a Virginia domiciled corporation and wholly-owned subsidiary of Markel was merged into Markel. As a result of this merger transaction, Markel, the ultimate controlling parent of the Company has become the sole shareholder of the Company.

CAPITALIZATION

Common Capital Stock

The Company amended its Certificate of Incorporation on May 20, 1991 to retain the authorized number of common stock shares at 30,000 and change the par value of each share of common stock from \$100 to \$300. The Certificate of Amendment filed with the Secretary of State of the State of Delaware states that the certificates representing shares of common stock which previously had a par value of \$100 per share thereafter represent shares of common stock having a par value of \$300 per share. As a result of the change of par value, the 15,000 shares of issued and outstanding shares at December 31, 1995, provided capital paid up of \$4,500,000.

All outstanding capital stock is owned by the parent, Markel Corporation, a publicly traded insurance holding company, located in Glen Allen, Virginia that trades on the New York Stock Exchange under the symbol MKL.

DIVIDENDS TO SHAREHOLDER

The Company paid dividends to Markel Corporation, its sole shareholder as follows for the three years under examination. The amounts paid amounted to:

| | |
|------|--------------|
| 2005 | \$47,017,746 |
| 2006 | -0- |
| 2007 | 86,330,478 |

MANAGEMENT AND CONTROL

The Bylaws provide that stockholders meetings shall be held on or about May 13th of each year in Richmond, Virginia or any other place or time so designated.

The number of directors shall be not less than three or more than 11. Vacancies and newly created directorships may be filled by a majority of the directors then in office, though less than a quorum, or by a sole remaining director, and the directors so chosen shall hold office until the next annual election. The business of the corporation shall be managed by or under the direction of its board of directors, which may exercise all powers of the corporation and do all such lawful acts and things as are not prohibited by statute or by the certificate of incorporation or by these bylaws, and as directed or required to be exercised or done by the shareholders.

The board may, by resolution, designate one or more committees, each committee to consist of one or more of the directors. In general the committees have the same authority as the board, but in no case may any committee have the authority to (1) amend the certificate of incorporation; (2) adopt an agreement of merger or consolidation; (3) recommend to the stockholders the sale, lease or exchange of property and assets; (4) recommend to the stockholders a dissolution of the corporation or a revocation of a dissolution; (5) amend the Bylaws; (6) have the power to issue a dividend; or (7) issue stock. Dividends may be declared by the Board of Directors at any regular or special meeting. They may be paid in cash, property or in shares of capital stock.

The following persons were elected to the Board of Directors on November 14, 2007 and were serving in that capacity at December 31, 2007:

Essex Insurance Company

Name and Residence

Principal Occupation

Alan Irving Kirshner
Montpelier, Virginia

Chairman of Markel Corporation and the
Company

Anthony Foster Markel
Richmond, Virginia

President of Markel Corporation, Vice
Chairman of the Company

Steven Andrew Markel
Richmond, Virginia

Vice Chairman of Markel Corporation and
Executive Vice President of the Company

William Bradley Dickler
Richmond, Virginia

President of the Company and Chief
Operating Officer

Richard Reeves Whitt III
Glen Allen, Virginia

Senior Vice President and Chief Financial
Officer of Markel Corporation

Paul William Springman
Richmond, Virginia

Executive Vice President of Markel
Corporation

Bradley James Kiscaden
Winnetka, Illinois

Chief Corporate Actuary of Markel
Corporation

The Bylaws state that the officers of the corporation shall be chosen by the board, and consist of a Chairman of the Board, a President, a Vice President, a Secretary and a Treasurer.

The board may choose any number of vice presidents and assistants.

The following persons were elected as officers on November 14, 2007 and were serving in that capacity at December 31, 2007:

Name

Office

Alan Irving Kirshner

Chairman

Anthony Foster Markel

Vice Chairman

Steven Andrew Markel

Executive Vice President

Essex Insurance Company

| | |
|------------------------------|--|
| William Bradley Dickler | President and Chief Operating Officer |
| Bruce Alan Kay | Vice President |
| Jill Grode Goldfine | Senior Vice President/Finance and Treasurer |
| Linda Sickman Rotz | Secretary |
| Anne Galbraith Waleski | Assistant Treasurer |
| Thomas Johnson Childress III | Assistant Secretary/Tax Director |
| Barbara Jean Childress | Assistant Secretary |
| Dewey Michael Jones | Assistant Secretary |
| Kathleen Anne Sturgeon | Assistant Secretary |

It was noted that written correspondence was submitted to the Delaware Department of Insurance in regards to the changes in officers and directors during the period under examination in compliance with 18 Del. C. § 4919.

HOLDING COMPANY SYSTEM

The Company is a member of an Insurance Holding Company System. The ultimate parent of the system is Markel Corporation, a Virginia corporation. The following is an organizational chart that reflects the identities and interrelationships between the Company and its affiliated US insurers as of December 31, 2007:

Essex Insurance Company

| <u>Name</u> | <u>NAIC Code</u> | <u>State of Domicile</u> | <u>% Ownership</u> |
|--|------------------|--------------------------|--------------------|
| Markel Corporation | | VA | |
| Essex Insurance Company | 39020 | DE | 100 |
| Gryphon Holding, Inc. | | DE | 100 |
| Deerfield Insurance Company | 37184 | IL | 100 |
| Associated International Insurance Company | 27189 | IL | 100 |
| Markel Insurance Company | 38970 | IL | 100 |
| Markel American Insurance Company | 28932 | VA | 100 |
| Shand/Evanston Group, Inc. | | VA | 100 |
| Evanston Insurance Company | 35378 | IL | 100 |

Please refer to Schedule Y, Part 1 of the annual statement for other affiliated domestic and foreign companies and insurers. Copies of the "Form B Holding Registration Statements" filed with the Delaware Insurance Department, during the period under examination, were reviewed. It appears that the Company has complied with the provisions of 18 Del. C. § 5004.

MANAGEMENT AGREEMENT

Effective January 1, 1992, the Company entered into a "Management Agreement" with its affiliate, Underwriting Management, Inc. (UMI), which replaced the previous management agreement. Pursuant to this agreement, the Company granted underwriting authority to UMI to enter into producer agreements; receive and accept proposals of insurance; provide limits of liability and amounts of coverages; issue binders for a maximum of thirty (30) days; and to negotiate, cede or purchase any reinsurance (either treaty or facultative). In all cases it is expressed that UMI operate only within the guidelines and ultimate authority of the Company.

The Company granted claims authority to UMI to adjust, settle, compromise, defend and litigate any and all claims arising out of the policies issued pursuant to this agreement. UMI also provided all employees; maintained complete underwriting and claim files, records and accounts of all transactions; and performed all other accounting functions. Subject to adjustment by mutual consent, UMI is compensated by a fee equal to 110% of their direct cost. This fee is paid on a monthly basis. Total fees paid to UMI under this agreement for 2007 were approximately \$143,699,093. This agreement was amended on September 24, 1993. The amendment provided for clarification of UMI's responsibilities to include business management services as may be necessary or appropriate to the operation of the business affairs of the Company.

AFFILIATE AGREEMENTS

There is a service agreement between Markel Corporation (Markel), Underwriting Management, Inc. (UMI) and the Company effective August 1, 2003 that allows Markel to issue checks on behalf of UMI and the Company.

Effective December 30, 1994, the Company entered into a "Tax Allocation Agreement" with all the other subsidiaries of the Markel Corporation (parent), as allowed by Section 1504 of the Internal Revenue Code. Pursuant to this agreement, the Company (and all other members) will compute its tax liability (including alternative minimum tax and environmental tax) in the manner it would regularly use in filing a separate federal income tax return, except that any intercompany transactions that are deferred on the parent's consolidated federal income tax return will be deferred in computing the separate return tax liability until the deferred intercompany transaction is no longer deferred and is recognized on the consolidated return. The

amount of any separate liability is paid to the parent. Any tax refund due to a member will be paid within thirty (30) days of filing the applicable consolidated return. This agreement was amended effective January 15, 1999 to delete and/or add parties to the agreement due to the acquisitions and/or deletions of subsidiaries within the Markel group of companies.

On May 21, 1998, the Company executed an affiliated Investment Advisory Agreement dated September 30, 1998 with Markel Gayner Asset Management, Inc. (Markel Gayner). The agreement allows Markel Gayner to manage a discretionary investment portfolio for the Company with the expressed objective of capital appreciation. The agreement allows for an annual investment advisory fee equal to 1% of the portfolio's market value payable in quarterly installments. Pursuant to this agreement, the total amount paid to Markel Gayner in 2007 was \$1,976,716.

Effective January 1, 2005 the Company and UMI entered into an agreement with the following affiliates:

- American Underwriting Managers Agency, Inc.
- Markel Service, Inc. d/b/a Markel Underwriters & Brokers
- Markel Southwest Underwriters, Inc.
- Markel Underwriting Managers, Inc.
- Markel West, Inc.
- Shand Morahan & Company, Inc.

These affiliated underwriting managers are compensated based on their actual expenses incurred.

The Company had at least one intercompany balance that was settled approximately 120 days after year end, which is contrary to Note # 10 D of the Notes to the financial statements which states "These arrangements require that intercompany balances be settled within 7 to 90 days, depending on the agreement."

Therefore,

It is recommended that the Company settle intercompany balances in accordance with the stated terms of the agreements or at least quarterly as recommended by SSAP 96 which amends SSAP 25.

TERRITORY AND PLAN OF OPERATION

Territory

As of December 31, 2007, the Company was licensed in only one state, Delaware. It writes in all other states and in the District of Columbia, Puerto Rico and Canada on a non-admitted basis as an unauthorized Excess and Surplus lines carrier. The largest volumes of business come from California, Florida, Illinois, Texas and New York.

Plan of Operation

The Excess and Surplus (E&S) market focuses on hard to place risks and risks that admitted insurers specifically refuse to write. E&S eligibility allows the Company to underwrite nonstandard market risks with more flexible policy forms and unregulated premium rates. This typically results in coverages that are more restrictive and more expensive than the standard admitted market. At December 31, 2007, the Company was licensed to write:

Health, Credit Health, Property, Surety, Marine and Transportation,
Casualty, including: Vehicle, Liability, Burglary and Theft, Personal
Property Floater, Glass, Boiler and Machinery, Credit, Leakage and Fire
Extinguisher Equipment, Malpractice, Elevator, Congenital Defects,
Livestock, Entertainment and Miscellaneous

The business is predominantly produced by an affiliated underwriting manager, Underwriting Management, Inc. (UMI). In addition, business is also produced by affiliated underwriting managers, American Underwriting Managers Agency, Inc. ("AUM"). Business is classified as primary general liability, product liability, excess and umbrella, primary inland marine, primary and excess property, primary and excess ocean marine and railroad. The Company's premium rates are generally based on ISO premium rates for general liability, property and transportation classes. Rates and terms are tailored to each risk based on individual facts and circumstances. The Company generally applies a surcharge to the base ISO rate. Inland marine and motor truck cargo rates are developed internally based upon the underwriters' experience and a base of data.

All third party agents are contracted with UMI. The Company has an agreement with UMI, an affiliate, whereby UMI is compensated at 110% of its direct costs. Fees are paid on a monthly basis and are adjusted within 90 days of year end to comply with limits set forth in the agreement.

A service agreement between Markel Corporation (Markel), UMI and the Company dated August 1, 2003 allows Markel to issue checks on behalf of UMI and the Company.

Business Plan

The Company does not maintain a formal long-range business plan, but does produce very extensive yearly business plans. The yearly plans provide a detailed analysis of each line of

business including key components, pricing, marketing and promotion, placement, producers and employees, support staff, and how the line of business performed in the previous year versus the financial goals and projections for the current year. The critical factors that impact each line of business are addressed in the current year.

GROWTH OF COMPANY

The following information was obtained from the Company's filed Annual Statements and covers the five preceding years:

| <u>Year</u> | <u>Admitted Assets</u> | <u>Surplus as Regards Policyholders</u> | <u>Net Premium Written</u> | <u>Net Income</u> |
|-------------|------------------------|---|----------------------------|-------------------|
| 2007 | \$1,143,954,141 | \$342,961,128 | \$349,868,382 | \$108,388,757 |
| 2006 | 1,201,163,806 | 334,160,947 | 434,560,131 | 91,565,002 |
| 2005 | 1,045,130,521 | 225,435,757 | 391,783,741 | 2,442,528 |
| 2004 | 939,451,888 | 276,509,052 | 391,385,526 | 54,269,597 |
| 2003 | 806,750,075 | 217,399,248 | 356,628,686 | 28,335,092 |

It is important to note that the Company has experienced growth in assets and liabilities that has been fairly consistent between 2004 and 2007. Surplus as regards policyholders has increased an average of 8% per year during the period under examination. Net income has been inconsistent during each of the three years covered by the exam. Growth over this most recent three year period has taken the form of the following:

- A 22% increase in admitted assets;
- A 24% increase in surplus as regards policyholders;
- An 11% decrease in net written premiums;
- A 100% increase in net income.

REINSURANCE

Ceded

The Company has a comprehensive reinsurance program that is designed to protect it against catastrophic losses in all lines of business written. The Company has a policy requiring all unauthorized reinsurers to provide the Company with irrevocable letters of credit or trust accounts for the Company's benefit, which can be drawn on in the event the reinsurer fails to reimburse the Company for its share of paid claims. The Company was the beneficiary of irrevocable letters of credit in the amount of \$45.5 million and trust accounts in the amount of \$26.7 million at December 31, 2007. In order to further reduce its credit risk, the Company seeks to do business only with financially sound reinsurance companies and regularly reviews the financial strength of all reinsurers used.

In regards to its program, the Company utilizes two types of reinsurance treaties: automatic and facultative. Automatic treaties are negotiated by the Company in two ways: 1) directly with the reinsurer; 2) or through reinsurance intermediaries (Aon Reinsurance Agency, Inc., Guy Carpenter & Company, Willis Re and Arthur J. Gallagher). Ninety to ninety-five percent (90-95%) of the business is placed through Aon Reinsurance Agency, Inc. Based on set limits, these treaties cover all policies written within the different lines of business. Under the terms of the treaties, the reinsurer is obligated to accept this business, as long as it is issued in regards to the terms of the treaty.

The second type of treaty involves facultative reinsurance, which is negotiated on a policy-by-policy basis, by the Company directly with the reinsurer. This type of reinsurance is

for those policies that have higher than normal limits or are not subject to the automatic treaties conditions, thus creating unique risk conditions or higher limits of exposure. Principle facultative reinsurers are Munich Reinsurance America, Berkley Insurance, General Reinsurance, Odyssey America and Swiss Re America.

The following is a summary of the Company's significant reinsurance programs in-force at December 31, 2007.

- **Casualty Excess of Loss** – the Company cedes 50% of \$1,000,000 excess of \$1,000,000 and 90% of \$3,000,000 excess of \$2,000,000 of all subject premiums and losses classified as primary liability and/or excess and umbrella liability.
- **Property** – the Company retains the first \$1,000,000 and cedes \$4,000,000 excess of \$1,000,000 on all policies, except for wind coverage within 50 miles of the East and Gulf Coasts. Any wind coverage is ceded to a 50% quota share up to \$5,000,000.
- **Special Property** – the Company cedes all earthquake/difference-in-conditions business to a 50% quota share up to \$10,000,000. The Company cedes all other perils excluding earthquake to a separate 50% quota share up to \$5,000,000 on any business classified as Special Property.
- **Inland Marine** – the Company retains the first \$1,000,000 and cedes \$4,000,000 excess of \$1,000,000 on all policies classified as Inland Marine.
- **Railroad First Party** – the Company retains the first \$1,000,000 and cedes \$4,000,000 excess of \$1,000,000 on all policies classified as Railroad First Party.
- **Railroad Third Party** – the Company retains the first \$1,000,000 and cedes \$4,000,000 excess of \$1,000,000 and \$5,000,000 excess of \$5,000,000 on all policies classified as Railroad Third Party.
- **Ocean Marine** – the Company retains the first \$1,000,000 and cedes \$4,000,000 excess of \$1,000,000 on all policies classified as Ocean Marine on a per risk basis. In addition to the per risk contract, there is also a per occurrence contract that is \$24,000,000 excess of \$1,000,000, but \$23,000,000 excess of \$2,000,000 for any named or numbered storms.
- **Catastrophe** – the Company also has a Catastrophe Excess of Loss for Earthquake occurrences \$100,000,000 excess of \$200,000,000, with one reinstatement.

The Company participated in several treaties, whereby it ceded to an affiliate as part of a fronting arrangement. They were as follows:

- An agreement between the Company and Markel American Insurance Company (MAIC). Effective January 1, 1995, it is a quota share treaty where the Company cedes, to MAIC, 100% of all business underwritten or managed by American Underwriting Managers Agency, Inc. (AUM) except as excluded by the treaty.
- An agreement between the Company and Markel Insurance Company (MIC), effective January 1, 1998. It is a quota share treaty where the Company cedes, to MIC, 100% of all business underwritten or managed by Markel Service Inc. d/b/a Markel Underwriters and Brokers Management Inc., except as excluded by the treaty.
- An agreement between the Company and Evanston Insurance Company (EIC), effective January 1, 1996. It is a quota share treaty where the Company cedes, to EIC, 100% of all business underwritten or managed by Shand Morahan & Company, Inc., except as excluded by the treaty.

Reinsurance premiums ceded to affiliates amounted to approximately \$21.6 million or 17% of the Company's total cessions.

Assumed

About 97% of the business was assumed from three affiliates: Evanston Insurance Company (EIC), Markel American Insurance Company and Markel Insurance Company (MIC), about 2% came from unaffiliated companies and 1% from Pools and Associations.

The bulk of the business was assumed from affiliates pursuant to the following fronting agreements:

- An agreement between the Company and MIC, effective January 1, 1998. It is a quota share treaty where MIC cedes to the Company 100% of all miscellaneous property and casualty business underwritten or managed by UMI, except as excluded by the treaty.

Essex Insurance Company

- An agreement between the Company and MAIC, effective August 14, 1995. It is a quota share treaty where MAIC cedes to the Company 100% of all business underwritten or managed by UMI, except as excluded by the treaty.
- An agreement between the Company and EIC, effective August 14, 1995. It is a quota share treaty where EIC cedes to the Company 100% of all business underwritten or managed by UMI, for the Company, except as excluded by the treaty.

Effective January 1, 2000, the Company entered into a Bulk Reinsurance Agreement with Investors Insurance Company of America (IICA) prior to the acquisition of IICA by Lumbermen's Mutual Casualty Company (Lumbermen's) on January 1, 2000. Pursuant to this agreement, the Company assumed loss, allocated loss adjustment expenses and uncollectible reinsurance on IICA policies which were in effect prior to the closing of the Stock Purchase Agreement between Lumbermen's and Investors Underwriting Managers, Inc., the direct parent of IICA, effective January 1, 2000. The reinsurance premium paid by IICA was equal to all non-cash equivalent assets of IICA existing prior to the closing of the Stock Purchase Agreement, less all liabilities other than loss reserves of IICA existing prior to the closing of the Stock Purchase Agreement.

ACCOUNTS AND RECORDS

The accounts and records reviewed included an evaluation of the Company's operational and organizational controls. The areas evaluated included computer systems, accounting systems, organizational structures, and the processing structure. In general, it has been determined that the Company does have sufficient levels of control in place for all the above areas.

During the course of the examination, the Company's books and records were reviewed and compared to reported items and values in the annual statements. No material discrepancies were noted.

It was noted that the Company does not maintain an audit committee. An audit committee has been established at the holding company level. The audit committee consists of four outside members of the board of directors of Markel Corporation. The audit committee charter requires a minimum of two meetings per year, plus "as many additional times as the Committee deems necessary."

The Markel Corporation internal audit department evaluates internal controls at each operational business unit and the corporate headquarters. There are no scope restrictions on the department's work. The internal audit department develops an annual audit plan that includes goals and objectives for the audit plan year. The department was made up of twelve qualified auditors that included two directors, two senior auditors, three managers, five staff auditors, plus support staff at December 31, 2007.

The General Interrogatories of the Company's 2007 Annual Statement indicates that the financial examination report as of December 31, 2004 became available on May 31, 2006. A review of the corporate minutes for the three year period of examination does not reflect "whether the previous examination report was reviewed by company directors."

Therefore,

It is recommended that the Company, "keep a complete permanent record of the proceedings of its board of directors and subordinate committees thereof," as required by the NAIC Annual Statement Instructions for Property/Casualty Companies and to come into compliance with Del. C. § 320(d), which requires adequate records to be kept.

FINANCIAL STATEMENTS

The following statements show the assets, liabilities, surplus and other funds of the Company, as determined by this examination, as of December 31, 2007.

Assets
Liabilities, Surplus and Other Funds
Underwriting and Investment Exhibit
Statement of Income
Capital and Surplus Account

It should be noted that the various schedules and exhibits might not add to the totals shown due to rounding. With the exception of the Losses and Loss Adjustment Expenses accounts, write-ups on the individual accounts in the Notes to Financial Statements section of this report are presented on the "exception basis." Only comments relative to adverse findings, material financial changes, or other significant regulatory concerns are noted.

ASSETS
DECEMBER 31, 2007

| | | | |
|--|-------------------------|--------------------|-------------------------|
| Bonds | \$ 794,466,026 | | \$ 794,466,026 |
| Common stocks | 204,757,982 | | 204,757,982 |
| Cash and short-term investments | 44,916,723 | | 44,916,723 |
| Investment income due and accrued | 10,766,639 | | 10,766,639 |
| Uncollected premiums and agents' balances in course of collection | 57,466,673 | \$2,775,333 | 54,691,340 |
| Deferred premiums, agents' balances and installments booked but deferred and not yet due | 22,970 | | 22,970 |
| Amounts recoverable from reinsurers | 19,125,771 | | 19,125,771 |
| Funds held by or deposited with reinsured companies | 2,368,290 | | 2,368,290 |
| Net deferred tax asset | 11,010,961 | | 11,010,961 |
| Claims advance | 869,229 | | 869,229 |
| Receivable - PMA Capital Insurance Company | 830,635 | 323,115 | 507,520 |
| Receivable - Specialty Surplus Insurance Company | 1,289,025 | 887,316 | 401,709 |
| Receivable - American Motorist Insurance Company | 94,191 | 50,590 | 43,601 |
| Receivable reinsurance interest | <u>5,380</u> | <u></u> | <u>5,380</u> |
| | | | |
| Totals | <u>\$ 1,147,990,495</u> | <u>\$4,036,354</u> | <u>\$ 1,143,954,141</u> |
| | | | |
| | | | |
| | | | |

Essex Insurance Company

LIABILITIES, SURPLUS AND OTHER FUNDS
DECEMBER 31, 2007

| | | <u>Note</u> |
|---|--------------------------------|-------------|
| Losses | \$ 443,200,985 | 1 |
| Reinsurance payable on paid losses and loss adjustment expenses | 68,153 | |
| Loss adjustment expenses | 173,402,847 | 1 |
| Commissions payable, contingent commissions and other similar charges | 13,509,291 | |
| Other expenses | 471,700 | |
| Taxes, licenses and fees due or accrued | 37,798 | |
| Current federal and foreign income taxes | 1,956,026 | |
| Unearned premiums | 148,713,291 | |
| Ceded reinsurance premiums payable | 11,585,981 | |
| Funds held by company under reinsurance treaties | 1,930,365 | |
| Amounts withheld or retained by company for account of others | 1,156,073 | |
| Provision for reinsurance | 442,200 | |
| Payable to parent, subsidiaries and affiliates | 3,523,777 | |
| Premium payable - Specialty Surplus Insurance Company | 847,033 | |
| Miscellaneous liability - American Nuclear Insurers | 86,155 | |
| Deposits held for New England Reinsurance Co. (PMA capital) | <u>61,338</u> | |
| | | |
| Total liabilities | \$ 800,993,013 | |
| | | |
| Common capital stock | 4,500,000 | |
| Gross paid in and contributed | 55,875,000 | |
| Unassigned Funds | <u>282,586,128</u> | |
| | | |
| Total Capital and Surplus | <u>\$ 342,961,128</u> | |
| | | |
| Total Liabilities, Surplus and Other Funds | <u><u>\$ 1,143,954,141</u></u> | |

UNDERWRITING AND INVESTMENT EXHIBIT
DECEMBER 31, 2007

| | | |
|---|--------------------|-----------------------|
| Income: | | |
| Premiums earned | \$ 381,659,472 | |
| Net investment income earned | 39,266,256 | |
| Net realized capital gains | 12,834,955 | |
| Miscellaneous income | <u>64,763</u> | |
| | | |
| Total income | | <u>\$ 433,825,446</u> |
| Expenses: | | |
| Losses incurred | \$ 98,818,909 | |
| Loss expenses incurred | 55,052,397 | |
| Other underwriting expenses incurred | <u>132,177,215</u> | |
| | | |
| Total expenses | | <u>\$ 286,048,521</u> |
| | | |
| Net income before federal income taxes incurred | | \$ 147,776,925 |
| Federal income taxes incurred | | 39,388,168 |
| | | |
| Net income | | <u>\$ 108,388,757</u> |
| | | |

CAPITAL AND SURPLUS ACCOUNT
DECEMBER 31, 2006 TO DECEMBER 31, 2007

| | | | |
|---|---------------------|-----------------------|--|
| | | | |
| | | | |
| | | | |
| Surplus as regards policyholders, December 31, 2006 | | \$334,160,947 | |
| Net Income | | <u>108,388,757</u> | |
| <u>Additions:</u> | | | |
| Change in provision for reinsurance | \$ 124,400 | | |
| | | | |
| Total additions | | <u>\$124,400</u> | |
| <u>Deductions:</u> | | | |
| Change in net unrealized capital gains (losses) | \$ (12,838,573) | | |
| Change in net deferred income tax | (452,075) | | |
| Change in nonadmitted assets | (91,850) | | |
| Dividends to stockholders | <u>(86,330,478)</u> | | |
| | | | |
| Total deductions | | <u>\$(99,712,976)</u> | |
| Net change in surplus as regards policyholders for the year | | <u>\$8,800,181</u> | |
| Surplus as regards policyholders, December 31, 2007 | | <u>\$342,961,128</u> | |
| | | | |

SCHEDULE OF EXAMINATION ADJUSTMENTS

There were no adjustments to the Company's annual statement as a result of this examination.

NOTES TO FINANCIAL STATEMENTS

(Note 1)

| | |
|---------------------------------|-----------------------------|
| Losses | \$443,200,985 |
| Loss Adjustment Expenses | <u>\$173,402,847</u> |
| Total | <u>\$616,603,832</u> |

Losses and Loss Adjustment Expenses

INS Consultants, Inc. (INS) was retained to perform an independent analysis of the Company's gross and net loss and loss adjustment expense reserves as of December 31, 2007. The Company's carried gross reserve of \$776.7 million is higher than the INS' estimate by \$113.2 million, or 14.6% of the carried reserve. The Company's carried net reserve of \$616.6 million is higher than the INS' estimate by \$121.2 million, or 19.7% of the carried reserve. Therefore, it was concluded that the Company's gross and net reserves for losses and loss adjustment expenses were adequate at December 31, 2007.

Data Verification

INS' findings were contingent on the successful completion of the verification of a sample of the Company's underlying loss and loss adjustment expense data. A total of twenty-two (22) claim files were reviewed for verification of a total of 121 attributes. No exceptions were noted in the sample. Therefore, it was concluded that the Company's underlying data for losses and loss adjustment expenses was adequate at December 31, 2007.

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 prior examination recommendation.

It was determined that the Company was in compliance with the recommendations during the current examination.

SUMMARY OF RECOMMENDATIONS

Examination recommendations as of December 31, 2007 consisted of the following:

Affiliates Agreements - It is recommended that the Company settle intercompany balances in accordance with the stated terms of the agreements or at least quarterly as recommended by SSAP 96, which amends SSAP 25. (Page 12)

Accounts and Records - It is recommended that the Company, "keep a complete permanent record of the proceedings of its board of directors and subordinate committees thereof," as required by the NAIC Annual Statement Instructions for Property/Casualty Companies and to come into compliance with 18 Del. C. § 320(d), which requires adequate records to be kept. (Page 19)

CONCLUSION

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

| <u>Description</u> | <u>December 31, 2007</u> | <u>December 31, 2004</u> | <u>Increase</u> |
|----------------------------------|--------------------------|--------------------------|-----------------|
| Admitted Assets | \$ 1,143,954,141 | \$ 939,451,888 | \$204,502,253 |
| Liabilities | 800,993,013 | 662,942,836 | 138,050,177 |
| Surplus as regards Policyholders | 342,961,128 | 276,509,052 | 66,452,076 |

Essex Insurance Company

We conclude that the Company is in compliance with the surplus requirements of 18 Del. C. § 511(a), for the kinds of insurance the Company is authorized to write. At December 31, 2007, that requirement amounted to \$750,000.

The assistance of Delaware's consulting actuarial firm, INS Consultants, Inc., is acknowledged.

Respectfully submitted,

Richard McKnight

J. Richard McKnight, CFE, FLMI
Examiner-In-Charge
State of Delaware

SUBSEQUENT EVENTS

On March 3, 2008, the Board of Directors of the Company declared an ordinary dividend of \$95,553,802, which was paid on March 20, 2008, to its sole shareholder of record and Parent, Markel Corporation. This dividend was paid by transfer of securities with a fair market value including accrued income of \$25,499,170.18 and cash in the amount of \$70,054,631.82.

On December 11, 2008, the Company received a capital contribution of securities with a fair market value of \$52,702,322 from its parent, Markel.