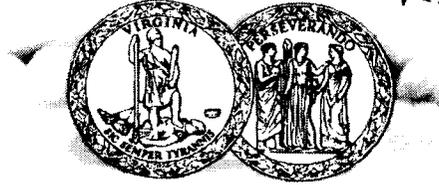


**ASSOCIATION EXAMINATION REPORT**  
**on**  
**COMMONWEALTH DEALERS LIFE**  
**INSURANCE COMPANY**  
**RICHMOND, VIRGINIA**  
**as of**  
**DECEMBER 31, 2010**

# COMMONWEALTH OF VIRGINIA

JACQUELINE K. CUNNINGHAM  
COMMISSIONER OF INSURANCE  
STATE CORPORATION COMMISSION  
BUREAU OF INSURANCE



P.O. BOX 1157  
RICHMOND, VIRGINIA 23218  
TELEPHONE: (804) 371-9741  
TDD/VOICE: (804) 371-9206  
<http://www.scc.virginia.gov/division/boi>

I, Jacqueline K. Cunningham, Commissioner of Insurance of the Commonwealth of Virginia, do hereby certify that the annexed copy of the Examination Report of Commonwealth Dealers Life Insurance Company as of December 31, 2010, is a true copy of the original report on file with this Bureau.

IN WITNESS WHEREOF, I have hereunto set my hand  
and affixed to the original the seal of the Bureau at the City  
of Richmond, Virginia this 15th day of March, 2012

A handwritten signature in cursive script that reads "Jacqueline K. Cunningham".

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Jacqueline K. Cunningham  
Commissioner of Insurance

(SEAL)

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Richmond, Virginia  
December 8, 2011

Honorable Jackie Cunningham  
Commissioner of Insurance  
Virginia Bureau of Insurance  
Richmond, Virginia

Honorable Sharon P. Clark  
Secretary, NAIC Southeastern Zone  
Kentucky Department of Insurance  
Frankfort, Kentucky

Dear Madams:

Pursuant to your instructions and by authority of § 38.2-1317 of the Code of Virginia, a National Association of Insurance Commissioners (NAIC) Association examination of the financial condition, records and affairs of the

**COMMONWEALTH DEALERS LIFE INSURANCE COMPANY**  
Richmond, Virginia

hereinafter referred to as the Company, has been completed. The report thereon is submitted for your consideration.

**DESCRIPTION**

The Company is a stock life insurance company and is licensed under and subject to the general insurance laws contained in Title 38.2 of the Code of Virginia. An examination was last performed as of December 31, 2007. This examination covers the period from January 1, 2008 through December 31, 2010, and was conducted by Examiners from the Virginia State Corporation Commission's (Commission) Bureau of Insurance (Bureau) who represented the NAIC's Southeastern Zone. Notice of the current examination was provided to all applicable NAIC zones.

**HISTORY**

On December 16, 1987, Commonwealth Dealers Life Insurance Company, an Arizona reinsurance Company (CDLIC-A), caused Rebel Insurance Company (Rebel) to be incorporated as a Virginia corporation. CDLIC-A was issued 1,000 shares of common

stock, which constituted all of the issued stock of Rebel, for \$100.00. On February 14, 1989, CDLIC-A contributed an additional \$2,500,000 in capital and surplus to Rebel.

Rebel was formed for the purpose of making formal application to the Commission for a license to write credit life insurance and credit accident and health insurance. On February 28, 1989, the Commission granted such a license to Rebel.

On March 24, 1989, the Commission approved the merger of CDLIC-A into Rebel and on April 17, 1989, the Arizona Department of Insurance approved the merger. Pursuant to the terms of the merger agreement, Rebel's name was changed to Commonwealth Dealers Life Insurance Company, a Virginia corporation. Effective January 1, 1993, North Carolina Life Insurance Company, an Arizona corporation, merged into the Company.

During the September 27, 2007 special meeting of the board, the board authorized and approved the plan of complete liquidation and voluntary dissolution of the Company.

### **MANAGEMENT AND CONTROL**

The Company's bylaws provide that its business and affairs are to be vested in a board of directors of which there shall be no less than five and no more than fifteen, a majority of which shall constitute a quorum. The board of directors are elected at the annual meeting of the stockholders.

The bylaws provide that the officers of the company shall be a chairman of the board, a president, one or more vice presidents, a secretary and a treasurer, who shall be elected by the board of directors. Two or more officers may be combined in one person except for the offices of the president and secretary. At December 31, 2010, the board of directors and elected officers of the Company were as follows:

<b><u>Directors</u></b>	<b><u>Principal Business Affiliation</u></b>
Richard G. Barkhouser	President and Owner Barkhouser Motors Danville, Virginia
Homer E. Derrick, Jr.	President Derrick Enterprises Lexington, Virginia
Richard D. Kern	President and Co-owner Kern Motor Company, Inc. Winchester, Virginia

Donald R. Lacefield	President Don Lacefield Holdings, Inc. Chapel Hill, NC
Joseph H. Nelson	President Davenport Motor Company of Rocky Mount, Inc. Rocky Mount, North Carolina

**Officers****Title**

Richard G. Barkhouser	President, Treasurer and Chairman
Richard D. Kern	Vice President and Secretary

The authorized amount of capital stock of the Company as of December 31, 2010 was 23,500,000 shares and is divided into the following classes:

- 3,500,000 shares with a par value of \$2.00 per share, designated as Voting Common Stock.
- 20,000,000 shares with a par value of \$2.00 per share, designated as B Participating Common Stock (non-voting).

As of December 31, 2010, 398,439 shares of Voting Common Stock and 230,117 shares of the B Participating Common Stock were issued and outstanding. All of the Company's outstanding stock was held by automobile dealers and certain officers and board members of the Company.

**DIVIDEND PAYMENTS TO STOCKHOLDERS**

On October 13, 2009, the Company requested approval for \$978,462 in dividend payments to stockholders. In a letter dated December 1, 2009, the Bureau did not object to the payment of the dividends.

**FIDELITY BOND AND OTHER INSURANCE**

The Company's third party administrator (Fortegra Financial Corporation) maintained fidelity insurance at year-end. The bond covers losses up to \$5,000,000, with a \$150,000 deductible. In addition, the Company maintained property, business liability and officers and directors liability coverages.

## **TERRITORY AND PLAN OF OPERATION**

The Company is licensed in Virginia to transact the business of life, accident and health, credit life and credit accident and health insurance. In addition, the Company is licensed in Delaware, Georgia, Florida, Indiana, Kentucky, Maryland, North Carolina, Ohio, Pennsylvania, South Carolina and Tennessee.

From inception through September 27, 2007, the Company was engaged in the business of direct writing credit life and credit accident and health insurance written through various automobile dealerships, the majority of whom are stockholders of the Company. The Company also wrote credit life and accident and health insurance on American Republic Insurance Company (American Republic) certificates. During a September 27, 2007 board meeting, the board authorized and approved the proposal for the Company to cease writing insurance policies, enter into run-off and, upon completion of such run-off, dissolve and terminate the Company. Since that time, the Company has ceased all ongoing business operations and is limiting its activities to those necessary to complete the run-off process. Effective December 1, 2007, the Company engaged LOTSolutions, Inc. (an affiliate of Fortegra Financial Corporation) to manage the run-off process with respect to the credit life and credit accident and health insurance business. A review of the Company's 2011 board minutes indicated that the run-off of the Company, with the exception of three remaining policies, will be completed by the end of 2014.

## **REINSURANCE**

### **Assumed:**

The Company had two indemnity reinsurance agreements in effect as of December 31, 2010 for assumed business. Under an agreement with American Republic, the Company assumed credit life and credit accident and health (A&H) policies that were originally written by American Republic, but which were produced by automobile dealers through the marketing efforts of the Company. All of the life policies, and the A&H policies issued in the two states where the Company was not licensed, were assumed by the Company. The Company assumed 100% quota share of the mortality and morbidity risks from American Republic on an automatic basis. As of December 31, 2010, the assumed American Republic life policies comprised 87% of the Company's total life reserves, while the assumed American Republic A&H policies were an immaterial portion of the Company's total A&H reserves.

Similarly, under an agreement with LOTS Reassurance Company (LOTS), the Company, through a retrocession, assumed credit A&H policies that were originally written by American Republic, but produced by automobile dealers through the marketing

efforts of the Company. All of the credit A&H policies that were not reinsured via the aforementioned American Republic agreement were ceded to LOTS, and then retroceded to the Company. The Company assumed 100% quota share of the risks from LOTS on an automatic basis. LOTS held the claim reserves and paid premiums on an earned basis, while the Company paid claims as incurred and paid any increase to the claim reserves. Thus, no reserves were held by the Company for this reinsurance.

Ceded:

The Company had two indemnity reinsurance agreements in effect at December 31, 2010 for ceded business. These two treaties were both with Rafiki Reinsurance Limited (Rafiki), an unauthorized alien reinsurer. The two treaties were both effective at the same time, one for credit life and the other for credit A&H business. Under the agreements, the Company reinsured 100% quota share of the mortality and morbidity (on an earned premium basis) risks for a few non-stockholder dealerships on an automatic basis. The amount of credit life and credit A&H reserves ceded to Rafiki was immaterial.

The total reserve credit taken by the Company at December 31, 2010 was only \$38,961. However, since Rafiki is an unauthorized reinsurer, the reinsurance reserve credit was appropriately reported as an offsetting liability in the Company's 2010 Annual Statement.

The Examiners reviewed all reinsurance reserves ceded and assumed for accuracy and no material errors were noted during this review. In addition, all reinsurance agreements were reviewed and found to include insolvency provisions.

### GROWTH OF THE COMPANY

The following data, taken from copies of annual statements filed with the Commission and the financial statements contained in examination reports, reflects the growth of the Company for the ten-year period ending December 31, 2010.

<u>Year</u>	<u>Admitted Assets</u>	<u>Liabilities</u>	<u>Common Capital Stock</u>	<u>Gross Paid-in &amp; Unassigned Funds (Surplus)</u>
2001	\$32,262,169	\$24,698,095	\$1,635,338	\$5,928,736
2002	31,945,537	24,724,122	1,619,578	5,601,837
2003	33,044,474	23,498,917	1,629,578	7,915,979
2004	29,750,755	23,763,907	1,343,542	4,643,306
2005	25,013,776	18,297,629	1,321,942	5,394,205
2006	21,140,225	15,900,626	1,307,942	3,931,657
2007	16,375,704	10,907,127	1,307,942	4,160,635
2008	13,877,998	6,466,658	1,307,942	6,103,398
2009	11,861,016	4,532,588	1,307,942	6,020,486
2010	10,021,920	2,213,482	1,257,112	6,551,326

### Life Insurance in Force

<u>Year</u>	<u>Credit Life</u>
2001	\$425,141,000
2002	422,701,000
2003	418,395,000
2004	398,243,000
2005	358,252,000
2006	290,250,000
2007	228,628,000
2008	134,874,000
2009	71,377,000
2010	33,185,000

## **SCOPE**

This is a full scope financial condition examination initiated and conducted under the provisions of Article 4, Chapter 13 of Title 38.2 of the Code of Virginia. The examination covers the period from January 1, 2008 through December 31, 2010. Assets were verified and liabilities were established at December 31, 2010.

The examination was conducted in accordance with the NAIC Financial Condition Examiners Handbook. The Handbook requires that the Bureau plan and perform the examination to evaluate the financial condition and identify prospective risks of the Company, assess corporate governance, identify and assess inherent risks within the Company, and evaluate system controls and procedures used to mitigate those risks. An examination also includes assessing the principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation, management's compliance with Statutory Accounting Principles and annual statement instructions when applicable to domestic state regulations.

All accounts and activities of the Company were considered in accordance with the risk-focused examination process.

**FINANCIAL STATEMENTS**

There follows a statement of financial condition as of December 31, 2010; a summary of operations for the year ended December 31, 2010; a reconciliation of capital and surplus for the period under review; a statement of cash flow for the year ended December 31, 2010; and a statement of Examiners' changes in capital and surplus at December 31, 2010. The financial statements are presented in accordance with Statutory Accounting Principles.

**ASSETS**

	<u>Assets</u>	Nonadmitted <u>Assets</u>	Net Admitted <u>Assets</u>
Bonds	\$4,877,435		\$4,877,435
Properties held for sale	314,667		314,667
Cash and short-term investments	<u>4,548,123</u>		<u>4,548,123</u>
Subtotals, cash and invested assets	\$9,740,225	\$0	\$9,740,225
Investment income due and accrued	47,411		47,411
Current federal income tax recoverable	229,885		229,885
Net deferred tax asset	11,102	6,703	4,399
Receivables from parent, subsidiaries and affiliates	253,815	253,815	0
Aggregate write-ins for other than invested assets	<u>513,000</u>	<u>513,000</u>	<u>0</u>
Total assets	<u><u>\$10,795,438</u></u>	<u><u>\$773,518</u></u>	<u><u>\$10,021,920</u></u>

**LIABILITIES, SURPLUS AND OTHER FUNDS**

Aggregate reserve for life contracts	\$495,229
Aggregate reserve for accident and health contracts	214,717
Contract claims:	
Life	20,825
Accident and health	114,165
Interest maintenance reserve	1,105,347
General expenses due or accrued	22,125
Taxes, licenses and fees due or accrued	1,399
Remittances and items not allocated	36,724
Dividends to stockholders declared and unpaid	44,368
Miscellaneous liabilities:	
Asset valuation reserve	119,621
Reinsurance in unauthorized companies	38,962
	<hr/>
Total liabilities	\$2,213,482
	<hr/>
Common capital stock	\$1,257,112
Gross paid in and contributed surplus	492,600
Unassigned funds (surplus)	6,058,726
	<hr/>
Total capital and surplus	\$7,808,438
	<hr/>
Total liabilities, capital and surplus	\$10,021,920
	<hr/> <hr/>

**SUMMARY OF OPERATIONS**

Premiums and annuity considerations for life and accident and health contracts	\$222,609
Net investment income	276,773
Amortization of Interest Maintenance Reserve	72,140
Commissions and expense allowances on reinsurance ceded	31,965
Aggregate write-ins for miscellaneous income	42,671
Total	<u>\$646,158</u>
Death benefits	\$272,439
Disability benefits and benefits under accident and health contracts	464,889
Increase in aggregate reserves for life and accident and health contracts	(1,170,541)
Total	<u>(\$433,213)</u>
Commissions on premiums, annuity considerations and deposit-type funds	(9,264)
Commissions and expense allowances on reinsurance assumed	137,130
General insurance expenses	513,597
Insurance taxes, licenses and fees	27,394
Total	<u>\$235,644</u>
Net gain from operations before federal income taxes	\$410,514
Federal income taxes incurred	8,992
Net gain from operations after federal income taxes and before realized capital (losses)	\$401,522
Net realized capital (losses)	(13)
Net income	<u><u>\$401,509</u></u>

**RECONCILIATION OF CAPITAL AND SURPLUS**  
**FOR PERIOD UNDER REVIEW**

	<u>2008</u>	<u>2009</u>	<u>2010</u>
Capital and surplus, December 31, prior year *	<u>\$5,468,577</u>	<u>\$7,411,340</u>	<u>\$7,328,428</u>
Adjustment for previous examination changes	\$76,092		
Net income	1,772,145	968,921	401,509
Change in net unrealized capital gains or (losses)	(97,191)	97,191	
Change in net deferred income tax	(43,459)	(27,799)	(9,669)
Change in nonadmitted assets and related items	(249,370)	(102,693)	14,511
Change in liability for reinsurance in unauthorized companies	450,955	104,015	54,737
Change in asset valuation reserve	74,601	(75,667)	(2,616)
Dividends to stockholders	(41,010)	(1,000,000)	21,538
Aggregate write-ins for gains and losses in surplus		<u>(46,880)</u>	
Net change in capital and surplus for the year	<u>\$1,942,763</u>	<u>(\$82,912)</u>	<u>\$480,010</u>
Capital and surplus, December 31, current year	<u><u>\$7,411,340</u></u>	<u><u>\$7,328,428</u></u>	<u><u>\$7,808,438</u></u>

\* Adjusted capital and surplus from previous examination report

**CASH FLOW****Cash from Operations**

Premiums collected net of reinsurance	\$222,609
Net investment income	307,683
Miscellaneous income	74,636
Total	<u>\$604,928</u>
Benefit and loss related payments	\$817,199
Commissions, expenses paid and aggregate write-ins for deductions	688,382
Federal income taxes (recovered)	(28,089)
Total	<u>\$1,477,492</u>
Net cash from operations	<u>(\$872,564)</u>

**Cash from Investments**

Proceeds from investments sold, matured or repaid:	
Bonds	\$2,900,860
Stocks	190,052
Total investment proceeds	<u>\$3,090,912</u>
Costs of investments acquired (long-term only):	
Bonds	\$133,714
Total investments acquired	<u>\$133,714</u>
Net cash from investments	<u>\$2,957,198</u>

**Cash from Financing and Miscellaneous Sources**

Cash provided (applied):	
Dividends to stockholders	(\$934,094)
Other cash (applied)	(88,982)
Net cash from financing and miscellaneous sources	<u>(\$1,023,076)</u>

**RECONCILIATION OF CASH AND SHORT-TERM INVESTMENTS**

Net change in cash and short-term investments	\$1,061,558
Cash and short-term investments:	
Beginning of the year	3,486,565
End of the year	<u>\$4,548,123</u>

**EXAMINERS' CHANGES IN CAPITAL AND SURPLUS**

	<u>Company</u>	<u>Examiners</u>	Increase (Decrease)
<u>Liabilities, Surplus and Other Funds</u>			
Common capital stock	\$1,307,942	\$1,257,112	(\$50,830)
Unassigned funds	6,007,896	6,058,726	<u>50,830</u>
Examiners' change in capital and surplus			<u><u>\$0</u></u>
Capital and surplus per the Company			\$7,808,438
Capital and surplus per the Examiners			<u>7,808,438</u>
Net change in capital and surplus			<u><u>\$0</u></u>

## RECOMMENDATIONS FOR CORRECTIVE ACTION

### Accounts and Records

1. Common Capital Stock \$1,257,112

The Examiners decreased this account by \$50,830 and increased unassigned funds by the same amount because the stockholders' capital stock account statements were not accurately reconciled to the original stock ledger. The Examiners recommend the Company take appropriate measures to ensure the common capital stock is accurately reported in future filings.

2. Unassigned funds \$6,058,726

The Examiners increased this account by \$50,830 and decreased common capital stock by the same amount because the stockholders' capital stock account statements were not accurately reconciled to the original stock ledger. The Examiners recommend the Company take appropriate measures to ensure the common capital stock is accurately reported in future filings.

### Management and Control

3. The Company was unable to provide conflict of interest statements for any of its officers and directors for 2008 and for two of its officers for 2009. This is the second consecutive examination report in which a recommendation regarding the Company's failure to obtain signed conflict of interest statements for each officer and director has appeared. The Examiners recommend that each director and officer complete a conflict of interest statement on an annual basis to ensure compliance with §§ 38.2-210 and 38.2-211 of the Code.
4. At December 31, 2010, the Examiners noted that the President owned slightly more than ten percent of the Company's voting stock. The ownership percentage in excess of ten percent resulted from redemptions of voting common stock that occurred over a number of years and not through the acquisition of additional shares of such stock. Code of Virginia § 38.2-1323, in part, states that "No person shall acquire or attempt to acquire, through merger or otherwise, control of any domestic insurer...unless the person has previously filed with the Commission...an application for approval of acquisition of control of the insurer...." Code of Virginia § 38.2-1322, in part, states that "Control shall be presumed to exist if any person directly or indirectly owns, controls, holds with the power to vote, or holds proxies representing collectively ten percent or more of the voting securities of any other person." The Examiners recommend the Company take appropriate steps to address this issue.

**SUBSEQUENT EVENTS**

On November 12, 2010, the Company requested approval for \$2,000,000 dividend payments to stockholders. In a letter dated January 20, 2011, the Commission did not object to the payment of the dividends.

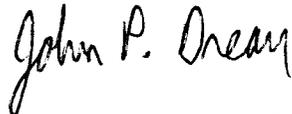
On March 1, 2011, the Company sold its Richmond, Virginia corporate office for \$405,000 and the board ratified this sale.

**CONCLUSION**

The courteous cooperation extended by the officers and employees of the Company during the course of the examination was sincerely appreciated.

In addition to the undersigned, Christopher Collins, AFE; William Knight, AFE; Hai Nguyen and Michael Peterson participated in the work of the examination.

Respectfully submitted,



John P. Drea, CFE  
Senior Insurance Examiner  
Commonwealth of Virginia  
Representing the Southeastern Zone, NAIC

**CDLIC**

STATE CORP. COMMISSION  
BUREAU OF INSURANCE

Commonwealth Dealers Life  
Insurance Company  
4720 Salisbury Road, Suite 20  
Jacksonville, FL 32256

2 MAR 12 AM 8:54

Commonwealth of Virginia  
Commissioner of Insurance  
David H. Smith, Chief Examiner  
P. O. Box 1157  
Richmond, VA 23218

RE: Commonwealth Dealers Life Insurance Company  
Examination Report as of December 31, 2010

Dear Mr. Smith:

As per your letter dated February 8, 2012 and the above referenced exam, it is Commonwealth Dealers Life Insurance Companies intent to not request a hearing regarding any matters identified in the exam report.

Regarding the items listed on page 15 of the exam report that discussed recommendations for corrective action it is Commonwealths intent to address each of these items needing corrective action and to comply with the request of the department. Under Accounts and Records item 1 and 2 – Commonwealth Dealers will keep an accurate account of the Capital Stock and report it accurately in all future filings.

Under the Management and Control section item 3 Commonwealth Dealers will make sure that all officers and directors sign the conflict of interest statements each year and those be kept on file to ensure compliance; item 4 it is Commonwealth Dealers intent to ask the department for an exemption for Richard Barkhouser's excess of A stock and those forms are currently being signed and submitted for review and hopefully approval by the department.

Thank you for your consideration of this response and please let us know if you need anything further.

Sincerely,



Richard Barkhouser  
President and Chairman of the Board

Cc: Kaye Biby