



STATE OF OREGON

DEPARTMENT OF CONSUMER AND BUSINESS SERVICES

INSURANCE DIVISION

REPORT OF FINANCIAL EXAMINATION

OF

**NORTH PACIFIC INSURANCE COMPANY
PORTLAND, OREGON**

NAIC COMPANY CODE 23892

DECEMBER 31, 2007

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SALUTATION

November 3, 2008

Alfred W. Gross, Commissioner
Chairman, NAIC Financial Condition (E) Committee
State Corporation Commission
Bureau of Insurance
Commonwealth of Virginia
PO Box 1157
Richmond, Virginia 23218

Morris J. Chavez, Superintendent
Secretary, NAIC Western Zone IV
PO Drawer 1269
Santa Fe, New Mexico 87504-1269

Honorable Cory Streisinger, Director
Department of Consumer and Business Services
State of Oregon
350 Winter Street NE, Room 440
Salem, Oregon 97301-3883

Dear Commissioner, Superintendent, and Director:

In accordance with your instructions and guidelines in the National Association of Insurance Commissioners (NAIC) Examiners Handbook, pursuant to ORS 731.300 and 731.302, respectively, we have examined the business affairs and financial condition of

**NORTH PACIFIC INSURANCE COMPANY
One Liberty Centre
650 NE Holladay Street
Portland, Oregon 97232**

NAIC Company Code 23892

hereinafter referred to as the "Company." The following report is respectfully submitted.

SCOPE OF EXAMINATION

This regularly scheduled examination of the Company was conducted as of December 31, 2007, covering the five year period then ended, and included a review of material transactions or events which occurred subsequent to the examination cut-off date and were noted during the examination.

The examination was conducted pursuant to ORS 731.300 and in accordance with procedures and guidelines prescribed by the NAIC for the purpose of determining the Company's financial condition, ability to fulfill its obligations, the nature of operations, and compliance with the insurance code. Accounting methods, internal control procedures, records and other supporting evidence were examined or tested by appropriate methods to the extent deemed necessary and appropriate for the type, volume and complexity of the accounting system and operations utilized by the Company. The record testing included, but was not limited to, assets, liabilities, income and expense related items. A review was also made of the corrective actions taken by the Company with respect to comments and recommendations in the previous financial report of examination as of December 31, 2002, published by the Oregon Insurance Division.

Concurrent with this examination, the Company's parent, Liberty Northwest Insurance Corporation, and an affiliate, Oregon Automobile Insurance Company, were also examined as of December 31, 2007. There was a separate report of financial examination made for each company.

COMPANY HISTORY

The Company was incorporated in Oregon on June 26, 1958, and received a Certificate of Authority on July 1, 1958. It was formed as a subsidiary of Oregon Automobile Insurance Company. Its original Certificate of Authority authorized the Company to transact property, casualty (including workers' compensation), marine & transportation, and surety lines.

Ownership of the parent, Oregon Automobile Insurance Company, was held by local interests until 1963, when all outstanding controlling stock was acquired by the American General Insurance Company of Houston, Texas. American General maintained control until November 1965, when it sold its interest to Northwestern National Insurance Company of Milwaukee, Wisconsin. Northwestern National Insurance Company transferred ownership to its parent, NN Corporation, in 1972. NN Corporation was merged into Armco Insurance Group, Inc, in 1980, which held control until acquired by General Accident Insurance Company of America. On July 2, 1998, as a result of the worldwide merger of General Accident, plc, and Commercial Union, plc, a new entity, CGU, plc, became the ultimate controlling parent. On June 1, 2001, the CGU Insurance Group (renamed OneBeacon Insurance Group) was acquired by the White Mountains Insurance Group, Ltd, from GCU, plc. On January 1, 2002, all of the issued and outstanding capital stock of Oregon Automobile Insurance Company was acquired by Liberty Northwest Insurance Corporation. Thereupon, the Company immediately paid a dividend to Liberty Northwest in the form of all issued and outstanding capital stock of the Company, at which point Liberty Northwest became the immediate parent.

During the period under examination, the Company joined the Liberty Mutual Agency Market strategic business unit. As described in the Reinsurance section below, effective January 1, 2006, the Company ceded all of its risks to the lead insurer in the unit, Peerless Insurance Company, at which point the Company became a fronting insurer for Peerless.

Capital Stock

Under Article III of the Article of Incorporation, the Company is authorized to issue 20,000 shares of common stock of \$260 par value common stock. The Company has issued 11,539 shares to its direct parent, Liberty Northwest Insurance Corporation, representing 100% of the shares outstanding. No additional capital was contributed to the Company during the period under examination.

Dividends to Stockholders and Other Distributions

The Company has not declared nor paid any dividends or made any distributions to its stockholder during the period under examination.

MANAGEMENT AND CONTROL

Board of Directors

Management and control of the Company is vested in a Board of Directors. Article III, Section 2, of the Company's Bylaws designates that the Board shall be comprised of not less than five members, the exact number thereof to be fixed by resolution. The Company's Board met all of the requirements of 732.305. As of December 31, 2007, the Company was governed by an eight member Board of Directors as follows:

<u>Name and Address</u>	<u>Principal Affiliation</u>	<u>Member Since</u>
Mary A. Augustyn Tigard, OR	VP of Finance Liberty Northwest Insurance Corporation	2007
Larry W. Becker Portland, OR	President and CEO Liberty Northwest Insurance Corporation	2003
James F. Dore Boston, MA	Treasurer and CFO Liberty Northwest Insurance Corporation	2005
John D. Doyle Southborough, MA	Vice President and Controller, Liberty Mutual Insurance Company	2006
Scott R. Goodby Marblehead, MA	Exec. VP and COO Liberty Northwest Insurance Corporation	2005
Gary R. Gregg Milton, MA	President and CEO Liberty Northwest Insurance Corporation	2005
Thomas H. Johnson* Portland, OR	General Counsel Liberty Northwest Insurance Corporation	2007
Christopher C. Mansfield Dedham, MA	Sr. VP and General Counsel Liberty Mutual Insurance Company	2005

*Thomas Johnson resigned from the Board in May 2008. The vacancy was not filled.

During the period 2003 to 2006, the Board had authorized three committees: an Executive Committee, Audit Committee, and Investment Committee. On November 15, 2006, the Board resolved to disband all three committees.

Officers

Principal officers serving at December 31, 2007 were as follows:

<u>Officer</u>	<u>Office</u>
Gary R. Gregg	President and Chief Executive Officer
Edmund C. Kenealy	Secretary
James F. Dore	Treasurer and Chief Financial Officer
Anthony A. Fontanes	Executive Vice President and Chief Investment Officer
Scott R. Goodby	Executive Vice President and Chief Operations Officer
Joseph A. Gilles	Executive Vice President

CONFLICT OF INTEREST

The Company has established a Code of Business Ethics and Conduct for its directors and senior management. This Code requires officers and directors to report annually any conflicts of interest or violations of ethical business practices to the Company. From a review of the completed conflict of interest questionnaires, it appeared that the affected personnel performed due diligence in completing the conflict of interest statements. No material conflicts of interest were noted.

CORPORATE RECORDS

Board of Director Minutes

In general, the review of 2003 to 2007 Board meeting minutes, as well as the various committees authorized by the Bylaws, indicated that the minutes support the transactions of the Company and the actions taken by its directors and officers. The minutes indicated that the Board approves investments in accordance with the provisions of ORS 733.730 and ORS 733.740. A quorum, as defined by ORS 731.302, met at all of the meetings held during the period under review. As noted earlier, all three committees of the Board were disbanded in 2006, and the Board as a whole now governs the Company's operations.

Articles of Incorporation

One change was made to the Articles of Incorporation during the period under examination. The Company increased the par value of its common stock from \$130 per share to \$260 per share. The Articles of Incorporation conformed with Oregon statutes.

Bylaws

Substantial changes were made to the Bylaws since the last examination:

- 1) The annual meeting date was changed from the 4th Friday in May, held in Portland, to a date, time and place fixed by the Board.
- 2) The number of board members was changed from between five and fifteen, to at least five or the exact number fixed by resolution by the Board.
- 3) Residency requirement for board members was silent in the old bylaws, now at least 1/4 of the Board must be residents of Oregon, and a majority may not be salaried officers of the Corporation.
- 4) Salaried officers formerly included a chairman, vice-chairman, president, vice-president, secretary and chief financial officer. New Bylaws require a president, a secretary and a treasurer.

The Bylaws conformed with Oregon statutes.

Holding Company Registration Statement

A holding company registration statement was filed for each year of this examination by the Company's parent, Liberty Northwest Insurance Corporation, in accordance with the provisions of ORS 732.552, ORS 732.554, and Oregon Administrative Rule (OAR) 836-027-0020(1).

Parent, Subsidiaries and Affiliates

The Company is part of a holding company system in which Liberty Mutual Holding Company, Inc. (LMHC), is the ultimate controlling entity. LMHC was formed after the demutualization of Liberty Mutual Insurance Company during 2001, under a mutual holding company system owned by the former policyholders of Liberty Mutual Insurance Company.

Other significant subsidiaries of LMHC include as follows:

LMHC Massachusetts Holdings, Inc. – a Massachusetts corporation 100% owned by LMHC.

It acts as an intermediate stock holding company within the mutual holding company system.

Liberty Mutual Group, Inc. (LMG) – a Massachusetts stock holding company 100% owned by LMHC Massachusetts Holdings. Liberty Mutual Group is based in Boston, Massachusetts, and through its subsidiaries has operations throughout the United States, employing approximately 41,000 people in over 900 offices worldwide.

Liberty Mutual Insurance Company (LMIC) – a Massachusetts stock property and casualty insurance company 100% owned by LMG.

Liberty Mutual Investment Advisors LLC (LMIA) – a Massachusetts limited liability company and an indirect subsidiary of LMIC. It was formed for the purpose of making, holding, and administering investments in designated asset sectors for the insurance companies within LMG.

Liberty Northwest Insurance Corporation (LNW) – an Oregon-domiciled stock property and casualty insurer 100% owned by LMIC. LNW owns all of the outstanding shares of the Company's common stock and would be considered the direct parent.

Affiliates of the Company include the following:

Oregon Automobile Insurance Company (OAIC) – an Oregon-domiciled stock property and casualty insurer.

Liberty Management Services, Inc. (LMS) – an Oregon corporation formed in 1987 as a claims servicing company, providing operational support for employers that are self-insured for workers' compensation.

Access Insurance Services Company (AISC) – an Oregon corporation formed in 2000 as an insurance agency to market property and casualty business.

Intercompany Agreements

The Company was party to the following agreements with its parent and affiliates as of December 31, 2007:

Memorandum of Understanding

The Company entered into an undated memorandum of understanding (MOU) with LNW, which specifies the general terms wherein common facilities and personnel may be shared. The MOU stated reimbursements are generally based on actual expenses.

Management Services Agreement

Effective January 1, 2006, the Company and LMIC entered into an agreement whereby LMIC will provide; a) accounting, financial, tax and auditing services, b) purchasing, payroll and employee benefits, c) information technology and support, d) policy administration and production, e) real estate management, f) legal, g) general administration, h) miscellaneous, and i) reinsurance negotiations. The Company will pay a reasonable fee to LMIC, including direct expenses and allocated expenses. There is no expiration date, but either party may terminate the agreement with 90 days written notice. An amendment dated December 31, 2007, requires all amounts owing between the parties be settled within 45 days of the end of each calendar quarter.

Cash Management Agreement

Effective February 22, 2002, the Company entered into an agreement with LMIA to make, hold, and administer certain positions in short-term investments. Compensation will be a fee equal to the reasonable expense of providing legal, auditing, investment, accounting and money management services, in addition to reimbursement of direct commissions, transaction fees, and custodial fees incurred. Exhibit A of the agreement described the permitted assets allowed for purchase. The agreement has no expiration date, but may be terminated immediately upon written notice by the Company, or with 30 days' written notice by LMIA.

Investment Management Agreement

Effective February 22, 2002, the Company entered into an agreement with LMIA to act as discretionary investment manager of all the invested assets held by the Company, subject to the guidelines, limitations, and objectives set by the Company's Board of Directors. The agreement terminates five years from execution, and may be renewed for a period not to exceed five years. Fees are charged monthly, equal to 3.4 basis points (annualized) on the average monthly par value of bonds and market value of equities. Effective January 1, 2007, LMIC replaced LMIA on an identical agreement.

Tax Sharing Agreement

On January 1, 2002, the company joined Liberty Mutual Holding Company, Inc., (LMHC) in a tax-sharing agreement. Under the agreement, the taxes payable shall be based on the separate tax return liability of each tax reporting segment, adjusted for any carryover,

carryback, credit, or other attribute. Estimated tax payments are due no later than the 12th day of April, June, September and December of each tax year.

FIDELITY BOND AND OTHER INSURANCE

The Company is covered against losses through a fidelity bond for risks up to \$125,000,000 in the aggregate, after a \$1,000,000 retention. This coverage was found to comply with the limits recommended by the NAIC. The Company is insured for directors and officers liability for losses up to \$125,000,000 in aggregate, after a \$25,000,000 deductible. Other major insurance coverages in force included company securities, financial institution bond, and workers' compensation. All coverages appeared adequate as of December 31, 2007.

STATUTORY DEPOSIT

The Company has a deposit with the Oregon Insurance Division, Department of Consumer Business Services, pursuant to the provisions of ORS 731.604 and 731.628. The deposit consisted of US Treasury Notes with a par value of \$1,150,000.

TERRITORY AND PLAN OF OPERATION

During the period under examination, the Company wrote property and casualty business, including a comprehensive set of personal and commercial coverages, through independent agents. At December 31, 2007, the Company wrote direct premiums in four of the six states in which it is licensed, as follows:

Alaska	\$	0
Idaho		15,691,656
Montana		2,078,370
Oregon		70,161,003
Utah		0
Washington		<u>60,405,258</u>
Total Direct Premium		<u>\$ 148,336,287</u>

The Company is a member of the Liberty Mutual Agency Market (LMAM) strategic business unit, which offers agribusiness protection, commercial lines, personal lines, and workers' compensation. It writes business in the Northwest Region under the following brands: American Fire and Casualty Company, Indiana Insurance Company, Liberty Northwest Insurance Corporation, North Pacific Insurance Company, The Ohio Casualty Insurance Company, Ohio Security Insurance Company, Oregon Automobile Insurance Company, Peerless Insurance Company and West American Insurance Company.

For the Northwest Region (which includes AK, ID, MT, OR, and WA), the Liberty Mutual group has established 17 sales offices staffed by approximately 800 employees.

GROWTH OF THE COMPANY

The growth of the Company since the last financial examination is reflected in the following schedule. The amounts were derived from Company's filed annual statements, except in those years where a report of examination has been published by the Oregon Insurance Division.

<u>Year</u>	<u>Assets</u>	<u>Liabilities</u>	<u>Surplus and Other Funds</u>	<u>Net Income (Loss)</u>
2002*	\$ 6,300,000	\$ 0	\$6,300,000	\$ 0
2003	7,845,720	1,545,720	6,300,000	0
2004	6,300,000	0	6,300,000	0
2005	6,300,000	0	6,300,000	0
2006	35,169,208	28,648,970	6,520,238	220,238
2007*	30,035,573	23,193,346	6,842,227	340,989

*Per examination

The changes in assets and liabilities reported in 2006 and 2007 were due to the effects of the 100% quota-share reinsurance agreement with Peerless Insurance Company.

LOSS EXPERIENCE

The following exhibit reflects the annual underwriting results of the Company over the last five years. The amounts were compiled from copies of the Company's filed annual statements and, where indicated, from examination reports.

<u>Year</u>	(1) <u>Premium Earned</u>	(2) <u>Losses and LAE Incurred</u>	(3) <u>Other Underwriting Expenses Incurred</u>	(2)+(3)/(1) <u>Combined Ratio</u>
2002*	\$0	\$0	\$0	0.0%
2003	0	0	0	0.0%
2004	0	0	0	0.0%
2005	0	0	0	0.0%
2006	0	0	0	0.0%
2007*	0	0	0	0.0%

*Per examination

REINSURANCE

Effective January 1, 2006, the Company entered into a 100% quota-share reinsurance agreement with an affiliate, Peerless Insurance Company, the lead insurer in the Liberty Mutual Agency Market strategic business group. The agreement calls for Peerless to assume all risks from first dollar.

Assumed Business

The Company did not assume any significant business.

Ceded Business

The quota share reinsurance agreement with Peerless described above is further broken down into nine contracts covering different layers and lines of business.

All Lines Casualty Excess of Loss

- \$10 million excess of \$10 million (\$15 million maximum for Terrorism)

Property Excess of Loss Reinsurance

- \$25 million excess of \$25 million
- \$50 million excess of \$50 million

Property Catastrophe Excess of Loss Reinsurance

- \$50 million excess of \$50 million
- \$50 million excess of \$100 million
- \$50 million excess of \$150 million
- \$50 million excess of \$200 million
- \$50 million excess of \$250 million
- \$50 million excess of \$300 million

Property Catastrophe Excess of Loss Reinsurance

- \$200 million excess of \$500 million
- \$350 million excess of \$750 million
- \$300 million excess of \$1,100 million
- \$250 million excess of \$1,400 million
- \$300 million excess of \$1,650 million

Workers' Compensation Clash Excess of Loss Reinsurance

- \$5 million excess of \$5 million ultimate net loss, any one loss occurrence

Workers' Compensation Catastrophe Excess of Loss Reinsurance

- \$75 million excess of \$25 million (excludes Terrorism)
- \$100 million excess of \$100 million
- \$300 million excess of \$200 million

Workers' Compensation Catastrophe Excess of Loss Reinsurance

- \$200 million excess of \$500 million (excludes Terrorism)
- \$300 million excess of \$700 million
- \$200 million excess of \$1,000 million (excludes CA earthquake)

Multi-line Terrorism Aggregate Excess of Loss Reinsurance

- \$200 million in excess of aggregate ultimate loss of \$150 million, subject to recoveries under TRIA of 2002 and Extension Act of 2005

Commercial Umbrella Excess of Loss Reinsurance

- Peerless is liable for 100% of the net loss in excess of \$5 million for each and every loss, each and every occurrence, not to exceed \$10 million.

Risk Retention and Transfer

The Company retained no risk on any one insured. As such, the Company was in compliance with the provisions of ORS 731.504. In addition, it was determined that the Company's pooled reinsurance agreements are reported in accordance with the requirements specified in the NAIC Accounting Practices and Procedures Manual, SSAP No. 63.

Insolvency Clause

Each of the reinsurance agreements contained a proper insolvency clause that specified payments would be made to a statutory successor without diminution in the event of insolvency, as required by the provisions of ORS 731.508.

ACCOUNTS AND RECORDS

In general, the Company's accounting and corporate records were maintained in a manner in which the financial condition was verifiable as required by the provisions of ORS 733.170, however, the examiners experienced significant delays in getting information from the Boston offices of Liberty Mutual Insurance Company. The Company should be aware of the provisions of ORS 731.308(3), which require timely and convenient access to records and require the officers, directors, employees and agents of the insurer to facilitate the examination.

The Company maintained its accounting records on a Statutory Accounting Principles (SAP) basis for NAIC Annual Statement reporting and adjusts to a Generally Accepted Accounting Principles (GAAP) basis of accounting for its purposes. The Company, as part of the combined Peerless Insurance Company Pool, is audited annually by the certified public accounting firm of Ernst & Young LLP. The Company (prior to 2006) and the combined

companies received an unqualified opinion for all years under review. The Company's accounting procedures, internal controls, and transaction cycles were reviewed during the planning and testing phase of the examination and no material exceptions were noted.

The following issues were noted as result of this examination:

Schedule P

The Company did not provide a copy of Schedule P with the 2007 annual statement filed with the Oregon Insurance Division and the NAIC I-Site electronic database. Due to the intercompany quota-share agreement, the Company retained no risk, and believed they were not required to complete the filing. At the request of the Oregon Insurance Division, the Company did complete a Schedule P and submitted it on May 28, 2008.

According to the NAIC Annual Statement Instructions for Property/Casualty manual, unless an insurer is party to a pooling arrangement and the lead insurer in the pool assumes 100% of the risks, the insured companies will be required to complete Schedule P.

I recommend the Company file Schedule P with all future filings of the annual statements in accordance with NAIC Annual Statement Instructions and ORS 731.574(1).

COMPLIANCE WITH PRIOR EXAMINATION RECOMMENDATIONS

The Company took corrective action with respect to the one recommendation made in the 2002 report of examination. The follow-up report was prepared on December 14, 2004.

SUBSEQUENT EVENT

On December 16, 2008, the director issued an Order of Exemption, Case No. INS 08-12-007, regarding a LMIC request dated October 27, 2008, to contribute on or before December 31, 2008, the shares of LNW downstream through intervening holding companies and ultimately to Peerless Insurance Company (“PIC”), a downstream subsidiary. Because the Company and OAIC were wholly-owned subsidiaries of LNW, they, along with two non-insurance subsidiaries of LNW, would become indirect wholly-owned subsidiaries of PIC.

The director determined the contribution of shares did not have the effect of changing or influencing the control or ownership of a domestic insurer since LMIC and LMHC would remain controlling parties of LNW, the Company, and OAIC as before the contribution. The proposed transaction thereby met the requirements for exemption from the provisions of ORS 732.521(1) pursuant to ORS 732.521(2).

FINANCIAL STATEMENTS

The following examination financial statements show the financial condition of North Pacific Insurance Company:

- Assets
- Liabilities, Surplus and Other Funds
- Summary of Operations
- Reconciliation of Surplus for the Period Since the last Examination

The financial statements are presented on the basis of statutory accounting practices permitted or prescribed by the Oregon Insurance Division as of December 31, 2007.

NORTH PACIFIC INSURANCE COMPANY
ASSETS
December 31, 2007

ASSETS	Balance Per Company	Examination Adjustments	Balance Per Examination	Notes
Bonds	\$ 8,362,039	\$ -	\$ 8,362,039	1
Cash, cash equivalents and short-term investments	1,300,604		1,300,604	1
Aggregate write-ins for invested assets	-		-	
Subtotal, cash and invested assets	<u>9,662,643</u>	<u>-</u>	<u>9,662,643</u>	
Investment income due and accrued	92,586		92,586	
Reinsurance				
Amounts recoverable from reinsurers	6,681,278		6,681,278	
Receivable from parent, subsidiaries and affiliates	13,370,085		13,370,085	
Aggregate write-ins for other than invested assets	228,981		228,981	
From Separate Accounts, Segregated Accounts and Protected Cell Accounts	-		-	
Total Assets	<u>\$ 30,035,573</u>	<u>\$ -</u>	<u>\$ 30,035,573</u>	

NORTH PACIFIC INSURANCE COMPANY
LIABILITIES, SURPLUS AND OTHER FUNDS
December 31, 2007

	Balance Per Company	Examination Adjustments	Balance Per Examination	Notes
LIABILITIES, SURPLUS AND OTHER FUNDS				
Losses	\$ -	\$ -	\$ -	2
Reinsurance payable on paid loss and loss adjustment expenses	79,761		79,761	
Loss adjustment expenses	-		-	2
Current federal and foreign income taxes	97,879		97,879	
Net deferred tax liability	19,000		19,000	
Ceded reinsurance premiums payable	14,041,253		14,041,253	
Payable to parent, subsidiaries and affiliates	8,955,453		8,955,453	
Protected cells liabilities	-		-	
Total Liabilities	<u>\$ 23,193,346</u>	<u>\$ -</u>	<u>\$ 23,193,346</u>	
Common capital stock	3,000,140		3,000,140	
Gross paid in and contributed surplus	178,204		178,204	
Unassigned funds (surplus)	<u>3,663,883</u>	<u>-</u>	<u>3,663,883</u>	
Surplus as regards policyholders	<u>\$ 6,842,227</u>	<u>-</u>	<u>\$ 6,842,227</u>	
Total Liabilities, Surplus and other Funds	<u><u>\$ 30,035,573</u></u>	<u><u>\$ -</u></u>	<u><u>\$ 30,035,573</u></u>	

NORTH PACIFIC INSURANCE COMPANY
STATEMENT OF INCOME
For the Year Ended December 31, 2007

	Balance Per Company	Examination Adjustments	Balance Per Examination	Notes
UNDERWRITING INCOME				
Premiums earned	\$ -	\$ -	\$ -	
Deductions:				
Losses incurred	-		-	
Loss expenses incurred	-		-	
Other underwriting expenses incurred	-		-	
Aggregate write-ins for underwriting deductions	-		-	
Total underwriting deductions	-		-	
Net underwriting gain or (loss)	-		-	
INVESTMENT INCOME				
Net investment income earned	510,067		510,067	
Net realized capital gains or (losses)	(181)		(181)	
Net investment gain or (loss)	509,886		509,886	
OTHER INCOME				
Net gain or (loss) from agents' or premium balances charged off	-		-	
Finance and service charges not included in premiums	-		-	
Aggregate write-ins for miscellaneous income	-		-	
Total other income	-		-	
Dividends to policyholders	-		-	
Federal and foreign income taxes incurred	168,897	-	168,897	
Net income	\$ 340,989	\$ -	\$ 340,989	

NORTH PACIFIC INSURANCE COMPANY
RECONCILIATION OF SURPLUS FOR THE PERIOD SINCE LAST
EXAMINATION
For the Year Ended December 31, 2007

	<u>2007</u>	<u>2006</u>	<u>2005</u>	<u>2004</u>	<u>2003</u>
Surplus as regards policyholders, December 31, previous year	<u>\$6,520,238</u>	<u>\$6,300,000</u>	<u>\$6,300,000</u>	<u>\$6,300,000</u>	<u>\$6,300,000</u>
Net Income	340,989	220,238	0	0	0
Net transfers (to) from Protected Cell accounts	0	0	0	0	0
Change in unrealized capital gains (losses)	0	0	0	0	0
Change in net unrealized foreign exchange capital gain (loss)	0	0	0	0	0
Change in net deferred income tax	(19,000)	0	0	0	0
Change in nonadmitted assets	0	0	0	0	0
Change in provisions for reinsurance	0	0	0	0	0
Change in surplus notes	0	0	0	0	0
Cumulative effect of changes in accounting principles	0	0	0	0	0
Capital changes					
Paid in	0	1,500,070	0	0	0
Transferred from surplus (Stock Dividend)	0	0	0	0	0
Transferred to surplus	0	0	0	0	0
Surplus adjustments					
Paid in	0	(1,500,070)	0	0	0
Transferred to capital (Stock Dividend)	0	0	0	0	0
Tranferred from capital	0	0	0	0	0
Net remittances from or (to) Home Office	0	0	0	0	0
Dividends to stockholders	0	0	0	0	0
Change in Treasury Stock	0	0	0	0	0
Examination Adjustments	0	0	0	0	0
Aggregate write-ins for gains and losses in surplus	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
Net change in capital and surplus for the year	<u>321,989</u>	<u>220,238</u>	<u>0</u>	<u>0</u>	<u>0</u>
Surplus as regards policyholders, December 31, current year	<u>\$6,842,227</u>	<u>\$6,520,238</u>	<u>\$6,300,000</u>	<u>\$6,300,000</u>	<u>\$6,300,000</u>

NOTES TO THE FINANCIAL STATEMENTS

Note 1 - Investments

All of the Company's long-term bond investments were in US Treasury obligations. Cash and short-term deposits consisted of cash on deposit, a US Treasury bond, and two short-term money market funds. A comparison of the investments over the past five years is as follows:

<u>Year</u>	<u>A</u> <u>Bonds</u>	<u>B</u> <u>Cash and</u> <u>Short-term</u>	<u>Ratio</u> <u>A/</u> <u>Total Assets</u>	<u>Ratio</u> <u>B/</u> <u>Total Assets</u>
2003	\$6,523,568	\$ 1,322,152	83.1%	16.9%
2004	6,768,553	(2,892,171)	107.4%	(45.9)%
2005	6,972,858	(3,362,072)	110.7%	(53.4)%
2006	6,372,061	(3,085,462)	18.1%	(8.8)%
2007	8,362,039	1,300,604	27.8%	4.3%

The Board of Directors approved the investment transactions pursuant to ORS 733.740. As of December 31, 2007, invested assets of \$8,362,039, representing 86.5% of the total invested assets, were invested in amply secured obligations of the United States. This exceeded the amount that must be invested in these types of assets as required by ORS 733.580.

The Company entered into a global custody agreement with JP Morgan Chase dated January 10, 2002. This agreement did not contain a protection required under OAR 836-027-0200(4)(f), stating the custodian agrees to notify the Director of DCBS within three business days in the event the agreement is terminated or if 100% of the assets are withdrawn from any one custodial account. **I recommend the Company amend its custodial agreement with JP Morgan Chase to contain all of the protections of OAR 836-027-0200(4).**

Note 2 – Actuarial Reserves

The Company did not report loss reserves as a result of the 100% quota-share reinsurance agreement, under which 100% of losses were ceded to Peerless Insurance Company.

SUMMARY OF COMMENTS AND RECOMMENDATIONS

In addition to the following recommendations, DCBS has presented the Company with a management letter containing matters not considered material for purposes of this examination.

Page

- 18 I recommend the Company file Schedule P with all future filings of the annual statements in accordance with NAIC Annual Statement Instructions and ORS 731.574(1).
- 24 I recommend the Company amend its custodial agreement with JP Morgan Chase to contain all of the protections of OAR 836-027-0200(4).

CONCLUSION

During the five year period covered by this examination, the surplus of the Company has increased from \$6,300,000, as presented in the December 31, 2002, report of examination, to \$6,842,227, as shown in this report of examination. There were no adjustments made to the financial statements as a result of this examination. The comparative assets and liabilities are shown below:

	<u>2007</u>	<u>December 31,</u> <u>2002</u>	<u>Change</u>
Assets	\$30,035,573	\$6,300,000	\$23,735,573
Liabilities	<u>23,193,346</u>	<u>0</u>	<u>(23,193,346)</u>
Surplus	<u>\$ 6,842,227</u>	<u>\$6,300,000</u>	<u>\$ 542,227</u>

ACKNOWLEDGMENT

The cooperation and assistance extended by the officers and employees of the Company during the examination process are gratefully acknowledged.

In addition to the undersigned, Mark Giffin, CFE, and Michael P. Phillips, CFE, CPA, AES, insurance examiners for the State of Oregon, Department of Consumer and Business Services, Insurance Division, participated in the examination.

Respectfully submitted,

Greg A. Lathrop, CFE
Supervising Insurance Examiner
Department of Consumer and Business Services
State of Oregon

AFFIDAVIT

STATE OF OREGON)
) ss
County of Marion)

Greg A. Lathrop, CFE, being duly sworn, states as follows:

1. I have authority to represent the state of Oregon in the examination of North Pacific Insurance Company, Portland, Oregon.

2. The Insurance Division of the Department of Consumer and Business Services of the state of Oregon is accredited under the National Association of Insurance Commissioners Financial Regulation Standards and Accreditation.

3. I have reviewed the examination work papers and examination report, and the examination of North Pacific Insurance Company was performed in a manner consistent with the standards and procedures required by the Oregon Insurance Code.

The affiant says nothing further.

Greg A. Lathrop, CFE
Supervising Financial Examiner
Department of Consumer and Business Services
State of Oregon

Subscribed and sworn to me this _____ day of _____, 2009.

Notary Public for the State of Oregon

My Commission Expires: _____