

**EXAMINATION REPORT**  
**OF**  
**KNIGHT SPECIALTY INSURANCE COMPANY**  
**AS OF**  
**DECEMBER 31, 2022**

TRINIDAD NAVARRO  
COMMISSIONER



STATE OF DELAWARE  
DEPARTMENT OF INSURANCE

REPORT ON EXAMINATION  
OF  
KNIGHT SPECIALTY INSURANCE COMPANY  
AS OF  
DECEMBER 31, 2022

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.

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Trinidad Navarro  
Insurance Commissioner

Dated this 3 day of June, 2024

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May 22, 2024

Honorable Trinidad Navarro  
Commissioner of Insurance  
Delaware Department of Insurance  
1351 West North Street, Suite 101  
Dover, Delaware 19904

Dear Commissioner:

In compliance with instructions and pursuant to statutory provisions contained in Examination Certification No. 23.026, dated January 13, 2023, an examination has been made of the affairs, financial condition and management of

**KNIGHT SPECIALTY INSURANCE COMPANY**

hereinafter referred to as the Company or KSIC. The Company was incorporated under the laws of the State of Delaware as a stock company with its registered office located at 1807 North Market Street, Wilmington, Delaware 19802. The administrative offices of the Company are located at 4751 Wilshire Boulevard #111, Los Angeles, California 90010.

**SCOPE OF EXAMINATION**

We have performed our multi-state examination of the Company. The last examination was conducted as of December 31, 2019, and covered the three-year period from January 1, 2017 through December 31, 2019. This examination covers the three-year period from January 1, 2020 through December 31, 2022, and encompasses a general review of transactions during the period, the Company's business policies and practices, as well as management and relevant corporate

matters, with a determination of the financial condition of the Company as of December 31, 2022. Transactions subsequent to the examination date were reviewed where deemed necessary.

We conducted our examination in accordance with the *National Association of Insurance Commissioners (NAIC) Financial Condition Examiners Handbook* (Handbook) and generally accepted statutory insurance examination standards consistent with the Insurance Code and Regulations of the State of Delaware. The NAIC Handbook requires that we plan and perform the examination to evaluate the financial condition, assess corporate governance, identify current and prospective risks of the Company and evaluate system controls and procedures used to mitigate those risks. An examination also includes identifying and evaluating significant risks that could cause an insurer's surplus to be materially misstated both currently and prospectively.

All accounts and activities of the Company were considered in accordance with the risk-focused examination process. This may include assessing significant estimates made by management and evaluating management's compliance with Statutory Accounting Principles. The examination does not attest to the fair presentation of the financial statements included herein. If, during the course of the examination an adjustment is identified, the impact of such adjustment will be documented separately following the Company's financial statements.

This examination report includes significant findings of fact, pursuant to the General Corporation Law of the State of Delaware as required by 18 *Del. C.* § 321, along with general information about the insurer and its financial condition. There may be other items identified during the examination that, due to their nature, are not included within the examination report but are separately communicated to other regulators and/or the Company.

During the course of this examination, consideration was given to work performed by the Company's external accounting firm, RSM US LLP (RSM). Certain auditor work papers from

the December 31, 2022, and 2021 audit of the Company have been incorporated into the work papers of the examiners and have been utilized in determining the scope, areas of emphasis in conducting the examination and in the area of risk mitigation and substantive testing.

### **SUMMARY OF SIGNIFICANT FINDINGS**

The examination found the Company's investment in Hankey Capital, LLC (HC) in the amount of \$42.0 million as of December 31, 2022, did not comply with 18 *Del. C.* §1328 (2). The investment was subsequently disposed of and replaced with qualifying assets. As a result, there was no adjustment to the financial statements as reported by the Company as of December 31, 2022.

The examination found the Company's investment in Hankey Cash Management LLC (HCM) in the amounts of \$34.7 million as of December 31, 2022, did not comply with 18 *Del. C.* § 1328 (2). The investment was subsequently disposed of and replaced with qualifying assets. As a result, there was no adjustment to the financial statements as reported by the Company as of December 31, 2022.

The examination found the Company's investments in the publicly traded asset-backed securities issued by Westlake Financial Services (WFS) exceeded the investment limitation of 18 *Del. C.* § 1305 (1) by \$31.3 million as of December 31, 2022. The investment was subsequently disposed of and replaced with qualifying assets. As a result, there was no adjustment to the financial statements as reported by the Company as of December 31, 2022.

The examination found the trust agreement supporting the Company's reinsurance agreements with Knight Insurance Company Segregated Portfolio Company (KIC SPC) for the benefit of Hankey Re Segregated Portfolio Company (Hankey Re SPC) and Wilshire Re Segregated Portfolio Company (Wilshire Re SPC) did not comply with 18 *Del. C.* § 912, § 913

and 18 *Del. Admin. Code* § 1003-7.0 as of December 31, 2022. The trust agreement was subsequently terminated and replaced with a funds withheld arrangement, requiring a transfer of funds back to the Company from the reinsurer. The form of underlying collateral complies with all statutes and regulations. As a result, there was no adjustment to the financial statements as reported by the Company as of December 31, 2022.

## **COMPANY HISTORY**

The Company was incorporated under the laws of the State of Delaware on July 10, 2013, and began business on April 16, 2014. The Company was formed to write excess and surplus lines of insurance, with a significant portion of its business to be reinsured by its direct parent, Knight Insurance Company, Ltd. (KIC).

### **Capitalization**

The Company's Certificate of Incorporation authorizes the issue of 1,000,000 shares of common stock with a par value of \$1.00 per share. As of December 31, 2022, the Company had 1,000,000 common shares issued and outstanding totaling \$1,000,000. All outstanding common shares of the Company are owned by KIC. As of December 31, 2022, the Company reported gross paid-in and contributed surplus of \$44,274,388. There were no changes in capitalization during the examination period.

### **Dividends**

No stockholder dividends were declared or paid during the examination period.

## **MANAGEMENT AND CONTROL**

### **Directors**

Pursuant to the general Corporation Laws of the State of Delaware, as implemented by the Company's Certificate of Incorporation and bylaws, the business and affairs of the Company are

managed by or under the direction of its Board of Directors (Board). The Company's bylaws require that its Board consists of not less than three (3) or more than ten (10) members. Each Director is elected annually by the stockholder and holds office until the next annual election and until their successors are elected and qualified except as removed for cause and the successor elected by a special meeting of the stockholder. Directors duly elected and serving as of December 31, 2022, were as follows:

<u>Name</u>	<u>Title</u>
Don Robert Hankey	Chairman of the Board and Chief Executive Officer Hankey Group
Bret Conrad Hankey	President, Hankey Group
Amit Bhartkumar Shah	President, Knight Insurance Group
Gracia Slamet	Chief Financial Officer, Hankey Investment Company
John Martin Rygh	Secretary and General Counsel, Knight Insurance Group

#### Officers

Officers were elected by the Board in accordance with the bylaws during the period under examination. Elected officers may be a Chairman of the Board, President, Chief Executive Officer, Vice-President, Secretary and Treasurer. The Board may also elect or appoint additional Vice-Presidents, one or more Assistant Secretaries and Assistant Treasurers or other officers as deemed necessary. Any number of offices may be held by the same person. The primary officers serving as of December 31, 2022, were as follows:

<u>Name</u>	<u>Title</u>
Don Robert Hankey	Chairman and Chief Executive Officer
Amit Bhartkumar Shah	President
Jacqueline Leung	Chief Financial Officer and Treasurer
Robert Witold Jozwik *	Secretary and General Counsel
Bret Conrad Hankey	Assistant Secretary

\* Mr. Jozwik resigned effective at the close of business on November 30, 2023.



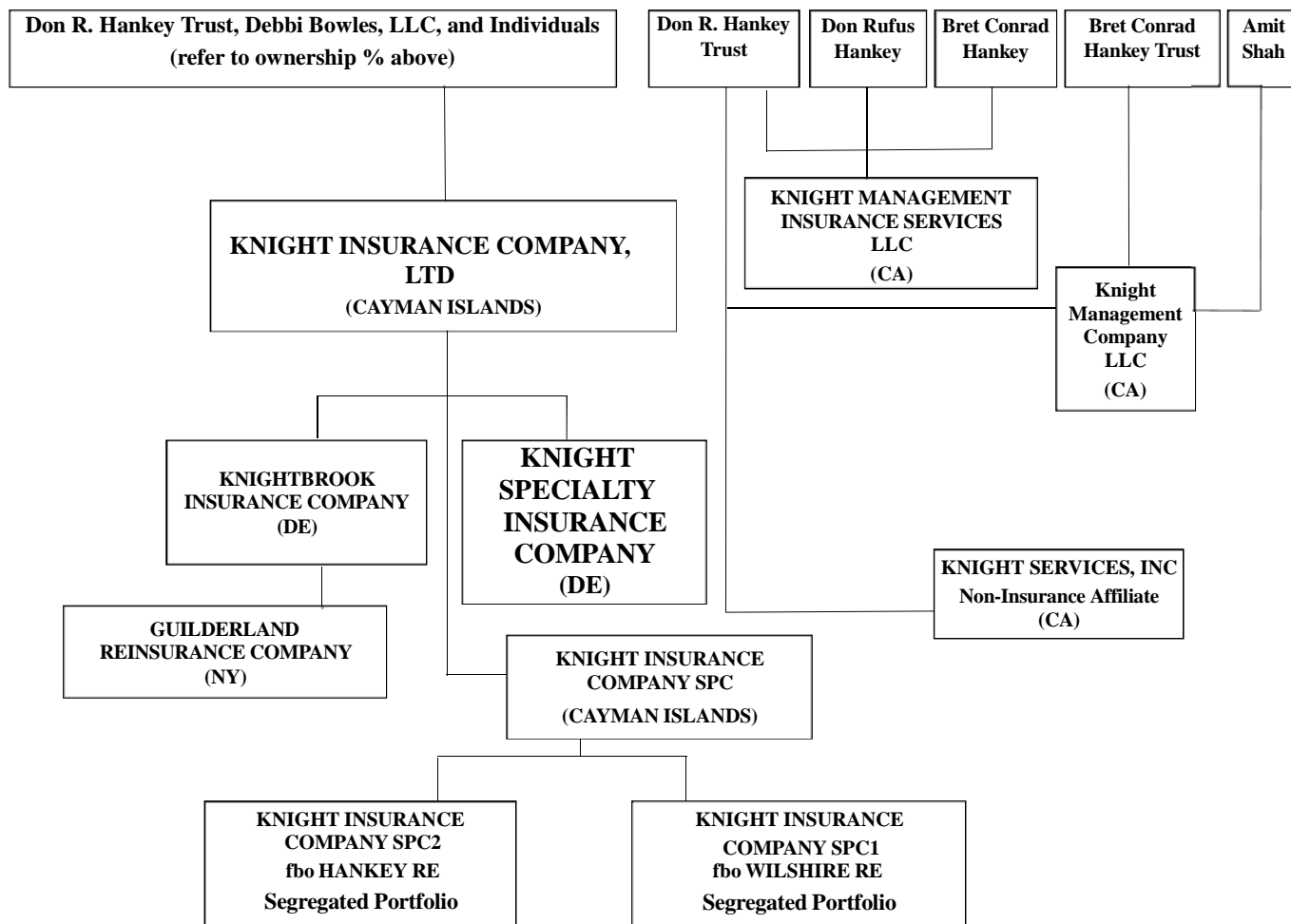
### Corporate Records

The recorded minutes of the shareholder and Board were reviewed for the period under examination. The recorded minutes of the Board adequately documented its meetings and approval of Company transactions and events including approval of investment transactions in accordance with 18 *Del. C.* § 1304. In addition, review of Company files indicated that written correspondence was submitted to the Department regarding changes in officers and directors during the period under examination in compliance with 18 *Del. C.* § 4919.

### Insurance Holding Company System

The Company is a member of an insurance holding company system known as the Knight Insurance Group (Group) as defined under 18 *Del. C.* § 5001 of the Delaware Insurance Code. The ultimate controlling party of the Group wholly owns KSIC's direct parent KIC, as follows: 94.25% by Don R. Hankey Trust, 2.29% by Debbi Bowles, LLC, 1.42% by Amit Bhartkumar Shah, 1.14% by Bret Conrad Hankey, 0.78% by Don Rufus Hankey, 0.10% by Jacqueline Leung, 0.01% by Aditya Samanta and 0.01% by Letian Zhao.

The following page has an organizational chart of the Group that reflects the legal entities and affiliated relationships within the insurance holding company system as of December 31, 2022:



Agreements with Affiliates

The following agreements with affiliates were in effect as of December 31, 2022:

*Management Agreement*

Effective November 1, 2013, KSIC and Knight Management Insurance Services, LLC (KMIS) became parties to an agreement, whereby KMIS provides management and administration services that includes, but not limited to, regulatory services, home office services, accounting services, claims management, accounting and cash records management, capital and other resources necessary to carry out the services specified in the agreement. Under the terms of the

agreement, KSIC will reimburse and compensate KMIS for reasonable out-of-pocket expenses incurred.

*Amended and Restated Underwriting Management Agreement*

Effective June 1, 2020, KSIC entered into an agreement with Knight Management Company LLC (KMC). Under the terms of the agreement, KMC will solicit, accept and receive applications for KSIC's authorized classes of coverage. KMC at its own expense, will secure reasonable underwriting information related to each risk insured by KSIC and when authorized, issue, renew and countersign policies, certificates, endorsements and binders. KMC will collect premium and has authority to adjust and pay claims and appoint subagents. Business produced and issued or renewed prior to the date of this agreement will remain under the Management Agreement with KMIS.

*Cash Management Agreement*

Effective August 20, 2019, Knight Services, Inc. (KSI) and KSIC entered into an agreement with respect to certain centralized cash management services to be performed by KSI from a deposit account established by KSI for the benefit of KSIC. KSIC is entitled to withdraw funds from the deposit account at any time, with no credit limit. On May 2, 2023, the agreement was amended to reflect an account restructuring that cancelled the original KSI bank account and replaced it with a new bank account established by HCM, who performs the cash management functions under the amended agreement.

*Investment Management Agreement*

Effective January 2, 2019, KIC and its subsidiaries, to include KSIC, entered into an Investment Management Agreement with Don Hankey as the Investment Advisor. The agreement

sets forth the terms by which Mr. Hankey shall manage the invested assets of KIC and its subsidiaries.

*Tax Sharing Agreement*

KSIC entered into a Tax Allocation Agreement for taxable years commencing on and after January 1, 2020, with other affiliates that together with KIC form entities in accordance with Internal Revenue Service Code. Under the terms of the agreement, each party calculates its federal corporate tax liability as if it were filing a separate return. KIC is responsible for filing and paying the federal corporate tax liabilities of the tax entities. If KSIC owes a tax amount if filed on a separate return, it shall pay KIC the amount due. If KSIC would be entitled to a refund if filed on a separate return, or generated losses or credits used to reduce the tax of the consolidated entities, KIC shall pay KSIC the amount due. All settlements under this agreement shall be made within 30 days of the filing of the estimated or actual consolidated federal corporate income tax return, except where a refund is due KIC, in which case, it may defer payments to KSIC within 30 days of receipt of such refund.

**TERRITORY AND PLAN OF OPERATION**

KSIC is licensed in the State of Delaware as a domestic surplus lines insurer eligible or approved to write business in all fifty (50) states. KSIC's business is written through a network of unaffiliated insurance agencies and brokers, with commercial auto liability as its primary line of business written for the year ended 2022 (60.2% of direct written premium). The majority or 58.9% of KSIC's business written in 2022 was in the following three (3) states: California (25.5%), Florida (24.3%) and New Jersey (9.1%).

**REINSURANCE**

The Company reported the following distribution of premiums written for the years ended December 31, 2022, and the prior examination date of December 31, 2019:

	<u>2022</u>	<u>2019</u>
Direct premiums written	\$ 167,845,743	\$ 71,859,580
Assumed premiums (from affiliates)	-	-
Assumed premiums (from non-affiliates)	<u>60,632,921</u>	<u>22,046,284</u>
Gross premiums written	\$ 228,478,664	\$ 93,905,864
Ceded premiums (to affiliates)	147,956,811	93,836,343
Ceded premiums (to non-affiliates)	<u>8,345,996</u>	<u>69,521</u>
Net premiums written	<u>\$ 72,175,857</u>	<u>\$ -</u>

The Company's reinsurance consists of assumed business from three non-affiliates, affiliated multi-line quota share (QS) business ceded to KIC and ceded business to other unaffiliated reinsurers with varying QS bases. In addition, in 2022, KSIC started ceding business to affiliated segregated portfolio companies sponsored by KIC SPC. The following is a summary of each significant reinsurance arrangement:

*Assumed Reinsurance (Non-Affiliates)*

In 2022, KSIC assumed the following business from three non-affiliate companies:

- Trisura Specialty Insurance Company  
General Liability and Property (Commercial Multiple Peril) lines of business covering commercial cannabis activity by offering general liability, products liability, cargo and property coverages for cultivation, manufacturing/processing, distribution, transportation and retail sales operations (68.5% of assumed premium in 2022).
- United Specialty Insurance Company  
Commercial Automobile, Property, General Liability, Inland Marine and miscellaneous coverages (22.2% of assumed premium in 2022).

- Clear Blue Specialty Insurance Company  
General Liability covering bars, taverns, sports bars, music venues, adult nightclubs, lounges, comedy clubs and jazz clubs (9.3% of assumed premium in 2022).

*Ceded Reinsurance (Affiliates)*

Effective January 1, 2014, with amendment #1, KSIC and KIC entered into a 100% QS multi-line reinsurance agreement, whereby KSIC cedes to KIC all premiums, losses and expenses related to its commercial auto liability and auto physical damage lines of business. A funds withheld account was established for the benefit of KSIC to secure and collateralize all obligations of KIC under the agreement.

Effective January 1, 2020, KSIC and KIC entered into a Reinsurance Recapture Agreement attaching to and forming a part of the above QS reinsurance agreement, whereby KSIC recaptures all the liabilities, claims and obligations from inception with respect to the Next Wave/CannGen, QuadScore, Safeherb and MEDM insurance programs.

Effective August 1, 2022, KSIC entered into varying QS agreements with KIC SPC, for and on behalf of Hankey Re SPC and Wilshire Re SPC, as follows:

- 50% QS reinsurance agreement with KIC SPC, for and on behalf of Wilshire Re SPC, covering KSIC's Allstar Trucking and TIE programs. These programs are supported by a beneficiary trust account to secure and collateralize all obligations of KIC SPC under the agreement.
- 20% QS reinsurance agreement with KIC SPC, for and on behalf of Hankey Re SPC, covering KSIC's Allstar Trucking, TIE, Coverwhale and One80 programs. These programs are supported by a beneficiary trust account to secure and collateralize all obligations of KIC SPC under the agreement.

*Ceded Reinsurance (Non-Affiliates)*

In 2022, KSIC ceded other liability (occurrence) business under the following three programs, each with multiple non-affiliate companies and varying QS bases: 1) QuadScore –

Property Program (effective August 1, 2022), 2) K&B Senior Living Program (effective August 1, 2022) and 3) Entertainment Risk Program (effective September 1, 2022).

### **FINANCIAL STATEMENTS**

The following financial statements, as reported and filed by the Company with the Department, are reflected in the following:

- Assets as of December 31, 2022
- Liabilities, Capital and Surplus as of December 31, 2022
- Statement of Income for the Year Ended December 31, 2022
- Reconciliation of Capital and Surplus for the Period from the Prior Examination as of December 31, 2019 to December 31, 2022

Knight Specialty Insurance Company

Assets  
As of December 31, 2022

	<u>Assets</u>	<u>Nonadmitted Assets</u>	<u>Net Admitted Assets</u>
Bonds	\$ 171,801,475	\$ -	\$ 171,801,475
Common stocks	222,835,069		222,835,069
Cash	37,803,869		37,803,869
Other invested assets	41,957,490		41,957,490
Investment income due and accrued	613,701		613,701
Uncollected premiums and agents' balances in the course of collection	5,380,798		5,380,798
Amounts recoverable from reinsurers	3,211,381		3,211,381
Net deferred tax asset	700,000		700,000
Receivable from parent, subsidiaries and affiliates	436,800		436,800
Aggregate write-ins for other than invested assets: Claim advance	5,021,373		5,021,373
Total	<u>\$ 489,761,956</u>	<u>\$ -</u>	<u>\$ 489,761,956</u>



Liabilities, Capital and Surplus  
As of December 31, 2022

		<u>Note</u>
Losses	\$ 30,358,509	1
Reinsurance payable on paid losses and loss adjustment expenses	3,762	
Loss adjustment expenses	2,993,318	1
Commissions payable, contingent commissions & other similar charges	9,963,213	
Other expenses	121,277	
Current federal and foreign income taxes	10,908,624	
Unearned premium reserve	26,750,277	
Ceded reinsurance premiums payable	817,275	
Funds held by company under reinsurance treaties	302,815,099	
Amounts withheld or retained by company for account of others	3,437,867	
Payable to parent, subsidiaries and affiliates	226,869	
Total Liabilities	<u>\$ 388,396,090</u>	
Common capital stock	1,000,000	
Gross paid in and contributed surplus	44,274,388	
Unassigned funds (surplus)	56,091,478	
Surplus as regards policyholders	<u>\$ 101,365,866</u>	
Total Liabilities, Capital and Surplus	<u><u>\$ 489,761,956</u></u>	

Statement of Income  
For the Year Ended December 31, 2022

<b>Underwriting Income</b>	
Premiums earned	<u>\$ 76,552,581</u>
<b>Deductions</b>	
Losses incurred	19,855,973
Loss adjustment expenses incurred	2,523,586
Other underwriting expenses incurred	<u>27,251,664</u>
Total underwriting deductions	<u>\$ 49,631,223</u>
Net underwriting gain or (loss)	<u>\$ 26,921,358</u>
<b>Investment Income</b>	
Net investment income earned	3,690,722
Net realized capital gains or (losses) less capital gains tax of \$114,260	<u>429,836</u>
Net investment gain or (loss)	<u>\$ 4,120,558</u>
<b>Other Income</b>	
Aggregate write-ins for miscellaneous income: Other Fee	<u>(75,000)</u>
Total other income	<u>\$ (75,000)</u>
Net income before dividends to policyholders	<u>\$ 30,966,916</u>
Net income after dividends to policyholders	<u>\$ 30,966,916</u>
Federal and foreign income taxes incurred	<u>6,143,881</u>
Net Income	<u><u>\$ 24,823,035</u></u>

Reconciliation of Capital and Surplus  
For the Period from the Prior Examination  
As of December 31, 2019 to December 31, 2022

	Common Capital Stock	Gross Paid-in and Contributed Surplus	Unassigned Surplus	Total
12/31/19	\$ 1,000,000	\$ 44,274,388	\$ 9,890,035	\$ 55,164,423
12/31/20 (1)			1,712,121	1,712,121
12/31/20 (2)			252,183	252,183
12/31/21 (1)			15,449,559	15,449,559
12/31/21 (2)			8,330,613	8,330,613
12/31/22 (1)			24,823,035	24,823,035
12/31/22 (2)			(4,366,068)	(4,366,068)
	<u>\$ 1,000,000</u>	<u>\$ 44,274,388</u>	<u>\$ 56,091,478</u>	<u>\$ 101,365,866</u>

(1) Net income

(2) Change in net unrealized capital gains or (losses) and change in net deferred income tax

**ANALYSIS OF CHANGES IN FINANCIAL STATEMENTS RESULTING FROM THE EXAMINATION**

There were adjustments to the Company's 2022 NAIC Annual Statement financial statements acknowledged during this examination. The Company's 2022 statutory audit report issued by RSM reflected adjustments that are associated with securities held under reinsurance treaties. Refer below to the financial statement adjustments as of December 31, 2022.

Statements of Admitted Assets, Liabilities, Capital and Surplus:	Per 2022 Audited Financial Report	Per 2022 NAIC Annual Statement	Variance
Equity securities	\$ 242,378,419	\$ 222,835,069	\$ 19,543,350
Funds held by company under reinsurance treaties	322,358,449	302,815,099	19,543,350

## **COMMENTS ON FINANCIAL STATEMENT ITEMS**

**Note 1:**

Losses	\$ 30,358,509
Loss Adjustment Expenses	\$ 2,993,318

The examination liability for the aforementioned captioned items of \$30,358,509 and \$2,993,318 are the same as reported by the Company as of December 31, 2022. The examination analysis of Loss and Loss Adjustment Expense reserves was conducted in accordance with Generally Accepted Actuarial Principles and Statutory Accounting Principles, including NAIC *Accounting Practices and Procedures Manual*, Statement of Statutory Accounting Principle No. 55 (SSAP No. 55).

## **SUBSEQUENT EVENTS**

Review of significant events subsequent to the examination date identified the following:

- The Company's investment in HC as of December 31, 2022, was subsequently disposed of and replaced with qualifying assets.
- The Company's investment in HCM as of December 31, 2022, was subsequently disposed of and replaced with qualifying assets.
- The Company's investments in the publicly traded asset-backed securities issued by WFS as of December 31, 2022, were subsequently disposed of and replaced with qualifying assets.
- The trust agreement supporting the Company's reinsurance with KIC SPC for and on behalf of Hankey Re SPC and Wilshire Re SPC as of December 31, 2022, was subsequently terminated and replaced with a funds withheld arrangement, requiring a transfer of funds back to the Company from the reinsurer. The form of underlying collateral complies with all statutes and regulations.

## **SUMMARY OF RECOMMENDATIONS**

There were no recommendations resulting from this examination.

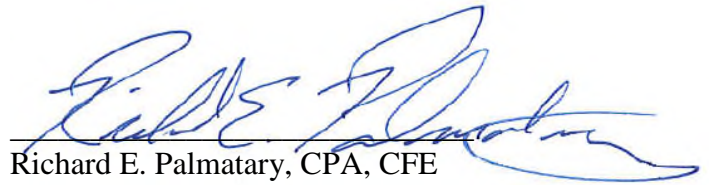
The assistance and cooperation of the consulting information systems firm, INS Services, Inc., the consulting actuarial firm, INS Consultants, Inc., the Company's outside audit firm, RSM, and the Company's management and staff was appreciated and is acknowledged.

Respectfully submitted,



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James M. Perkins, CFE  
Examiner-In-Charge  
State of Delaware



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Richard E. Palmatary, CPA, CFE  
Supervising Examiner  
State of Delaware

Knight Specialty Insurance Company

I, James M. Perkins, hereby verify and attest, under penalty of perjury, that the above is a true and correct copy of the examination report and findings submitted to the Delaware Department of Insurance pursuant to Examination Certification No. 23.026.

A handwritten signature in cursive script that reads "James M. Perkins". The signature is written in dark ink and is positioned above a horizontal line.

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James M. Perkins, CFE  
Examiner-In-Charge  
State of Delaware