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Theodore K. Nickel, Commissioner

State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

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DATE: November 30, 2018
TO: Amy J. Malm, Hearing Examiner
Kristin L. Forsberg
FROM: Michael A. Mancusi-Ungaro
Steven J. Junior

Wisconsin OCI
Exh #: 26
Case #: 18-C42836

SUBJECT: The Acquisition of Control and Merger of Unigard Indemnity Company by Sutton National Insurance Holdings LLC, Brickell Insurance Holdings LLC, and MTPC LLC (Case No. 18-C42836).

Executive Summary

This Form A recommendation memo concerns the announced acquisition of control and merger of Unigard Indemnity Company (“Unigard” or “domestic insurer”) by Sutton National Insurance Holdings, LLC, (“Sutton”), Brickell Insurance Holdings, LLC (“Brickell”), MTPC LLC (“MTPC”), and Mr. Steven Pasko (“Mr. Pasko”, and together with Sutton, Brickell, and MTPC the “Applicants”). Unigard is a Wis. Stat. Ch. 611 stock insurance corporation that is licensed as property and casualty insurer.

The Applicants are purchasing Unigard Indemnity Company from QBE Insurance Group Limited, a publicly traded holding company incorporated under the laws of Australia. All of the outstanding shares of common stock of the domestic insurer are currently directly owned by Unigard Insurance Company, a Wisconsin-domiciled insurance company (“UIC”). UIC is an indirect wholly owned subsidiary of QBE Holdings, Inc. (“QBE Holdings”). QBE Holdings is the holding company for all of QBE’s U.S. insurance companies.

Unigard provides basic commercial coverages including: commercial property and business income, commercial umbrella, business automobile, commercial inland marine, employment-related practices liability coverage, general liability and workers’ compensation. In addition, the company offers commercial package policies that include: Commercial Marketplace, Contractors Package Policy and a Comprehensive Policy that enables the policyholder to build customized insurance protection by combining multiple coverages under one policy. In personal lines, the company provides products in the personal automobile and homeowner’s lines of business. The company markets its products through a network of approximately 2,903 independent agencies.

Working with managing general agents (“MGAs”), the Applicants plan for Unigard to capitalize on a significant market opportunity in the program insurance space, which has seen direct premiums grow substantially over the last several years. By addressing the large market demand for insurance carriers in the program insurance space, and selectively providing underwriting alignment through risk-sharing with its reinsurance partners, competitive fees from MGAs, an experienced management team and a strong MGA pipeline anchored by Atlas General Insurance (“Atlas”), Unigard seeks to be a leader in the P&C, Accident & Health and program insurance markets.

The Applicants expect that Unigard's reinsurance program will include cessions to reinsurers with which Atlas has existing relationships, in addition to other reinsurers placed in the broker market by JLT Re, a reinsurance broker and consultant.

The company is licensed in Arizona, California, Colorado, Idaho, Illinois, Montana, Nevada, New York, North Carolina, Ohio, Oregon, Pennsylvania, Tennessee, Utah, Washington and Wisconsin. Unigard is also party to a Stipulation and Order issued on May 17, 2012 by the Office of the Commissioner of Insurance, State of Wisconsin, Case No. 12-C34427 for Blue Ridge Indemnity, General Casualty of WI, General Casualty Insurance Company, National Farmers Union Property and Casualty, Regent Insurance Company, Southern Fire & Casualty Company, Southern Guaranty Insurance Company, Southern Pilot Insurance Company, Unigard Indemnity Company and Unigard Insurance Company.

The Stipulation and Order places certain restrictions related to the companies' reinsurance treaty with Equator Reinsurance, Ltd as well as specific requirements related to statutory surplus, risk-based capital level and gross premium written to surplus ratio. According to the stipulation and order:

- Each company shall maintain surplus in excess of its security surplus standard pursuant to s. 623.12 Wis. Stat and s. Ins. 51.80(4) Wis. Adm. Code
- Each company shall maintain a ratio of total adjusted capital to authorized control level risk-based capital of not less than 275%.
- Each company shall maintain a ratio of gross premiums written to surplus of less than 800%.

The Applicants' future plans for Unigard are described in detail in the Plan of Operations. The Applicants intend to establish the domestic insurer as a leading carrier for property and casualty and short-tail accident and health lines of business, working with managing general agents in the program insurance market. The domestic insurer will pursue state and line license expansion, with the goal of operating in all 50 U.S. states within three years.

The Applicants expect that the domestic insurer will enter into a services agreement with 777 Partners LLC ("777") for general administrative support, as described in the Plan of Operations. The Applicants expect that the domestic insurer will also enter into a third-party services agreement with Atlas General Insurance for support on originations, underwriting, claims management, and various administrative functions.

Following the Closing, subject to making the required regulatory filings, the Applicants plan to change the name of the domestic insurer to Sutton National Insurance Company.

The Plan of Operations also includes three-year statutory financial projections for the domestic insurer, along with the assumptions used to develop the financial projections, for calendar years 2019 through 2021.

Except as may arise in the ordinary course of business, the Applicants have no present plans for the domestic insurer to declare an extraordinary dividend, to liquidate the domestic insurer, to sell any of the domestic insurer's assets (other than asset sales in the ordinary course of business), or to merge the domestic insurer with any person.

None of the Applicants or any of their respective affiliates or subsidiaries currently writes any insurance business in Wisconsin or in any other U.S. state. Thus, the Proposed Acquisition will not produce any market share increase in the direct written insurance premium in any line of business in Wisconsin. As a result the Proposed Acquisition will not substantially lessen competition in insurance in Wisconsin or tend to create a monopoly.

When looking at the other businesses controlled, owned or otherwise directed by Mr. Pasko, there are some concerns. Certain entities owned by him, via his control of a private partnerships like 777 Partners and 666 Partners, seem to be engaged in riskier businesses, such as direct business lending, installment consumer lending, or "credit relief services." These entities are risky because there is often a disconnect between the price charged for services and the actual value of the services provided to consumers, especially so with "credit relief" operations. Direct lending also generates significant civil disputes – either on behalf or against the lender. During review of the Proposed Acquisition, OCI has had to ask twice whether certain entities were owned, either in part or outright, after the initial non-disclosure of many entities on Mr. Pasko's biographical affidavit.

After reviewing the Stock Purchase Agreement, the Business Plan, biographical affidavits and the Form A, the proposed acquisition of control should be approved. As requested by Applicant, and because 777 is an affiliate of the Applicants because Mr. Steven Pasko holds indirectly 25% of the voting interests in 777, a filing to request the Commissioner's non-disapproval of the services agreement under Wis. Stat. § 617.21 and Wis. Admin. Code § Ins 40.02(2) (d) was submitted under separate cover.

It was agreed as a condition of regulatory approval that since the vast majority of the business operations will be handled outside of Wisconsin, Sutton will begin a redomestication process after closing with the redomestication to be completed no later than December 31, 2020.

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The Transaction

The Stock Purchase Agreement provides that UIC will sell to Sutton Holdings all of the issued and outstanding shares of capital stock of the domestic insurer at the closing. As a result of the proposed acquisition, the domestic insurer will become a direct wholly owned subsidiary of Sutton Holdings. Sutton Holdings, in turn, is a direct wholly owned subsidiary of Brickell Holdings. All of the voting interests of Brickell Holdings are owned by MTCP, which is wholly owned by Mr. Steven Pasko.

Pursuant to the terms of the stock purchase agreement, as full consideration for the sale of all of the issued and outstanding shares of capital stock of the Domestic Insurer, Sutton Holdings will pay to UIC an amount (the "Purchase Price") equal to the sum of (i) \$218,750 multiplied by the number of Authorized States, excluding any Authorized State as to which there is a license deficiency (the parameters of which are set forth in the Stock Purchase Agreement) as of the closing date,¹ and (ii) an amount equal to the Domestic Insurer's capital and surplus as of the closing date, all of which shall consist of cash and existing deposits of cash or securities with state insurance regulators ("Acceptable Financial Assets"). Prior to the closing, UIC shall cause the Domestic Insurer to transfer assets to UIC or to an affiliate of UIC to reduce the domestic insurer's remaining acceptable financial assets to an amount equal to no less than \$7 million and no more than \$8 million (the "Asset Transfer").

At the Closing, as described in the Stock Purchase Agreement, the Domestic Insurer will enter into the following reinsurance and related agreements with UIC and/or other QBE affiliates, pursuant to which the Domestic Insurer's outstanding policy liabilities and existing reinsurance obligations will be assumed by UIC (the "Related Reinsurance Agreements"):

- i. a Loss Portfolio Transfer Agreement pursuant to which 100% of the Domestic Insurer's net retained liabilities relating to policies issued or assumed by the Domestic Insurer prior to the Closing will be reinsured by UIC, in order to sell the Domestic Insurer to the Applicants as "a clean shell";
- ii. a related Administrative Services Agreement pursuant to which UIC will assume the administration of all such policies and all related ceded reinsurance agreements;
- iii. a Pooling Assignment and Assumption Agreement pursuant to which the Domestic Insurer will assign to UIC, and UIC will assume, all of the Domestic Insurer's rights and obligations under an existing intercompany reinsurance pooling agreement among the Domestic Insurer, UIC, QBE Insurance Corporation and other QBE affiliates; and
- iv. two endorsements to existing QBE affiliated quota share reinsurance contracts pursuant to which the Domestic Insurer will assign to UIC, and UIC will assume all of the Domestic Insurer's rights and obligations under such affiliated quota share reinsurance contracts.

¹ In the event that, as of the Closing date, there is a deficiency as to one or more Authorized States, to the extent that any such deficiency is cured within 90 days after the Closing, then Sutton Holdings has agreed to pay UIC an amount equal to \$218,750 for each Authorized State as to which a deficiency that existed at the Closing has been cured.

The Stock Purchase Agreement attached as Exhibit A to the Form A includes as exhibits forms of each related reinsurance agreement. In addition, the Applicants understand that certain QBE intercompany agreements (the “Intercompany Contracts”) will be terminated, amended or unwound to remove the domestic insurer as a party to such agreements as of or prior to the Closing.

The Stock Purchase Agreement provides that the consummation of the transactions contemplated thereunder is conditioned, among other things, on the receipt of governmental approvals, including: (i) the approval of this Application by the Commissioner; (ii) the non-disapproval of the Related Reinsurance Agreements by the Commissioner; (iii) the non-disapproval by the Commissioner of the termination, amendment or unwinding of the Intercompany Contracts; and (iv) the non-disapproval by the Commissioner of the Asset Transfer (if and to the extent that the Asset Transfer would constitute an extraordinary dividend).

Mid-transaction, OCI was notified that AM Best would not give the Applicants’ insurance operations an A- rating due to AM Best’s concerns with the holding company structure. The Applicants updated the Form A on November 7, 2018 and proposed a new holding company structure that would satisfy third-party rating agency requirements for an A- rating.

Originally, Item 2(b) of the Form A stated that the non-voting “Series B” interest comprising 75% of the economic interest in Brickell Holdings are held by three outside investors. Such Series B interest holders have no voting interests or any other ability to direct or cause the direction of the management and policies of Brickell Holdings. The remaining 25% economic interest in Brickell Holdings is held by MTCP (Mr. Pasko’s investment vehicle) along with 100% of the voting Series A interests in Brickell Holdings.

The November 7th proposed change adds a new Series C class of interest holders to the Brickell Holdings capital structure. The Series B interests, comprising 37.5% of the economic interest in Brickell Holdings will be held by 777 Partners LLC directly, rather than through the three investors in 777 Partners. The Series C interest, also comprising 37.5% of the economic interests in Brickell Holdings will be held in equal shares by three outside investors affiliated with Leadenhall Capital Partners LLP, a London based investment manager. The Series B and C interest holders will have no voting interests as members of Brickell Holdings or any other ability to direct or cause the direction of the management and policies of Brickell Holdings. The Series B and C interest holders will, however, have certain limited rights granted to them to protect their investments as minority investors with respect to material transactions involving Brickell Holdings. The remaining 25% economic interest in Brickell Holdings will continue to be held by MTCP, Mr. Pasko’s single member LLC, along with 100% of the voting Series A shares in Brickell Holdings. Thus, Mr. Pasko will be the ultimate controlling person of the domestic insurer following the proposed acquisition.

The additional change indicated in the November 7th letter to OCI indicated that previously described purchase price would be funded by loan of from 777 to Brickell Holdings of \$105 million, and that Brickell Holdings will contribute the loan proceeds to Sutton Holdings, which will use such proceeds to purchase the shares of the domestic insurer and to capitalize the domestic insurer. This has now been changed. In lieu of the loan, the Applicants now expect that Brickell Holdings will be capitalized by contributions from the Series B member 777 and the three Series C member Leadenhall investors. Each of 777 and the three Leadenhall investors will contribute in the aggregate \$52.5 million to Brickell Holdings – for a combined total of \$105 million. Brickell Holdings will then contribute \$105 million to Sutton Holdings who will use such proceeds to purchase the shares and capitalize the domestic insurer.

The Insurers

Unigard Indemnity Company:

As stated above, Unigard Indemnity Company is a traditional property and casualty insurance company headquartered in Sun Prairie, Wisconsin. Unigard provides basic commercial property and business income, commercial umbrella, business automobile, commercial inland marine, employment-related practices liability coverage, general liability and workers' compensation. In addition, the company offers commercial package policies that include: Commercial Marketplace, Contractors Package Policy and a Comprehensive Policy that enables the policyholder to build customized insurance protection by combining multiple coverages under one policy. In personal lines, the company provides products in the personal automobile and homeowner's lines of business. The company markets its products through a network of approximately 2,903 independent agencies in 16 states.

Unigard is licensed in the following states: Arizona, California, Colorado, Idaho, Illinois, Montana, Nevada, New York, North Carolina, Ohio, Oregon, Pennsylvania, Tennessee, Utah, Washington, and Wisconsin.

Years Ended December 31:

	<u>2017</u>	<u>2016</u>	<u>2015</u>	<u>2014</u>	<u>2013</u>
Total Admitted Assets	7,628,019	18,855,055	40,351,062	47,840,215	55,240,945
Total Liabilities	125,097	11,418,449	28,575,383	35,244,687	42,291,676
Surplus	7,502,922	7,436,605	11,775,679	12,595,528	12,949,268
Net Underwriting Gain (Loss)	-	-	516,697	(196,822)	(2,058,909)
Net Income (Loss)	66,317	84,044	650,576	(232,101)	(2,169,852)
RBC	5347%	2129%	480%	491%	414%
Excess Compulsory Surplus	5,502,922	5,436,606	8,506,391	9,005,434	8,187,508
Excess Security Surplus	4,702,922	4,636,606	7,198,676	7,569,397	6,282,804

The Identity and Background of the Applicants

The name and current business address of each Applicant:

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Directors and Officers of Sutton National Insurance Holdings LLC:

Name	Position
Thomas R. Dickson	Manager
William E. Hitselberger	Manager
Steven W. Pasko	Manager
William R. Trzos	Manager

Directors and Executive Officers of Brickell Insurance Holdings LLC:

Steven W. Pasko, Director and CEO

Directors and Executive Officers of MTCP LL:

Steven W. Pasko, Sole Member

Proposed Officers and Directors of Unigard Indemnity Company:

Name	Position
Steven W. Pasko	Director
Thomas R. Dickson	Director
William R. Trzos	Director and Chief Executive Officer and President
William E. Hitselberger	Director and Chief Financial Officer and Treasurer
Ryan W. Clarkson	Chief Operating Officer
Ryan S. Kirby	General Counsel & Secretary

A review of the confidential biographical affidavits for the above listed officers and directors did not raise any concerns.

Nature, Source and Amount of Consideration

Pursuant to the Stock Purchase Agreement, Sutton Holdings has agreed to buy all of the issued and outstanding shares of capital stock of the Domestic Insurer for the Purchase Price, subject to the terms and conditions of the Stock Purchase Agreement, including the receipt of the requisite regulatory approvals. The Purchase Price will be funded by contributions from the Series B member 777 and the three Series C member Leadenhall investors. Each of 777 and the three Leadenhall investors will contribute in the aggregate \$52.5 million to Brickell Holdings – for a combined total of \$105 million. Brickell Holdings

will then contribute \$105 million to Sutton Holdings who will use such proceeds to purchase the shares and capitalize the domestic insurer. 777 is deemed to be an affiliate of the Applicants because Mr. Steven Pasko holds indirectly 25% of the voting interests in 777.

To the extent the contribution from Sutton Holdings to the Domestic Insurer is subject to Wis. Stat. § 617.21 and Wis. Admin. Code § Ins 40.04(2) (a), the Applicants respectfully request that the Commissioner permit the contribution in connection with action on this Application.

The Applicants and QBE determined the nature and amount of the consideration for the Proposed Acquisition and the other terms and conditions of the Stock Purchase Agreement through arm's-length negotiation.

Originally, Item 2(b) of the Form A stated that the non-voting "Series B" interest comprising 75% of the economic interest in Brickell Holdings are held by three outside investors. Such Series B interest holders have no voting interests or any other ability to direct or cause the direction of the management and policies of Brickell Holdings. The remaining 25% economic interest in Brickell Holdings is held by MTCP (Mr. Pasko's investment vehicle) along with 100% of the voting Series A interests in Brickell Holdings.

The November 7th proposed change adds a new Series C class of interest holders to the Brickell Holdings capital structure. The Series B interests, comprising 37.5% of the economic interest in Brickell Holdings will be held by 777 Partners LLC directly, rather than through the three investors in 777 Partners. The Series C interest, also comprising 37.5% of the economic interests in Brickell Holdings will be held in equal shares by three outside investors affiliated with Leadenhall Capital Partners LLP, a London based investment manager. The Series B and C interest holders will have no voting interests as members of Brickell Holdings or any other ability to direct or cause the direction of the management and policies of Brickell Holdings. The Series B and C interest holders will, however, have certain limited rights granted to them to protect their investments as minority investors with respect to material transactions involving Brickell Holdings. The remaining 25% economic interest in Brickell Holdings will continue to be held by MTCP, Mr. Pasko's single member LLC, along with 100% of the voting Series A shares in Brickell Holdings. Thus, Mr. Pasko will be the ultimate controlling person of the domestic insurer following the proposed acquisition.

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The 611.72(3) Standard

Wisconsin Statute s. 611.72(3) (am) creates a five part test to for the Commissioner to use when evaluating the merger or acquisition of a domestic stock insurance company. It reads, in relevant part:

(am) The commissioner shall approve the plan if the commissioner finds...that it would not violate the law or be contrary to the interests of the insureds of any participating domestic corporation or of the Wisconsin insureds of any participating nondomestic corporation and that:

1. After the change of control, the domestic stock insurance corporation or any domestic stock insurance corporation controlled by the insurance holding corporation would be able to satisfy the requirements for the issuance of a license to write the line or lines of insurance for which it is presently licensed;
2. The effect of the merger or other acquisition of control would not be to create a monopoly or substantially to lessen competition in insurance in this state;
3. The financial condition of any acquiring party is not likely to jeopardize the financial stability of the domestic stock insurance corporation or its parent insurance holding corporation, or prejudice the interests of its Wisconsin policyholders;
4. The plans or proposals which the acquiring party has to liquidate the domestic stock insurance corporation or its parent insurance holding corporation, sell its assets, merge it with any person or make any other material change in its business or corporate structure or management, are fair and reasonable to policyholders of the domestic stock insurance corporation or in the public interest; and
5. The competence and integrity of those persons who would control the operation of the domestic stock insurance corporation or its parent insurance holding corporation are such that it would be in the interest of the policyholders of the corporation and of the public to permit the merger or acquisition of control.

These five requirements are analyzed below.

s. 611.72(3) (am) 1: After reviewing the documents provided by the Applicant in their Form A filing, OCI Staff believes that the Applicant is able to satisfy s. 611.72(3) (am) 1, Wis. Stat. To reach this conclusion, OCI Staff has relied heavily on the proposed business plan and the financial strength of the ultimate controlling person, Mr. Steven Pasko.

s. 611.72(3)(am)2: It is OCI's opinion that a Form E analysis is not necessary as this proposed merger involves operations that have not written business in the last two years, and involved lines of business that are subject to robust competition. As such, the risk that this transaction would eliminate competition for P&C or workers compensation insurance in Wisconsin is essentially nonexistent. OCI's initial examination of the potential competitive effects concluded that approving the acquisition would not violate the competitive standards set forth in s. Ins 40.025(4), Wis. Adm. Code.

s. 611.72(3) (am) 3: Paragraph 3 requires that the financial condition of any acquiring party is not likely to jeopardize the financial stability of the domestic insurance corporation or its parent insurance corporation, or prejudice the interest of its Wisconsin policyholders. After reviewing the documents provided by the Applicants, the concern that Sutton Holdings and Mr. Pasko's affiliated non-insurance operations would jeopardize the financial condition of Unigard is deemed minimal. OCI, however, will monitor compliance with s. 611.72(3) (am) 3, Wis. Stat., going forward.

s. 611.72(3) (am) 4: Paragraph 4 requires that the post-transaction plans to change the business structure be “fair and reasonable to policyholders of the domestic stock insurance corporation or in the public interest.” Review of the Form A and its supporting documents raise no concerns that certain customers would be prejudiced post-transaction. Compliance with s. 611.72(3) (am) 4, Wis. Stat., is expected and not a significant concern at this time.

s. 611.72(3) (am) 5: Paragraph 5 requires that OCI review the biographical affidavits of the proposed officers and directors of the Applicants. All biographical affidavits were signed under the penalty of perjury, but upon review, significant life events were not disclosed for certain proposed officers and directors. An example of one is a 1996 Chapter 7 bankruptcy. While this review did raise several certain concerns, OCI Staff ultimately decided that the proposed officers and directors are acceptable for the purpose of operating a Wisconsin domestic insurer.

Conclusion

The plan for the acquisition of control of Unigard Indemnity Company by Sutton National Insurance Holdings, LLC, Brickell Insurance Holdings, LLC, MTPC LLC, and Mr. Steven Pasko should be approved, subject to the following conditions subsequent:

- a) Amended and Restated Articles of Incorporation and Amended and Restated Bylaws, which change the name of Unigard Indemnity Company to Sutton National Insurance Company, shall be filed within ten (10) calendar days of the consummation of the proposed change in control.
- b) Unigard Insurance Company, under its new name of Sutton National Insurance Company, consents to a stipulation and order issued by the Office of the Commissioner of Insurance under s. 601.41, Wis. Stat., which shall be in a form substantially similar to that provided in Exhibit 27 in the record of this proceeding, within thirty (30) calendar days of the consummation of the proposed change in control.
- c) The share purchases and capital contributions specifically described in the plan for the acquisition of control of Unigard Indemnity Company (to be renamed Sutton National Insurance Company) are hereby nondisapproved and no separate notice need be filed or separate nondisapproval obtained for such share purchases and capital contributions pursuant to s. 617.21, Wis. Stat., and s. Ins 40.04 (2) (a), Wis. Adm. Code. The provisions of s. 617.21, Wis. Stat., and s. Ins 40.04 (2) (a), Wis. Adm. Code, shall govern, if applicable, any other share purchases and capital contributions and any dividends by Unigard Indemnity Company.
- d) The proposed Intercompany Service Agreement by and between Sutton National Insurance Company and 777 Partners LLC as filed in Exhibit 17 in the record of this proceeding, is hereby nondisapproved.
- e) The affiliated agreements that were non-disapproved in a letter dated November 27, 2018, to John Svoboda, Senior Vice President and Regulatory Officer, QBE North America, from Kristin L. Forsberg, OCI, dated November 27, 2018, nondisapproving agreements to disengage Unigard Indemnity Company from the QBE Group, subject to approval by QBE North America’s Board of Directors and the approval of the

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Form A by the OCI is included in the record of this proceeding as Exhibit # 23. Unigard Indemnity Company shall file executed copies of the agreements listed in this letter with the OCI within ten (10) calendar days of the consummation of the proposed change in control.