

MIKE KREIDLER  
STATE INSURANCE COMMISSIONER

STATE OF WASHINGTON



OFFICE OF  
INSURANCE COMMISSIONER  
HEARINGS UNIT

Fax: (360) 664-2782

Patricia D. Petersen  
Chief Hearing Officer  
(360) 725-7105

Phone: (360) 725-7000  
www.insurance.wa.gov

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2009 JAN 26 A 11: 39

Hearings Unit, DIC  
Patricia D. Petersen  
Wendy Galloway  
Chief Hearing Officer  
Paralegal  
(360) 725-7002  
[wendyg@oic.wa.gov](mailto:wendyg@oic.wa.gov)

BEFORE THE STATE OF WASHINGTON  
OFFICE OF INSURANCE COMMISSIONER

In the Matter of the )  
Proposed Acquisition and Control of: )  
 )  
NATIONAL MERIT INSURANCE )  
COMPANY, a Washington domiciled )  
property and casualty insurer and subsidiary )  
of DIRECT RESPONSE CORPORATION, )  
by )  
TRINITY UNIVERSAL INSURANCE )  
COMPANY, )  
 )  
 )  
Applicant. )

NO. G08-0182

ORDER APPROVING  
ACQUISITION OF CONTROL

TO: Jeffrey Gingold, Esq.  
Attorney for Trinity Universal Insurance Company  
Lane Powell PC  
1420 5th Avenue, Suite 4100  
Seattle, WA 98101-2338

COPIES TO: Thomas Hrdlick, Esq.  
Attorney for Trinity Universal Insurance Company  
Foley & Lardner LLP  
777 E. Wisconsin Avenue  
Milwaukee WI 53202

Samuel L. Fitzpatrick, General Counsel  
Trinity Universal Insurance Company  
c/o Unitrin, Inc.  
One East Wacker Drive  
Chicago, IL 60601

Mailing Address: P. O. Box 40255 • Olympia, WA 98504-0255  
Street Address: 5000 Capitol Blvd. • Tumwater, WA 98501



Howard Hoffen, CEO  
Metalmark Subadvisor LLC  
1177 Avenue of the Americas  
New York, NY 10036

John Bick, Esq.  
Counsel for Metalmark  
Davis Polk & Wardwell  
450 Lexington Avenue  
New York, New York 10017

Hal Belodoff, President  
The Plymouth Rock Company Incorporated  
695 Atlantic Avenue  
Boston, MA 02111

David Fine, Esq.  
The Plymouth Rock Company  
Ropes & Gray  
One International Place  
Boston MA 02110-2624

Colleen M. Granahan, Esq.  
The Plymouth Rock Company Incorporated  
695 Atlantic Avenue  
Boston, MA 02111

James Stone, CEO  
The Plymouth Rock Company Incorporated  
695 Atlantic Avenue  
Boston, MA 02111

Mory Katz, CEO  
Direct Response Corporation  
500 South Broad Street  
Meriden, CT 06450

Susan Claflin, Esq.  
Vice President, General Counsel and Secretary  
Direct Response Corporation  
500 South Broad Street  
Meriden, CT 06450

**AND TO:** Mike Kreidler, Insurance Commissioner  
Vernon Stoner, Chief Deputy Insurance Commissioner  
James T. Odiorne, Deputy Commissioner, Company Supervision Division  
Carol Sureau, Deputy Commissioner, Legal Affairs Division  
Marcia Stickler, Attorney, Legal Affairs Division  
Ronald J. Pastuch, Holding Company Manager, Company Supervision Division  
Office of Insurance Commissioner  
PO Box 40255  
Olympia, WA 98504-0255

## I. INTRODUCTION

Pursuant to Chapter 48.04 RCW, Chapter 34.05 RCW, RCW 48.31B.015, and Chapter 284-18 WAC, and after notice to interested parties and persons (see notice detailed below), the above-entitled matter came on regularly for hearing before the undersigned commencing at 12:00 p.m., (PST) on January 9, 2009 in the Office of the Insurance Commissioner, 5000 Capitol Boulevard, Tumwater, Washington 98501. All persons to be affected by the above-entitled matter were given the right to be present at such hearing, during the presentation of testimony, and had reasonable opportunity to inspect all documentary evidence, to examine witnesses and present oral and written statements. The Insurance Commissioner was represented by Marcia Stickler, Staff Attorney in his Legal Affairs Division. The Applicant, Trinity Universal Insurance Company, was represented by Jeffrey Gingold, Esq. of Lane Powell PC in Seattle as local counsel and by Thomas Hrdlick, Esq. of Foley and Lardner LLP in Milwaukee, who appeared and participated by telephone. Direct Response Corporation was represented by Susan Claflin, Vice President, General Counsel and Secretary of Direct Response Corporation. Metalmark Capital LLC, Metalmark Subadvisor LLC, MSCP III 892 Investors L.P., Morgan Stanley Capital Partners III, L.P., DR Investors L.P., DR Investors II, L.P., and Morgan Stanley Capital Investors, L.P. were represented by John Bick, attorney of Davis Polk & Wardwell, New York, New York, who appeared and participated by telephone.

## II. NATURE OF PROCEEDING

By filing a Form A (which is its preacquisition notification and application for approval of this proposed acquisition) dated September 24, 2008 and filed with the Insurance

Commissioner on September 25, 2008, the Applicant, Trinity Universal Insurance Company, seeks the Insurance Commissioner's approval of its proposed acquisition of control of National Merit Insurance Company, a Washington domiciled insurance company. On December 4, 2008, the Insurance Commissioner designated the undersigned to conduct the proceeding and make the final decision in this matter, with no input from the Insurance Commissioner or members of his staff aside from evidence presented at hearing. In transferring the Form A to the undersigned, the Insurance Commissioner indicated that the Form A was complete and the matter was ready for hearing.

The Applicant proposes to acquire control of National Merit Insurance Company by acquiring all of the issued and outstanding common stock of National Merit Insurance Company's ultimate parent company, Direct Response Corporation, in a negotiated acquisition. The Applicant proposes to acquire such outstanding stock from present shareholders Morgan Stanley Capital Partners III, L.P., MSCP III 892 Investors, L.P., Morgan Stanley Capital Investors, L.P., DR Investors, L.P., DR Investors II, L.P., James M. Stone, The Plymouth Rock Company Incorporated, and Mory Katz. RCW 48.31B.015, part of the Washington Insurer Holding Company Act, requires that the Insurance Commissioner shall approve the acquisition unless, after public hearing to examine the evidence and determine whether the proposed acquisition satisfies the applicable statutory criteria, the Insurance Commissioner determines it should not be approved.

### **III. FINDINGS OF FACT**

The undersigned designee of the Insurance Commissioner, having considered the presentation of the parties including written and oral evidence presented at the hearing, and the documents on file herein including the Form A Statement Regarding the Acquisition of Control of a Domestic Insurer dated September 24, 2008 and filed with the Commissioner on September 25, 2008, the exhibits to the Form A, and the entire hearing file, makes the following Findings of Fact:

1. The hearing was duly and properly convened and all substantive and procedural requirements under the laws of the state of Washington have been satisfied.

2. National Merit Insurance Company (National Merit) is a Washington domiciled stock insurance corporation with its headquarters in Bellevue, Washington. National Merit holds Washington Certificate of Authority No. 1278, NAIC No. 39004, which authorizes it to transact property, marine and transportation, vehicle, general casualty and surety insurance. National Merit is a wholly owned subsidiary of Response Indemnity Company of Delaware, a Delaware stock insurance corporation. In turn, Response Indemnity Company of Delaware is a wholly owned subsidiary of Direct Response Corporation (DRC) a publicly traded Delaware general business corporation. [Ex. 1, Form A, Organization Charts.]

3. Trinity Universal Insurance Company, (the Applicant herein), is a Texas domiciled stock insurance corporation. The Applicant holds NAIC Certificate of Authority No. 1865, authorizing it to transact property, marine and transportation, vehicle, general casualty and surety insurance since 1992. The Applicant is wholly owned by Unitrin, Inc., an Illinois based publicly held diversified financial services company with subsidiaries engaged in the property and casualty insurance, life, and health insurance and automobile finance businesses. The only business of Unitrin is holding, directly or indirectly, the issued and outstanding common stock of its subsidiaries and marketable securities. Through its acquisition of Direct Response Corporation, the Applicant would acquire control of National Merit and other insurance company subsidiaries of Direct Response Corporation domiciled in California, Connecticut and New York. Through its ownership of the Applicant, Unitrin would be the ultimate controlling person of NMIC following Applicant's acquisition of Direct Response Corporation. [Ex. 1, Form A, Organization Charts; Oral and Written Testimony of David F. Bengston.]

4. The Applicant proposes to acquire indirect control over Direct Response Corporation and all of its subsidiaries including National Merit by purchasing all of the issued and outstanding common stock of Direct Response Corporation, totaling 266,460.58350 shares, from its current shareholders, which are: Morgan Stanley Capital Partners III, L.P. (holding approximately 40.117% of the shares of Direct Response Corporation), MSCP III 892 Investors, L.P. (4.11%), Morgan Stanley Capital Investors, L.P. (1.124%), DR Investors, L.P. (38.99%), DR Investors II, L.P. 5.11%). Each of these five entities are investment vehicles in the form of limited partnerships; all of these limited partners are part of Metalmark Subadvisor LLC, a Delaware limited liability corporation. Investment management and control of these five entities has been

delegated to Metalmark Subadvisor LLC by their respective general partners. [Ex., 1, Organization chart of Metalmark/Morgan Stanley investment vehicles and their investments.] The other current shareholders are James M. Stone (2.47%); The Plymouth Rock Company Inc. (8.01%); and Mory Katz (.08%). (Collectively, all current shareholders are hereinafter referred to as the "Shareholders.") [Ex. 1, Form A including Stock Purchase Agreement dated August 29, 2008; December 17, 2008 extension to the 2004 Shareholders Agreement; and Oral and Written Testimony of Bengston.]

5. The Applicant proposes to acquire the shares by purchasing them from the Shareholders at a purchase price of Two Hundred Twenty Million Dollars (\$220,000,000), plus or minus, as the case may be, certain adjustments relating to (i) the after-tax appreciation or depreciation of the securities portfolio owned by Direct Response Corporation and its subsidiaries, and (ii) the consolidated GAAP net after-tax income or loss of Direct Response Corporation and its subsidiaries, in each case for the period from January 1, 2008 through a date determined in accordance with the terms of the agreement between the parties (discussed below). Said purchase price will come from current internal resources; the Applicant sold equity securities generating cash proceeds of \$343 million during the month of October 2008 and plans to use these proceeds to fund the acquisition and will not borrow any funds to pay the purchase price. [Ex. 1, Form A including Stock Purchase Agreement; the December 17, 2008 extension to the 2004 Shareholders Agreement Oral and Written Testimony of Bengston.]

6. On September 25, 2008, Applicant properly filed its Form A Statement Regarding the Acquisition of Control of a Domestic Insurer – National Merit Insurance Company, a subsidiary of Direct Response Corporation by Trinity Universal Insurance Company dated September 24, 2008, which was considered a request for approval of Trinity's proposed acquisition of National Merit as part of its purchase of Direct Response Corporation. [Ex. 1, Form A.] The Form A includes 1) substantial information and agreements concerning this proposed acquisition as required by the OIC, including organizational charts of the various entities and other detailed legal and financial information; and 2) information and agreements relative to the issues which must be the subject of these findings as required by the OIC. Said Form A was deemed to be complete and satisfactory by the OIC on December 4, 2008, as containing the information

required by the OIC Insurance Commissioner and by applicable statute. [Ex. 1, Form A; Oral and Written Testimony of Ronald J. Pastuch.]

7. After the proposed acquisition of control, National Merit will continue to 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. [Oral and Written Testimony of Pastuch; Oral and Written Testimony of James A. Schulte.]

8. The effect of this proposed acquisition of control of National Merit would not be substantially to lessen competition in insurance in this state or tend to create a monopoly therein. [Exhibit 1, Form A; Oral and Written Testimony of Pastuch; Oral and Written Testimony of Schulte.]

9. The financial condition of the Applicant is not such as might, after completion of the proposed acquisition, jeopardize the financial stability of Direct Response Corporation or National Merit or prejudice the interests of National Merit's policyholders. [Ex. 1, Form A; Oral and Written Testimony of Pastuch; Oral and Written Testimony of Schulte.]

10. The Applicant has no plans or proposals to liquidate National Merit, sell its assets, consolidate or merge it with any person, or to make any other material change in its business or corporate structure or management, which are unfair and unreasonable to National Merit's policyholders or not in the public interest. [Ex. 1, Form A; Oral and Written Testimony of Pastuch; Oral and Written Testimony of Schulte.]

11. It cannot be found that the competence, experience, and integrity of those persons who would control the operation of Direct Response Corporation and National Merit after the proposed acquisition are such that it would not be in the interest of National Merit's policyholders or of the public to permit this proposed acquisition of control. [Ex. 1, Form A; Oral and Written Testimony of Pastuch; Oral and Written Testimony of Schulte.]

12. It is not likely that this proposed acquisition of National Merit is hazardous or prejudicial to the insurance buying public. [Ex. 1, Form A; Oral and Written Testimony of Pastuch; Oral and Written Testimony of Schulte.]

13. After completion of this proposed acquisition, all rights and privileges of National Merit's policyholders will be preserved. [Oral and Written Testimony of Schulte.]

14. The Notice of Hearing herein [Ex. 1], which contains information concerning this proposed acquisition and the public hearing thereon, was published in its entirety on the Washington State Insurance Commissioner's website on December 19, 2008 and continuously from that time until the date of the hearing herein. Said forms of notice are in the form, and contain the information, that is required by the undersigned. It is here found that this notice constitutes reasonable and adequate notice to interested parties.

15. As indicated in the subject Notice of Hearing [Ex. 1, page 5] entered by the undersigned on December 19, 2008 and published as set forth in Finding 14 above, all interested parties were given the opportunity to submit any comments on, or objections to, this proposed acquisition to the undersigned. All interested parties were also advised in said Notice of Hearing that they would be given the opportunity to present evidence at hearing and to examine and cross-examine witnesses and offer oral and written arguments, and in connection therewith to conduct discovery proceedings. No objections or communications of any kind were received by the undersigned from non-parties. Further, no communications of any kind were received from outside parties by the Applicant or Direct Response Corporation. [Oral Testimony of Schulte.] Further, no objections were received by the OIC. [Oral and Written Testimony of Pastuch.] Based upon this evidence, it is here found that no reasonable objection to this proposed acquisition exists.

16. The sole witness appearing on behalf of the Insurance Commissioner was Ronald J. Pastuch, Holding Company Manager in the Company Supervision Division of the Office of the Insurance Commissioner. Mr. Pastuch presented his testimony in a detailed and credible manner and exhibited no apparent biases.

17. James A. Schulte, CPCU, President of the Applicant, testified on behalf of the Applicant. Mr. Schulte presented his testimony in a detailed and credible manner and exhibited no inappropriate biases.

18. David F. Bengston, CPA, FLMI, Vice President of Unitrin, Vice President of the Applicant, and a member of the Applicant's Board of Directors, testified on behalf of the

Applicant. Mr. Bengston presented his testimony in a detailed and credible manner and exhibited no inappropriate biases.

19. Based upon the above Findings of Facts, which address the statutory criteria for filing, review and approval of acquisitions of control of insurers domiciled in Washington State, and which criteria were set forth by the undersigned in the above-referenced Notice of Hearing, it is here found that this proposed acquisition satisfies those criteria, and that therefore the application of Trinity Universal Insurance Company for approval of its proposed acquisition of control of Direct Response Corporation including National Merit Insurance Company, on the terms specified in its Form A, should be granted, with consummation of the acquisition to occur as soon as the parties have complied with all other statutes which govern this transaction and as governed by the abovereferenced Stock Purchase Agreement and the December 17, 2008 extension to the 2004 Shareholders Agreement.

#### **IV. CONCLUSIONS OF LAW**

The undersigned, having made the above Findings of Fact, hereby makes the following Conclusions of Law:

1. Pursuant to Chapter 48.31B RCW, the Insurance Commissioner has jurisdiction over the plan of acquisition and change of control of National Merit Insurance Company.
2. On September 25, 2008, the Applicant, Trinity Universal Insurance Company, properly filed its Form A dated September 24, 2008, and said application, together with notice of the Direct Response Corporation shareholders' agreement extending the agreed upon date of the proposed acquisition, contains the information required by RCW 48.31B.015(2).
3. After the proposed acquisition of control, National Merit Insurance Company, which is an indirect wholly-owned subsidiary of Direct Response Corporation, will continue to be able to satisfy the requirements for the issuance of a license to write the line or lines of insurance for which the company is presently licensed, as contemplated by RCW 48.31B.015(4)(a)(i).
4. The financial condition of Trinity Universal Insurance Company, is such that the financial stability of National Merit Insurance Company will not be jeopardized by the

acquisition, and the interests of the National Merit Insurance Company's policyholders will not be prejudiced, as contemplated by RCW 48.31B.015(4)(a)(iii).

5. After completion of this proposed acquisition, there are no plans to liquidate National Merit Insurance Company, sell its assets, consolidate or merge it with any person, or make any other material change in its business or corporate structures or management which are unfair or unreasonable to policyholders of the insurer or not in the public interest, as contemplated by RCW 48.31B.015(4)(a)(iv).

6. The competence, experience, and integrity of those persons who will control the operation of Direct Response Corporation and National Merit Insurance Company are such that this acquisition would not be against the interest of the National Merit Insurance Company policyholders or of the public, as contemplated by RCW 48.31B.015(4)(a)(v).

7. The proposed acquisition of National Merit Insurance Company is not likely to be hazardous or prejudicial to the insurance buying public, as contemplated by RCW 48.31B.015(a)(vi).

8. Reasonable notice to interested parties has been given, and no reasonable objections exist.

9. The provisions of the Insurance Code of the State of Washington, Chapter 48.31B RCW, and specifically RCW 48.31B.015 governing approval of acquisitions, have been met. Pursuant to Chapter 48.31 RCW, and specifically RCW 48.31B.015, Trinity Universal Insurance Company's request for approval of this proposed acquisition should be granted and consummation of the acquisition may occur as soon as the parties have complied with all other statutes which govern this transaction and as governed by the abovereferenced Stock Purchase Agreement and the December 17, 2008 extension to the 2004 Shareholders Agreement.

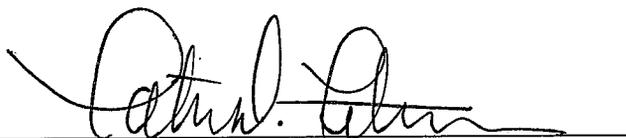
## **V. ORDER**

On the basis of the foregoing Findings of Fact and Conclusions of Law, to the effect that the statutory criteria for approval of this proposed acquisition have been met, and to the effect that approval of this proposed acquisition should be granted,

**IT IS HEREBY ORDERED** that the application of Trinity Universal Insurance Company for the Insurance Commissioner's approval of its proposed acquisition of Direct Response Corporation including National Merit Insurance Company, a Washington domiciled insurer, upon the terms included into evidence in this proceeding, is **GRANTED** effective January 9, 2009, by oral order entered by the undersigned at the conclusion of the hearing. Consummation of this transaction may occur as soon as the parties have complied with all other statutes which govern this transaction and as governed by the abovereferenced Stock Purchase Agreement and the December 17, 2008 extension to the 2004 Shareholders Agreement.

This Order is entered pursuant to Title 48 RCW, and specifically RCW 48.31B.015 and regulations applicable thereto, and Title 34 RCW and regulations applicable thereto.

**ENTERED** at Tumwater, Washington, this 26<sup>th</sup> day of January, 2009.



PATRICIA D. PETERSEN  
Presiding Officer  
Chief Hearing Officer

Declaration of Mailing

I declare under penalty of perjury under the laws of the State of Washington that on the date listed below, I mailed or caused delivery of a true copy of this document to the parties listed above.

DATED this 26<sup>th</sup> day of January, 2009.

  
WENDY GALLOWAY