

REPORT ON EXAMINATION
OF
FLORIDA LAWYERS MUTUAL
INSURANCE COMPANY
ORLANDO, FLORIDA

AS OF
DECEMBER 31, 2003

BY THE
OFFICE OF INSURANCE REGULATION

TABLE OF CONTENTS

| | |
|--|----|
| LETTER OF TRANSMITTAL | - |
| SCOPE OF EXAMINATION..... | 1 |
| Status of Adverse Findings from Prior Examination..... | 2 |
| HISTORY | 3 |
| General | 3 |
| Profitability..... | 3 |
| Dividends to Policyholders | 3 |
| Management | 3 |
| Conflict of Interest Procedure..... | 5 |
| Corporate Records..... | 5 |
| Acquisitions, Mergers, Disposals, Dissolutions, and Purchase or Sales through Reinsurance | 6 |
| Surplus Debentures | 6 |
| AFFILIATED COMPANIES | 7 |
| ORGANIZATIONAL CHART | 8 |
| FIDELITY BOND AND OTHER INSURANCE | 9 |
| PENSION, STOCK OWNERSHIP, AND INSURANCE PLANS..... | 9 |
| STATUTORY DEPOSITS | 9 |
| INSURANCE PRODUCTS AND RELATED PRACTICES..... | 10 |
| Territory and Plan of Operation | 10 |
| Treatment of Policyholders | 10 |
| REINSURANCE | 10 |
| Assumed | 10 |
| Ceded | 11 |
| ACCOUNTS AND RECORDS | 11 |
| Custodial Agreement..... | 12 |
| Investment Manager Agreements | 12 |
| Independent Auditor Agreement | 14 |

| | |
|---|----|
| Risk-Based Capital..... | 12 |
| FINANCIAL STATEMENTS PER EXAMINATION..... | 12 |
| Assets | 13 |
| Liabilities, Surplus and Other Funds | 14 |
| Statement of Income | 15 |
| COMMENTS ON FINANCIAL STATEMENTS..... | 16 |
| Liabilities | 16 |
| COMPARATIVE ANALYSIS OF CHANGES IN SURPLUS..... | 17 |
| SUMMARY OF FINDINGS | 18 |
| SUBSEQUENT EVENTS..... | 18 |
| CONCLUSION | 19 |

Tallahassee, Florida
May 21, 2004

Kevin M. McCarty
Director
Office of Insurance Regulation
State of Florida
Tallahassee, Florida 32399-0326

Dear Sir:

Pursuant to your instructions, in compliance with Section 624.316, Florida Statutes (FS), and in accordance with the practices and procedures promulgated by the National Association of Insurance Commissioners (NAIC), we have conducted an examination as of December 31, 2003, of the financial condition and corporate affairs of:

**FLORIDA LAWYERS MUTUAL INSURANCE COMPANY
3504 LAKE LYNDA DRIVE, SUITE 325
ORLANDO, FLORIDA 32817**

Hereinafter referred to as the "Company". Such report of examination is herewith respectfully submitted.

SCOPE OF EXAMINATION

This examination covered the period of January 1, 2001 through December 31, 2003. The Company was last examined by representatives of the Florida Office of Insurance Regulation (Office) as of December 31, 2000. This examination commenced with planning at the Office on March 15, 2004 to March 19, 2004. The fieldwork commenced on March 22, 2004, and was concluded as of May 21, 2004. The examination included any material transactions and/or events occurring subsequent to the examination date and noted during the course of the examination.

This financial examination was a statutory financial examination conducted in accordance with the Financial Examiners Handbook, Accounting Practices and Procedures Manual and annual statement instructions promulgated by the NAIC as adopted by Rules 69O-137.001(4) and 69O-138.001, Florida Administrative Code (FAC), with due regard to the statutory requirements of the insurance laws and rules of the State of Florida.

In this examination, emphasis was directed to the quality, value and integrity of the statement assets and the determination of liabilities, as those balances affect the financial solvency of the Company.

The examination included a review of the corporate records and other selected records deemed pertinent to the Company's operations and practices. In addition, the NAIC IRIS ratio report, the A.M. Best Report, the Company's independent audit reports and certain work papers prepared by the Company's independent certified public accountant (CPA) were reviewed and utilized where applicable within the scope of this examination.

We valued and/or verified the amounts of the Company's assets and liabilities as reported by the Company in its annual statement as of December 31, 2003. Transactions subsequent to year-end 2003 were reviewed where relevant and deemed significant to the Company's financial condition.

This report of examination is confined to financial statements and comments on matters that involve departures from laws, regulations or rules, or which are deemed to require special explanation or description.

Status of Adverse Findings from Prior Examination

The following is a summary of significant adverse findings contained in the Office's prior examination report as of December 31, 2000, along with resulting action taken by the Company in connection therewith.

Custodial Agreement

The Company maintained securities with Merrill Lynch, who was not a qualified custodian per Rule 69O-143.041, FAC. The Company did not have a custodial agreement with Merrill Lynch per Rule 69O-143.042, FAC.

Resolution: The Company moved their securities to a qualified custodian, Mellon Trust Company, per Rule 69O-143.041, FAC and executed a custodial agreement that was in compliance with Rule 69O-143.042, FAC.

HISTORY

General

The Company was incorporated in Florida on May 27, 1987 and commenced business on November 25, 1988 as Florida Lawyers Mutual Insurance Company.

In accordance with Section 624.401(1), FS, the Company was authorized to transact other liability insurance coverage in Florida on December 31, 2003:

The articles of incorporation and the bylaws were not amended during the period covered by this examination.

Profitability of Company

The Company reported an underwriting loss of (\$385,718), for the year ending December 31, 2001. The Company reported underwriting gains of \$851,764, and \$2,500,833 for the years ending December 31, 2002, and 2003, respectively. For each of those years the Company reported net investment gains of \$718,979, \$912,218, and \$1,354,721, respectively.

Dividends to Policyholders

The Company did not declare or pay dividends to its policyholders for the period under examination.

Management

The annual shareholder meeting for the election of directors was held in accordance with Sections 607.1601 and 628.231, FS. Directors serving as of December 31, 2003, were:

Directors

| Name and Location | Principal Occupation |
|--|---|
| Donald Layton Braddock Jacksonville, Florida | Lawyer |
| Philip Allan Disque Fort Lauderdale, Florida | CPA |
| Ava Kirshenbaum Doppelt Orlando, Florida | Lawyer |
| Raymond Frank Ferrero, Jr. Fort Lauderdale, Florida | Lawyer |
| John Dudley Goodlette Naples, Florida | Lawyer |
| John Franklin Harkness, Jr. Tallahassee, Florida | Director; Executive Director of the Florida Bar |
| Ronald C. LaFace Tallahassee, Florida | Lawyer |
| Dennis Ketler Larry Pensacola, Florida | Lawyer |
| William Earl Loucks Daytona Beach, Florida | Lawyer |
| Lake Henry Lytal, Jr. West Palm Beach, Florida | Lawyer |
| Stephen Andrew Rappenecker Gainesville, Florida | Lawyer |
| Robert Max Sondak Miami, Florida | Lawyer |
| Clyde Lawrence Stagg Tampa, Florida | Lawyer |
| Clyde Gary Williams Tallahassee, Florida | Lawyer |
| Craig Anthony Gibbs Jacksonville, Florida | Lawyer |

The Board of Directors in accordance with the Company's bylaws appointed the following senior officers:

Senior Officers

| Name | Title |
|---------------------|--------------|
| William Earl Loucks | President |
| Philip Allan Disque | Treasurer |
| Ronald C. LaFace | Secretary |

The Company's board appointed several internal committees in accordance with Section 607.0825, FS. The following were the principal internal board committees and their members as of December 31, 2003:

Executive Committee

Ray Ferrero, Jr. ¹
William E. Loucks ²
Donald L. Braddock
Philip A. Disque
C. Gary Williams
Ronald C. LaFace
Robert M. Sondak
C. Lawrence Stagg

Audit Committee

Donald L. Braddock ¹
John F. Harkness, Jr. ²
Robert M. Sondak
C. Gary Williams
Craig Gibbs

Investment Committee

Philip A. Disque¹
Donald L. Braddock
Lake T. Lytal, Jr.
Ronald C. LaFace

¹ Chairman

² Vice-Chairman

Conflict of Interest Procedure

The Company had adopted a policy statement requiring annual disclosure of conflicts of interest, in accordance with Section 607.0832, FS. No exceptions were noted during this examination period.

Corporate Records

The recorded minutes of the shareholder, board of directors, and all committee meetings were reviewed for the period under examination. The recorded minutes of the Board adequately

documented its meetings and approval of Company transactions in accordance with Section 607.1601, FS, including the authorization of investments as required by Section 625.304, FS.

There was documentation in the minutes reviewed that the Company's directors reviewed the previous examination report.

Acquisitions, Mergers, Disposals, Dissolutions, and Purchase or Sales Through Reinsurance

The Company had no acquisitions, mergers, disposals, dissolutions, and purchase or sales through reinsurance.

Surplus Debentures

Beginning in 1987, the Company offered up to \$15,000,000, five percent Series A surplus certificates in denominations of \$500 per certificate. The expiration date of this offering was June 5, 1989. Such certificates subscribed to prior to January 31, 1988, were offered at a purchase price of \$475 per certificate. Beginning on June 6, 1989, the Company offered up to \$5,000,000, five percent Series C surplus certificates in denominations of \$500 per certificate. The expiration date of this offering was June 1997. The certificates were non-interest bearing and were repayable only at the discretion of the board of directors, with prior approval of the Office. In 1999, the Company revised its certificate redemption policy whereby a planned redemption of the certificates would commence in 2002.

The Company reported redemptions of Series A certificates of \$26,542, \$525,253, and \$17,879 for the years 2001, 2002, and 2003, respectively. The Company reported redemptions of Series C certificates of \$11,654, \$18,444, and \$19,357 for the years 2001, 2002, and 2003, respectively. As

of December 31, 2003, \$1,411,947 in Series A and \$2,473,863 in Series C certificates were outstanding.

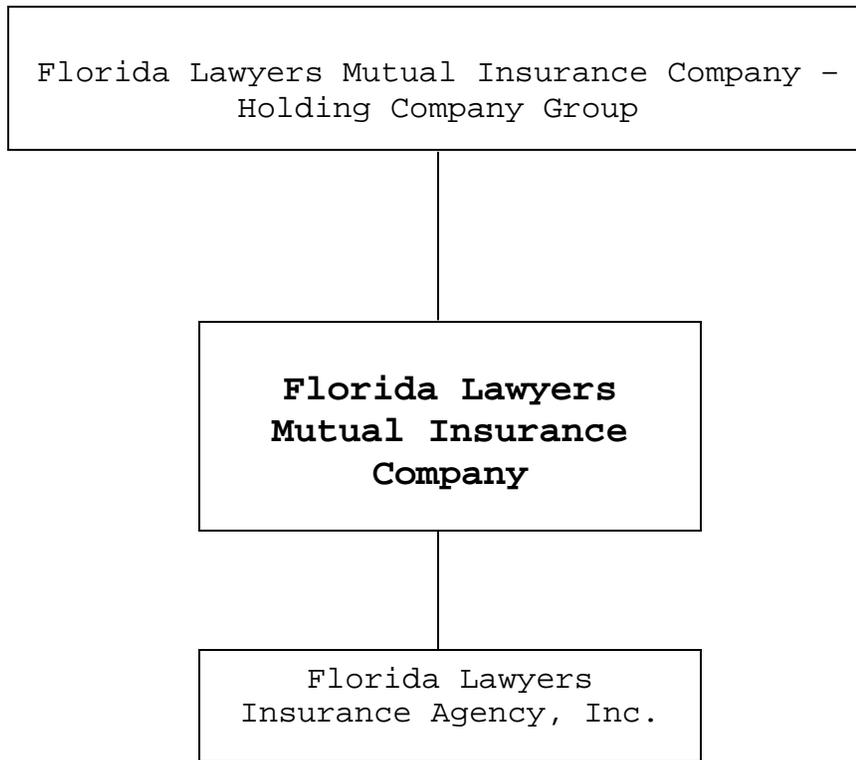
AFFILIATED COMPANIES

The Company was a member of an insurance holding company system as defined by Rule 69O-143.045(3), FAC. The latest holding company registration statement was filed with the State of Florida on July 14, 2003, as required by Section 628.801, FS, and Rule 69O-143.046, FAC. An amendment to that holding company registration statement was filed on November 13, 2003.

There were no agreements in effect between the Company and its affiliates.

A simplified organizational chart as of December 31, 2003, reflecting the holding company system is shown below. Schedule Y of the Company's 2003 annual statement provided a list of all related companies of the holding company group.

**FLORIDA LAWYERS MUTUAL INSURANCE COMPANY
ORGANIZATIONAL CHART
DECEMBER 31, 2003**



FIDELITY BOND AND OTHER INSURANCE

The Company maintained fidelity bond coverage up to \$1,000,000 with a deductible of \$100,000, which adequately covered the suggested minimum amount of coverage for the Company as recommended by the NAIC.

PENSION, STOCK OWNERSHIP, AND INSURANCE PLANS

The Company's employees were transferred to an employee leasing corporation in 2003. Under that agreement the Company paid a 50% match on employee funds contributed to the defined contribution savings plan.

STATUTORY DEPOSITS

The following securities were deposited with the State of Florida as required by Section 624.411, FS:

| State | Description | Par Value | Market Value |
|--------------------------------|-----------------------------------|-------------------|-------------------|
| FL | SunTrust Bank CD, 1.09%, 11/28/04 | \$ 75,000 | \$ 75,000 |
| FL | SunTrust Bank CD, 1.19%, 12/27/04 | 175,000 | 175,000 |
| Total Florida Special Deposits | | <u>\$ 250,000</u> | <u>\$ 250,000</u> |

INSURANCE PRODUCTS AND RELATED PRACTICES

Territory and Plan of Operation

The Company was authorized to transact insurance in the State of Florida, in accordance with Section 624.401(2), FS.

Treatment of Policyholders

The Company had established procedures for handling written complaints in accordance with Section 626.9541(1)(j), FS.

The Company maintained a claims procedure manual that included detailed procedures for handling each type of claim.

REINSURANCE

The reinsurance agreements reviewed were found to comply with NAIC standards with respect to the standard insolvency clause, arbitration clause, transfer of risk, reporting and settlement information deadlines. The following is a summary of the Company's reinsurance program:

Assumed

The Company did not assume risk.

Ceded

The Company ceded risk on an excess of loss basis through four reinsurance treaties: a casualty excess of loss treaty (\$750,000 excess of \$250,000), a casualty first excess cession (\$1,000,000 excess of \$1,000,000), a casualty second excess cession (\$3,000,000 excess of \$2,000,000), and a casualty excess cession (\$5,000,000 excess of \$5,000,000). The Company also had two facultative treaties in place at year-end for \$10,000,000 excess of \$10,000,000. The Company had the option to seek facultative coverage through their intermediary, Willis Re, Inc. on any risk.

The reinsurance contracts were reviewed by the Company's appointed actuary and were utilized in determining the ultimate loss opinion.

ACCOUNTS AND RECORDS

An independent CPA audited the Company's statutory basis financial statements annually for the years 2001, 2002 and 2003, in accordance with Section 624.424(8), FS. Supporting work papers were prepared by the CPA as required by Rule 69O-137.002, FAC.

The Company's accounting records were maintained on a computerized system. The Company's balance sheet accounts were verified with the line items of the annual statement submitted to the Office.

The Company maintained its principal operational offices in Orlando, Florida, where this examination was conducted.

The Company and non-affiliates had the following agreements:

Custodial Agreement

The Company had a custodial agreement with Mellon Trust Company, which was in compliance with Rule 69O-143.042, FAC.

Investment Manager Agreements

The Company had investment manager agreements with Conseco Capital Management, Inc., Froleys, Revy Investment Co. Inc., and Alliance Capital Management, L. P. to manage, invest, and reinvest all assets under their supervision. Custody of these accounts were transferred to Mellon Trust Company during 2003.

Independent Auditor Agreement

The Company had an independent auditor agreement with Strohm Ballweg, LLP.

Risk-Based Capital

The Company reported its risk-based capital at an adequate level.

FINANCIAL STATEMENTS PER EXAMINATION

The following pages contain financial statements showing the Company's financial position as of December 31, 2003, and the results of its operations for the year then ended as determined by this examination. Adjustments made as a result of the examination are noted in the section of this report captioned, "Comparative Analysis of Changes in Surplus."

FLORIDA LAWYERS MUTUAL INSURANCE COMPANY
Assets

DECEMBER 31, 2003

| Classification | Per Company | Examination Adjustments | Per Examination |
|--|--------------|----------------------------|-----------------|
| Bonds | \$23,842,254 | | \$23,842,254 |
| Stocks: | | | |
| Preferred | 211,708 | | 211,708 |
| Common | 3,634,755 | | 3,634,755 |
| Cash & Short-term investments | 8,585,158 | | 8,585,158 |
| Investment income due & accrued | 229,190 | | 229,190 |
| Premiums and considerations | | | |
| Deferred premiums | 1,238,703 | | 1,238,703 |
| Reinsurance | | | |
| Amounts recoverable from reinsurers | 11,983 | | 11,983 |
| Other amounts receivable under reinsurance contracts | 32,883 | | 32,883 |
| Net deferred tax asset | 680,004 | | 680,004 |
| EDP Equipment | 251 | | 251 |
| | <hr/> | | |
| Totals | \$38,466,889 | \$0 | \$38,466,889 |
| | <hr/> <hr/> | | |

FLORIDA LAWYERS MUTUAL INSURANCE COMPANY
Liabilities, Surplus and Other Funds

DECEMBER 31, 2003

| <i>Liabilities</i> | <i>Per Company</i> | <i>Examination Adjustments</i> | <i>Per Examination</i> |
|---|---------------------|------------------------------------|----------------------------|
| Losses | \$7,887,511 | \$0 | \$7,887,511 |
| Loss adjustment expenses | 6,398,897 | 0 | 6,398,897 |
| Other expenses | 93,772 | 0 | 93,772 |
| Taxes, licenses and fees | 59,064 | 0 | 59,064 |
| Current federal and foreign income taxes | 203,908 | 0 | 203,908 |
| Unearned premium | 3,111,498 | 0 | 3,111,498 |
| Advance premiums | 1,092,819 | 0 | 1,092,819 |
| Ceded reinsurance premiums payable | 648,637 | 0 | 648,637 |
| Provision for reinsurance | 75,997 | 0 | 75,997 |
| Aggregate write-ins for liabilities | 4,444,794 | 0 | 4,444,794 |
| Total Liabilities | \$24,016,898 | \$0 | \$24,016,898 |
| Aggregate write-ins for other than special surplus funds | 3,885,810 | 0 | 3,885,810 |
| Gross paid in and contributed surplus | 299,235 | 0 | 299,235 |
| Unassigned funds (surplus) | 10,264,946 | 0 | 10,264,946 |
| Surplus as regards policyholders | 14,449,991 | 0 | 14,449,991 |
| Total liabilities, capital and surplus | \$38,466,889 | \$0 | \$38,466,889 |

FLORIDA LAWYERS MUTUAL INSURANCE COMPANY
Statement of Income

DECEMBER 31, 2003

Underwriting Income

| | |
|---|--------------------|
| Premiums earned | \$8,566,357 |
| DEDUCTIONS: | |
| Losses incurred | 2,736,350 |
| Loss expenses incurred | 1,623,339 |
| Other underwriting expenses incurred | 1,705,836 |
| Aggregate write-ins for underwriting deductions | 0 |
| Total underwriting deductions | <u>\$6,065,525</u> |
| Net underwriting gain or (loss) | \$2,500,833 |

Investment Income

| | |
|--|--------------------|
| Net investment income earned | \$1,108,216 |
| Net realized capital gains or (losses) | 246,505 |
| Net investment gain or (loss) | <u>\$1,354,721</u> |

Other Income

| | |
|---|-----------------|
| Net gain or (loss) from agents' or premium balances charged off | |
| Finance and service charges not included in premiums | \$154,724 |
| Aggregate write-ins for miscellaneous income | (73,464) |
| Total other income | <u>\$81,261</u> |

| | |
|---|--------------------|
| Net income before dividends to policyholders and before federal & foreign income taxes | \$3,936,815 |
| Dividends to policyholders | |
| Net Income, after dividends to policyholders, but before federal & foreign income taxes | <u>\$3,936,815</u> |
| Federal & foreign income taxes | <u>1,028,908</u> |
| Net Income | \$2,907,907 |

Capital and Surplus Account

| | |
|--|--------------|
| Surplus as regards policyholders, December 31 prior year | \$10,116,667 |
|--|--------------|

Gains and (Losses) in Surplus

| | |
|--|----------------------------|
| Net Income | \$2,907,907 |
| Net unrealized capital gains or losses | 992,723 |
| Change in net deferred income tax | 874,171 |
| Change in non-admitted assets | (328,244) |
| Change in provision for reinsurance | (75,997) |
| Surplus adjustments: Paid in | (37,236) |
| Aggregate write-ins for gains and losses in surplus | 0 |
| Examination Adjustment | 0 |
| Change in surplus as regards policyholders for the year | <u>\$4,333,324</u> |
| Surplus as regards policyholders, December 31 current year | <u><u>\$14,449,991</u></u> |

COMMENTS ON FINANCIAL STATEMENTS

Liabilities

Losses and Loss Adjustment Expenses \$14,286,408

An outside actuarial firm appointed by the Board of Directors, rendered an opinion that the amounts carried in the balance sheet as of December 31, 2003, make a reasonable provision for all unpaid loss and loss expense obligations of the Company under the terms of its policies and agreements.

The Office actuary reviewed work papers provided by the Company and was in concurrence with this opinion.

FLORIDA LAWYERS MUTUAL INSURANCE COMPANY
Comparative Analysis of Changes in Surplus

DECEMBER 31, 2003

The following is a reconciliation of surplus as regards policyholders between that reported by the Company and as determined by the examination.

| | |
|---|--------------|
| Surplus as Regards Policyholders per December 31, 2003, Annual Statement | \$14,449,991 |
|---|--------------|

| | <u>PER</u> <u>COMPANY</u> | <u>PER</u> <u>EXAM</u> | <u>INCREASE</u> <u>(DECREASE)</u> <u>IN SURPLUS</u> |
|--|------------------------------|---------------------------|---|
| ASSETS: | | | |
| No adjustment needed. | | | |
| LIABILITIES: | | | |
| No adjustment needed. | | | |
| Net Change in Surplus: | | | <u>0</u> |
| Surplus as Regards Policyholders December 31, 2003, Per Examination | | | <u><u>\$14,449,991</u></u> |

SUMMARY OF FINDINGS

Compliance with previous directives

The Company has taken the necessary actions to comply with the comments made in the 2000 examination report issued by the Office.

Current examination comments and corrective action

There are no examination directives or corrective actions required by the Company as a result of this examination.

SUBSEQUENT EVENTS

There have been no significant subsequent events as of the reporting date of this examination.

CONCLUSION

The customary insurance examination practices and procedures as promulgated by the NAIC have been followed in ascertaining the financial condition of **Florida Lawyers Mutual Insurance Company** as of December 31, 2003, consistent with the insurance laws of the State of Florida.

Per examination findings, the Company's surplus as regards policyholders was \$14,449,991, which was in compliance with Section 624.408, FS.

In addition to the undersigned, Michael F. Hampton, CPA, CFE, DABFA, CFE, Financial Examiner/Analyst Supervisor, Jerry Golden, Financial Examiner/Analyst II, and Larry Steinert, Actuary, participated in the examination.

Respectfully submitted,

Rose M. Cady
Financial Examiner/Analyst II
Florida Office of Insurance Regulation