

REPORT ON EXAMINATION
OF
FEDERATED NATIONAL INSURANCE
COMPANY
LAUDERDALE LAKES, FLORIDA

AS OF
DECEMBER 31, 2009

BY THE
OFFICE OF INSURANCE REGULATION

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TALLAHASSEE, FLORIDA

July 1, 2010

Kevin M. McCarty
Commissioner
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, 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, 2009, of the financial condition and corporate affairs of:

**FEDERATED NATIONAL INSURANCE COMPANY
3661 W. OAKLAND PARK BLVD., SUITE 300
LAUDERDALE LAKES, FLORIDA 33311-1156**

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, 2005, through December 31, 2009. The Company was last examined by representatives of the Florida Office of Insurance Regulation (Office) as of December 31, 2004. This examination commenced with planning at the Office on March 29, 2010 to April 2, 2010. The fieldwork commenced on April 5, 2010, and concluded as of July 1, 2010.

This financial examination was a statutory financial examination conducted in accordance with the Financial Condition 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, with due regard to the statutory requirements of the insurance laws and rules of the State of Florida.

The Financial Condition Examiners Handbook requires that the examination be planned and performed to evaluate the financial condition and identify prospective risks of the Company by obtaining information about the Company including corporate governance, identifying and assessing inherent risks within the Company, and evaluating system controls and procedures used to mitigate those risks. An examination also includes assessing the principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation and management's compliance with Statutory Accounting Principles and annual statement instructions when applicable to domestic state regulations.

All accounts and activities of the Company were considered in accordance with the risk-focused examination process.

This report of examination is confined to significant adverse findings, a material change in the financial statements or other information of regulatory significance or requiring regulatory action. The report comments on matters that involved departures from laws, regulations or rules, or which were deemed to require special explanation or description.

SUMMARY OF SIGNIFICANT FINDINGS

Current Exam Findings

The following is a summary of material adverse findings, significant non-compliance findings, or material changes in the financial statements noted during this examination.

General

A material prospective risk exists regarding the company's ability to generate an underwriting profit in the future based on prior history of reinsurance costs and loss experience. The company's growth trend is unfavorable, and the company's surplus is currently being stabilized by parent company contributions, affiliate surplus notes, and deferral of a \$3,600,000 surplus note maturity date. Refer to the Subsequent Events section below regarding the contribution, surplus note and deferral. The reporting of the prospective risk is in line with Rule 69O-138.001, Florida Administrative Code, which adopts the NAIC Financial Condition Examiners Handbook (Handbook) as guidance. The Handbook states the examination report may also include a discussion of material prospective risks of the company.

Prior Exam Findings

The following is a summary of significant adverse findings contained in the Office's prior examination report as of December 31, 2004, along with resulting action taken by the Company.

General: The Company's organizational chart did not include ultimate controlling persons as directed in the annual statement instructions, It also did not include the two-character state abbreviation for all domestic insurers as directed in the annual statement instructions. Edward D. Lawson and Michelle V. Lawson meet this criteria, and as such, should be included in the organizational chart. **Resolution:** The Company included Edward J. Lawson and Michelle V. Lawson's name on Schedule Y – Part 1 of the organizational chart as suggested, including the two character-state abbreviation for the domestic insurers.

Corporate Records: The Company's Board of Directors (Board) meeting minutes did not include a review of the prior examination report. **Resolution:** The Company included the review of the examination reports and documented the review in the minutes of the Board of Directors meetings.

Investments: The Company did not have investments authorized by the Board or an authorized committee as required by Section 625.304, Florida Statutes. **Resolution:** The Company authorized it's parent's investment committee and Board of Directors to act on behalf of the Company and included the authorization in the corporate minutes.

Custody Agreement: The Company's custody agreement with Merrill Lynch did not meet the requirements of Rule 69O-143.042(2), Florida Administrative Code. **Resolution:** The Company replaced Merrill Lynch as custodian of its investments with M & T Bank.

Asset Write-ins:

The Company had a surplus note of \$3,600,000 and a note receivable of \$2,500,000 misclassified under details of write-ins for invested assets on the asset page on the filed annual statement. **Resolution:** The Company's surplus note of \$3,600,000 and note receivable of \$2,500,000 were converted into cash in February of 2005.

The Company has taken the necessary actions to comply with the comments made in the 2004 examination report issued by the Office.

SUBSEQUENT EVENTS

On March 31, 2010, the Company received \$5 million from its parent, 21st Century Holding Company (TCHC) in the form of a paid in contribution and \$5 million in the form of a surplus note from an affiliate, American Vehicle Insurance Company (AVIC).

On May 20, 2010, the Company requested and obtained approval from the Office for an extension of time to repay its surplus note from TCHC in the amount of \$3,600,000 with a maturity date of June 30, 2010. The company extended the maturity date to June 30, 2015.

HISTORY

General

The Company was incorporated in Florida on January 6, 1992, and commenced business on April 1, 1992, as Federated National Insurance Company.

The Company was authorized to transact the following insurance coverage in Florida on December 31, 2009:

| | |
|----------------------------------|---------------------------------|
| Fire | Homeowners multiple peril |
| Allied Lines | PPA physical damage |
| Private passenger auto liability | Commercial Auto physical damage |
| Commercial automobile liability | |

The Company was authorized by the Office to assume 30,000 policies from Citizens Property Insurance Corporation (Citizens) beginning January 19, 2009. The Company was authorized by the Office to assume an additional 45,000 policies from Citizens beginning December 15, 2009. The Company has taken steps to generate new business in addition to renewing the business assumed from Citizens, such as diversifying into the fire line as part of a commercial residential property program and focusing on diversifying geographical concentration and risk exposure of its homeowners business line.

The Company's Articles of Incorporation and Bylaws were amended during the period covered by this examination. On August 16, 2005, the Articles of Incorporation and By-Laws were amended to reflect the Company's primary place of business change to 3661 West Oakland Park Blvd, Lauderdale Lakes, FL 33311.

Dividends to Stockholders

The Company did not declare or pay dividends during the examination period.

Capital Stock and Capital Contributions

As of December 31, 2009, the Company's capitalization was as follows:

| | |
|--|-------------|
| Number of authorized common capital shares | 10,000,000 |
| Number of shares issued and outstanding | 1,500,000 |
| Total common capital stock | \$1,500,000 |
| Par value per share | \$1.00 |

Control of the Company was maintained by its parent, TCHC, who owned 100% of the stock issued by the Company.

Surplus Debentures

The Company entered into a surplus debenture with TCHC for \$3,600,000 in February, 2005, and received required approval from the Office in compliance with Section 628.401, Florida Statutes. Interest is accrued on the surplus debenture at the Prime Rate plus 2 ½ % annually. The principal amount and any accrued and unpaid paid interest is payable by June 30, 2015.

The Company entered into a surplus debenture with AVIC for \$5,000,000 in March 2010 and received required approval from the Office in compliance with Section 628.401, Florida Statutes. Interest is accrued on the surplus debenture at the rate of 6% annually. The principal amount and any accrued and unpaid paid interest is payable by March 31, 2015.

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

The Company did not have any acquisitions, mergers, disposals, dissolutions, and purchase or sales through reinsurance during the examination period.

CORPORATE RECORDS

The recorded minutes of the shareholder, Board of Directors, and certain internal committees were reviewed for the period under examination. The recorded minutes of the Board adequately documented its meetings and approval of Company transactions and events in accordance with Section 607.1601, Florida Statutes, including the authorization of investments as required by Section 625.304, Florida Statutes.

Conflict of Interest

The Company adopted a policy statement requiring annual disclosure of conflicts of interest in accordance with the NAIC Financial Condition Examiners Handbook adopted by Rule 690-138.001, Florida Administrative Code.

MANAGEMENT AND CONTROL

Management

The annual shareholder meeting for the election of directors was held in accordance with Sections 607.1601 and 628.231, Florida Statutes. Directors serving as of December 31, 2009, were:

Directors

| Name and Location | Principal Occupation |
|--|--|
| Michael Herbert Braun Lauderdale Lakes, Florida | President Federated National Insurance Company |
| James Gordon Jennings III Lauderdale Lakes, Florida | V.P. Risk Management Federated National Insurance Company |
| George Santos Berwig Lauderdale Lakes, Florida | Attorney Federated National Insurance Company |

Ydania Concepcion
Lauderdale Lakes, Florida

Controller
Federated National Insurance Company

Manuel Simon Amich
Lauderdale Lakes, Florida

Information Technology Director
Federated National Insurance Company

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

Senior Officers

| Name | Title |
|-----------------------|-----------|
| Michael Herbert Braun | President |
| George Santos Berwig | Secretary |
| Ydania Concepcion | Treasurer |

The Company's Board appointed several internal committees in accordance with Section 607.0825, Florida Statutes. The committees also included members of TCHC's Board of Directors and management. Following were the principal internal Board committees and their members as of December 31, 2009:

| Audit Committee | Investment Committee | Compensation Committee |
|-----------------------------------|-------------------------|-------------------------------------|
| Jenifer G. Kimbrough ¹ | Carl Dorf ¹ | Richard W. Wilcox, Jr. ¹ |
| Carl Dorf | Peter J. Prygelski, III | Bruce F. Simberg |
| Richard W. Wilcox, Jr. | Bruce F. Simberg | Carl Dorf |
| | Charles B. Hart, Jr. | Jenifer G. Kimbrough |

| SOX Steering Committee | Emergency Committee |
|--------------------------------------|-------------------------------|
| J. Gordon Jennings, III ¹ | Michael H. Braun ¹ |
| Donald G. Braun | Peter J. Prygelski, III |
| Manuel S. Amich | Stephen C. Young |
| C. Brian Turnau | Thomas J. Spitalny |
| Tracy Wiggan | Donald G. Braun, Jr. |
| | J. Gordon Jennings, III |
| | Tracy Wiggan |
| | George S. Berwig |
| | C. Brian Turnau |
| | Christopher Clouse |
| | Manuel S. Amich |
| | Rebecca L. Campillo |

Chairman ¹

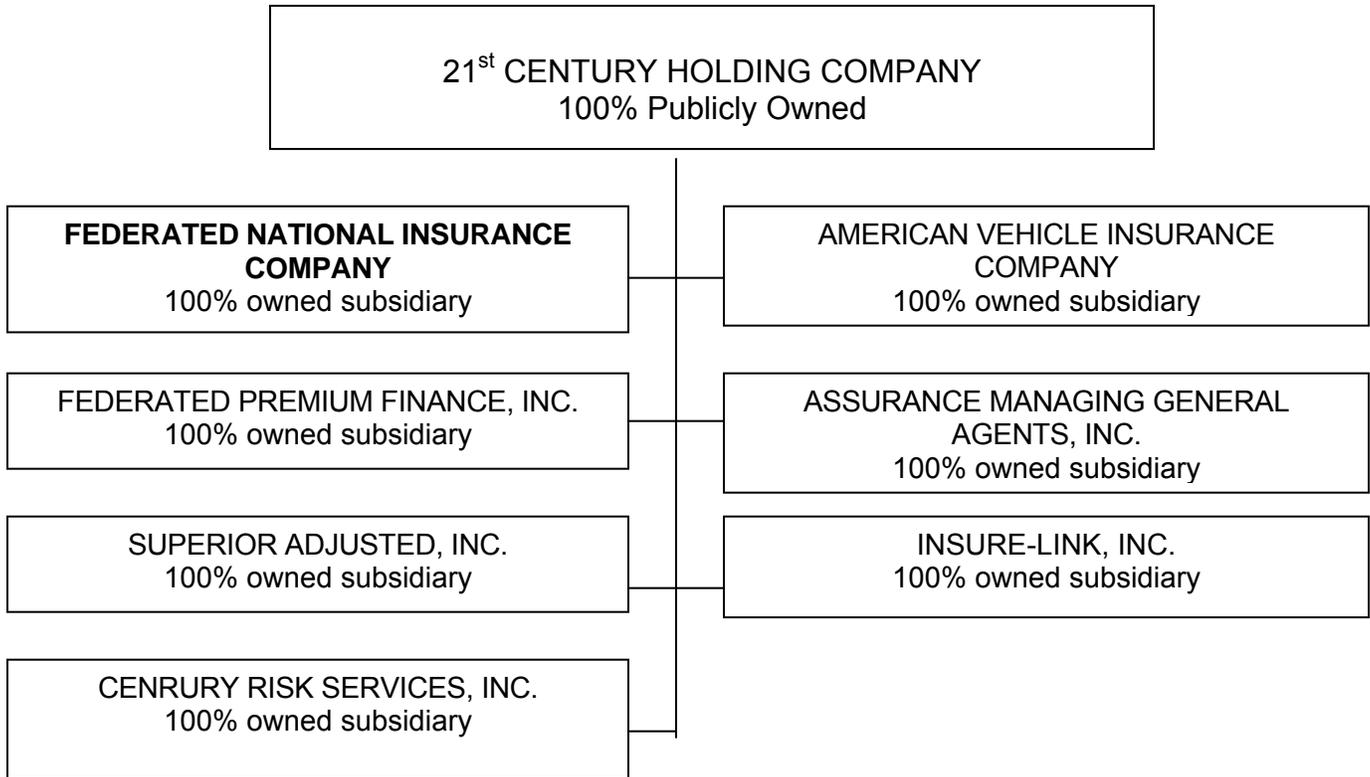
Affiliated Companies

The Company was a member of an insurance holding company system as defined by Rule 69O-143.045(3), Florida Administrative Code. The latest holding company registration statement was filed with the State of Florida on February 17, 2010 as required by Section 628.801, Florida Statutes, and Rule 69O-143.046, Florida Administrative Code.

An organizational chart as of December 31, 2009, reflecting the holding company system, is shown below. Schedule Y of the Company's 2009 annual statement provided a list of all related companies of the holding company group.

**FEDERATED NATIONAL INSURANCE COMPANY
Organizational Chart**

DECEMBER 31, 2009



The following agreements were in effect between the Company and its affiliates:

Tax Allocation Agreement

The Company, along with its parent, TCHC, and affiliates, filed a consolidated federal income tax return. On December 31, 2009, the method of allocation between the Company and TCHC was on a separate-entity basis. Each member of the group recorded an inter-company income tax receivable or payable with TCHC. Within ninety (90) days of the remittance by TCHC of any income tax payment to the taxing authorities, all inter-company tax receivables/payables were settled.

Cost Sharing Agreement

The Company and TCHC entered in cost sharing agreement on January 1, 2003. Either party paid expenses on behalf of the other such as, but not limited to, payroll and supplies. The parent and Company reimbursed each other for expenses paid on behalf of the other within 90 days of the payment.

Management Agreement

The Company and TCHC entered in cost sharing agreement on January 2, 2007. The parent company assisted the Company in all aspect of management including review and improving financial goals and compliance with legal and regulatory mandates.

Managing General Agent Agreement

The Company had a Managing General Agency Agreement entered into January 1, 2005, with affiliate Assurance Managing General Agents, INC (AMGA). Under the agreement, the

Company engaged AMGA as its Managing General Agent (MGA) pursuant to Section 626.7451, Florida Statutes, to provide statistical reports; underwrite, market, administer and manage the policies; and negotiate reinsurance agreements. The MGA agreed to market, underwrite, administer and manage policies on behalf of the Company.

Claim Service Agreement

The Company entered into an agreement with Superior Adjusting, Inc. on January 1, 2003, to process claims and claims legal administration for all lines of business written by the Company. The Company paid Superior Adjusting, Inc. a fee equal to 4.5% of the earned premiums, net of premium cancellations and endorsements until termination of this agreement. Additionally, Superior Adjusting, Inc. was entitled to a 15% collection fee for all subrogation receipts and a 10% collection fee for all salvage collection.

FIDELITY BOND

As of December 31, 2009, the Company maintained fidelity bond coverage up to \$850,000. The Company increased its fidelity bond coverage up to \$900,000 with a deductible of \$100,000 on May 4, 2010, which adequately covered the suggested minimum recommended by the NAIC.

PENSION, STOCK OWNERSHIP AND INSURANCE PLANS

The Company had no Retirement Plan, deferred Compensation program or any Other Postretirement Benefit Plan.

TERRITORY AND PLAN OF OPERATIONS

The Company was authorized to transact insurance only in the State of Florida.

Treatment of Policyholders

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

The Company maintained a claims procedure manual that included detailed procedures for handling each type of claim in accordance with Section 626.9541(1) (i) 3a, Florida Statutes.

COMPANY GROWTH

The Company experienced a significant underwriting loss of \$20.9 million as of December 31, 2009, compared to a prior year gain of \$863 thousand. The Company had an unfavorable trend of reported net losses of \$2.2 million and \$12.2 million in 2008 and 2009 respectively. The losses were due primarily to the cost of reinsurance, wind mitigation credits, and loss development. The Company developed initiatives to generate an underwriting profit in future years. To reduce reinsurance costs the Company planned to perform re-inspections of properties and verify credits and credentials associated with wind mitigation. The Office approved a 14.9% premium rate increase for the Company's homeowner's business assumed from Citizens, beginning July 1, 2010, and a 19% premium rate increase for its voluntary homeowners policies effective November, 2009.

Profitability of Company

The following table shows the profitability trend (in dollars) of the Company for the period of examination, as reported in the filed annual statements.

| | 2009 | 2008 | 2007 | 2006 | 2005 |
|----------------------------------|--------------|-------------|-------------|-------------|-------------|
| Premiums Earned | 29,617,876 | 37,429,203 | 62,283,880 | 48,040,899 | 47,935,442 |
| Net Underwriting Gain/(Loss) | (20,830,477) | 863,231 | 11,495,576 | (2,180,507) | (4,675,671) |
| Net Income | (12,212,144) | (2,218,186) | 15,281,654 | 1,719,134 | (2,236,646) |
| Total Assets | 77,398,252 | 76,373,503 | 91,523,370 | 95,049,991 | 69,234,257 |
| Total Liabilities | 56,373,730 | 44,880,964 | 59,196,743 | 75,529,719 | 58,030,617 |
| Surplus As Regards Policyholders | 21,024,521 | 31,492,539 | 32,326,627 | 19,520,272 | 11,203,640 |

LOSS EXPERIENCE

The Company's loss experience was due primarily to nine hurricanes since 2004: Four storms in 2004, four in 2005, and one, Hurricane Fay, in 2008. The Company experienced significant adverse development in loss experience related to the hurricanes of 2004 and 2005. In 2008, reported loss grew by \$8.8 million, which is 5.6% over the total reported loss as of December 31, 2007. In 2009, reported loss grew by \$6.5 million, which is 3.9% over total reported loss as of December 31, 2008. Based on discussions with management, the majority of the development is due to policy holders requesting additional indemnity for damages after the claims were closed. An independent actuarial firm, AMI Risk Consultants, was engaged to review the Statutory Loss and Loss Adjustment expense reserves carried on the Company's balance sheet as of December 31, 2009. AMI Risk Consultants concluded that the amounts carried in the balance sheet as of December 31, 2009, made a reasonable provision for all

unpaid loss and loss expense obligations of the Company under the terms of its policies and agreements.

REINSURANCE

The reinsurance agreements reviewed complied with NAIC standards with respect to the standard insolvency clause, arbitration clause, transfer of risk, reporting and settlement information deadlines.

Assumed

The Company assumed risk from Citizens in various take out amounts pursuant to filed Consent Orders from the Office. All of the Company's assumed reinsurance was through the Citizens takeout process. The Company assumed 24,783 policies from Citizens during the calendar year 2009.

Ceded

The Company ceded premiums to the Florida Hurricane Catastrophe Fund and a number of private reinsurers. All of the reinsurance with private reinsurers was purchased through intermediary Aon Benfield.

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

ACCOUNTS AND RECORDS

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

An independent CPA audited the Company's statutory basis financial statements annually for the years 2005, 2006, 2007, 2008, and 2009, in accordance with Section 624.424(8), Florida Statutes. Supporting work papers were prepared by the CPA as required by Rule 69O-137.002, Florida Administrative Code.

The Company's accounting records were maintained on a retail accounting system. The Company utilized third-party providers for their core information technology functions relating to underwriting, premium and claims processing. The applications were outsourced web-based applications where the third-party provider maintained the application, performed systems development and maintenance, as well as handled the method of access to those applications.

The Company and non-affiliates had the following agreements:

Custodial Agreement

The Company entered into a custodial agreement with M & T Investment Group effective April 28, 2008, and an agreement with U.S. Bank effective March 31, 1998. The agreements were in compliance with the provisions of Rule 690-143.042, Florida Administrative Code.

Independent Auditor Agreement

The Company entered into an independent auditor agreement with De Meo, Young, McGrath for annual statutory audit services for the year ending December 31, 2009.

INFORMATION TECHNOLOGY REPORT

ParenteBeard LLC performed an evaluation of the information technology and computer systems of the Company. Results of the evaluation were noted in the Information Technology Report provided to the Company.

STATUTORY DEPOSITS

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

| STATE | Description | Par Value | Market Value |
|------------------------|-------------------------------------|--------------------|--------------------|
| FL | US Treasury N/B, 7.250%, 05/15/2016 | 30,000 | 37,137 |
| FL | US Treasury N/B 4.375%, 08/15/2012 | 1,000,000 | 1,075,860 |
| TOTAL SPECIAL DEPOSITS | | <u>\$1,030,000</u> | <u>\$1,112,997</u> |

FINANCIAL STATEMENTS PER EXAMINATION

The following pages contain financial statements showing the Company's financial position as of December 31, 2009, 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."

FEDERATED NATIONAL INSURANCE COMPANY
Assets

DECEMBER 31, 2009

| | Per Company | Examination Adjustments | Per Examination |
|--|--------------|----------------------------|-----------------|
| Bonds | \$38,464,216 | | \$38,464,216 |
| Stocks: | | | |
| Common | 10,436,286 | | 10,436,286 |
| Cash | 5,721,108 | | 5,721,108 |
| Receivables for securities | 385,349 | | 385,349 |
| Investment income due and accrued | 544,407 | | 544,407 |
| Agents' Balances: | | | |
| Uncollected premium | 3,497,706 | | 3,497,706 |
| Deferred premium | 147,389 | | 147,389 |
| Reinsurance: | | | |
| Amounts recoverable from reinsurers | 3,737,679 | | 3,737,679 |
| Current federal and foreign income recoverable & interest thereon | 6,484,441 | | 6,484,441 |
| Net deferred tax asset | 1,530,115 | | 1,530,115 |
| Aggregate write-in for other than invested assets | 6,449,555 | | 6,449,555 |
| | <hr/> | | |
| Totals | \$77,398,252 | \$0 | \$77,398,252 |
| | <hr/> <hr/> | | |

FEDERATED NATIONAL INSURANCE COMPANY
Liabilities, Surplus and Other Funds

DECEMBER 31, 2009

| | Per Company | Examination Adjustments | Per Examination |
|---|---------------------|----------------------------|---------------------|
| Losses | \$13,738,967 | | \$13,738,967 |
| Loss adjustment expenses | 4,865,625 | | 4,865,625 |
| Commissions payable | 849,391 | | 849,391 |
| Other expenses | 103,818 | | 103,818 |
| Taxes, licenses and fees | 160,497 | | 160,497 |
| Unearned premium | 16,659,826 | | 16,659,826 |
| Advanced premium | 2,015,080 | | 2,015,080 |
| Ceded reinsurance premium payable | 16,497,954 | | 16,497,954 |
| Funds held by company under reinsurance treaties | 57,770 | | 57,770 |
| Provision for reinsurance | 99,846 | | 99,846 |
| Payable to parent, subsidiaries and affiliates | 1,324,956 | | 1,324,956 |
| Total Liabilities | \$56,373,730 | \$0 | \$56,373,730 |
| Aggregate write-ins for special surplus funds | \$240,205 | | \$240,205 |
| Common capital stock | 1,500,000 | | 1,500,000 |
| Surplus notes | 3,600,000 | | 3,600,000 |
| Gross paid in and contributed surplus | 29,661,272 | | 29,661,272 |
| Unassigned funds (surplus) | (13,976,956) | | (13,976,956) |
| Surplus as regards to policy holders | \$21,024,521 | | \$21,024,521 |
| Total liabilities, surplus and other funds | \$77,398,252 | \$0 | \$77,398,252 |

**FEDERATED NATIONAL INSURANCE COMPANY.
Statement of Income**

DECEMBER 31, 2009

Underwriting Income

| | | |
|---|--------------------|----------------|
| Premiums earned | | \$29,617,876 |
| | Deductions: | |
| Losses incurred | | 22,922,373 |
| Loss expenses incurred | | 6,785,812 |
| Other underwriting expenses incurred | | 20,740,167 |
| Aggregate write-ins for underwriting deductions | | 0 |
| Total underwriting deductions | | \$50,448,353 |
| Net underwriting gain or (loss) | | (\$20,830,477) |

Investment Income

| | | |
|--|--|-------------|
| Net investment income earned | | \$1,092,491 |
| Net realized capital gains or (losses) | | 835,709 |
| Net investment gain or (loss) | | \$1,928,200 |

Other Income

| | | |
|---|--|----------------|
| Net gain or (loss) from agents' or premium balances charged off | | |
| Finance and service charges not included in premiums | | \$197,897 |
| Aggregate write-ins for miscellaneous income | | 7,794 |
| Total other income | | \$205,692 |
| Net income before dividends to policyholders and before federal & foreign income taxes | | (\$18,696,585) |
| Dividends to policyholders | | |
| Net Income, after dividends to policyholders, but before federal & foreign income taxes | | (\$18,696,585) |
| Federal & foreign income taxes | | (6,484,441) |
| Net Income | | (\$12,212,144) |

Capital and Surplus Account

| | | |
|--|--|----------------|
| Surplus as regards policyholders, December 31 prior year | | \$31,492,539 |
| Net Income | | (\$12,212,144) |
| Net unrealized capital gains or losses | | 1,001,001 |
| Change in net deferred income tax | | (252,043) |
| Change in nonadmitted assets | | 682,433 |
| Change in provision for reinsurance | | 72,531 |
| Surplus adjustments: Paid in | | 0 |
| Aggregate write-ins for gains and losses in surplus | | 240,205 |
| Examination Adjustment | | 0 |
| Change in surplus as regards policyholders for the year | | (\$10,468,018) |
| Surplus as regards policyholders, December 31 current year | | \$21,024,521 |

A comparative analysis of changes in surplus is shown below

FEDERATED NATIONAL INSURANCE COMPANY
Comparative Analysis Of Changes In Surplus

DECEMBER 31, 2009

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
December 31, 2009, per Annual Statement \$21,024,521

| | <u>PER</u> <u>COMPANY</u> | <u>PER</u> <u>EXAM</u> | <u>INCREASE</u> <u>(DECREASE)</u> <u>IN SURPLUS</u> |
|--|------------------------------|---------------------------|---|
| ASSETS: | | | |
| No Adjustments | | | |
| LIABILITIES: | | | |
| No Adjustments | | | |
| Net Change in Surplus: | | | <u>0</u> |
| Surplus as Regards Policyholders December 31, 2009, Per Examination | | | <u>\$21,024,521</u> |

COMMENTS ON FINANCIAL STATEMENTS

Liabilities

Losses and Loss Adjustment Expenses \$18,604,592

An outside actuarial firm, Merlinos & Associates, Inc. appointed by the Board of Directors, rendered an opinion that the amounts carried in the balance sheet as of December 31, 2009, made a reasonable provision for all unpaid loss and loss expense obligations of the Company under the terms of its policies and agreements.

An independent actuarial review performed on behalf of the Office was in concurrence with this opinion.

Capital and Surplus

The amount reported by the Company of \$21,024,521, exceeded the minimum of \$5,637,373 required by Section 624.408, Florida Statutes.

SUMMARY OF RECOMMENDATIONS

General

We recommend a limited scope examination be conducted to review the Company's implementation of their 2010-2011 reinsurance structure, its affect on the Company's ability to fund future policy holder obligations, and the status of management actions plans for achieving an underwriting profit in 2010.

CONCLUSION

The insurance examination practices and procedures as promulgated by the NAIC have been followed in ascertaining the financial condition of **FEDERATED NATIONAL INSURANCE COMPANY** as of December 31, 2009, consistent with the insurance laws of the State of Florida.

Per examination findings, the Company's Surplus as regards policyholders was \$21,024,521, in compliance with Section 624.408, Florida Statutes.

In addition to the undersigned, John Romano, CPA, Examiner-In-Charge, Jennifer Cox, Participating Examiner, Philip Schmoyer, IT Consultant representing ParenteBeard, LLC, and Gail Flannery, FCAS, MAAA, Consulting Actuary, AMI Risk Consultants, Inc. participated in the examination. Mark Brown, Reinsurance/Financial Specialist of the Office also participated in the examination.

Respectfully submitted,

Kethessa Carpenter, CPA
Financial Examiner/Analyst Supervisor
Florida Office of Insurance Regulation