

REPORT ON EXAMINATION
OF
FIDELITY FIRE & CASUALTY COMPANY
LAKE MARY, FLORIDA
AS OF
DECEMBER 31, 2007

BY THE
OFFICE OF INSURANCE REGULATION

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Tallahassee, Florida

December 19, 2008

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, 2007, of the financial condition and corporate affairs of:

FIDELITY FIRE & CASUALTY COMPANY
200 Colonial Center Parkway, Suite 100
LAKE MARY, FLORIDA 32746

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, 2007 through December 31, 2007. This was a second year examination of the Company. This examination commenced with planning at the Florida Office of Insurance Regulation (Office), on September 8, 2008 through September 19, 2008. The fieldwork commenced on September 22, 2008, and was concluded as of December 19, 2008.

This financial examination was a statutory financial examination conducted in accordance with the NAIC Financial Condition Examiners Handbook, Accounting Practices and Procedures Manual and Annual Statement Instructions for Property/Casualty Companies 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 NAIC 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 surveillance examination process.

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 reports, the Company's independent audit reports and certain work papers prepared by the Company's independent certified public accountant (CPA), and other reports as considered necessary were reviewed and utilized where applicable within the scope of this examination.

This report of examination was confined to financial statements and comments on matters that involved departures from laws, regulations or rules, or which were 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, 2006, along with resulting action taken by the Company in connection therewith.

The Company did not submit its Certification of Compliance with Executive Order 13224, which states that it implemented and complied with procedures to detect and prevent transactions with terrorists and terrorist support organizations. **Resolution:** The Company submitted its Certificate of Compliance with Executive Order 13224 in January of 2008.

HISTORY

General

The Company was incorporated under Florida law on April 9, 2004, and commenced business on May 26, 2005, as Fidelity Fire & Casualty Company. The Company is a member of a holding company with the ultimate parent being Fidelity Insurance Holdings, Inc.

The Company was party to Consent Order #81765-05-CO dated March 26, 2005, regarding the application for the issuance of a Certificate of Authority. At December 31, 2007, the Company, as outlined below, was not in compliance with that consent order.

- Paragraph 19 requires prior approval from the Office prior to contracting with a Managing General Agent (MGA). The Company entered into such a contract on March 1, 2007, but did not obtain prior approval from the Office.
- Paragraph 18e requires that the affiliated MGA hold the funds collected on behalf of the Company in a fiduciary capacity in a trust account. Such a trust account is also required by Section 626.7451 (3), Florida Statutes. A trust account has not been established as required by both the Consent Order and 626.7451 (3), Florida Statutes.
- Paragraph 18j requires that the affiliated MGA provide a written notice to insured individuals advising them of the identity of, and relationship among, the affiliate, the policyholder, and the insurer. Such a notice has not been provided to insured individuals.

Subsequent Event: The Company amended the MGA agreement and approval was obtained from the Office on February 19, 2008.

The Company was authorized to transact the following insurance coverage in Florida on December 31, 2007:

Fire	Allied Lines	Homeowners Multi Peril
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The Company had not written Allied Lines nor removed the line of business from the Certificate of Authority as of December 31, 2007, and was not in compliance with Section 624.430 (1), Florida Statutes.

Capitalization

As of December 31, 2007, the Company's capitalization was as follows:

Number of authorized common capital shares	100,000
Number of shares issued and outstanding	100,000
Total common capital stock	\$4,000,000
Par value per share	\$40

Control of the Company was maintained by its parent, Fidelity Insurance Holdings, Inc, which owned 100% of the stock issued by the Company.

The Company's original common stock certificate issued reflected a par value on the certificate of \$.01 rather than the appropriate amount of \$1.

Effective November 15, 2007, the articles of incorporation were amended to restate the par value of the common stock from \$1 to \$40. The original common stock certificate was not canceled and a certificate with the new par value issued.

Subsequent Event:

On February 8, 2008, the Company canceled common stock certificate number one and issued number two with the proper par value of \$40.

On March 30, 2007, the Company received a capital contribution of \$4,400,000 from its parent, Fidelity Insurance Holdings, Inc. The capital contribution was allocated \$3,900,000 to capital stock and \$500,000 to gross paid in and contributed surplus.

The capital stock increase of \$3,900,000 increased the par value of each outstanding share of common capital stock from \$1 to \$40 and brought the total value of common capital stock to \$4,000,000.

The \$500,000 increase to gross paid in and contributed surplus brought the total amount to \$7,400,000 at December 31, 2007.

Profitability of Company

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

	2007	2006
Premiums Earned	2,891,719	0
Net Underwriting Gain/(Loss)	180,580	(19,422)
Net Income	156,992	63,752
Total Assets	17,377,235	5,903,045
Total Liabilities	6,657,825	5,000
Surplus as Regards Policyholders	10,719,410	5,898,045

Dividends to Stockholders

The Company did not pay or declare any dividends during the period covered by this examination.

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, 2007, were:

Directors

Name and Location

Principal Occupation

Lanier Miles Porter
Longwood, Florida

Chief Executive Officer of the Company

Harold Mack Humphrey
Miami, Florida

Insurance Agent

Leman Miles Porter
Heathrow, Florida

President of the Company

Willis Thomas King, Jr.
Lake Mary, Florida

Chairman of the Board of Directors
of the Company

Dwayne Richard Williams
Winter Springs, FL

Treasurer of the Company

The Board of Directors, in accordance with the Company's bylaws, appointed the following senior officers that were serving at December 31, 2007:

Senior Officers

Name

Title

Lanier Miles Porter

Chief Executive Officer

Leman Miles Porter

President

Dwayne Richard Williams

Treasurer

Benjamin Andrew Treuil

Chief Financial Officer

Following are the principal internal board committees and their members as of December 31, 2007:

Audit Committee

Investment Committee

Emily King*

Willis Thomas King*

Dwayne Richard Williams

Leman Miles Porter

Harold Mack Humphrey

Benjamin Andrew Treuil

James Accursio

Dwayne Richard Williams

Mitchell Rabin

*Chairman

The Company maintained an audit committee, as required by Section 624.424(8) (c), Florida Statutes. The Company's treasurer was an audit committee member, which was not in compliance with Section 624.424(8) (c), Florida Statutes.

Conflict of Interest Procedure

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 69O-138.001, Florida Administrative Code. The minutes of the Board of Directors meetings did not reflect review and approval of the Conflict of Interest Statements as required by the NAIC Financial Condition Examiners Handbook and Section 607.0832(2), Florida Statutes.

Subsequent Event:

The Board of Directors met October 28, 2008, and approved the Conflict of Interest Statements.

Corporate Records

The recorded minutes of the shareholder, Board of Directors, and certain internal committees were reviewed for the period under examination. As noted above under Conflict of Interest, the recorded minutes of the Board of Directors did not initially reflect review and approval of the Conflict of Interest Statements.

The recorded minutes of the Board of Directors did not reflect review of the prior examination report as of December 31, 2006, as required by the NAIC Financial Condition Examiners Handbook.

Subsequent Event:

The Board of Directors met October 28, 2008, and reviewed the prior examination report as of December 31, 2006.

With the exception of the two preceding items, the minutes of the Board of Directors 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.

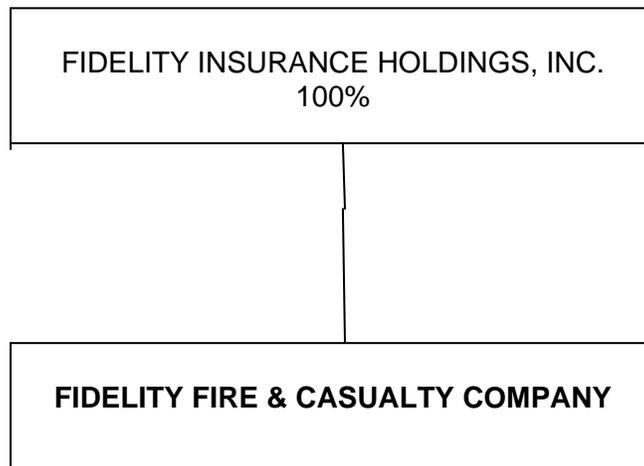
AFFILIATED COMPANIES

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 August 1, 2007, as required by Section 628.801, Florida Statutes, and Rule 69O-143.046, Florida Administrative Code.

A simplified organizational chart as of December 31, 2007, reflecting the holding company system, is shown below. Schedule Y of the Company's 2007 annual statement provided a list of all related companies of the holding company group.

**FIDELITY FIRE & CASUALTY COMPANY
ORGANIZATIONAL CHART**

DECEMBER 31, 2007



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

Tax Allocation Agreement

The Company, along with its parent and affiliates, filed a consolidated federal income tax return. On December 31, 2007, the method of allocation between the companies was based upon calculations on a separate return basis.

Management Agreement

The Company entered into a Management Agreement on March 1, 2007, with its parent, Fidelity Insurance Holdings, Inc., to provide financial, investment, benefit, reinsurance, and other

management services. The parent received 5 percent of net earned premium for the services provided.

Managing General Agent Agreement

The Company entered into a Managing General Agent agreement on March 1, 2007, with an affiliate, Fidelity Insurance Managers, Inc., (MGA) to provide underwriting, marketing and related claim services.

Effective February 19, 2008, the agreement was amended and currently contains the following provisions. The MGA received 10 percent of net earned premium for underwriting services, marketing, and related administrative services, 10.5 percent of net written premium as commissions on new and renewal business production, and a \$25 MGA processing fee. The MGA received 15.5 percent of gross incurred losses, or 1 percent for a catastrophe loss, for the claim services provided, along with 40% of recoveries from subrogation claims that are brought by the Company. The Company was responsible for all legal fees and costs along with all fees for consultants and experts.

As noted earlier in this report, the Company did not get prior approval for the original agreement from the Office as required by Consent Order #81765-05-CO. The amended agreement was submitted to and approved by the Office prior to execution.

As noted earlier in this report, the MGA did not hold funds in a fiduciary manner in a trust account as required by Consent Order #81765-05-CO and Section 626.7451 (3), Florida Statutes.

As noted earlier in this report, Consent Order #81765-05-CO required that the affiliate MGA provide a written notice approved by the insurer to insured individuals advising them of the identity of, and relationship among, the affiliate, the policyholder, and the insurer. Such a notice has not been provided to insured individuals.

FIDELITY BOND COVERAGE

The Company maintained fidelity bond coverage up to \$450,000 with a deductible of \$10,000, 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 had no pension, stock ownership, or insurance plans as of December 31, 2007.

STATUTORY DEPOSITS

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

STATE	Description	Book Value	Fair Value
FL	Cash	<u>\$ 250,000</u>	<u>\$ 250,000</u>
	TOTAL FLORIDA DEPOSITS	<u>\$ 250,000</u>	<u>\$ 250,000</u>
	TOTAL SPECIAL DEPOSITS	<u>\$ 250,000</u>	<u>\$ 250,000</u>

INSURANCE PRODUCTS

Territory

The Company was authorized to transact insurance in Florida. The Company received authorization from South Carolina in March of 2008.

Treatment of Policyholders

The Company had 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.

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 did not assume policies during 2007.

Ceded

The Company ceded risk on an excess of loss basis to various authorized and unauthorized reinsurers as listed on Schedule F, Part 3 of the annual statement. The primary authorized

reinsurers were various Syndicates of Lloyd's. The Company participated in the Florida Hurricane Catastrophe Fund.

The reinsurance contracts were reviewed by the Company's appointed actuary and were utilized in determining the ultimate loss opinion. The Company used an affiliate as an intermediary, Frontline Insurance Managers, Inc.

ACCOUNTS AND RECORDS

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

An independent CPA audited the Company's statutory basis financial statements annually for the years 2006 and 2007, 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 computerized system. The Company's balance sheet accounts were verified with the line items of the annual statement submitted to the Office.

The Company and non-affiliates had the following agreements:

Custodial Agreement

The Company had a custodial agreement with Bank of America that was in compliance with all requirements of Rule 69O-143.042, Florida Administrative Code.

Independent Auditor Agreement

The Company had an agreement with Thomas, Howell, Ferguson, PA to perform an audit of its statutory financial statements for the years 2006 and 2007

FINANCIAL STATEMENTS PER EXAMINATION

The following pages contain financial statements showing the Company's financial position as of December 31, 2007, and the results of its operations for the year then ended as determined by this examination. There were no adjustments made as a result of the examination.

FIDELITY FIRE & CASUALTY COMPANY
Assets

DECEMBER 31, 2007

	Per Company	Examination Adjustments	Per Examination
Cash	\$29,898	\$0	\$29,898
Short term investments	14,500,000		14,500,000
Investment income due and accrued	62,997		62,997
Premiums and considerations:			
Uncollected premium	719,460		719,460
Deferred premium	1,787,672		1,787,672
Net deferred tax asset	277,208		277,208
Totals	\$17,377,235	\$0	\$17,377,235

FIDELITY FIRE & CASUALTY COMPANY
Liabilities, Surplus and Other Funds

DECEMBER 31, 2007

	Per Company	Examination Adjustments	Per Examination
Losses	\$503,231	\$0	\$503,231
Loss adjustment expenses	72,088		72,088
Commissions payable	(345,626)		(345,626)
Other expenses	14,325		14,325
Taxes, licenses and fees	186,709		186,709
Current federal income taxes	543,372		543,372
Unearned premium	3,982,985		3,982,985
Advance premium	156,137		156,137
Ceded reinsurance premiums payable	933,902		933,902
Payable to parent, subsidiaries and affiliates	480,079		480,079
Aggregate write-ins for liabilities	130,623		130,623
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Total liabilities	\$6,657,825	\$0	\$6,657,825
Common capital stock	\$4,000,000		4,000,000
Gross paid in and contributed surplus	7,400,000		7,400,000
Unassigned funds (surplus)	(680,590)		(680,590)
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Surplus as regards policyholders	\$10,719,410		10,719,410
	<hr/>		
Total liabilities, surplus and other funds	\$17,377,235	\$0	\$17,377,235
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FIDELITY FIRE & CASUALTY COMPANY
Statement of Income

DECEMBER 31, 2007

Underwriting Income

Premiums earned	\$2,891,719
Deductions:	
Losses incurred	1,096,104
Loss expenses incurred	182,550
Other underwriting expenses incurred	1,432,485
Aggregate write-ins for underwriting deductions	0
Total underwriting deductions	\$2,711,139
Net underwriting gain or (loss)	\$180,580

Investment Income

Net investment income earned	\$509,958
Net realized capital gains or (losses)	0
Net investment gain or (loss)	\$509,958

Other Income

Net gain or (loss) from agents' or premium balances charged off	\$0
Finance and service charges not included in premiums	9,826
Aggregate write-ins for miscellaneous income	0
Total other income	\$9,826
Net income before dividends to policyholders and before federal & foreign income taxes	\$700,364
Dividends to policyholders	0
Net Income, after dividends to policyholders, but before federal & foreign income taxes	\$700,364
Federal & foreign income taxes	543,372
Net Income	\$156,992

Capital and Surplus Account

Surplus as regards policyholders, December 31 prior year	\$5,898,045
Net Income	\$156,992
Change in net deferred income tax	283,572
Change in non-admitted assets	(19,199)
Change in excess statutory over statement reserves	3,900,000
Surplus adjustments: Paid in	500,000
Examination Adjustment	0
Change in surplus as regards policyholders for the year	\$4,821,365
Surplus as regards policyholders, December 31 current year	\$10,719,410

COMMENTS ON FINANCIAL STATEMENTS

Liabilities

Losses and Loss Adjustment Expenses \$575,319

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, 2007, made a reasonable provision for all unpaid loss and loss expense obligations of the Company under the terms of its policies and agreements.

INS Consultants, Inc. (INS) was retained by the Office to conduct a review of the Company's loss and loss adjustment expense reserves as of December 31, 2007, in conjunction with the financial condition examination.

INS found the Company's gross and net loss and loss adjustment expense reserves at December 31, 2007, to be reasonably stated.

Capital and Surplus

The amount reported by the Company of \$10,719,410, exceeded the minimum of \$4,000,000 required by Section 624.408, Florida Statutes.

A comparative analysis of changes in surplus is shown below.

**FIDELITY FIRE & CASUALTY COMPANY
COMPARATIVE ANALYSIS OF CHANGES IN SURPLUS**

DECEMBER 31, 2007

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, 2007, per Annual Statement	\$10,719,410
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	<u>PER COMPANY</u>	<u>PER EXAM</u>	<u>INCREASE (DECREASE) IN SURPLUS</u>
ASSETS:			
No adjustments			\$0
LIABILITIES:			
No adjustments			\$0
Net Change in Surplus:			0
Surplus as Regards Policyholders December 31, 2007, Per Examination			\$10,719,410

SUMMARY OF FINDINGS

Compliance with previous directives

There were no items of interest or corrective action that have not been resolved by the Company regarding findings in the examination as of December 31, 2006.

Current examination comments and corrective action

The following is a brief summary of items of interest and corrective action to be taken by the Company regarding findings in the examination as of December 31, 2007.

The Company was party to Consent Order 81765-05-CO dated March 26, 2005, with the Office regarding the application for the issuance of a Certificate of Authority. At December 31, 2007, as outlined below, the Company was not in compliance with that consent order.

- Paragraph 18e requires that the affiliated MGA hold the funds collected on behalf of the Company in a fiduciary capacity in a trust account. Such a trust account is also required by Section 626.7451 (3) Florida Statutes. A trust account has not been established as required by both the Consent Order and 626.7451 (3), Florida Statutes.
- Paragraph 18j requires that the affiliated MGA provide a written notice to insured individuals advising them of the identity of, and relationship among, the affiliate, the policyholder, and the insurer. Such a notice has not been provided to insured individuals.

We recommend that the Company comply with all provisions of Consent Order #81765-05-CO.

The Company had not written Allied Lines nor removed the line of business from the Certificate of Authority as of December 31, 2007, and was not in compliance with Section 624.430 (1), Florida Statutes. **We recommend the removal of the line of business as required by Section 624.430 (1), Florida Statutes.**

The Company's treasurer was an audit committee member, which was not in compliance with Section 624.424(8) (c), Florida Statutes. **We recommend that the Company's Board of Directors appoint members to the audit committee to comply with Section 624.424(8) (c), Florida Statutes.**

CONCLUSION

The insurance examination practices and procedures as promulgated by the NAIC have been followed in ascertaining the financial condition of **Fidelity Fire & Casualty Company** as of December 31, 2007, consistent with the insurance laws of the State of Florida.

Per examination findings, the Company's Surplus as Regards Policyholders was \$10,719,410, in compliance with Section 624.408, Florida Statutes.

In addition to the undersigned, Patricia Casey Davis, CFE, CPA, INSRIS Supervising Examiner; Michael F. Hampton, CPA, CFE, INSRIS Examiner in Charge; and Samita Lamsal, OIR Financial Examiner/Analyst II, participated in the examination. We also recognize Michael W. Morro, ACAS, MAAA and James R. Neidermyer, FCAS, MAAA of INS Consultants, Inc. participation in the examination.

Respectfully submitted,

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