

**REPORT ON EXAMINATION**  
**OF**  
**FIRST COLONIAL INSURANCE**  
**COMPANY**

**JACKSONVILLE, FLORIDA**

**AS OF**  
**DECEMBER 31, 2011**

**BY THE**  
**FLORIDA OFFICE OF INSURANCE REGULATION**

## TABLE OF CONTENTS

<b>LETTER OF TRANSMITTAL</b> .....	-
<b>SCOPE OF EXAMINATION</b> .....	1
<b>SUMMARY OF SIGNIFICANT FINDINGS</b> .....	2
CURRENT EXAM FINDINGS.....	2
PRIOR EXAM FINDINGS.....	2
<b>HISTORY</b> .....	2
GENERAL .....	2
DIVIDENDS TO STOCKHOLDERS.....	3
CAPITAL STOCK AND CAPITAL CONTRIBUTIONS.....	3
SURPLUS NOTES .....	3
ACQUISITIONS, MERGERS, DISPOSALS, DISSOLUTIONS, AND PURCHASE OR SALES THROUGH REINSURANCE .....	4
<b>CORPORATE RECORDS</b> .....	4
CONFLICT OF INTEREST.....	4
<b>MANAGEMENT AND CONTROL</b> .....	5
MANAGEMENT .....	5
AFFILIATED COMPANIES .....	6
ORGANIZATIONAL CHART .....	7
TAX ALLOCATION AGREEMENT.....	8
SERVICE AND EXPENSE AGREEMENT .....	8
INVESTMENT MANAGEMENT AGREEMENT .....	8
<b>FIDELITY BOND AND OTHER INSURANCE</b> .....	8
<b>PENSION, STOCK OWNERSHIP AND INSURANCE PLANS</b> .....	9
<b>TERRITORY AND PLAN OF OPERATIONS</b> .....	9
TREATMENT OF POLICYHOLDERS .....	10
<b>COMPANY GROWTH</b> .....	10
PROFITABILITY OF COMPANY .....	11
<b>LOSS EXPERIENCE</b> .....	11
<b>REINSURANCE</b> .....	11
ASSUMED .....	12
CEDED .....	12
<b>ACCOUNTS AND RECORDS</b> .....	12
CUSTODIAL AGREEMENT .....	13
THIRD PARTY ADMINISTRATIVE SERVICES AGREEMENTS .....	13
INDEPENDENT AUDITOR AGREEMENT .....	13
<b>INFORMATION TECHNOLOGY REPORT</b> .....	13
<b>STATUTORY DEPOSITS</b> .....	14
<b>FINANCIAL STATEMENTS PER EXAMINATION</b> .....	15

ASSETS .....	16
LIABILITIES, SURPLUS AND OTHER FUNDS .....	17
STATEMENT OF INCOME .....	18
COMPARATIVE ANALYSIS OF CHANGES IN SURPLUS .....	19
<b>COMMENTS ON FINANCIAL STATEMENTS.....</b>	<b>20</b>
LIABILITIES .....	20
CAPITAL AND SURPLUS .....	20
<b>CONCLUSION.....</b>	<b>21</b>

September 28, 2012

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, Rule 69O-138.005, Florida Administrative Code, 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, 2011, of the financial condition and corporate affairs of:

**FIRST COLONIAL INSURANCE COMPANY  
1776 AMERICAN HERITAGE LIFE DRIVE  
JACKSONVILLE, FLORIDA 32224**

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, 2011. The Company was last examined by representatives of the Florida Office of Insurance Regulation (Office) as of December 31, 2006. This examination commenced with planning at the Office on June 25, 2012, to June 29, 2012. The fieldwork commenced on July 10, 2012, and concluded as of September 28, 2012.

This financial examination was a multi-state 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**

There were no material findings or exceptions noted during the examination as of December 31, 2011.

### **Prior Exam Findings**

There were no findings, exceptions or corrective action to be taken by the Company for the examination as of December 31, 2006.

## **HISTORY**

### **General**

The Company was incorporated in Florida on February 17, 1987, and commenced business on April 28, 1987, as First Colonial Insurance Company.

The Company was authorized to transact the following insurance coverage in Florida on various dates beginning 1987 and continues to be authorized as of December 31, 2011:

Ocean marine  
Auto warranties

Inland marine  
Other liability

Prepaid legal  
Credit  
Miscellaneous casualty

Private passenger auto physical damage  
Service warranties (non-auto)

The Articles of Incorporation and the Bylaws were not amended during the period covered by this examination.

### **Dividends to Stockholders**

The Company did not declare or paid any dividends during the period of this examination.

### **Capital Stock and Capital Contributions**

As of December 31, 2011, the Company's capitalization was as follows:

Number of authorized common capital shares	5,000,000
Number of shares issued and outstanding	2,500,000
Total common capital stock	\$2,500,000
Par value per share	\$1.00

Control of the Company was maintained by its parent, American Heritage Life Insurance Company, who owned 100% of the stock issued by the Company, who in turn was 100% owned by American Heritage Life Investment Corporation, a wholly owned subsidiary of Allstate Corporation, a Delaware corporation. The ultimate controlling parent was the Allstate Corporation, a publicly traded company.

The parent contributed \$1,516,672 in the form of a commercial mortgage on property to the Company as of March 27, 2009.

### **Surplus Notes**

The Company did not have any surplus notes during the period of this examination.

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

On January 19, 2010, the Office approved the Disclaimer of Affiliation application submitted for Blackrock, Inc.'s indirect acquisition of more than 5%, but less than 10%, of the voting shares of First Colonial Insurance Company.

The Company had no other acquisitions, mergers, disposals, and purchase or sales through reinsurance during the period of this examination.

## **CORPORATE RECORDS**

The recorded minutes of the Shareholder, Board of Directors (Board) 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 compliance with the NAIC Financial Condition Examiners Handbook adopted by Rule 69O-138.001, Florida Administrative Code and 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 69O-138.001, Florida Administrative Code.

## MANAGEMENT AND CONTROL

### Management

The annual shareholder meeting for the election of directors was held in accordance with Section 628.231, Florida Statutes. Directors serving as of December 31, 2011, were:

#### Directors

<b>Name and Location</b>	<b>Principal Occupation</b>
Donald John Bailey Northbrook, Illinois	Chief Executive Officer First Colonial Insurance Company
Thomas Matthew Goldstein Northbrook, Illinois	Senior Vice President Allstate Insurance Company
Douglas John Herberger Jacksonville, Florida	President First Colonial Insurance Company
Elizabeth Ann Mahin Jacksonville, Florida	Executive Allstate Insurance Company
Sharyn Patricia Rudoff Northbrook, Illinois	Director Allstate Insurance Company

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

#### Senior Officers

<b>Name</b>	<b>Title</b>
Douglas John Herberger	President
Donald John Bailey	Chief Executive Officer
Mario Rizzo	Treasurer
Mary Jovita McGinn	Secretary
Samuel Henry Pilch	Chief Financial Officer
Richard Clayton Crist, Jr.	Senior Vice President
Teresa Jean Dalenta	Senior Vice President
Thomas Matthew Goldstein	Senior Vice President
David Scott Harper (a)	Senior Vice President
Jeffrey John McRae	Senior Vice President
Steven Carl Verney (a)	Senior Vice President & Assistant Treasurer

(a) On July 17, 2012 David Scott Harper resigned as Senior Vice President and Assistant Treasurer and Steven Carl Verney was appointed Assistant Treasurer in addition to his Senior Vice President role.

The Company utilized the audit committee of the parent company, American Heritage Life Insurance Company, in accordance with Section 624.424(8)(c), Florida Statutes. Following were members of the audit committee as of December 31, 2011:

**Audit Committee**

Matthew E. Winter <sup>1</sup> (b)  
Gregory J. Guidos  
Samuel H. Pilch

<sup>1</sup> Chairman

(b) Resigned on April 12, 2012, and was replaced by Donald Civgin as Audit Committee Chairman.

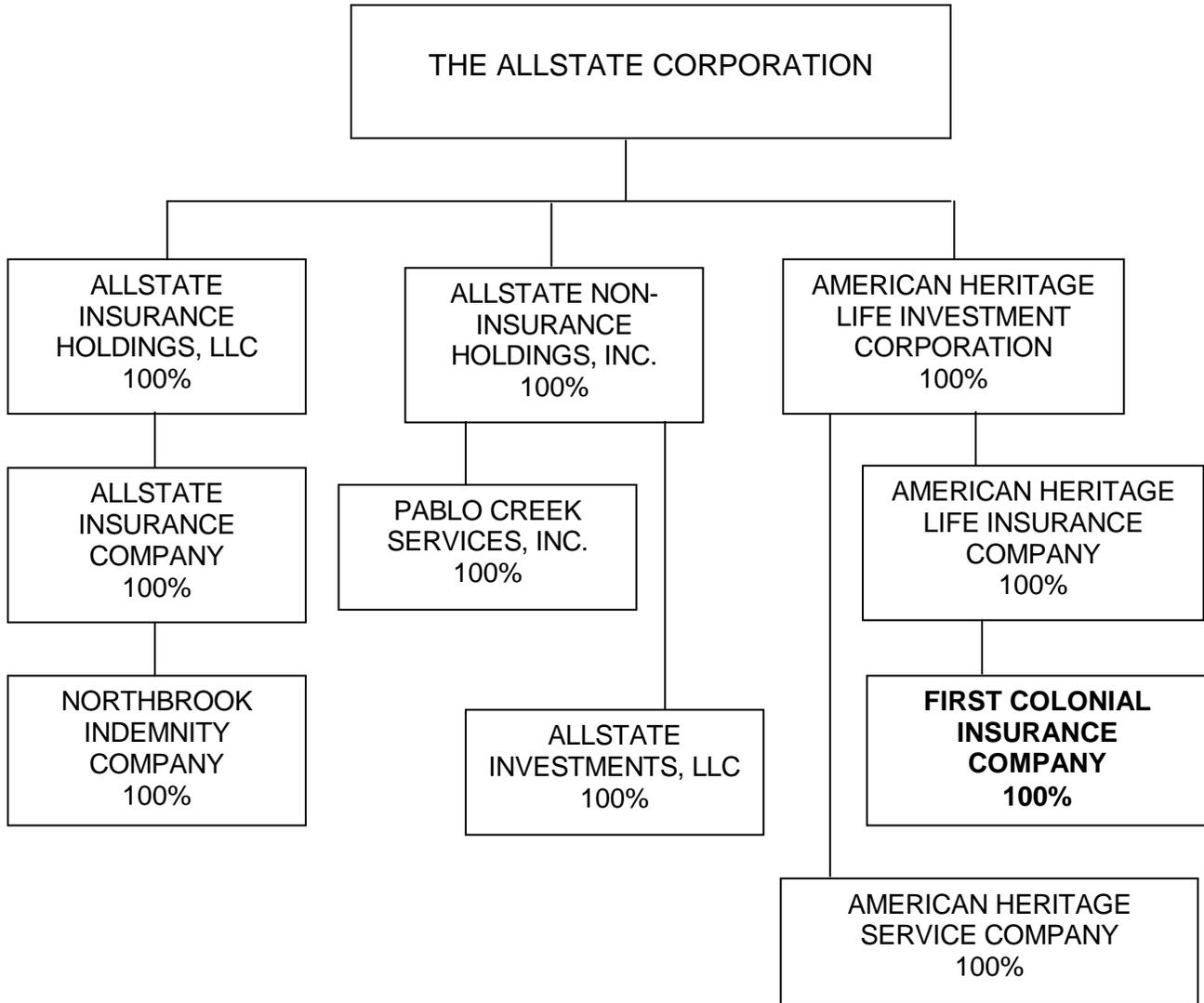
**Affiliated Companies**

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 April 18, 2012, as required by Section 628.801, Florida Statutes, and Rule 69O-143.046, Florida Administrative Code.

An organizational chart as of December 31, 2011, reflecting the holding company system, is shown on the following page. Schedule Y of the Company's 2011 annual statement provided a list of all related companies of the holding company group.

**FIRST COLONIAL INSURANCE COMPANY  
ORGANIZATIONAL CHART**

**DECEMBER 31, 2011**



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

### **Tax Allocation Agreement**

The Company, along with its ultimate parent, The Allstate Corporation, and other affiliated companies, filed a consolidated federal income tax return. On December 31, 2011, the method of allocation between the companies was based upon calculations on a separate return basis.

### **Service and Expense Agreement**

The Company and other affiliated companies had a service and expense agreement with the ultimate parent, The Allstate Corporation, for services including marketing, claims, underwriting and policyholder services.

### **Investment Management Agreement**

The Company and other affiliated companies had an investment management agreement with Allstate Investments, LLC to provide investment management services.

## **FIDELITY BOND AND OTHER INSURANCE**

The Company was included in the American Heritage Life Insurance Company's fidelity bond coverage up to \$4,000,000 with a deductible of \$500,000 which adequately provided for the suggested minimum amount of coverage for the Company as recommended by the NAIC of \$1,000,000.

The Allstate Corporation also maintained Directors and Officers (D&O) liability insurance coverage with limits of up to \$10,000,000 for wrongful acts (fiduciary), up to \$15,000,000 for all wrongful acts other than wrongful acts, and aggregate limit of liability of up to \$25,000,000 with \$0 retention. The Allstate Corporation provided other insurance coverage, such as automobile liability, workers' compensation, excess workers' compensation, property, general liability, and surety bonds.

## **PENSION, STOCK OWNERSHIP AND INSURANCE PLANS**

The Company utilizes the services of Allstate Insurance Company employees. Allstate Insurance Company and The Allstate Corporation provided various benefits, including defined benefit pension plans, certain health care and life insurance benefits for certain eligible employees and retired employees and participation in the Allstate 401(k) Savings Plan. The Company was allocated an appropriate share of the costs associated with these benefits in accordance with the Agreement.

## **TERRITORY AND PLAN OF OPERATIONS**

The Company was authorized to transact insurance in the following states and the District of Columbia:

Alabama	Alaska	Arizona	Arkansas	Colorado
Delaware	Florida	Georgia	Hawaii	Idaho
Illinois	Indiana	Iowa	Kansas	Kentucky
Louisiana	Maine	Maryland	Massachusetts	Michigan
Minnesota	Mississippi	Missouri	Montana	Nebraska
Nevada	New Hampshire	New Jersey	New Mexico	New York
North Carolina	North Dakota	Ohio	Oklahoma	Oregon
Pennsylvania	Rhode Island	South Carolina	South Dakota	Tennessee
Texas	Utah	Vermont	Virginia	Washington
West Virginia	Wisconsin			

## **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 decrease in the Company's earned premiums beginning in 2010 was due substantially to the automobile downturn in 2009, which resulted in lower used car prices and fewer new car sales. Due to the Company's concentration and reliance on the automobile industry, results were largely dependent on the state of the automobile industry, which has begun to recover in recent years. The decrease in underwriting and net income in 2011 was due largely to \$27 million in expenses incurred related to the settlement of a lawsuit. In recent years, surplus continued to grow with positive, though declining net income.

## 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.

	<b>2011</b>	<b>2010</b>	<b>2009</b>	<b>2008</b>	<b>2007</b>
Premiums Earned	73,396,576	76,728,462	179,528,580	101,485,225	117,040,474
Net Underwriting Gain/(Loss)	(563,221)	13,865,263	1,213,805	(43,578,448)	5,552,698
Net Income	1,073,655	17,599,830	13,741,290	(16,836,463)	12,691,267
Total Assets	349,660,457	312,039,450	311,088,542	382,676,477	379,568,851
Total Liabilities	199,227,289	171,934,074	190,939,395	276,345,241	256,526,162
Surplus As Regards Policyholders	150,433,168	140,105,377	120,149,147	106,331,236	123,042,688

## LOSS EXPERIENCE

During the current examination period, the Company showed favorable development overall, with the exception of unfavorable development in 2009 resulting from the decline in the automobile industry, which has recovered since. The favorable development since 2010 was a result of the recovering automobile industry. The one and two-year net loss developments at the end of the current examination period were both favorable at \$8.7 million and \$8.4 million, respectively.

## 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 on a quota share basis from affiliated and non-affiliated insurance companies.

## **Ceded**

The Company ceded risk on a quota share basis to authorized and unauthorized reinsurers. The Company ceded to numerous producer owned reinsurance companies on a 100% quota share basis. The reserves were collateralized by trust and/or letters of credit.

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 Jacksonville, Florida.

An independent CPA audited the Company's statutory basis financial statements annually for the years 2007, 2008, 2009, 2010 and 2011, 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 in the financials module of an enterprise application developed and licensed from a third party software developer. The Company also licensed a variety of other modules from the same enterprise software developer. These modules, as well as other licensed third party and internally developed applications, systematically interfaced

with the financials module, to provide the data necessary to create the Company's financial statements.

The Company and non-affiliates had the following agreements:

### **Custodial Agreement**

The Company maintained a custodial agreement with Citibank, N.A. executed on February 3, 2011. The agreement was in compliance with Rule 690-143.042, Florida Administrative Code.

### **Third Party Administrative Services Agreements**

The Company utilized eight non-affiliated third party administrators (TPAs) to produce a portion of its insurance business. The TPAs were responsible for services that included development, marketing and administration of programs including procurement of contractual liability and service contract reimbursement insurance policies, premium collection, policy maintenance, and claims administration.

### **Independent Auditor Agreement**

The Company contracted with an external independent CPA firm to perform the annual audit of its financial statements as required by Rule 690-137.002 (7) (c), Florida Administrative Code.

## **INFORMATION TECHNOLOGY REPORT**

Scott Langstein, CISA, IT Manager, of Cerebres, LLC (subcontractor of Lewis & Ellis, Inc.) 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 and with various state officials as required or permitted by law:

STATE	Description	Par Value	Market Value
FL	US TBDS, 7.25%, 08/15/2022	\$ 300,000	\$454,078
FL	USTBDS, 8.13%, 08/15/2021	800,000	1,253,000
FL	USTBDS, 7.13%, 02/15/2023	1,050,000	1,589,961
FL	USTBDS, 7.63%, 11/15/2022	500,000	778,438
FL	USTBDS, 7.88%, 02/15/2021	<u>150,000</u>	<u>228,902</u>
TOTAL FLORIDA DEPOSITS		<u>\$2,800,000</u>	<u>\$4,302,379</u>
GA	USTBDS, 7.25%, 08/15/22	\$ 35,000	\$ 52,976
LA	USTNTS, 4.00%, 08/14/12	100,000	103,332
MA	USTBDS, 8.12%, 05/15/21	300,000	466,782
MA	USTBDS, 6.62%, 02/15/27	200,000	307,750
NV	USTBDS, 8.12%, 08/15/19	500,000	743,594
NH	USTBDS, 6.25%, 08/15/23	500,000	715,625
NM	USTBDS, 8.12%, 08/15/19	300,000	446,156
NC	USTBDS, 8.12%, 08/15/19	175,000	260,258
NC	USTBDS, 8.00%, 11/15/21	125,000	195,371
OK	USTBDS, 8.12%, 08/15/21	300,000	469,875
SC	USTBDS, 8.00%, 11/15/21	175,000	273,520
VA	USTBDS, 7.25%, 08/15/22	450,000	681,117
TOTAL OTHER DEPOSITS		<u>\$3,160,000</u>	<u>\$4,716,356</u>
TOTAL SPECIAL DEPOSITS		<u>\$5,960,000</u>	<u>\$9,020,936</u>

## **FINANCIAL STATEMENTS PER EXAMINATION**

The following pages contain financial statements showing the Company's financial position as of December 31, 2011, 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."

**FIRST COLONIAL INSURANCE COMPANY**

**Assets**

**DECEMBER 31, 2011**

	<b>Per Company</b>	<b>Examination Adjustments</b>	<b>Per Examination</b>
Bonds	\$309,962,385		\$309,962,385
Mortgage loans on real estate			
First liens	900,722		900,722
Cash and short-term investments	10,123,518		10,123,518
Other investments	624,477		624,477
Interest and dividend income due & accrued	2,646,426		2,646,426
Agents' balances:			
Uncollected premium	4,892,173		4,892,173
Reinsurance recoverable from reinsurers	255,028		255,028
Funds held by or deposited with reinsured companies	689		689
Other amounts recievable under reinsurance contracts	458,474		458,474
Net deferred tax asset	17,790,249		17,790,249
Receivable from parents, subsidiaries and affiliates	1,952,114		1,952,114
Aggregate write-in for other than invested assets	54,204		54,204
	<hr/>		
Totals	<u>\$349,660,457</u>	<u>\$0</u>	<u>\$349,660,457</u>

**FIRST COLONIAL INSURANCE COMPANY**  
**Liabilities, Surplus and Other Funds**

**DECEMBER 31, 2011**

	<b>Per Company</b>	<b>Examination Adjustments</b>	<b>Per Examination</b>
Losses	\$9,350,504		\$9,350,504
Loss adjustment expenses	68,390		68,390
Commissions payable, contingent commissions and other similar charges	1,682,813		1,682,813
Other expenses	34,744,748		34,744,748
Taxes, licenses and fees	463,099		463,099
Current federal and foreign income taxes on realized capital gains (losses)	14,704,089		14,704,089
Unearned premium	125,348,422		125,348,422
Ceded reinsurance premiums payable (net of ceding commissions)	3,079,068		3,079,068
Funds held under reinsurance treaties	54,296		54,296
Remittances and items not allocated	32,280		32,280
Provision for reinsurance	981,853		981,853
Payable to parent, subsidiaries and affiliates	6,300,559		6,300,559
Payable for securities	37,168		37,168
Aggregate write-ins for liabilities	2,379,999		2,379,999
<b>Total Liabilities</b>	<b>\$199,227,289</b>		<b>\$199,227,289</b>
Aggregate write-ins for special surplus funds	\$3,896,971		\$3,896,971
Common capital stock	2,500,000		2,500,000
Gross paid in and contributed surplus	126,261,672		126,261,672
Unassigned funds (surplus)	17,774,526		17,774,526
Surplus as regards policyholders	\$150,433,168		\$150,433,168
<b>Total liabilities, surplus and other funds</b>	<b>\$349,660,457</b>		<b>\$349,660,457</b>

**FIRST COLONIAL INSURANCE COMPANY**  
**Statement of Income**

**DECEMBER 31, 2011**

**Underwriting Income**

Premiums earned		\$73,396,576
	<b>Deductions:</b>	
Losses incurred		\$16,254,041
Loss expenses incurred		331,057
Other underwriting expenses incurred		57,374,699
Total underwriting deductions		\$73,959,798
Net underwriting gain or (loss)		(\$563,221)

**Investment Income**

Net investment income earned		\$10,443,172
Net realized capital gains or (losses)		3,809,105
Net investment gain or (loss)		\$14,252,277

**Other Income**

Net gain or (loss) from agents' or premium balances charged off		(\$48,377)
Aggregate write-ins for miscellaneous income		(2,417)
Total other income		(\$50,795)

Net income before dividends to policyholders and before federal & foreign income taxes		\$13,638,262
Dividends to policyholders		0
Net Income, after dividends to policyholders, but before federal & foreign income taxes		\$13,638,262
Federal & foreign income taxes		12,564,607
Net Income		\$1,073,655

**Capital and Surplus Account**

Surplus as regards policyholders, December 31 prior year		\$140,105,377
Net Income		\$1,073,655
Net unrealized capital gains or losses		441,191
Change in net deferred income tax		8,954,199
Change in provision for reinsurance		(477,751)
Change in non-admitted assets		229,699
Aggregate write-ins for gains and losses in surplus		106,801
Examination Adjustment		0
Change in surplus as regards policyholders for the year		\$10,327,792
Surplus as regards policyholders, December 31 current year		\$150,433,168

A comparative analysis of changes in surplus is shown below.

**FIRST COLONIAL INSURANCE COMPANY**  
**Comparative Analysis of Changes in Surplus**

**DECEMBER 31, 2011**

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, 2011, per Annual Statement	\$150,433,168
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	<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			
LIABILITIES: No Adjustment			
Net Change in Surplus:			<u>0</u>
Surplus as Regards Policyholders December 31, 2011, Per Examination			<u><u>\$150,433,168</u></u>

## COMMENTS ON FINANCIAL STATEMENTS

### Liabilities

**Losses and Loss Adjustment Expenses** \$9,418,894

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, 2011, made a reasonable provision for all unpaid loss and loss expense obligations of the Company under the terms of its policies and agreements.

The Office consulting actuary, Greg Wilson, FCAS, MAAA, of Lewis & Ellis, Inc., reviewed the loss and loss adjustment expense work papers provided by the Company and he was in concurrence with this opinion.

### Capital and Surplus

The amount of Capital and surplus reported by the Company of \$150,433,168, which exceeded the minimum of \$14,126,253 required by Section 624.408, Florida Statutes.

## CONCLUSION

The insurance examination practices and procedures as promulgated by the NAIC have been followed in ascertaining the financial condition of **First Colonial Insurance Company** as of December 31, 2011, consistent with the insurance laws of the State of Florida.

Per examination findings, the Company's surplus as regards policyholders was \$150,433,168, which exceeded the minimum of \$14,126,253 as required by Section 624.408, Florida Statutes.

In addition to the undersigned, Sarah Lucibello, CPA, CFE, Examiner-In-Charge and Kate Bolbas, CFE, CPA, Amy Carter, CPA, and Lindsey Pittman, CPA, CFE, Participating Examiners, of Lewis and Ellis, Inc. participated in the examination. John Romano, CPA, CFE, Examination Manager, of ParenteBeard LLC also participated in the examination. In addition, Greg Wilson, FCAS, MAAA, consulting actuary of Lewis & Ellis, Inc., and Scott Langstein, CISA, IT Manager of Cerebres, LLC and Kyra Brown, APIR, Financial Specialist, and Billy Poulos, CIA, CGAP, Reinsurance/Financial Specialist, of the Office also participated in the examination.

Respectfully submitted,

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Mary M. James, CFE, CPM  
Financial Administrator  
Florida Office of Insurance Regulation