

REPORT ON EXAMINATION
OF
FIRST COLONIAL INSURANCE
COMPANY
JACKSONVILLE, FLORIDA

AS OF
DECEMBER 31, 2003

BY THE
OFFICE OF INSURANCE REGULATION

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Tallahassee, Florida
January 14, 2005

Honorable John Morrison
Secretary, Western Zone, NAIC
Commissioner
Montana Department of Insurance
840 Helena Avenue
Helena, Montana 59601

Honorable Diane Koken
Secretary, Northeastern Zone, NAIC
Commissioner
Pennsylvania Insurance Department
1326 Strawberry Square, 13th floor
Harrisburg, Pennsylvania 17120

Honorable Jim Atterholt
Secretary, Midwestern Zone, NAIC
Acting Commissioner
Indiana Department of Insurance
311 W. Washington Street, Suite 300
Indianapolis, Indiana 46204-2787

Honorable John Oxendine
Secretary, Southeastern Zone, NAIC
Commissioner
2 Martin Luther King Jr. Drive
Floyd Memorial Bldg, 704 West Tower
Atlanta, Georgia 30334

Kevin M. McCarty
Commissioner
Office of Insurance Regulation
State of Florida
Tallahassee, Florida 32399-0329

Dear Madam and Sirs:

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:

**FIRST COLONIAL INSURANCE COMPANY
1776 AMERICAN HERITAGE LIFE DRIVE
JACKSONVILLE, FL 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, 2000 through December 31, 2003. The Company was last examined by representatives of the Florida Office of Insurance Regulation (Office) as of December 31, 1999. This examination commenced, with planning at the Office, on September 13, 2004, to September 17, 2004. The fieldwork commenced on September 20, 2004, and was concluded as of January 14, 2005. 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 an association zone 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, 1999, along with resulting action taken by the Company in connection therewith.

Corporate Records

There was no documentation in the minutes reviewed, that the Company directors reviewed the previous examination report.

Resolution: There was documentation that the Company directors reviewed the latest examination report.

Reinsurance

The Company acted as a fronting agent for specified unauthorized insurers, which were not approved reinsurers.

Resolution: The Company no longer acts as a fronting agent.

A letter of credit issued on behalf of Colonial Reinsurance Company listed American Heritage Life Insurance Company as beneficiary.

Resolution: The letter of credit was changed to reflect the name of the Company.

Bonds

An investment transferred from an affiliate on March 10, 2000, was incorrectly reported on Schedule D of the 1999 Annual Statement.

Resolution: The Company has correctly reported items on their subsequent annual and quarterly filings.

HISTORY

General

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

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

Credit
Inland Marine
Private Passenger Automobile Physical Damage
Automobile Warranties
Service Warranties

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

Capital Stock

As of December 31, 2003, 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 percent of the stock issued by the Company, who in turn was 100 percent owned by The Allstate Corporation, a Delaware corporation.

Profitability of Company

The Company reported an underwriting gain of \$1,239,613 for the year ending December 31, 2000 and underwriting losses of \$676,955, \$12,053,944, and \$13,173,302 for the years ending December 31, 2001, 2002, and 2003, respectively. The Company reported net investment gains of \$304,756, \$2,049,129, \$1,649,229, and \$2,772,674, for the years ending December 2000, 2001, 2002, and 2003, respectively.

Dividends to Stockholders

The Company did not declare or pay dividends to its stockholder during the period of this 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
Anton Wanderon Jacksonville, Florida	Director, President
Gary Scott Stere Jacksonville, Florida	Director
Gregory James Guidos Jacksonville, Florida	Director, Treasurer
David Andrew Bird Jacksonville, Florida	Director, Chairman of the Board, CEO
Charles Calvin Baggs Jacksonville, Florida	Director
William Harrison Monie, Jr. Jacksonville, Florida	Director

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

Senior Officers

Name	Title
Anton Wanderon	President
Gregory James Guidos	Treasurer
Gary Scott Stere	Secretary

The parent company used internal committees for all subsidiaries, including the following, in accordance with Section 607.0825, FS:

Executive Committee
Audit Committee
Finance & Investment Committee

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 Executive and Investment 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.

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

There were no acquisitions, mergers, disposals, dissolutions, or purchase or sales through reinsurance.

Surplus Debentures

The Company had no surplus debentures.

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 August 9, 2004, as required by Section 628.801, FS, and Rule 69O-143.046, FAC.

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

Cost Sharing and Management Fee Agreement

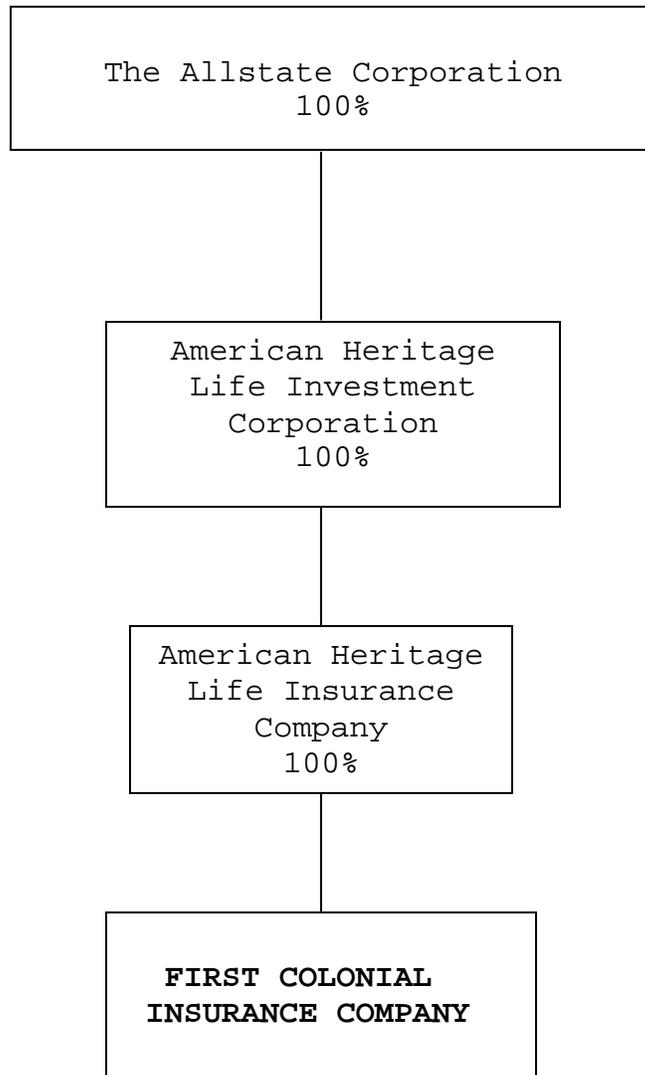
The Company had a cost sharing and management fee agreement with its parent, American Heritage Life Insurance Company, to provide services to the Company for day-to-day operations of certain property, equipment and facilities.

MGA Agreement

The Company entered into an agreement with Credit Guard of Florida, Inc., who acted as an MGA as defined under Section 626.091, FS.

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.

**FIRST COLONIAL INSURANCE COMPANY
ORGANIZATIONAL CHART
DECEMBER 31, 2003**



FIDELITY BOND AND OTHER INSURANCE

The Allstate Corporation had a fidelity bond in the amount of \$50,000,000 with a deductible of \$25,000,000 for all of its subsidiaries. The Allstate Corporation received approval from the Illinois Department of Insurance on November 20, 2000 to increase the maximum deductible for fidelity bond coverage from \$500,000 to \$25,000,000. The Allstate Corporation provided all other insurance coverage for their subsidiaries.

PENSION, STOCK OWNERSHIP, AND INSURANCE PLANS

The Company had no employees.

STATUTORY DEPOSITS

The following securities were deposited with the State of Florida as required by Section 624.411, FS, and with various state officials as required or permitted by law:

State	Description	Par Value	Market Value
FL	USTNTS, 6.5%, 10/15/06	\$ 300,000	\$ 334,125
FL	USTBDS, 7.625%, 11/15/22	500,000	654,845
FL	USTBDS, 7.875%, 02/15/21	150,000	199,595
FL	USTBDS, 8.125%, 08/15/21	800,000	1,091,000
FL	USTNTS, 5.5%, 05/15/09	<u>1,050,000</u>	<u>1,167,800</u>
TOTAL FLORIDA DEPOSITS		\$2,800,000	\$3,447,365
GA	USTBDS, 7.25%, 08/15/22	\$ 35,000	\$ 44,177
LA	USTBDS, 4.00%, 11/15/12	20,000	19,806
MA	USTBDS, 8.125%, 05/15/21	300,000	408,843
MA	USTBDS, 6.625%, 02/15/27	200,000	238,876
NV	USTBDS, 8.125%, 08/15/19	500,000	675,470
NH	USTBDS, 6.25%, 08/15/23	500,000	569,844

NM	FED HM BANK,5.91%,03/27/08	120,000	132,188
NC	USTBDS,8.125%, 08/15/19	175,000	236,415
NC	USTBDS, 8.00%, 11/15/21	125,000	168,829
OK	USTBDS,8.125%, 08/15/21	300,000	409,125
SC	USTBDS, 8.00%, 11/15/21	175,000	236,360
VA	USTBDS, 7.25%, 08/15/22	450,000	567,986
TOTAL OTHER DEPOSITS		<u>\$2,900,000</u>	<u>\$3,707,919</u>
Total Special Deposits		<u>\$5,700,000</u>	<u>\$7,155,283</u>

INSURANCE PRODUCTS AND RELATED PRACTICES

Territory and Plan of Operation

The Company was authorized to transact insurance in the following states and the District of Columbia, in accordance with Section 624.401(2), FS:

Alabama	Alaska	New Mexico	Arkansas	Colorado	Delaware
Florida	Georgia	Idaho	Illinois	Indiana	Iowa
Kansas	Kentucky	Louisiana	Maine	Maryland	Massachusetts
Michigan	Minnesota	Mississippi	Missouri	Montana	Nebraska
New Jersey	Nevada	North Dakota	Ohio	Oklahoma	North Carolina
Oregon	Pennsylvania	Rhode Island	South Dakota	Tennessee	South Carolina
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), 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 (except as noted below), reporting and settlement information deadlines.

Assumed

The Company assumed certain risks under various reinsurance contracts with affiliated and non-affiliated insurance companies.

Ceded

The Company ceded risk under various reinsurance contracts with affiliated and non-affiliated insurance companies.

The Company had numerous 100% quota share reinsurance agreements with producer owned reinsurance companies (PORC) and ceded business to approximately 151 PORC's. The reserves were collateralized by trust accounts and/or letters of credit.

The Company's reinsurance agreement with RGA Reinsurance Company, Inc. in Barbados contained a termination clause, that included payment of the memorandum account, which affected transfer of risk. On January 1, 2005, the agreement was amended to eliminate the memorandum account.

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 2000, 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 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 Jacksonville, Florida, where this examination was conducted.

The Company and non-affiliates had the following agreements:

Custodial Agreement

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

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."

FIRST COLONIAL INSURANCE COMPANY
Assets

DECEMBER 31, 2003

Classification	Per Company	Examination Adjustments	Per Examination
Bonds	\$85,741,407		\$85,741,407
Stocks:			
Preferred	981,578		981,578
Common	1,258		1,258
Cash:			
On deposit	937,794		937,794
Short-term investments	11,488,576		11,488,576
Agents' Balances:			
Uncollected premium	25,509,689		25,509,689
Reinsurance recoverable	915,426		915,426
Net deferred tax asset	3,188,275		3,188,275
Interest and dividend income due & accrued	1,141,446		1,141,446
Receivable from PSA	3,100,266		3,100,266
Aggregate write-in for other than invested assets	44,161		44,161
Totals	\$133,049,876	\$0	\$133,049,876

FIRST COLONIAL INSURANCE COMPANY
Liabilities, Surplus and Other Funds

DECEMBER 31, 2003

Liabilities	Per Company	Examination Adjustments	Per Examination
Losses	\$4,600,735		\$4,600,735
Loss adjustment expenses	212,557		212,557
Commissions payable	6,764,012		6,764,012
Other expenses	1,384,630		1,384,630
Unearned premium	63,743,375		63,743,375
Funds held under reinsurance treaties	10,316,640		10,316,640
Provision for reinsurance	2,211,554		2,211,554
Drafts outstanding	1,048,502		1,048,502
Aggregate write-ins for liabilities	<u>2,000,000</u>		<u>2,000,000</u>
Total Liabilities	\$92,282,005		\$92,282,005
Common capital stock	\$2,500,000		\$2,500,000
Gross paid in and contributed surplus	47,745,000		47,745,000
Unassigned funds (surplus)	<u>(9,477,130)</u>		<u>(9,477,130)</u>
Surplus as regards policyholders	<u>\$40,767,870</u>		<u>\$40,767,870</u>
Total liabilities, capital and surplus	<u>\$133,049,875</u>	<u>\$0</u>	<u>\$133,049,875</u>

FIRST COLONIAL INSURANCE COMPANY
Statement of Income

DECEMBER 31, 2003

Underwriting Income

Premiums earned	\$29,726,925
DEDUCTIONS:	
Losses incurred	15,939,272
Loss expenses incurred	142,580
Other underwriting expenses incurred	31,132,404
Aggregate write-ins for underwriting deductions	(4,314,029)
Total underwriting deductions	<u>\$42,900,227</u>
Net underwriting gain or (loss)	(\$13,173,302)

Investment Income

Net investment income earned	\$3,240,602
Net realized capital gains or (losses)	(467,928)
Net investment gain or (loss)	<u>\$2,772,674</u>

Other Income

Net income before dividends to policyholders and before federal & foreign income taxes	(\$10,400,628)
Dividends to policyholders	<u>0</u>
Net Income, after dividends to policyholders, but before federal & foreign income taxes	(\$10,400,628)
Federal & foreign income taxes	<u>0</u>
Net Income	(\$10,400,628)

Capital and Surplus Account

Surplus as regards policyholders, December 31 prior year	\$33,289,910
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Gains and (Losses) in Surplus

Net Income	(\$10,400,628)
Change in net deferred income tax	3,657,779
Change in nonadmitted assets	(1,903,362)
Change in provision for reinsurance	129,171
Capital changes: Paid in	495,000
Surplus adjustments: Paid in	15,500,000
Aggregate write-ins for gains and losses in surplus	0
Examination Adjustment	0
Change in surplus as regards policyholders for the year	<u>\$7,477,960</u>
Surplus as regards policyholders, December 31 current year	<u><u>\$40,767,870</u></u>

COMMENTS ON FINANCIAL STATEMENTS

Liabilities

Losses and Loss Adjustment Expenses	<u>\$4,813,292</u>
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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.

FIRST COLONIAL 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	\$40,767,870
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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 needed.			
LIABILITIES:			
No adjustment needed.			
Net Change in Surplus:			0
Surplus as Regards Policyholders December 31, 2003, Per Examination			\$40,767,870

SUMMARY OF FINDINGS

Compliance with previous directives

The Company has taken the necessary actions to comply with the comments made in the 1999 examination report issued by the Office.

Current examination comments and corrective action

There were no items of interest or corrective action to be taken by the Company regarding findings in the examination as of December 31, 2003.

SUBSEQUENT EVENTS

The Company made an amendment to their reinsurance agreement with RGA Reinsurance Company, Inc. Barbados, to eliminate the memorandum account, effective January 1, 2005.

CONCLUSION

The customary 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, 2003, consistent with the insurance laws of the State of Florida.

Per examination findings, the Company's surplus as regards policyholders was \$40,767,870, which was in compliance with Section 624.408, FS.

In addition to the undersigned, Fred Tarnell, CPA, Examiner/Analyst and Joseph Boor, Actuary, participated in the examination.

Respectfully submitted,

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

Michael Hampton, CPA, CFE, DABFA, CFE, CPM
Financial Examiner/Analyst Supervisor
Florida Office of Insurance Regulation