

REPORT ON EXAMINATION
OF
LIBERTY AMERICAN INSURANCE
COMPANY
PINELLAS PARK, FLORIDA

AS OF
DECEMBER 31, 2004

BY THE
OFFICE OF INSURANCE REGULATION

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Tallahassee, Florida

August 5, 2005

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 (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, 2004, of the financial condition and corporate affairs of:

**LIBERTY AMERICAN INSURANCE COMPANY
7785 66th STREET NORTH
PINELLAS PARK, FLORIDA 33781**

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, 2002 through December 31, 2004. The Company was last examined by representatives of the Florida Office of Insurance Regulation (Office) as of December 31, 2001. This examination commenced, with planning at the Office, on May 23, 2005, to May 25, 2005. The fieldwork commenced on May 26, 2005, and was concluded as of August 5, 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 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 (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 and the Company's independent audit reports 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, 2004. Transactions subsequent to year-end 2004 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, 2001, along with resulting action taken by the Company in connection therewith.

Cash and Short Term Investments

The Company issued checks rather than drafts and erroneously reported the outstanding check balance as drafts outstanding rather than as a reduction of cash.

Resolution: The Company is now reporting the checks outstanding correctly as a reduction of cash.

Agents' Balances – In Course of Collection

The Company was a member of an inter-company reinsurance and pooling agreement and erroneously reported the pooling transactions as affiliated transactions.

Resolution: The Company is now reporting the pooling transactions correctly.

Agents' Balances – Earned but Unbilled

Audit premiums were incorrectly reported as amounts receivable from parents, subsidiaries, and affiliates rather than as earned but unbilled premiums.

Resolution: The Company is now reporting audit premiums correctly and not part of receivable from parents, subsidiaries, and affiliates.

Other Expenses

The Company included amounts for unpaid taxes, licenses and fees, as other expenses.

Resolution: The Company is now classifying amounts for unpaid taxes, licenses and fees on the correct line on the annual statement.

Funds Held Under Reinsurance Treaty

The Company failed to place 100 percent of the reinsurance premiums ceded into the "Funds Withheld" account in accordance with the aggregate excess of loss treaty.

Resolution: The Company is now in compliance with their excess of loss treaty.

Ceded Reinsurance Premiums Payable

The Company incorrectly calculated the ceded balances payable.

Resolution: The Company is now correctly calculating the ceded balances payable.

HISTORY

General

The Company was incorporated in Florida on October 28, 1997 and commenced business on December 30, 1998 as Mobile United Property and Casualty Insurance Company, Inc. The name was subsequently changed to Liberty American Insurance Company on February 18, 2000.

At December 31, 2004, Frances M. Maguire was reported as owning 15.5% of Philadelphia Consolidated Holding Corporation (PCHC), pursuant to Exhibit 2 as submitted with the holding company registration statement dated April 14, 2005. Section 628.461(1), FS, requires Office approval of the acquisition of 5% or more of an insurer's outstanding voting securities.

Subsequent event:

On June 7, 2005, the Company sent an application package to the Office for Frances M. Maguire, as required in Section 628.461, FS, for those stockholders who have acquired 5% or more of the outstanding voting capital stock of the Company; which was approved by the Office.

In accordance with Section 624.401(1), FS, the Company was authorized to transact the following insurance coverage in Florida on December 31, 2004:

Homeowners Multi Peril
Inland Marine
Workers Compensation (*)
Mobile Home Multi Peril
Commercial Automobile Liability (*)
(*) reinsurance only

Commercial Multi Peril (*)
Other Liability (*)
Accident and Health (*)
Mobile Home Physical Damage (*)
Commercial Auto Physical Damage (*)

The Company has not written insurance coverage for the last three years in the line of business of accident and health. On July 17, 2005, the Company requested that the Office remove the accident and health line from the Company's certificate of authority.

Capital Stock

As of December 31, 2004, the Company's capitalization was as follows:

Number of authorized common capital shares	3,000,000
Number of shares issued and outstanding	2,000,000
Total common capital stock	\$2,000,000
Par value per share	\$1.00

Control of the Company was maintained by its parent, Liberty American Insurance Group, Inc., who owned 100% of the stock issued by the Company, who in turn was 100% owned by PCHC.

Profitability of Company

The following table shows the profitability trend (in dollars) of the Company for the period of examination.

	2004	2003	2002
Premiums Earned	62,861,743	57,157,884	42,118,635
Net Underwriting Gain/(Loss)	(1,805,475)	4,935,404	687,187
Net Income	5,195,395	4,722,043	2,212,716
Total Assets	74,166,256	110,558,196	83,289,467
Total Liabilities	47,820,954	88,461,590	65,142,855
Surplus As Regards Policyholders	26,345,302	22,096,606	18,146,612

Dividends to Stockholders

In accordance with Section 628.371, FS, the Company declared and paid dividends to its stockholder in 2002 and 2003 in the amounts of \$2,900,000 and \$2,210,000, respectively. No dividends were paid in 2004.

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, 2004, were:

Directors

Name and Location	Principal Occupation
James J. Maguire, Jr. Philadelphia, Pennsylvania	Chairman
Phillip D. Eldridge Pinellas Park, Florida	President and CEO
Craig P. Keller Philadelphia, Pennsylvania	Executive Vice President
T. Bruce Meyer Lutz, Florida	Sr. Vice President
Charles B. Sadler Pinellas Park, Florida	Vice President

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

Senior Officers

Name	Title
Phillip D. Eldridge	President and CEO
Craig P. Keller	Executive Vice President and Secretary

T. Bruce Meyer

Sr. Vice President and Treasurer

Charles B. Sadler

Vice President

The Company's board appointed several internal committees in accordance with Section 607.0825, FS. The following was the principal internal board committee and its members as of December 31, 2004:

Audit Committee

James J. Maguire, Jr., Chairman

Craig P. Keller

Philip D. Eldridge

Conflict of Interest Procedure

The Company 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 certain internal 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

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

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 April 14, 2005, 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:

Tax Allocation Agreement

The Company, along with its parent, filed a consolidated federal income tax return. On December 31, 2004, the method of allocation between the Company and its parent was subject to written agreement approved by the Board of Directors. Allocation is based on separate return calculations with current credit for net losses.

Managing General Agency (MGA) Agreement

The Company had an MGA agreement with Mobile Homeowners Insurance Agencies (MHIA), an affiliate. The agreement has been continuous since May 24, 2000. The Company, in consideration for the services rendered, agreed to pay MHIA a \$25.00 per policy MGA fee plus a percentage of premium based on the line of business written.

Claims Handling Agreement

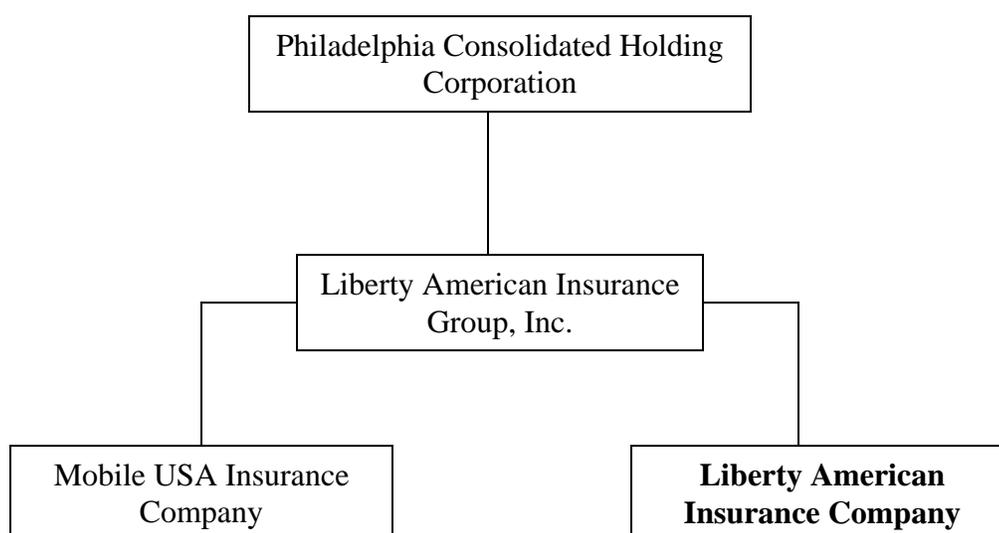
The Company entered into a claims handling agreement with its affiliate, MHIA, effective January 1, 1999. MHIA had the authority to monitor, supervise, report and handle all claims arising out of

policies issued by the agent for the mobile homeowners line of business. MHIA also had authority for the payment of losses, expenses and check writing authority in the amounts designated by the Company.

A simplified organizational chart as of December 31, 2004, reflecting the holding company system, is shown below. Schedule Y of the Company's 2004 annual statement provided a list of all related companies of the holding company group.

**LIBERTY AMERICAN INSURANCE COMPANY
ORGANIZATIONAL CHART**

DECEMBER 31, 2004



FIDELITY BOND AND OTHER INSURANCE

The Company maintained fidelity bond coverage up to \$10,000,000 with a retention of \$200,000, which adequately covered the suggested minimum amount of coverage for the Company and its affiliates as recommended by the NAIC.

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	U.S. Treasury note 5.875%, 11/15/2004	\$ 400,000	\$ 405,640
FL	U.S. Treasury note 1.75%, 12/31/2004	<u>50,000</u>	<u>50,000</u>
TOTAL SPECIAL DEPOSITS		<u>\$ 450,000</u>	<u>\$ 455,640</u>

INSURANCE PRODUCTS AND RELATED PRACTICES

Territory

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

Treatment of Policyholders

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

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

REINSURANCE

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

Assumed

The Company, along with its affiliates Mobile USA Insurance Company (MUSA) and Philadelphia Insurance Company (PIC), assumed business through an inter-company reinsurance and pooling agreement from Philadelphia Indemnity Insurance Company (PIIC). All participants ceded 100 percent of their net written premiums to PIIC, who in turn, retro ceded 10 percent of the combined total to MUSA, PIC, and the Company. In October of 2004, the inter-company pooling agreement

with PIC and PIIC was dissolved. The Company along with MUSA, entered into an inter-company reinsurance pooling agreement whereby MUSA ceded 100 percent of its net written premiums to the Company. The Company then retro ceded 50 percent of the combined net total back to MUSA.

Ceded

The Company ceded risk on a quota share and excess of loss basis to authorized and unauthorized reinsurers who secured their reinsurance balances as unauthorized reinsurers or the Company set up a provision for reinsurance liability. The primary reinsurers were MUSA, an authorized affiliate, and Empire Fire and Marine Insurance Company, an authorized reinsurer.

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 2002, 2003 and 2004, in accordance with Section 624.424(8), FS. Supporting work papers were prepared by the CPA as required by Rule 69O-137.002, FAC.

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

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

The Company and non-affiliates had the following agreements:

Custodial Agreement

The Company utilized the custodial services of CTC Illinois Trust Company (Custodian), a subsidiary of The Bank of New York, Inc. The safekeeping agreement between the Company and the Custodian contained the appropriate safeguards and controls as required by Rule 690-143.042, FAC.

Investment Management Agreement

The Company utilized the investment services of General Re – New England Asset Management, Inc.

Risk-Based Capital

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

Information Technology (IT) Report

An information technology evaluation was performed by Tracy Gates, CISA, CPA of Highland Clark, LLC. There were several issues concerning the logical and physical security of the computerized claims system.

- The claims system did not provide functional level security. Users with network access could also gain access to all the functions in the claim system. This access compromised the Company's internal control processes over claims check processing and segregation of duties between underwriting, claims, and accounting. Management responded to this issue on July 7, 2005, stating that functional level security was added to the

existing claims system to limit a user's access to the check writing and reserving modules of the system. Printed claim checks were currently retrieved from the check printer by personnel outside of the accounting and claims departments who have no access to the claims system. Physical security over the check printer was being enhanced to limit access only to authorized personnel. Also, claim check review duties were now rotated among various claims department personnel so that the initiation of a check request and the review of the printed check were segregated.

- An inspection of the SQL logins for the data warehouse database noted that four logins had no password assigned. One of those logins also had a blank login name. This inspection also noted four obsolete Windows logins from the old JERNT Windows domain. These accounts were no longer active since JERNT has been replaced by the LAIGNT domain. In response to these issues, management made two immediate corrections, which were inspected and confirmed by the IT specialist examiner on June 10, 2005: All logins without appropriate password protection or login name assignments have been either deleted or the appropriate security information has been added. The proper procedures for creation of logins has been documented and reviewed with appropriate personnel to prevent future occurrences.

FINANCIAL STATEMENTS PER EXAMINATION

The following pages contain financial statements showing the Company's financial position as of December 31, 2004, 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."

LIBERTY AMERICAN INSURANCE COMPANY
Assets

DECEMBER 31, 2004

Classification	Per Company	Examination Adjustments	Per Examination
Bonds	\$17,877,736		\$17,877,736
Stocks:			
Preferred	1,019,140		1,019,140
Common	2,117,488		2,117,488
Cash:			
On hand	14,955,569		14,955,569
Short-term investments	6,055,793		6,055,793
Receivable for securities	48,891		48,891
Investment income due & accrued	241,916		241,916
Premiums and considerations			
Uncollected premium	8,938,570		8,938,570
Deferred premium	416,118		416,118
Reinsurance recoverable	11,148,714		11,148,714
Other amounts receivable under reinsurance contracts	218,444		218,444
Federal income tax recoverable	6,625,699		6,625,699
Net deferred tax asset	1,338,444		1,338,444
Receivable from PSA	3,163,735		3,163,735
Totals	\$74,166,257	\$0	\$74,166,257

LIBERTY AMERICAN INSURANCE COMPANY
Liabilities, Surplus and Other Funds

DECEMBER 31, 2004

Liabilities	Per Company	Examination Adjustments	Per Examination
Losses	\$5,234,989		\$5,234,989
Reinsurance payable on loss and loss adjustment expense	16,599,643		16,599,643
Loss adjustment expenses	1,257,907		1,257,907
Other expenses	23,521		23,521
Taxes, licenses and fees	(125,340)		(125,340)
Unearned premium	18,587,649		18,587,649
Advance premiums	336,804		336,804
Ceded reinsurance payable	5,064,437		5,064,437
Funds held under reinsurance treaties	321,218		321,218
Provision for reinsurance	271,000		271,000
Payable to parent, subsidiaries and affiliates	193,577		193,577
Aggregate write-ins for liabilities	<u>55,547</u>		<u>55,547</u>
Total Liabilities	\$47,820,952		\$47,820,952
Common capital stock	\$2,000,000		\$2,000,000
Gross paid in and contributed surplus	14,300,000		14,300,000
Unassigned funds (surplus)	<u>10,045,302</u>		<u>10,045,302</u>
Surplus as regards policyholders	<u>\$26,345,302</u>		<u>\$26,345,302</u>
Total liabilities, capital and surplus	<u>\$74,166,254</u>	<u>\$0</u>	<u>\$74,166,254</u>

LIBERTY AMERICAN INSURANCE COMPANY
Statement of Income

DECEMBER 31, 2004

Underwriting Income

Premiums earned	\$62,861,743
DEDUCTIONS:	
Losses incurred	36,256,321
Loss expenses incurred	7,640,998
Other underwriting expenses incurred	20,769,898
Aggregate write-ins for underwriting deductions	0
Total underwriting deductions	<u>\$64,667,217</u>
Net underwriting gain or (loss)	(\$1,805,474)

Investment Income

Net investment income earned	\$3,774,379
Net realized capital gains or (losses)	411,187
Net investment gain or (loss)	<u>\$4,185,566</u>

Other Income

Net gain or (loss) from agents' or premium balances charged off	
Finance and service charges not included in premiums	73,539
Aggregate write-ins for miscellaneous income	(58,032)
Total other income	<u>\$15,507</u>

Net income before dividends to policyholders and before federal & foreign income taxes	\$2,395,599
Dividends to policyholders	
Net Income, after dividends to policyholders, but before federal & foreign income taxes	<u>\$2,395,599</u>
Federal & foreign income taxes incurred	<u>(2,799,797)</u>
Net Income	\$5,195,396

Capital and Surplus Account

Surplus as regards policyholders, December 31 prior year	\$22,096,606
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Gains and (Losses) in Surplus

Net Income	\$5,195,396
Net unrealized capital gains or losses	794,400
Change in non-admitted assets	1,632,232
Change in provision for reinsurance	(271,000)
Change in net deferred income tax	(3,102,331)
Surplus adjustments: Paid in	0
Aggregate write-ins for gains and losses in surplus	0
Examination Adjustment	
Change in surplus as regards policyholders for the year	<u>\$4,248,697</u>
Surplus as regards policyholders, December 31 current year	<u><u>\$26,345,303</u></u>

COMMENTS ON FINANCIAL STATEMENTS

Liabilities

Losses and Loss Adjustment Expenses \$6,492,896

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, 2004, 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.

**LIBERTY AMERICAN INSURANCE COMPANY
COMPARATIVE ANALYSIS OF CHANGES IN SURPLUS**

DECEMBER 31, 2004

Surplus as Regards Policyholders
per December 31, 2004, Annual Statement \$26,345,302

	<u>PER COMPANY</u>	<u>PER EXAM</u>	<u>INCREASE (DECREASE) IN SURPLUS</u>
ASSETS:	No adjustment needed		\$0
LIABILITIES:	No adjustment needed		\$0
Net Change in Surplus:			<u>0</u>
Surplus as Regards Policyholders December 31, 2004, Per Examination			<u><u>\$26,345,302</u></u>

SUMMARY OF FINDINGS

Compliance with previous directives

The Company has taken the necessary actions to comply with the comments made in the 2001 examination report issued by the Office.

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, 2004.

CONCLUSION

The customary insurance examination practices and procedures as promulgated by the NAIC have been followed in ascertaining the financial condition of **Liberty American Insurance Company** as of December 31, 2004, consistent with the insurance laws of the State of Florida.

Per examination findings, the Company's surplus as regards policyholders was \$26,345,302, which was in compliance with Section 624.408, FS.

In addition to the undersigned, the following personnel participated in the examination, Mary James, CFE, CPM, Financial Examiner/Analyst Supervisor, Richard Shaffer, Financial Examiner/Analyst, and Joe Boor, FCAS, Office Actuary. We also recognize the participation of Highland Clark, LLC in the examination.

Respectfully submitted,

James D. Collins
Financial Examiner/Analyst II
Florida Office of Insurance Regulation