

REPORT ON EXAMINATION
OF
MEDMAL DIRECT INSURANCE
COMPANY

JACKSONVILLE, FLORIDA

AS OF
DECEMBER 31, 2012

BY THE
FLORIDA OFFICE OF INSURANCE REGULATION

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November 18, 2013

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 690-138.005, 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, 2012, of the financial condition and corporate affairs of:

**MEDMAL DIRECT INSURANCE COMPANY
245 RIVERSIDE AVENUE, SUITE 550
JACKSONVILLE, FL 32202**

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, 2012, through December 31, 2012. The Company was last examined by representatives of the Florida Office of Insurance Regulation ("Office") as of December 31, 2011. This examination commenced with planning at the Office during the week of August 5, 2013, to August 9, 2013. The fieldwork commenced on September 4, 2013, and concluded as of November 18, 2013.

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 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 examination process.

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

SUMMARY OF SIGNIFICANT FINDINGS

Current Exam Findings

The findings noted during this examination period have been resolved by the Company subsequent to the examination date. However, the findings or exceptions are discussed in detail in the body of the examination report.

Prior Exam Findings

The following is a summary of significant adverse findings contained in the Office's prior examination report as of December 31, 2011, along with resulting action taken by the Company in connection therewith.

The Company was party to Consent Order 110831-10-CO filed June 10, 2010, regarding the application for the issuance of a Certificate of Authority. The Company failed to comply with the following provision of this consent order:

There was no custodian agreement between the Company and Merrill Lynch & Company, Inc. (Merrill Lynch) as required by Rule 69O-143.042, Florida Administrative Code. Resolution: The Company executed a custodian agreement with Merrill Lynch during the examination and the executed copy met the requirements of Rule 69O-143.042, Florida Administrative Code.

The Company was not in compliance with Executive order 13224. Resolution: On July 20, 2012, the Company provided completed Terrorism Sanctions questionnaires and certified compliance with executive order 13224.

The reinsurance intermediary agreement with Lockton Re did not meet the requirements of Section 626.7492(4)(5), Florida Statutes. Resolution: The Company provided an amended contract with Lockton Re during the examination. The amended contract met all of the requirements of Section 626.7492(4)(5), Florida Statutes.

SUBSEQUENT EVENTS

The examination team noted the following significant events that occurred subsequent to the examination date of December 31, 2012:

On March 11, 2013, the Board of Directors (Board) elected a third member to the Audit Committee. On August 6, 2013, the Company received a waiver from the Office concerning compliance with Section 624.424(8)(c), Florida Statutes in regards to audit committee independence.

The Company received Certificates of Authority to write business in the states of Texas on July 31, 2013 and North Carolina on September 3, 2013.

On March 14, 2013, the Company amended their Articles of Incorporation to change the par value from \$1 per share to \$.50 per share. This amendment was done in order for the Company

to meet the minimum capital and surplus requirements for the State of Texas. The amendment to the Articles of Incorporation was approved by the Office on May 17, 2013.

On September 26, 2013, the Board approved the issuance of 120 shares for a capital contribution of \$1.2 million from MedMal Direct Insurance Group, LLC, (“MedMal Group”) the Company’s parent.

On November 13, 2013, the Board elected a third member to the Investment Committee.

HISTORY

General

The Company was incorporated in Florida on June 14, 2010, and commenced business on June 17, 2010, as MedMal Direct Insurance Company.

The Company was party to Consent Order 110831-10-CO filed June 10, 2010, regarding the application for the issuance of a Certificate of Authority.

The Company was authorized to transact Medical Malpractice insurance coverage in Florida on June 17, 2010 and continued to be authorized as of December 31, 2012. The Company was authorized to transact Casualty (Excluding Workers’ Compensation) coverage in Georgia on December 12, 2012.

The Bylaws were not amended during the period covered by this examination. The Articles of Incorporation were amended on March 14, 2013, which changed the par value from \$1 per share to \$.50 per share.

Dividends to Stockholders

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

Capital Stock and Capital Contributions

As of December 31, 2012, the Company's capitalization was as follows:

Number of authorized common capital shares	10,000,000
Number of shares issued and outstanding	9,500,120
Total common capital stock	\$9,500,120
Par value per share	\$1.00

Control of the Company was maintained by MedMal Group, who owned 100% of the stock issued by the Company, who in turn was 100% owned by Physicians Trust, LLC, a Florida corporation. During 2012, the MedMal Group contributed a total of \$3.7 million in cash and cash equivalents to the Company for 2,500,120 shares of common stock.

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

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

CORPORATE RECORDS

The recorded minutes of the Shareholder, 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 periodic 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, 2012, were:

Directors

Name and Location	Principal Occupation
Carter Byrd Bryan Jacksonville, Florida	Director MedMal Direct Insurance Company
Timothy Robert Bone Jacksonville, Florida	President MedMal Direct Insurance Company
Philip Butler Ball Jacksonville, Florida	Chief Executive Officer MedMal Direct Insurance Company

Michael John Wallace
Saint Johns, Florida

Vice President and Chief Financial Officer
MedMal Direct Insurance Company

Christopher McNeill Ball
Jacksonville, Florida

Chief Executive Officer
Wingard Creative

In accordance with the Company's bylaws, the Board appointed the following senior officers:

Senior Officers

Name	Title
Phillip Butler Ball	Chief Executive Officer
Timothy Robert Bone	President
Michael John Wallace	Vice President and Chief Financial Officer
Carter Byrd Bryan	Chairman

The Company's Board appointed several internal committees. Following were the principal internal board committees and their members as of December 31, 2012:

Audit Committee

Michael John Wallace¹
Philip Butler Ball

Investment Committee

Philip Butler Ball¹
Michael John Wallace

¹ Chairman

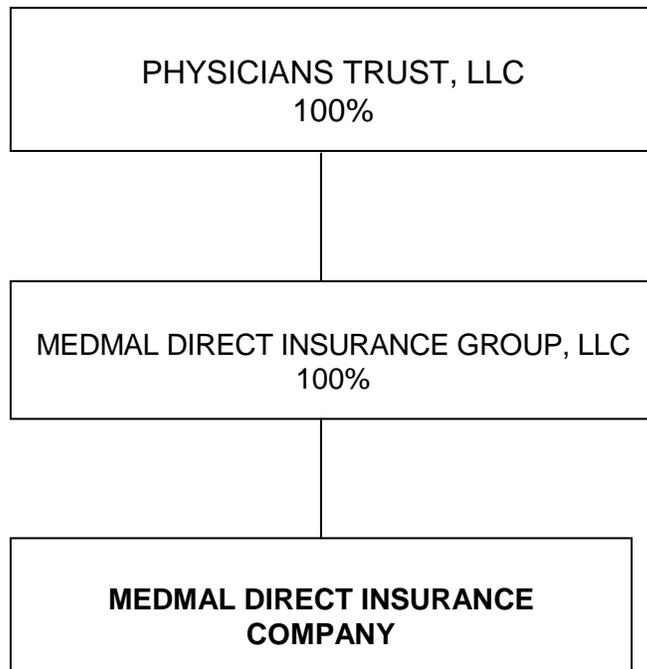
The Audit Committee was comprised of two senior officers of the Company; therefore, the Company was not in compliance with Section 624.424(8)(c), Florida Statutes, which states that the Board shall establish an Audit Committee of three or more directors. **Subsequent Event:** On March 11, 2013, the Board elected a third member to the Audit Committee which satisfied the requirement of Section 624.424(8)(c), Florida Statutes, regarding membership requirements.

Affiliated Companies

The Company was a member of an insurance holding company system as defined by Rule 69O-143.045(3), Florida Administrative Code. The latest holding company registration statement was filed with the State of Florida on February 26, 2013, as required by Section 628.801, Florida Statutes, and Rule 69O-143.046, Florida Administrative Code.

An organizational chart as of December 31, 2012, reflecting the holding company system, is shown below. Schedule Y of the Company's 2012 annual statement provided a list of all related companies of the holding company group.

MEDMAL DIRECT INSURANCE COMPANY ORGANIZATIONAL CHART DECEMBER 31, 2012



The following agreement was in effect between the Company and its affiliate:

Service Agreement

The Company entered into a Service Agreement on June 11, 2010 with the MedMal Group, whereby personnel was provided to perform certain services for the benefit of the Company, including but not limited to, sales and marketing, accounting and financial reporting, operations and regulatory. The Company paid the MedMal Group a fee equal to one hundred and fifteen percent (115%) of the actual compensation and related personnel costs incurred as a result of providing these services to the Company.

FIDELITY BOND

The Company maintained fidelity bond coverage up to \$1,000,000 with a deductible of \$50,000, which reached the suggested minimum as recommended by the NAIC. The coverage was effective for the period December 1, 2012 through December 1, 2013.

PENSION, STOCK OWNERSHIP AND INSURANCE PLANS

The Company had no employees and therefore no pension, stock ownership or insurance plans.

TERRITORY AND PLAN OF OPERATIONS

The Company was authorized to transact insurance in the following states:

Florida

Georgia

Subsequent event: The Company received Certificates of Authority to write business in the State of Texas on July 31, 2013 and in the State of North Carolina on September 3, 2013.

Treatment of Policyholders

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

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

COMPANY GROWTH

The Company experienced significant growth in written and earned premiums during 2012. The Company's operating results improved during 2012, but it continued to experience net losses in 2012 primarily attributable to start up costs and expenses related to the continued expansion into new areas. The Company marketed directly to prospects through the internet, mailing, referrals, seminars, conventions, meetings and other means of direct market. The Company only issued business in the State of Florida during 2012. However, currently the Company is issuing business in Florida, Georgia and Texas. With the expansion into new states and time to gain market share in all states, the Company anticipates continued significant premium growth over the next several years.

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.

	2012	2011	2010
Premiums Earned	6,268,821	2,368,062	231,681
Net Underwriting Gain/(Loss)	(1,142,281)	(1,216,562)	(661,673)
Net (Loss)	(577,768)	(1,067,195)	(609,200)
Total Assets	17,468,994	9,114,314	6,134,267
Total Liabilities	8,547,915	3,380,787	1,133,062
Surplus As Regards Policyholders	8,921,079	5,733,527	5,001,205

LOSS EXPERIENCE

During the current examination period, the Company showed favorable loss development overall. The one and two-year net loss developments at the end of the current examination period were both favorable at \$38,000 and \$3,000, 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 did not assume any reinsurance during the period of this examination.

Ceded

The Company ceded risk on a quota share and excess of loss basis to various Lloyd's Syndicates in order to limit its financial exposure to large claims by using Lockton Re as their reinsurance intermediary. The treaty period covered claims made from March 1, 2011 through March 1, 2014. Under the per risk coverage, the reinsurers paid up to \$750,000 per loss insured, in excess of \$250,000. Under the clash coverage, the reinsurers paid up to \$500,000 per loss occurrence, in excess of \$500,000. Each loss occurrence under the clash coverage provision comprised at least three insureds. The reinsurance agreement provided for adjustable premiums based on ceded incurred losses. There were no ceded incurred losses during the year ended December 31, 2012.

The Company also utilized three unauthorized reinsurers during the period of this exam. There were no letters of credit established for these un-authorized reinsurers. However, the amounts recoverable(s) from these reinsurers were insignificant.

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 statement for the year 2012 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 prepared using Intuit QuickBooks to support general ledger activity, cash collections and payables. Microsoft Dynamics was used for processing claims and underwriting. Microsoft Excel was used primarily for rating, but also to support general ledger entries, accounting calculations, fixed asset details, and other accounting functions.

Subsequent event: Microsoft Dynamics was implemented as of June 12, 2013, and replaced Intuit QuickBooks as the financial system. In addition, the Company began using Clearwater Analytics on October 1, 2013 for the accounting of investments.

The Company and non-affiliates had the following agreements:

Custodial Agreement

The Company utilized Merrill Lynch as its custodian during the period covered by this examination. The Company executed a custodian agreement on August 16, 2012 that met all requirements of Rule 69O-143.042, Florida Administrative Code.

On September 23, 2013, the Investment Committee appointed BlackRock Investment Management, LLC, as a discretionary investment manager with full power and authority to transact purchases and sales of currencies, securities and other instruments subject to the limitations within the Company's investment policies.

Endorsement Agreement

The Company entered into an endorsement agreement November 29, 2011 with PSS World Medical, Inc. (PSS) whereby PSS endorses the Company to its clients. The Company and PSS employed joint direct marketing to their clients through mailers and joint sales representative visits.

Subsequent event: In March, 2013, PSS became a subsidiary of McKesson Corporation. Effective, July 1, 2013, the Company suspended the endorsement agreement with PSS and, as of the date of this report, was in negotiation with McKesson Corporation regarding a new agreement.

Lease Agreements

The Company completed an operating lease for its former office space effective from July 1, 2010 through July 1, 2012 with One Independent Square, LLC. The Company executed a new five year lease agreement for office space with PKY Fund II (Parkway Realty) effective May 7, 2012. Rent expense for the two agreements was \$143,587 and \$126,621 for years ended December 31, 2012 and December 31, 2011.

The Company subleased office space to an unaffiliated party, Bryan Group, effective August 1, 2010 with a termination date of July 31, 2013. Rental income related to the sublease agreement was \$31,226 for the years ended December 31, 2012 and December 31, 2011.

Information Technology Agreement

The Company entered into an agreement with NetTech Consultants, Inc. (NetTech) on August 24, 2012. NetTech provided the Company with Information Technology services including performance, availability & predictive failure monitoring, patch monitoring & management, virus definition monitoring and management, systems administration, systems maintenance, emergency support, and monthly review meetings. The Company paid NetTech for the services on a specified fee schedule per device on a monthly basis. The Company entered into a new agreement with NetTech on August 1, 2013.

Reinsurance Intermediary Agreement

The Company entered into a reinsurance intermediary agreement with Lockton Re on March 1, 2012 that met the requirements of Section 626.7492 (4) (5), Florida Statutes.

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 69O-137.002 (7) (c), Florida Administrative Code.

INFORMATION TECHNOLOGY REPORT

David Mills, CISA, CGEIT, CRISC, MCSE, IT Consulting Partner at Carr, Riggs, and Ingram, LLC, performed an evaluation of the information technology and computer systems of the Company. Results of the evaluation were noted in the Information Technology Report provided to the Company.

STATUTORY DEPOSITS

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

STATE	Description	Par Value	Market Value
FL	Cash	<u>\$ 250,000</u>	<u>\$ 250,000</u>
TOTAL SPECIAL DEPOSITS		<u>\$ 250,000</u>	<u>\$ 250,000</u>

FINANCIAL STATEMENTS PER EXAMINATION

The following pages contain financial statements showing the Company's financial position as of December 31, 2012, 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."

MEDMAL DIRECT INSURANCE COMPANY
Assets

DECEMBER 31, 2012

	Per Company	Examination Adjustments	Per Examination
Bonds	\$9,529,926		\$9,529,926
Stocks:			
Common	1,650,428		1,650,428
Cash and Short-Term Investments	3,476,204		3,476,204
Agents' Balances:			
Uncollected premium	1,883,164		1,883,164
Interest and dividend			
income due & accrued	16,873		16,873
Net deferred tax asset	879,392		879,392
Aggregate write-in for			
other than invested assets	33,007		33,007
Totals	<u>\$17,468,994</u>	<u>\$0</u>	<u>\$17,468,994</u>

MEDMAL DIRECT INSURANCE COMPANY
Liabilities, Surplus and Other Funds

DECEMBER 31, 2012

	Per Company	Examination Adjustments	Per Examination
Losses	\$3,032,863		\$3,032,863
Loss adjustment expenses	896,208		896,208
Other expenses	144,248		144,248
Taxes, licenses and fees	32,622		32,622
Unearned premiums	3,729,733		3,729,733
Advance premium	547,660		547,660
Ceded reinsurance premiums payable net of ceding commissions	(985,998)		(985,998)
Payable for securities	1,150,579		1,150,579
Total Liabilities	\$8,547,915	\$0	\$8,547,915
Common capital stock	\$9,500,120		\$9,500,120
Gross paid in and contributed surplus	1,199,880		1,199,880
Unassigned funds (surplus)	(1,778,921)		(1,778,921)
Surplus as regards policyholders	\$8,921,079	\$0	\$8,921,079
Total liabilities, surplus and other funds	\$17,468,994	\$0	\$17,468,994

MEDMAL DIRECT INSURANCE COMPANY
Statement of Income

DECEMBER 31, 2012

Underwriting Income

Premiums earned		\$6,268,821
	Deductions:	
Losses incurred		\$2,821,216
Loss expenses incurred		1,252,874
Other underwriting expenses incurred		3,337,012
Aggregate write-ins for underwriting deductions		0
Total underwriting deductions		<u>\$7,411,102</u>
Net underwriting gain or (loss)		(\$1,142,281)

Investment Income

Net investment income earned		\$235,238
Net realized capital gains or (losses)		311,060
Net investment gain or (loss)		<u>\$546,298</u>

Other Income

Net gain or (loss) from agents' or premium balances charged off		\$0
Finance and service charges not included in premiums		0
Aggregate write-ins for miscellaneous income		18,215
Total other income		<u>\$18,215</u>
Net income before dividends to policyholders and before federal & foreign income taxes		(\$577,768)
Dividends to policyholders		0
Net Income, after dividends to policyholders, but before federal & foreign income taxes		(\$577,768)
Federal & foreign income taxes		0
Net Income		<u><u>(\$577,768)</u></u>

Capital and Surplus Account

Surplus as regards policyholders, December 31 prior year		\$5,513,527
Net Income		(\$577,768)
Net unrealized capital gains or losses		(28,515)
Change in net deferred income tax		268,645
Change in non-admitted assets		45,190
Change in provision for reinsurance		0
Change in excess statutory over statement reserves		0
Capital changes: Paid in		2,500,120
Surplus adjustments: Paid in		1,199,880
Aggregate write-ins for gains and losses in surplus		0
Examination Adjustment		0
Change in surplus as regards policyholders for the year		<u>\$3,407,552</u>
Surplus as regards policyholders, December 31 current year		<u><u>\$8,921,079</u></u>

A comparative analysis of changes in surplus is shown below.

MEDMAL DIRECT INSURANCE COMPANY
Comparative Analysis of Changes in Surplus

DECEMBER 31, 2012

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, 2012, per Annual Statement	\$8,921,079
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	<u>PER COMPANY</u>	<u>PER EXAM</u>	<u>INCREASE (DECREASE) IN SURPLUS</u>
ASSETS: No Adjustment			
LIABILITIES: No Adjustment			
Net Change in Surplus:			<u>0</u>
Surplus as Regards Policyholders December 31, 2012, Per Examination			<u><u>\$8,921,079</u></u>

COMMENTS ON FINANCIAL STATEMENTS

Liabilities

Losses and Loss Adjustment Expenses \$3,929,071

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, 2012, 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's consulting actuary, Christopher Burkhalter, FCAS, MAAA of Bickerstaff, Whatley, Ryan & Burkhalter, 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 \$8,921,079, exceeded the minimum of \$4,000,000 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 **MedMal Direct Insurance Company** as of December 31, 2012, consistent with the insurance laws of the State of Florida.

Per examination findings, the Company's surplus as regards policyholders was \$8,921,079, which exceeded the minimum of \$4,000,000 required by Section 624.408, Florida Statutes.

In addition to the undersigned, R. Dale Miller, CPA, CFE, CFF, Examiner-In-Charge, John M. Romano, CPA, CFE, Examination Manager of ParenteBeard, LLC, participated in the examination. Andrea Harbison, CPA, Francois Houde, CPA, CA, CFE, CISA, Mike Whitney, CPA, and Thomas Montalbano, CPA, Participating Examiners, of Carr, Riggs & Ingram, LLC, also participated in the examination. Additionally, Christopher Burkhalter, FCAS MAAA, consulting actuary of Bickerstaff, Whatley, Ryan & Burkhalter and David Mills, CISA, CGEIT, CRISC, MCSE, Lead IT Specialist of Carr, Riggs & Ingram, LLC are recognized for participation in the examination.

Respectfully submitted,

Robin Brown, CFE
Chief Examiner
Florida Office of Insurance Regulation