

**REPORT ON EXAMINATION**  
**OF**  
**PHYSICIANS INSURANCE COMPANY**

**POMPANO BEACH, FLORIDA**

**AS OF**  
**DECEMBER 31, 2004**

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

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Tallahassee, Florida

April 7, 2006

Kevin M. McCarty  
Commissioner  
Office of Insurance Regulation  
State of Florida  
Tallahassee, Florida 32399-0326

Dear Sir:

Pursuant to your instructions, in compliance with Section 624.316, Florida Statutes, and in accordance with the practices and procedures promulgated by the National Association of Insurance Commissioners (NAIC), we have conducted an examination of December 31, 2004, of the financial condition and corporate affairs of:

**PHYSICIANS INSURANCE COMPANY**  
3200 NE 14<sup>TH</sup> Street  
Pompano Beach, FL 33062

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, 2004 through December 31, 2004. This was the Company's first financial examination by representatives of the Florida Office of Insurance Regulation (Office). This examination commenced with planning at the Office, on January 25, 2006 and resumed again from January 30, 2006 through February 3, 2006. The fieldwork commenced on February 7, 2006, and was concluded as of April 7, 2006. 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, 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 Company's independent audit reports and certain work papers prepared by the Company's independent certified public accountant (CPA) were reviewed 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.

## **HISTORY**

### **General**

The Company was incorporated in Florida on January 31, 2003, under the laws of the State of Florida, as a stock property and casualty insurer and commenced business on March 7, 2003.

The Company issued approximately 51% (205,000 shares) of its outstanding common shares to Daniel R. O'Neal, an individual resident of the State of Florida. The remaining 49% (195,000 shares) of the Company's issued and outstanding common shares were issued to American Physicians Assurance Corporation (APA), a Florida-licensed property and casualty insurer domiciled in the State of Michigan.

On December 31, 2004, Mr. O'Neal acquired all of the APA common shares in the Company for the purchase price of \$3,000,000 pursuant to a promissory note executed to APA. Mr. O'Neal paid for these shares in monthly installments. Payment for these shares were secured under the note by Mr. O'Neal's shares of Company's stock pursuant to a stock pledge agreement. The Office granted approval to Mr. O'Neal's Form A filing in Consent Order 80862-05-CO, dated February 26, 2003.

As of December 31, 2004, the Company maintained a certificate of authority (COA) in the State of Florida to write medical malpractice.

The Company amended the articles of incorporation and the bylaws during the period covered by this examination. Article VII was amended to correct a statutory citation regarding indemnification. Article XII was added to provide existing shareholders with preemptive rights to purchase unissued shares of the Company.

### Capital Stock

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

Number of authorized common capital shares	500,000
Number of shares issued and outstanding	400,000
Total common capital stock	\$ 400,000
Par value per share	\$1.00

As of December 31, 2004, the control of the Company was maintained by Daniel R. O'Neal.

### 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 of the Company.

	<b>2004</b>	<b>2003</b>
Premiums Earned	2,305,664	610,563
Net Underwriting Gain/(Loss)	177,469	(742,412)
Net Income	235,379	(698,024)
Total Assets	9,599,529	6,600,632
Total Liabilities	4,996,678	2,185,307
Surplus As Regards Policyholders	4,602,851	4,415,325

## Dividends to Stockholders

No dividends to its stockholder were declared during the examination period.

## Management

The annual shareholder meeting for the election of directors was held in accordance with Sections 607.1601 and 628.231, Florida Statutes. Directors serving as of December 31, 2004, were:

### Directors

<b>Name and Location</b>	<b>Principal Occupation</b>
Daniel R. O'Neal Pompano Beach, FL	Chief Executive Officer; President, Managed Information Services, Inc.
Pamela N. Browning Pompano Beach, FL	Chief Operating Officer
Rebecca M. Brocard-Santiago Boca Raton, FL	Chief Financial Officer
Dennis M. Faulkner Pembroke Pines, FL	Vice President of Claims
*Frank H. Freund Lansing, MI	CFO of APA

\*As of December 31, 2004, all of APA common shares were acquired by Mr. O'Neal. As a result of this transaction, Mr. Freund no longer served as Director of the Company.

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

### Senior Officers

<b>Name</b>	<b>Title</b>
Daniel R. O'Neal	Chief Executive Officer

Pamela N. Browning

Chief Operating Officer

Rebecca M. Brocard-Santiago

Chief Financial Officer

As of December 31, 2004, the Company's Board appointed the following committee and its members in accordance with Section 607.0825, Florida Statutes:

**Finance Committee**

Rebecca M. Brocard-Santiago, Chair Person

Daniel R. O'Neal

Frank H. Freund

Chris J. Waterson

The Company did not maintain an audit committee as required under Section 624.424 (8), Florida Statutes.

Subsequent Event: During the examination, the Board established an audit committee to comply with Section 624.424 (8) (c), Florida Statutes.

**Conflict of Interest Procedure**

The Company had not adopted a policy statement requiring annual disclosure of conflicts of interest, as required in the NAIC Financial Condition Examiners Handbook.

Subsequent Event: During the examination, the Company provided copies of the conflict of interest statements of all of the Board of Directors listed in the annual statement.

**Corporate Records**

The recorded minutes of the shareholder, Board of Directors, 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 in accordance with Section

607.1601, Florida Statutes, including the authorization of investments as required by Section 625.304, Florida Statutes.

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

On December 31, 2004, Daniel O'Neal, CEO, acquired all of the outstanding common shares of the Company issued to APA.

### **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), Florida Administrative Code. The latest holding company registration statement was filed with the State of Florida on May 27, 2005. The Company disclosed 100% acquisition of common shares of American Physicians Insurance Company by Daniel O'Neal as required by Section 628.801, Florida Statutes and Rule 69O-143.046, Florida Administrative Code.

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

### **Software Licensing Agreement**

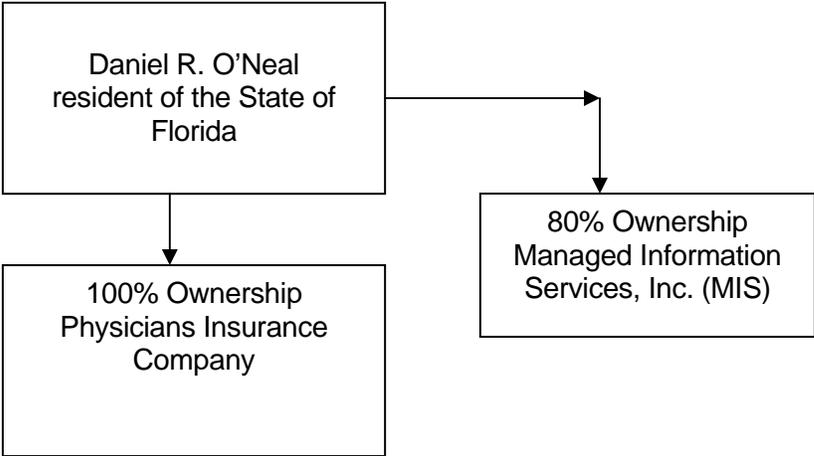
On February 1, 2003, the Company entered into a software license agreement with an affiliate, Managed Information Services, Inc. (MIS), to enable the Company to process Physicians & Surgeons line of business. As consideration for the services rendered, the Company agreed to

pay MIS a one-time charge of \$25,000 and a fee of \$4,000 per month. Additional fees were paid for the on-site maintenance and support service.

An organizational chart as of December 31, 2004, reflecting the holding company system, is shown below.

**PHYSICIANS INSURANCE COMPANY  
ORGANIZATIONAL CHART**

**DECEMBER 31, 2004**



## FIDELITY BOND AND OTHER INSURANCE

During the period covered under this examination, the Company did not maintain fidelity bond coverage as recommended by the NAIC. The Company maintained other insurance coverage usual to the operation of an insurer.

Subsequent event: MIS, an affiliate, maintained fidelity bond coverage up to \$500,000 with a deductible amount of \$5,000. On November 16, 2005, the Company was added to this policy by the means of an endorsement. This insurance adequately covered the suggested minimum amount of coverage for the Company as recommended by the NAIC.

## PENSION

Eligible employees were covered by a qualified defined contribution pension plan sponsored by the Company. The Company contributed up to 1% each year into this plan.

## STATUTORY DEPOSITS

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

<u>State</u>	<u>Description</u>	<u>Par Value</u>	<u>Market Value</u>
FL	Cash Deposit	\$ 250,000	\$ 280,365
TOTAL SPECIAL DEPOSITS		<u>\$ 250,000</u>	<u>\$ 280,365</u>

## **INSURANCE PRODUCTS AND RELATED PRACTICES**

### **Territory**

At December 31, 2004, the Company was authorized to transact medical malpractice insurance in the State of Florida. The latest market conduct exam concluded by the Office as of October 13, 2005, had no material exceptions that impacted the solvency of the Company.

### **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.

## **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 risk during the period covered by this examination.

### **Ceded**

During 2004, the Company ceded \$4,349,000 in written premiums to the various reinsurers on an excess of loss basis through a reinsurance intermediary. The Company ceded \$189,000 in written premiums to one reinsurer on a quota share basis. The Company utilized two unauthorized

reinsurers as listed on Schedule F-Part 5. Letters of credit were adequately established for these reinsurers.

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

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

During 2005, the Company moved to its current address located in Pompano Beach, Florida. The Company maintained its principal operational offices in Pompano Beach, Florida, where this examination was conducted.

The Company and non-affiliates had the following agreements:

**Custodial Agreement**

The Company amended its custodial agreement with Northern Trust Bank of Florida, N.A. on July 16, 2004. The amended custodial agreement met all of the requirements of Rule 69O-143.042, Florida Administrative Code, with one exception, as described below:

The custodial agreement did not contain a clause which stated that the agreement must be terminable by the Company on not more than thirty (30) days' notice, as required by Rule 69O-143.042 (2) (o), Florida Administrative Code.

**Stock Pledge Agreement**

On December 31, 2004, Daniel R. O'Neal (pledger) entered into a stock pledge agreement with American Assurance Physicians Corporation (lender) to secure the purchase of the lender's common shares in the Company. The pledger delivered to the lender the certificates representing all of the stock (400 common shares) of the Company as required under the terms of the stock pledge agreement.

**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, 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."

**PHYSICIANS INSURANCE COMPANY**  
**Assets**

**DECEMBER 31, 2004**

Classification	Per Company	Examination Adjustments	Per Examination
Bonds	\$2,371,443		\$2,371,443
Cash:			
On deposit	1,773,571		1,773,571
Short-term investments	2,497,673		2,497,673
Interest and dividend income due & accrued	12,605		12,605
Agents' Balances:			
Uncollected premium	2,458,949		2,458,949
Amounts recoverable from reinsurers	217,660		217,660
Current federal & foreign income Tax recoverable & interest thereon	146,308		146,308
Net deferred tax asset	76,174		76,174
Aggregate write-ins for other than invested assets	45,146		45,146
Totals	\$9,599,529	\$0	\$9,599,529

**PHYSICIANS INSURANCE COMPANY**  
**Liabilities, Surplus and Other Funds**

**DECEMBER 31, 2004**

Liabilities	Per Company	Examination Adjustments	Per Examination
Losses	\$1,017,779		\$1,017,779
Loss adjustment expenses	479,625		479,625
Commissions payable on paid loss and loss adjustment expenses	251,237		251,237
Other expenses	25,683		25,683
Current federal and foreign income taxes	34,016		34,016
Unearned premium	1,605,532		1,605,532
Advance premiums	75,229		75,229
Ceded reinsurance premiums payable	1,507,577		1,507,577
Total Liabilities	<u>\$4,996,678</u>		<u>\$4,996,678</u>
Common capital stock	\$400,000		\$400,000
Gross paid in and contributed surplus	4,600,000		4,600,000
Unassigned funds (surplus)	(397,149)		(397,149)
Surplus as regards policyholders	<u>\$4,602,851</u>		<u>\$4,602,851</u>
Total liabilities, capital and surplus	<u><u>\$9,599,529</u></u>		<u><u>\$9,599,529</u></u>

**PHYSICIANS INSURANCE COMPANY**  
**Statement of Income**

**DECEMBER 31, 2004**

**Underwriting Income**

Premiums earned	\$2,305,664
DEDUCTIONS:	
Losses incurred	995,976
Loss expenses incurred	602,189
Other underwriting expenses incurred	530,030
Aggregate write-ins for underwriting deductions	0
Total underwriting deductions	<u>\$2,128,195</u>
Net underwriting gain or (loss)	\$177,469

**Investment Income**

Net investment income earned	\$62,271
Net realized capital gains or (losses)	(109)
Net investment gain or (loss)	<u>\$62,162</u>

**Other Income**

Net gain or (loss) from agents' or premium balances charged off	\$0
Finance and service charges not included in premiums	29,764
Aggregate write-ins for miscellaneous income	0
Total other income	<u>\$29,764</u>
Net income before dividends to policyholders and before federal & foreign income taxes	\$269,395
Dividends to policyholders	0
Net Income, after dividends to policyholders, but before federal & foreign income taxes	<u>\$269,395</u>
Federal & foreign income taxes	<u>34,016</u>
Net Income	\$235,379

**Capital and Surplus Account**

Surplus as regards policyholders, December 31 prior year	\$4,415,325
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**Gains and (Losses) in Surplus**

Net Income	\$235,379
Change in non-admitted assets	(13,666)
Change in net deferred income tax	(34,187)
Examination Adjustment	0
Change in surplus as regards policyholders for the year	<u>\$187,526</u>
Surplus as regards policyholders, December 31 current year	<u><u>\$4,602,851</u></u>

## COMMENTS ON FINANCIAL STATEMENTS

### Liabilities

<b>Losses and Loss Adjustment Expenses</b>	<u>\$1,497,404</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, 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.

**PHYSICIANS INSURANCE COMPANY  
COMPARATIVE ANALYSIS OF CHANGES IN SURPLUS**

**DECEMBER 31, 2004**

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, 2004, Annual Statement	\$4,602,851
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	<u>PER COMPANY</u>	<u>PER EXAM</u>	<u>INCREASE (DECREASE) IN SURPLUS</u>
<b>ASSETS:</b>			
No adjustment			
<b>LIABILITIES:</b>			
No adjustment			
Net Change in Surplus:			0
Surplus as Regards Policyholders December 31, 2004, Per Examination			\$4,602,851

## SUMMARY OF FINDINGS

### **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.

### **Custodial Agreement**

The custodial agreement did not contain a clause which stated that the agreement must be terminable by the Company on not more than 30 days notice, as required by Rule 690-143-042 (2) (o), Florida Administrative Code. **We recommend the Company add the clause to the custodial agreement as required in Rule 690-143.042 (2) (o), Florida Administrative Code.**

## SUBSEQUENT EVENT

During 2005, the Company amended its articles of incorporation to change the par value of the Company stock from \$1.00 per share to \$2.50 per share. The approval was granted by the Office on May 19, 2005.

## CONCLUSION

The customary insurance examination practices and procedures as promulgated by the NAIC have been followed in ascertaining the financial condition of **PHYSICIANS 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 \$4,602,851 which was in compliance with Section 624.408, Florida Statutes.

In addition to the undersigned, John Berry, Financial Examiner/Analyst Supervisor, Jay Ambler, Financial Examiner/Analyst II, and Joe Boor, FCAS, Office Actuary, participated in the examination.

Respectfully submitted,

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Samita Lamsal  
Financial Examiner/Analyst II  
Florida Office of Insurance Regulation