

**EXAMINATION REPORT**

**OF**

**PRIVILEGE UNDERWRITERS RECIPROCAL EXCHANGE**

**FORT LAUDERDALE, FLORIDA**

**AS OF**

**DECEMBER 31, 2014**

**BY THE**

**FLORIDA OFFICE OF INSURANCE REGULATION**

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February 26, 2016

David Altmaier  
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, 2014, of the financial condition and corporate affairs of

Privilege Underwriters Reciprocal Exchange  
800 Corporate Drive, Suite 420  
Fort Lauderdale, Florida 33334

hereinafter referred to as the "Reciprocal". Such report of examination is herewith respectfully submitted.

## **SCOPE OF EXAMINATION**

This examination covered the period of January 1, 2010 through December 31, 2014. The Reciprocal was last examined by representatives of the Florida Office of Insurance Regulation (Office) covered the period of January 1, 2009 through December 31, 2009. This examination commenced with planning at the Office on July 27, 2015 to July 31, 2015. The fieldwork commenced on July 27, 2015 and concluded as of February 26, 2016.

The examination was a single state examination conducted in accordance with the NAIC Financial Condition Examiners Handbook. The Handbook requires that the examination is planned and performed to evaluate the financial condition, assess corporate governance, identify current and prospective risks of the Reciprocal and evaluate system controls and procedures used to mitigate those risks. An examination also includes identifying and evaluating significant risks that could cause a Reciprocal's surplus to be materially misstated both currently and prospectively.

All accounts and activities of the Reciprocal were considered in accordance with the risk-focused examination process. This may include assessing significant estimates made by management and evaluating management's compliance with Statutory Accounting Principles.

This examination report includes significant findings of fact, as mentioned in Section 624.319, Florida Statutes and general information about the insurer and its financial condition. There may be other items identified during the examination that, due to their nature (e.g., subjective conclusions, proprietary information, etc.), are not included within the examination report but separately communicated to other regulators and/or the Reciprocal.

## **SUMMARY OF SIGNIFICANT FINDINGS**

### **Current Examination Findings**

The following is a summary of material adverse findings, significant non-compliance findings or material changes in the financial statements.

### **Affiliated Agency Agreements**

The Reciprocal did not formally file agency agreements which was not in compliance with Section 628.255, Florida Statutes, which states the following: "No director, officer, or other person having effective control of a domestic insurer shall receive, and no such insurer shall pay to such person, a commission or other compensation with respect to particular risks insured by the insurer, unless such commission or other compensation is paid pursuant to a contract filed with and approved by the office."

### **Investments**

The Reciprocal made several investments that were not compliant with Section 625.332(1)(b), Florida Statutes.

### **Prior Examination Findings**

There were no findings, exceptions, or corrective action to be taken by the Reciprocal for the examination as of December 31, 2009.

## RECIPROCAL HISTORY

### General

The Reciprocal was incorporated in Florida on January 23, 2007, and commenced business on January 29, 2007, as Privilege Underwriters Reciprocal Exchange. The Reciprocal was a non-assessable unincorporated aggregation of subscribers governed by a Subscribers Advisory Committee (“SAC”) which is similar to a board of directors.

The Reciprocal was managed by its Attorney-in-Fact (“AIF”), Pure Risk Management, LLC (PRM). The AIF managed all of the operations of the Reciprocal and was owned by Privilege Underwriters, Inc.

The Reciprocal was party to Consent Order 133183-13-CO , filed March 5, 2013 , in order to enter into a request to allocate \$1,500,000 in surplus contributions to the Subscribers’ Savings Account for the Reciprocal’s members active as of December 31, 2012. The Reciprocal was in compliance with that order.

The Reciprocal was party to Consent Order 150755-14-C0, filed February 26, 2014, in order to enter into a request to allocate \$5,000,000 in surplus contributions to the Subscribers’ Savings Account for the Reciprocal’s members active as of December 31, 2013. The Reciprocal was in compliance with that order.

The Reciprocal was party to Consent Order 169989-15-CO, filed March 9, 2015, in order to enter into a request to allocate \$8,000,000 in surplus contributions to the Subscribers’ Savings Account for the Reciprocal’s members active as of December 31, 2014. The Reciprocal was in compliance with that Order.

The Reciprocal was authorized pursuant to Chapter 629, Florida Statutes, to transact the following insurance coverage in Florida on January 23, 2007 and continued to be authorized for the insurance coverage as of December 31, 2014:

Homeowners multi peril	Inland Marine
Private passenger auto physical damage	Private passenger auto liability
Other liability-occurrence	Ocean Marine

The Reciprocal was authorized to transact the Allied Lines insurance coverage in Florida on June 13, 2012, and continued to be authorized for the insurance coverage as of December 31, 2014:

The SAC Charter was not amended during the period covered by this examination.

### **Dividends**

The Reciprocal does not have stockholders.

### **Allocation to Subscribers**

The Reciprocal was approved to make a one-time allocation to the Subscribers' Savings Accounts in the amount of \$1,000,000 as of December 31, 2010, \$1,500,000 as of December 31, 2012, \$5,000,000 as of December 31, 2013, and \$8,000,000 as of December 31, 2014.

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

The Reciprocal was a non-assessable reciprocal and, therefore, had no capital stock.

## Surplus Notes

The Reciprocal issued surplus notes on January 25, 2007, in the amount of \$10,000,000 to Trident III, LP and Trident III Professionals Fund, LP. In addition, on June 4, 2007, the Reciprocal issued surplus notes totaling \$24,000,000 to an affiliate, Privilege Underwriters, Inc. (PUI). Furthermore, on June 13, 2007, the Reciprocal issued surplus notes in the amount of \$17,000,000 to the State Board of Administration of Florida. On August 5, 2008, two of the Reciprocal's surplus notes totaling \$34,000,000 were transferred to PURE Insurance Company (PIC). On June 30, 2014, the principal of \$34,000,000 of the surplus notes originally issued to PIC was satisfied. The Reciprocal obtained approval on June 30, 2014 from the Office prior to payment of principal on the surplus notes receivable due to PIC. Due and unpaid interest as of December 31, 2014, in the amount of \$8,484,893 related to subordinated surplus notes that were not approved for payment. The Reciprocal must obtain approval from the Office prior to payment of principal and/or interest on the surplus notes. Surplus as of December 31, 2014 is \$68,680,639, consisting of three third-party notes and member contributions listed in the table on the following page:

<b>Description</b>	<b>Amount</b>
<b>Third-Party Note 1:</b> Issued on June 13, 2007, to the Florida State Board of Administration. Bears interest at the 10-year Treasury Bond rate, currently 2.50%, maturing in June 2022.	\$10,622,093
<b>Third-Party Note 2:</b> Issued on June 30, 2014, to Athene Annuity and Life Assurance. Bears interest at 12-month LIBOR plus 7.75% per annum, maturing in July 2021.	\$13,600,000
<b>Third-Party Note 3:</b> Issued on June 30, 2014, to ASG Pure Holding Inc. Bears interest at 12-month LIBOR plus 7.75% per annum, maturing in July 2021.	\$20,400,000
Member Surplus contributions	\$79,667,099
Unassigned Funds	<hr/> (\$55,608,553)
<b>Subscriber Surplus as of December 31, 2014</b>	<hr/> <b>\$68,680,639</b> <hr/>

On December 22, 2015, the Reciprocal issued a surplus note to XL Finance (Ireland) LTD, an affiliate, for \$25,000,000. No compliance issues were identified regarding the issuance and payments made on Surplus Notes during this examination period.

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

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

## **CORPORATE RECORDS**

The recorded minutes of the Subscribers Advisory Committee (SAC) were reviewed for the period under examination through the end of field work. The recorded minutes of the SAC adequately documented its meetings and approval of Reciprocal transactions and events, in compliance with NAIC Financial Condition Examiners Handbook adopted by Rule 690-138.001, Florida Administrative Code, including the authorization of investments as required by Section 625.304, Florida Statutes.

### **Conflict of Interest**

The Reciprocal adopted a policy statement requiring annual disclosure of conflicts of interest in accordance with the NAIC Financial Condition Examiners Handbook adopted by Rule 690-138.001, Florida Administrative Code.

## **MANAGEMENT AND CONTROL**

### **Management**

The annual SAC meeting was held in accordance with Section 629.201, Florida Statutes. A document titled "Powers of the Subscriber's Advisory Committee" set forth the terms and conditions upon which the SAC shall operate. Members serving as the SAC as of December 31, 2014 are shown on the following page:

## Subscribers Advisory Committee Members

<b>Name and Location</b>	<b>Principal Occupation</b>
Ross J. Buchmueller Larchmont, New York	President & CEO, Pure Group Companies
Josephine A. Cummings Brooklyn, New York	CEO, The Joey Company
Douglas G. Fields Province, Florida	Senior VP, Oswald Trippe & Co.
Richard A. Jacobs Delray Beach, Florida	Principal/Managing Director Bostonia Global Securities, LLC
James H. McLaughlin Darien, Connecticut	CEO, J.H. McLaughlin, & Co.
William W. Wilson Key Largo, Florida	Consultant

The SAC in accordance with the Reciprocal's bylaws appointed the following senior officers:

**Senior Officers**

<b>Name</b>	<b>Title</b>
Ross J. Buchmueller	President & CEO
Martin Hartley	Executive Vice President & COO
Jeffrey Paraschac	Executive Vice President & CFO

Subsequent to December 31, 2014, Jennifer Lawrence was appointed as Senior Vice President, General Counsel & Corporate Secretary.

The Reciprocal maintained internal committee functions through the SAC with general responsibilities outlined in the Powers of the Subscribers Advisory Committee. The Audit Committee was comprised of the following individuals that were also members of the SAC:

**Audit Committee**

- William W. Wilson <sup>1</sup>
- Douglas G. Fields
- Richard A. Jacobs
- James H. McLaughlin
- Josephine A. Cummings
- Ross J. Buchmueller

The Reciprocal maintained an audit committee, as required by Section 624.424(8)(c), Florida Statutes.

The SAC is the primary governing body of the Reciprocal as to exercising subscribers' rights and contractually appointing its Attorney in Fact (AIF) which operates as outsourced management of the Reciprocal. The Board of the AIF, Privilege Underwriters, Inc. (PUI), appoints and governs the management of the Reciprocal. Mr. Buchmueller was a member of both SAC and the AIF's Board. Any overlap indications of Mr. Buchmueller were recorded only under the SAC heading, as the AIF's appointed SAC member. The AIF does not have a Board; its Board is that of the parent affiliate, it contractually delegated all operational duties to, PUI.

## AIF's Board of Directors (PUI Board of Directors)

<b>Name and Location</b>	<b>Principal Occupation</b>
Ross J. Buchmueller Companies Larchmont, New York	President & CEO, Pure Group
John S. Baine Companies Columbus, Ohio	Executive, Nationwide
James D. Carey LLC Riverside, Connecticut	Principal, Stone Point Capital,
Peter M. Mundheim LLC New York, New York	Principal, Stone Point Capital,
Nicholas D. Zerbib LLC Larchmont, New York	Principal, Stone Point Capital,

Subsequent to December 31, 2014, Christopher Harrington and Tagar Olson were appointed to the PUI Board of Directors.

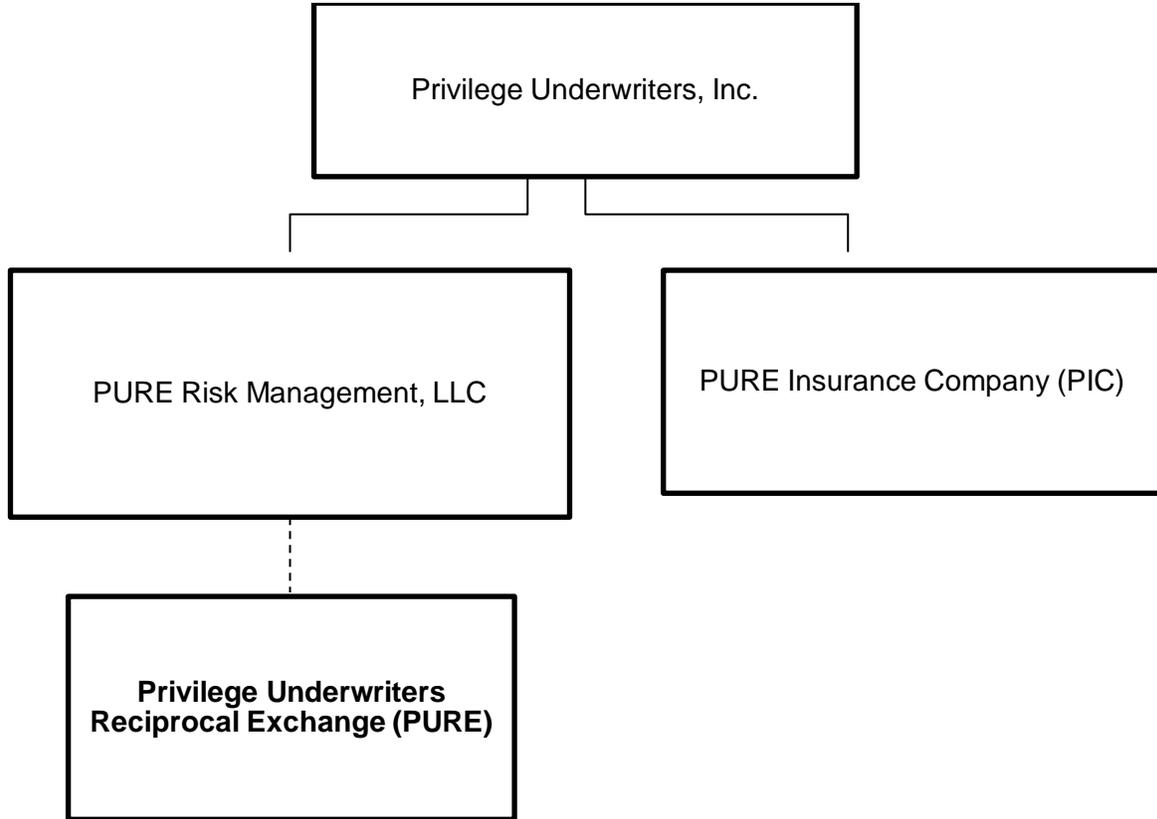
The SAC operated as the Audit Committee of the Reciprocal.

Director Richard Jacobs was appointed on September 15, 2011. The Office did not receive notification until April 5, 2012; therefore, the appointment of Director Richard Jacobs occurred without timely notice in accordance with Section 628.261, Florida Statutes and Rule 69O-143.046 (6), Florida Administrative Code, which an insurer to keep current the information required to be disclosed in the Insurance Company Holding System Registration Statement within 15 calendar days after the end of the month of the change.

**Affiliated Companies**

The most recent holding company registration statement was filed with the Office on March 11, 2016, as required by Section 628.801, Florida Statutes, and Rule 69O-143.046, Florida Administrative Code.

**Privilege Underwriters Reciprocal Exchange  
Organizational Chart  
December 31, 2014**



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

### **Subscribers Agreement and Power of Attorney**

Each new Subscriber signed a Subscriber's Agreement and Power of Attorney which appointed PRM as the AIF and allowed the AIF to conduct the lawful business of the Reciprocal. Each Subscriber agreed to make a surplus contribution for five years. The surplus contribution was a percentage of the policy premium (10% for Homeowner and Watercraft policies and 4% for all other policies).

### **Attorney - in - Fact Agreement**

The Reciprocal, being a non-assessable reciprocal insurer and as prescribed by Chapter 629, Florida Statutes, entered into an Attorney-in-Fact agreement with PRM, on January 24, 2007, which was revised on April, 18, 2014. The agreement provided, in general, that PRM manage the affairs of the Reciprocal to include premiums and claims administration services and periodic reporting of the Reciprocal's financials to the SAC.

In consideration of the Underwriting and Marketing services provided to the Reciprocal, PRM receives as compensation an amount equal to 17% of the Gross Written Premium of the Reciprocal. 2014 fees incurred under this agreement amounted to \$59,413,400. In return for services provided in the servicing and management of claims, PRM was to receive a fee to be equal to 5% of Gross Earned Premium. These percentages may be adjusted at any time as agreed to by both the Reciprocal and PRM with written approval by the Office. Loss adjustment expenses in excess of \$2,500 per claim were paid by the Reciprocal. 2014 fees incurred under this agreement amounted to \$14,694,400.

## **Broker Agency Agreement**

The Reciprocal and PUI entered into a Broker Agency agreement. PUI received a 10% commission on policies written for policies with commission and entered into a distinct professional services agreement with members for non-commission policies. The Reciprocal was not involved in the collection of fees between PUI and members. Commissions paid to PUI under this agreement during 2014 amounted to \$890,794.

The Reciprocal did not formally file agency agreements with the Office, including the following: Privilege Underwriters, Inc. (PUI affiliate); Insurance Intermediaries, Inc. The business written and commission earned by these agencies were not in compliance with Section 628.255, Florida Statutes. **Subsequent Event:** The agreement with Insurance Intermediaries, Inc. is no longer in effect and therefore, no corrective action is required to correct the agreement.

## **Investments**

The Company made several investments that were not compliant with Section 625.332(b). The Company invested \$3,500,000 in Eagle Point Credit Company Inc., a publicly traded company managed by Eagle Point and majority owned (8,700,000 of 13,800,000 outstanding shares) by Stone Point's Trident V Fund reported on Schedule D were not disclosed to the Office for consent. Affiliate Stone Point Capital LLC owned a majority interest, via its Trident funds, in Eagle Point Credit Management, which formed a Cayman Islands hedge fund in 2012 called Eagle Point Credit US LP, which was managed by Eagle Point. The Reciprocal invested \$3,500,000 in Eagle Point Credit US LP, a Cayman Islands hedge fund managed/controlled by Eagle Point and affiliates and \$2,000,000 in Sound Point Credit Opportunities Fund LP, a hedge fund managed/controlled by Sound Point Capital Management LP, an affiliate of Ellipse Holdings, LLC,

which is owned by several Stone Point principals. These items were reported on Schedule BA, but were not disclosed appropriately as affiliated.

In June 2015, PUI entered into a definitive agreement to recapitalize with equity investments from funds managed by Stone Point Capital LLC, KKR & Co. LP and the management team. As part of the transaction, funds managed by Stone Point Capital will maintain a majority stake in Privilege Underwriters, while KKR will acquire a minority stake. As a part of this recapitalization, two new layers of partnership entities were created: Privilege Group Holdings LP (PGH LP) became owner of PUI via an indirect acquisition and Privilege Group Holdings GP (PGHGP) became the general partner of PGH LP. The private equity ownership percentage is equal in PGH GP and PGH LP, respectively.

### **Reinsurance Pooling Agreement**

The Reciprocal was party to a reinsurance pooling agreement with PURE Insurance Company as noted in the reinsurance section.

### **Fidelity Bond and Other Insurance**

The Reciprocal maintained fidelity bond coverage up to \$3,000,000 (\$6,000,000 aggregate), with a deductible of \$10,000, which reached the suggested minimum as recommended by the NAIC. The Reciprocal also maintained Directors and Officers (D&O) liability insurance coverage to an aggregate limit of liability of \$20,000,000 with retention of \$50,000.

The Reciprocal was a named insured under the above referenced policies issued to the PURE Group of Insurance Companies.

## **Pension, Stock Ownership, and Insurance Plans**

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

Nationwide no longer owns a minority ownership interest in the parent company Privilege Underwriters, Inc., as of August 14, 2015.

## **TERRITORY AND PLAN OF OPERATIONS**

The Reciprocal was authorized to transact insurance in 49 states (including the District of Columbia) with pending applications in Alaska and Idaho as of December 31, 2014.

## **Treatment of Policyholders**

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

## **REINSURANCE**

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

## **Assumed**

The Reciprocal had no assumed business at December 31, 2014.

## **Ceded**

The Reciprocal ceded risk on a quota share and excess of loss basis to various reinsurers. Quota share agreements were entered into for each of the Reciprocal's lines of business. In addition, the Reciprocal obtained coverage through the Florida Hurricane Catastrophe Fund (FHCF), and obtained property excess of loss reinsurance for catastrophic events. Effective June 1, 2009, the Reciprocal had a number of reinsurance agreements with various subscribers under an amended and revised contract with Guy Carpenter and also with General Reinsurance Corporation. Various quota share percentages for each line of business were ceded under separate agreements.

The reinsurance contracts were reviewed by the Reciprocal's appointed actuary and were utilized in determining the ultimate loss opinion.

The Reciprocal participated in a 50% pooling agreement with its affiliate, PURE, whereby PURE assumed 50% of the business and related liabilities net of outside reinsurance. This contract was effective as of the inception of PURE on August 5, 2008.

On November 16, 2015, XL Reinsurance America Inc., (XL Re) became a limited partner of Privilege Group Holdings, LP. XL Re (Catlin) is a material reinsurer for the Reciprocal.

## **ACCOUNTS AND RECORDS**

The Reciprocal maintained its principal operational offices in White Plains, New York, where this examination was conducted.

The Reciprocal's accounting records were maintained on a third party vendor software program developed by SAGE called MAS500. MASS500 was incorporated by the Reciprocal at inception in 2007. The Intacct system, previously used as for account payable, was expanded in 2014 to include the general ledger. The accounting system has been supported by an internal information technology department as well as external vendors. The Reciprocal's balance sheet accounts were verified with the line items of the annual statement submitted to the Office.

The Reciprocal and non-affiliates had the following agreements.

### **Custodial Agreement**

The Reciprocal entered into a custodial agreement with TD Bank, NA dated October 10, 2008 and with US Bank, dated September 17, 2014. Both agreements contained all the requirements of Rule 69O-143.042, Florida Administrative Code.

### **Investment-Management Agreement**

The Reciprocal entered into an investment-management agreement with GenRe – New England Asset Management, Inc., (GenRe), a corporation organized under the laws of the state of Delaware to make all investment decisions for and provide investment accounting services for the Reciprocal.

On December 22, 2011, the Reciprocal entered into a new agreement with Wellington Management Company, LLP, a limited partnership organized under laws of the Commonwealth of Massachusetts to manage, supervise and direct the Reciprocal's investment and reinvestment of assets in the account subject to the Reciprocal objectives and guidelines. The guidelines were revised March, 2014. They have full discretion to establish accounts and execute transactions with brokers. Clearwater manages all of the accounting and processing transactions for Wellington.

### **Claims Service Agreement**

The Reciprocal entered into a claims service agreement with CEI Insurance Services (CEI), whereas CEI provided certain online application claims auto adjusting services and had developed a nationwide network of vehicle repair vendors to provide vehicle repairs or appraisals for CEI and the Reciprocal.

### **Independent-Auditor Agreement**

An independent CPA, EisnerAmper LLP, audited the Reciprocal's statutory basis financial statements annually for the years 2010, 2011, 2012, 2013 and 2014 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.

## **INFORMATION TECHNOLOGY REPORT**

Brian Menard, AES, CFE, CISA of AGI Services performed an evaluation of the information technology and computer systems of the Reciprocal. Results of the evaluation were noted in the Information Technology Report provided to the Reciprocal.

## 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:

<b>State</b>	<b>Description</b>	<b>Par Value</b>	<b>Market Value</b>
FL		<u>\$2,565,422</u>	<u>\$2,546,404</u>
TOTAL FLORIDA DEPOSITS		\$2,565,422	\$2,546,404
AL		1,099,535	1,101,507
GA		35,014	35,039
MA		109,686	109,571
NV		209,911	210,288
NH		1,019,671	1,020,561
NM		309,115	308,791
NC		424,820	425,582
SC		125,048	125,138
TX		2,598,900	2,603,562
VA		<u>506,220</u>	<u>504,185</u>
TOTAL OTHER DEPOSITS		\$6,437,920	\$6,444,224
TOTAL SPECIAL DEPOSITS		<u>\$9,003,342</u>	<u>\$8,990,628</u>

## **FINANCIAL STATEMENTS**

The examination does not attest to the fair presentation of the financial statements included herein. If an adjustment is identified during the course of the examination, the impact of such adjustment will be documented separately following the Reciprocal's financial statements. Financial statements, as reported and filed by the Reciprocal with the Florida Office of Insurance Regulation, are reflected on the following pages:

## Privilege Underwriters Reciprocal Exchange

### Assets

December 31, 2014

	Per Reciprocal	Examination Adjustments	Per Examination
Bonds	\$64,398,899		\$64,398,899
Stocks:			
Preferred	507,810		507,810
Common	6,200,742		6,200,742
Cash and Short-Term Investments	53,044,257		53,044,257
Other investments	5,688,015		5,688,015
Investment Income due and accrued	487,513		487,513
Agents' Balances:			
Uncollected premium	3,968,058		3,968,058
Deferred premium	68,367,246		68,367,246
Reinsurance recoverable	17,289,003		17,289,003
Totals	<u>\$219,951,543</u>		<u>\$219,951,543</u>

**Privilege Underwriters Reciprocal Exchange**  
**Liabilities, Surplus and Other Funds**  
**December 31, 2014**

	Per Reciprocal	Examination Adjustments	Per Examination
Losses	\$16,914,121		\$16,914,121
Loss adjustment expenses	2,449,339		2,449,339
Commissions payable, contingent commissions, and other similar charges	15,785,138		15,785,138
Other expenses	3,419,049		3,419,049
Taxes, licenses and fees	3,486,234		3,486,234
Ceded reinsurance premium payable	34,560,892		34,560,892
Unearned premium	48,858,230		48,858,230
Funds held under reinsurance treaties	16,837,793		16,837,793
Payable for securities	1,338,504		1,338,504
Advance premiums	3,092,887		3,092,887
Payable to parent, subsidiaries and affiliates	4,519,216		4,519,216
Aggregate write-ins for liabilities	9,502		9,502
Total Liabilities	\$151,270,905		\$151,270,905
Common capital stock			
Surplus notes payable	44,622,093		44,622,093
Gross paid in and contributed surplus	79,667,099		79,667,099
Unassigned funds (surplus)	(55,608,553)		(55,608,553)
Surplus as regards policyholders	68,680,639		68,680,639
Total liabilities, surplus and other funds	\$219,951,544		\$219,951,544

**Privilege Underwriters Reciprocal Exchange**  
**Statement of Income and Capital and Surplus Account**  
**December 31, 2014**

	2014	2013	2012	2011	2010
<b>Underwriting Income</b>					
Premiums Earned	\$85,627,410	\$60,226,956	\$36,364,071	\$23,858,961	\$13,455,488
<b>Deductions:</b>					
Losses incurred	\$39,268,074	\$25,400,171	\$19,740,925	\$13,617,860	\$5,584,824
Loss adjustment expenses incurred	8,058,968	5,870,649	4,826,695	2,841,172	2,548,964
Other underwriting expenses incurred	45,040,634	35,535,923	23,017,855	14,887,024	9,418,656
Total underwriting deductions	<u>\$92,367,676</u>	<u>\$66,806,743</u>	<u>\$47,585,475</u>	<u>\$31,346,056</u>	<u>\$17,552,444</u>
Net underwriting gain or (loss)	(\$6,740,266)	(\$6,579,787)	(\$11,221,404)	(\$7,487,095)	(\$4,096,956)
<b>Investment Income</b>					
Net investment income earned	(\$7,172,808)	(\$2,900,609)	\$619,509	(\$1,836,047)	(\$1,375,432)
Net realized capital gains or (losses) less capital gains tax	253,087	115,569	768,882	408,564	973,717
Net investment gain (loss)	<u>(\$6,919,721)</u>	<u>(\$2,785,040)</u>	<u>\$1,388,391</u>	<u>(\$1,427,483)</u>	<u>(\$401,715)</u>
Net income	<u><u>(\$13,659,987)</u></u>	<u><u>(\$9,364,827)</u></u>	<u><u>(\$9,833,013)</u></u>	<u><u>(\$8,914,578)</u></u>	<u><u>(\$4,498,671)</u></u>
<b>Capital and Surplus Account</b>					
Surplus as regards policyholders, December 31 prior year	\$60,081,415	\$53,187,920	\$51,444,148	\$51,837,293	\$49,978,129
Net Income	(\$13,659,987)	(\$9,364,827)	(\$9,833,013)	(\$8,914,578)	(\$4,498,671)
Net unrealized capital gains or losses	243,793	44,460	0	0	0
Change in net derred income tax	0	0	0	(857,812)	(2,598,374)
Change in non-admitted assets	77,775	(138,870)	64,534	818,022	2,769,814
Change in surplus notes	(1,465,116)	(1,465,116)	(1,465,116)	(1,232,558)	(750,000)
Surplus adjustments: paid in	23,402,759	17,817,848	12,977,367	9,793,781	6,936,395
Change in surplus as regards policyholders for the year	<u>\$8,599,224</u>	<u>\$6,893,495</u>	<u>\$1,743,772</u>	<u>(\$393,145)</u>	<u>\$1,859,164</u>
Surplus as regards policyholders, December 31 current year	<u><u>\$68,680,639</u></u>	<u><u>\$60,081,415</u></u>	<u><u>\$53,187,920</u></u>	<u><u>\$51,444,148</u></u>	<u><u>\$51,837,293</u></u>

**Privilege Underwriters Reciprocal Exchange**  
**Comparative Analysis of Changes in Surplus**  
**December 31, 2014**

The following is a reconciliation of surplus as regards policyholders between that reported by the Reciprocal and as determined by the examination.

Surplus as Regards Policyholders	
December 31, 2014, per Annual Statement	\$68,680,639

	Per Reciprocal	Per Exam	Increase (Decrease) In Surplus
ASSETS:			
No Adjustment			
LIABILITIES			
No Adjustment			
Net Change in Surplus:			_____
Surplus as Regards Policyholders			
December 31, 2014, Per Examination			<u>\$68,680,639</u>

## **COMMENTS ON FINANCIAL STATEMENTS**

### **Liabilities**

#### **Losses and Loss Adjustment Expenses**

An outside actuarial firm, Perr & Knight, appointed by the SAC, rendered an opinion that the amounts carried in the balance sheet as of December 31, 2014, made a reasonable provision for all unpaid loss and loss expense obligations of the Reciprocal under the terms of its policies and agreements.

The examination consulting actuary, Alan Kaliski, FCAS, MAAA of AGI Services, reviewed the Loss and Loss Adjustment Expense reserves carried in the Reciprocal's balance sheet as of December 31, 2014 and he was in concurrence with this opinion.

#### **Capital and Surplus**

The amount reported by the Reciprocal of \$68,680,639 exceeded the minimum of \$8,816,187 required by Section 624.408, Florida Statutes.

## **SUMMARY OF RECOMMENDATIONS**

### **Affiliated Agency Agreements**

We recommend that the Reciprocal comply with Section 628.255, Florida Statutes, by filing with the Office all affiliated agency agreements.

### **Investments**

We recommend the Reciprocal comply with Section 625.332(1)(b), Florida Statutes.

## CONCLUSION

The insurance examination practices and procedures as promulgated by the NAIC have been followed in ascertaining the financial condition of **Privilege Underwriters Reciprocal Exchange** as of December 31, 2014, consistent with the insurance laws of the State of Florida.

Per examination findings, the Reciprocal's surplus as regards policyholders was \$68,680,639, which exceeded the minimum of \$8,816,187 required by Section 624.408, Florida Statutes.

In addition to the undersigned, Scott Eady, CFE, CPA, Examiner-in-Charge, and Brian Menard, CFE, CISA, IT Specialist, Alan Kaliski, FCAS, MAAA, Actuary, and Helene Bradley, CPA, Participating Examiner, of AGI Services participated in the examination. Members of the Office who participated in the examination include Jonathan Frisard, CPA, Financial Examiner/Analyst Supervisor, Examination Manager, Michael Goldgisser, Reinsurance Financial Specialist and Marie Stuhlmuller, Financial Specialist, Participating Examiners.

Respectfully submitted,

Lamar Downs, CPA  
Deputy Chief Examiner  
Florida Office of Insurance Regulation