

**REPORT ON THE LIMITED-SCOPE EXAMINATION**  
**OF**  
**SEMINOLE CASUALTY INSURANCE**  
**COMPANY**

**TAMARAC, FLORIDA**

**OF THE**

**Loss Reserves and Loss Adjustment Expenses**  
**Reinsurance Program**  
**and**  
**Information Technology Systems**

**As of September 30, 2009**

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

## TABLE OF CONTENTS

<b>LETTER OF TRANSMITTAL .....</b>	<b>-</b>
<b>SCOPE OF EXAMINATION .....</b>	<b>1</b>
<b>HISTORY .....</b>	<b>2</b>
GENERAL .....	2
<b>LIMITED-SCOPE AREAS .....</b>	<b>2</b>
LOSSES AND LAE RESERVES .....	2
REINSURANCE PROGRAM.....	4
INFORMATION TECHNOLOGY SYSTEMS .....	5
ACCOUNTS AND RECORDS .....	6
<b>ORGANIZATIONAL CHART .....</b>	<b>7</b>
<b>FINANCIAL STATEMENTS PER EXAMINATION.....</b>	<b>8</b>
<i>Assets</i> .....	9
<i>Liabilities</i> .....	10
<i>Statement of Income</i> .....	11
<b>COMPARATIVE ANALYSIS OF CHANGES IN SURPLUS .....</b>	<b>12</b>
<b>COMMENTS ON FINANCIAL STATEMENTS.....</b>	<b>13</b>
BONDS .....	13
AMOUNTS RECOVERABLE FROM REINSURERS .....	13
LOSSES AND LOSS ADJUSTMENT RESERVES.....	14
CEDED REINSURANCE PREMIUMS PAYABLE .....	14
FUNDS HELD BY COMPANY UNDER REINSURANCE CONTRACTS .....	15
<b>SUMMARY OF EXAM FINDINGS .....</b>	<b>16</b>
SUPPORT FOR ACTUARIAL OPINION.....	16
MATERIAL ERRORS IN FINANCIAL REPORTING .....	16
<b>SUBSEQUENT EVENTS.....</b>	<b>17</b>
BOARD OF DIRECTORS.....	17
SHAREHOLDER CHANGE .....	17
DETERIORATION IN POLICYHOLDERS SURPLUS .....	17
<b>CONCLUSION.....</b>	<b>18</b>

Tallahassee, Florida

April 26, 2010

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 as of September 30, 2009, of the financial condition and corporate affairs of:

**SEMINOLE CASUALTY INSURANCE COMPANY  
6691 N. NOB HILL ROAD  
TAMARAC, FLORIDA 33321**

Hereinafter referred to as the "Company". Such report of examination is herewith respectfully submitted.

## **SCOPE OF EXAMINATION**

This was a limited-scope examination of the Company to the extent and in the manner directed by the Florida Office of Insurance Regulation (Office). To the extent applicable, the examination was conducted in accordance with the guidance of the National Association of Insurance Commissioners (NAIC) Financial Condition Examiner's Handbook, the NAIC Accounting Practices and Procedures Manual, the Florida Statutes, and the Florida Administrative Code. The limited-scope examination differs in many respects from that of a full-scope examination or an audit performed in accordance with generally accepted auditing standards.

In accordance with the provisions of Section 624.316, Florida Statutes, the Office called a statutory limited-scope examination of the Company to cover the period ending December 31, 2008, and events subsequent. The examination commenced on March 23, 2009; however, due to the reportable conditions and preliminary examination findings, the Company requested and was granted approval to roll the examination date forward to September 30, 2009. All current reinsurance contracts, schedule P data, losses and loss adjustment expense (LAE) reserves and Information Technology systems supporting the claims and reinsurance programs were examined as of September 30, 2009. Management was also interviewed to obtain a full understanding of their philosophy, short and long-term goals and strategies outlined to achieve those goals. Subsequent events that could affect the company were also reviewed.

This limited-scope examination as of September 30, 2009, also involved a review of all of the remedial and corrective actions taken by the Company to address and/or satisfy the preliminary findings disclosed as of December 31, 2008. The field work was concluded on April 26, 2010.

Highland Clark, LLC was engaged by the Office to perform this examination. Taylor Walker and Associates was utilized by Highland Clark for the examination actuarial analysis and review.

## HISTORY

### General

The Company was incorporated in Florida on June 9, 1988, and commenced business on December 21, 1988, as the Seminole Casualty Insurance Company.

In accordance with Section 624.401(1), Florida Statutes, the Company was authorized to transact the following insurance coverage's in Florida on September 30, 2009.

Fire	Allied Lines
Homeowners	Other Liability
Private Passenger Auto Physical Damage	Private Passenger Auto Liability
Commercial Auto Liability	Commercial Auto Physical Damage

## LIMITED-SCOPE AREAS

### Losses and LAE Reserves

On February 28, 2009, the Company's consulting actuary issued a "No Opinion" Opinion on the Company's reserves as of December 31, 2008. This "No Opinion" was based upon the unavailability of reliable loss data from the Company. The Company indicated the problem with the reliable loss data was caused by changes in the way their Maryland claims administrator, National Adjustment Bureau, reported claims data.

Due to the "No Opinion" and problems cited by the Company related to the loss data, the Office called for a limited scope examination of the Company on March 20, 2009.

The Company provided revised loss data to its consulting actuary, increased the reserves by \$500,000 and amended the year-end 2008 annual statement. On April 6, 2009, the consulting actuary issued a "Reasonable Opinion", but noted that the Company's reserves were at the very low end of the acceptable range.

The examination actuary performed an analysis of the actual development as of March 31, 2009, and this analysis originally indicated a need for a significant and material increase to the Company's reserves as of December 31, 2008. Due to the magnitude of this adverse development and errors in claim count data, examination adjustments were indicated.

The Company asserted that the examination actuary's findings were based on flawed data and requested approval from the Office to roll the examination as-of-date forward to September 30, 2009 to provide management time to take corrective action and conduct a full review of the loss details and claims count data. On August 12, 2009, the field examination team discussed the Company's request and roll-forward protocol with the Office's Chief Examiner. The request was granted and it was agreed that the fieldwork would be postponed until after the Company filed their 2009 third quarter statement.

As of December 31, 2008, and September 30, 2009, the Company booked reserves for losses and loss adjustment expenses that were less than its consulting actuary's mid-point estimate.

**Subsequent Event:** As of December 31, 2009, the Company booked reserves for losses and loss adjustment expenses in the amount of \$10,936,292, which was \$14,292 over its consulting actuary's mid-point estimate of \$10,922,000.

The Company's consulting actuary only included a one page summary to support his Statement of Actuarial Opinion for 2008. The NAIC Annual Statement Instructions and Actuarial Standards of Practice #9 require a comprehensive narrative report in support of the Statement of Actuarial Opinion. In September 2010, the Company replaced the consulting actuary with Mr. Charles C. Emma, FCAS, MAAA, of EVP Streff.

### **Reinsurance Program**

Effective January 1, 2008, the Company entered into a new two-year quota share reinsurance agreement covering the Company's private passenger and commercial automobile business with Aspen Insurance Limited. This new arrangement exhibited some positive changes, specifically, a reduction in the reinsurer margin from 5.0% to 4.0%, and removal of the loss corridor and no cap on Extra Contractual Obligations (ECO) and Excess of Policy Limits (XPL) losses (other than the aggregate contract caps). Effective January 1, 2009, the Aspen agreement was amended to allow a 60% cession rate. This reinsurance arrangement required the Company to add additional collateral to account for unauthorized reinsurance.

The Company reported a Funds-held liability account to collateralize the credit for unauthorized reinsurance. However, the Aspen reinsurance agreement also required the Company to pledge assets to a trust for the benefit of Aspen to offset amounts in the Funds-held liability account. Under statement of Statutory Accounting Principals (SSAP) A-785, the trust arrangement invalidated the Funds-held account as collateral, since the funds were not held, but rather fully negotiated to a trust that benefited the reinsurer.

During the roll-forward period, the Company remediated the deficient collateral by obtaining increased letters of credit from the unauthorized reinsurers but continued to admit the assets pledged to the trust and carry the corresponding Funds-held account on their balance sheet.

This presentation unnecessarily inflated the balance sheet by increasing both assets and liabilities and was not in compliance with Section 69O-137.001(2), Florida Administrative Code, requiring the Company to file a full and true statement of its financial condition, transactions, and affairs. Additionally, SSAP No. 4, requires that pledged assets not available for the benefit of the Company's policyholders and claimants be non-admitted.

**Subsequent Event:** Beginning with the Third Quarter 2010, the Company listed the pledged assets (\$3,292,249) as non-admitted and removed the Funds Held for Reinsurance (reported as \$1,810,146 as of June 30, 2010). The Office has accepted both the pledged assets and the related liability, Funds Held for Reinsurance, as of September 30, 2009; however, the Office still maintains concerns that the Company may not have the right of offset as used.

### **Information Technology Systems**

Data origination for the Company involved a combination of in-house custom-developed systems, third-party hosted web applications for point of sale and claims reporting, as well as policy and claims output reports provided by general agencies and claims administrators for the Maryland book of business.

The examination evaluated automated controls over claims and reinsurance accounting and financial reporting as it related to the general ledger and Schedule P. The Company used Peachtree for general ledger accounting. All entries were manually keyed into Peachtree from reports generated by in-house systems and reports provided by the general agency, National Insurance Underwriters (NIU) and claims administrator, National Adjustment Bureau (NAB). The Company had indicated issues with the change control processes at NAB. Furthermore, neither NIU nor NAB had obtained a service auditor's report on the effectiveness of controls placed in operation (SAS-70 Type II).

**Subsequent Event:** The Company had noted deterioration in the results of its Maryland program over the past several quarters. In response to this performance, recurring data reporting issues, and concerns regarding the economics of the contract, the Company began to take steps in 2009 to amend the terms of the contract retroactive to January 1, 2009. Those efforts ultimately proved unsuccessful and, as a result, the Company terminated its agreement with NIU and NAB effective December 31, 2009, subject to statutory requirements relating to the “run-off” of the business. This mitigated the need to obtain SAS-70 reports from these service providers.

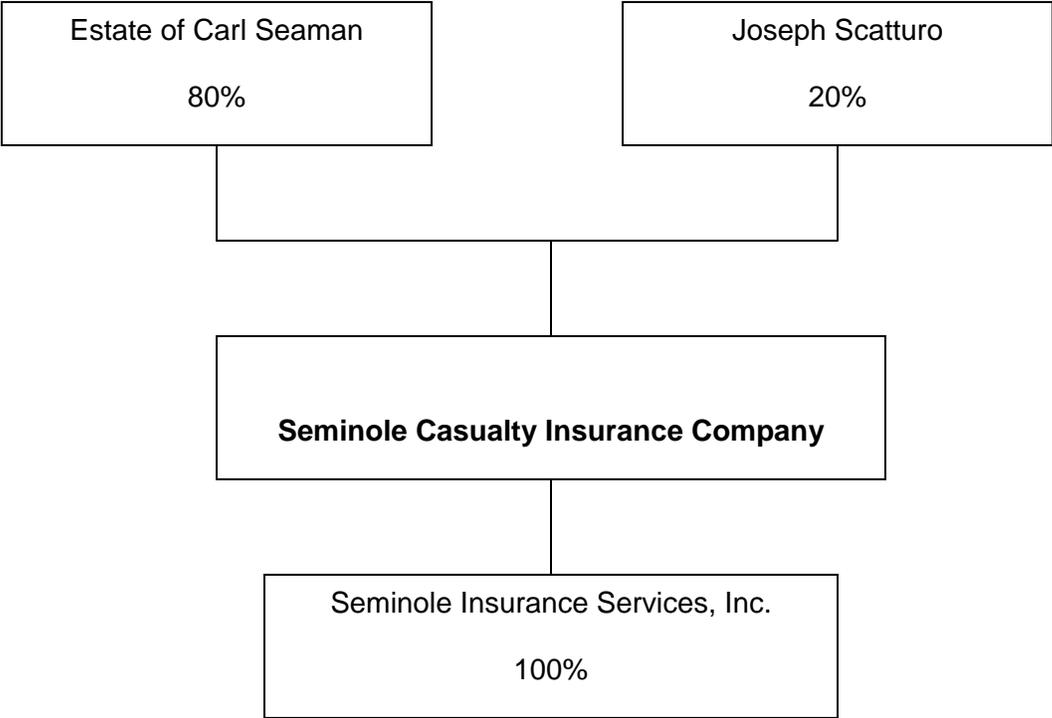
### **Accounts and Records**

The examination was unable to reconcile the amounts recoverable from reinsurers to ceded loss and LAE for the 3rd quarter 2009. Upon examination inquiry, management responded that the Amounts recoverable asset had been overstated by \$2,275,637 on the third quarter 2009 statement due to an entry booked in anticipation of commuting a reinsurance contract. The Company and reinsurer later determined to postpone the commutation until after year-end 2009, but the Company failed to reverse the entry prior to filing the September 30, 2009, quarterly statements. The entry overstated both assets and liabilities by \$2,275,637 and had no effect on surplus. The Company had found this error subsequent to the September 30, 2009 filing of the quarterly statement, but did not make timely disclosure to the Office. The Company’s third quarter statement was not prepared in compliance with Section 69O-137.001(2), Florida Administrative Code, which requires a full and true statement of financial condition, transactions, and affairs.

**Subsequent Event:** The Company recorded reversing entries as of December 31, 2009, which corrected the reported ceded loss and loss adjustment expenses in the December 31, 2009, annual statement.

Below is a simplified Organizational Chart of the Company. A comprehensive Organizational Chart appears in the 2008 Annual Statement.

**SEMINOLE CASUALTY INSURANCE COMPANY**  
**ORGANIZATIONAL CHART**  
**SEPTEMBER 30, 2009**



## **FINANCIAL STATEMENTS PER EXAMINATION**

The following pages contain financial statements showing the Company's financial position as of September 30, 2009, 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."

**SEMINOLE CASUALTY INSURANCE COMPANY**

**September 30, 2009**

**Assets**

	<u>Per Company</u>	<u>Examination Adjustments</u>	<u>Per Examination</u>
Bonds	\$ 23,241,026		\$ 23,241,026
Stocks			
Preferred stocks	159,200		159,200
Common stocks	1,417,232		1,417,232
Real estate			
Properties occupied by the company (net of encumbrances)	2,963,267		2,963,267
Cash and short term investments	3,194,724		3,194,724
Subtotals, cash and invested assets	\$ 30,975,449		\$ 30,975,449
Investment income due and accrued	306,250		306,250
Premiums and considerations			
Uncollected premiums and agents' balances in the course of collection	896,455		896,455
Deferred premiums	9,939,861		9,939,861
Reinsurance			
Amounts recoverable from reinsurers	8,211,984	(2,275,637)	5,936,347
Other amounts receivable under reinsurance contracts	1,183,541		1,183,541
Current federal and foreign income tax recoverable	2,271,004		2,271,004
Net deferred tax asset	788,440		788,440
EDP equipment and software	279,108		279,108
Total assets	\$ 54,852,092	\$ (2,275,637)	\$ 52,576,455

**SEMINOLE CASUALTY INSURANCE COMPANY**

**September 30, 2009**

**Liabilities**

	<b>Per Company</b>	<b>Examination Adjustments</b>	<b>Per Examination</b>
Losses	\$ 9,276,153		\$ 9,276,153
Loss adjustment expenses	1,106,773		1,106,773
Commissions payable	509,485		509,485
Other expenses	491,656		491,656
Taxes licenses and fees	95,506		95,506
Unearned premium	12,689,602		12,689,602
Ceded reinsurance premiums payable	11,720,574	(2,275,637)	9,444,937
Funds held by company for reinsurance	10,197,802		10,197,802
Payable to parent, subsidiaries and affiliates	43,023		43,023
Aggregate write-ins for liabilities	22,207		22,207
Total liabilities	\$ 46,152,781	\$ (2,275,637)	\$ 43,877,144
Common capital stock	\$ 2,000,000		\$ 2,000,000
Surplus notes	3,770,000		3,770,000
Gross paid in and contributed capital	6,720,000		6,720,000
Unassigned funds (surplus)	(3,790,689)		(3,790,689)
Surplus as regard policyholders	\$ 8,699,311		\$ 8,699,311
Total liabilities captial and surplus	\$ 54,852,092	\$ (2,275,637)	\$ 52,576,455

**SEMINOLE CASUALTY INSURANCE COMPANY**

**September 30, 2009**

**Statement of Income**

**Underwriting Income**

Premiums earned	\$	21,305,948
<b>Deductions</b>		
Losses incurred		14,769,941
Loss adjustment expenses incurred		4,306,993
Other underwriting expenses incurred		8,657,062
Total underwriting deductions	\$	<u>27,733,996</u>
Net underwriting gain or (loss)	\$	(6,428,048)

**Investment Income**

Net investment income earned	\$	845,455
Net realized capital gains or (losses)		(210,076)
Net investment gain (loss)	\$	<u>635,379</u>

**Other Income**

Finance and service charges not included in premium	\$	2,275,315
Aggregate write-ins for miscellaneous income		105,537
Total other income	\$	<u>2,380,852</u>
Net income before dividends to policyholders	\$	(3,411,817)
Federal and foreign income taxes incurred		(1,400,000)
Net income	\$	<u><u>(2,011,817)</u></u>

**Capital and Surplus Account**

Surplus as regard policyholders, December 31 prior year	\$	9,813,315
Net income for current year	\$	(2,011,817)
Change in net unrealized capital gains or (losses)		737,861
Change in net deferred income tax		(1,296,114)
Change in non-admitted assets		1,456,066
Examination Adjustments		
Change in surplus as regards policyholders		<u>(1,114,002)</u>
Surplus as regards policyholders	\$	<u><u>8,699,313</u></u>

**COMPARATIVE ANALYSIS OF CHANGES IN SURPLUS**

**SEMINOLE CASUALTY INSURANCE COMPANY**

**September 30, 2009**

Surplus as Regards Policyholders as of September 30, 2009 quarterly statement				\$	8,699,311
			<b>Increase (Decrease) in Surplus</b>		
	<b>Per Company</b>	<b>Per Examination</b>			
Assets:					
Amounts recoverable from reinsurers	8,211,984	5,936,347	(2,275,637)		
Liabilities:					
Ceded reinsurance premiums payable	11,720,574	9,444,937	2,275,637		
Net Change in Surplus					<u>0</u>
Surplus as Regards Policyholders as of September 30, 2009 per Examination				\$	<u>8,699,311</u>

## COMMENTS ON FINANCIAL STATEMENTS

### Assets

**Bonds** **\$23,241,026**

The Company had a quota share reinsurance agreement with Aspen Reinsurance which contained a provision requiring the Company to maintain a trust for the benefit of the reinsurer in an amount that corresponded with the Funds-held liability retained by the Company. As of September 30, 2009, the Company reported \$23,241,026 in Bonds and provided documentation showing that \$10,314,191 was pledged as collateral in connection with the reinsurance trust. **Subsequent**

**Event:** On the Third Quarter 2010 Report, the Company listed the pledged assets as non-admitted. The Office has accepted the pledged assets as admitted as of September 30, 2009; however, there are concerns that the Company may not have the right of offset as claimed.

**Amounts recoverable from reinsurers** **\$5,936,347**

The Company reported \$8,211,984 in Amounts recoverable from reinsurers. The examination was unable to reconcile these amounts to ceded loss and LAE for the third quarter 2009. Upon examination inquiry, management responded that the Amounts recoverable asset had been overstated by \$2,275,637 on the third quarter 2009 statement due to an entry booked in anticipation of commuting a reinsurance contract. The Company and reinsurer later determined to postpone the commutation until after year-end 2009, but the Company failed to correct the entry. The reported amount was not in compliance with Section 69O-137.001(2) Florida Administrative Code. An examination adjustment was indicated to correct the overstated asset with the corresponding offset to the Ceded premiums payable liability account.

## **Liabilities**

### **Losses and Loss Adjustment Reserves \$10,382,926**

The Company booked net reserves for Losses and Loss Adjustment Expenses in the amount of \$10,382,926. The examination actuary determined that this amount was within a reasonable estimated range of reserves.

The examination actuary also determined the opening actuary's estimated range of reserves, from \$10,261,000 to \$12,541,000, was reasonable.

### **Ceded reinsurance premiums payable \$9,444,937**

The Company reported \$11,720,574 in Ceded reinsurance premiums payable. The examination evaluated the underlying ceding commissions and found that profit commission had been understated by \$2,275,637 due to an entry booked in anticipation of commuting a reinsurance contract. The Company and reinsurer later determined to postpone the commutation until after year-end 2009, but the Company failed to correct the entry. The reported amount was not in compliance with Section 69O-137.001(2) Florida Administrative Code. An examination adjustment was indicated to correct the overstated liability with the corresponding offset to the Amounts recoverable from reinsurers asset account.

**Funds held by company under reinsurance contracts****\$10,197,802**

The Company reported \$10,197,802 in the Funds-held liability account. However, this account was invalid as collateral since the funds were not held, but rather fully negotiated to a trust that benefited the unauthorized reinsurer. The examination found that this method of reporting unnecessarily inflated the balance sheet by increasing both assets and liabilities and was not in compliance with Section 69O-137.001(2) Florida Administrative Code.

**Subsequent event:** On the Third Quarter 2010 Report, the Company listed the pledged assets as non admitted and made the corresponding reduction in the funds held liability. Based on this and subsequent discussions with the Company, the Office has accepted the Funds Held for Reinsurance, however, there is still concern regarding the Company's right of offset.

## SUMMARY OF EXAM FINDINGS

The following is a brief summary of items of interest and corrective action taken or to be taken by the Company regarding findings in the limited scope examination as of September 30, 2009.

### **Support for actuarial opinion**

The Company's Consulting Actuary included a one page summary to support his Statement of Actuarial Opinion for 2008. **We recommend that the Company notify its consulting actuary that pursuant to the annual statement instructions and Actuarial Standards of Practice #9, a comprehensive narrative report is required to support the Statement of Actuarial Opinion.**

### **Material errors in financial reporting**

The examination was unable to reconcile the amounts recoverable to ceded loss and loss LAE due to an entry that had been booked in error and not corrected or timely reported to the Office as required by Section 69O-137.001(2) Florida Administrative Code. **We recommend that the Company document and implement internal control procedures to help ensure accurate reporting of transactions in the general ledger and quarterly and annual statements.**

## **SUBSEQUENT EVENTS**

### **Board of Directors**

The Board of Directors appointed Linda Sharon Seaman as Chairperson of the Board to fill the vacancy in the Company's Board of Directors created due to the death of Director Carl Seaman effective June 1, 2009.

### **Shareholder Change**

The Estate of Carl Seaman replaced Carl Seaman as the 80% Shareholder in the Quarterly Statement as of September 30, 2009. The Annual Statement as of December 31, 2009 lists the Estate as the 100% Shareholder.

### **Deterioration in Policyholders Surplus**

The Company reported Policyholders Surplus in the amount of \$8,422,636, in the Annual Statement as of December 31, 2009, while the amount for year-end 2008 was \$9,813,315. The decrease of \$1,390,679 from the prior year was approximately 14% and represents a further deterioration of Surplus.

## CONCLUSION

The insurance examination practices and procedures as promulgated by the NAIC have been followed in ascertaining the financial condition of **SEMINOLE CASUALTY INSURANCE COMPANY** as of September 30, 2009, consistent with the insurance laws of the State of Florida.

Per examination findings, the Company's Surplus as regards policyholders was \$8,699,311 and was in compliance with Section 624.408, Florida Statutes.

In addition to the undersigned, Joseph Peiso, ARe, Reinsurance Specialist, Tracy Gates, CISA, Information Technology Specialist, Brent Sallay, FCAS, MAAA Examination Actuary, and John Coleman, CFE, participated in the examination.

Respectfully submitted,

---

Kethessa Carpenter, CPA  
Financial Examiner/Analyst Supervisor  
Florida Office of Insurance Regulation