

**REPORT ON EXAMINATION**  
**OF**  
**STAR CASUALTY INSURANCE**  
**COMPANY**  
**MIAMI, FLORIDA**

**AS OF**  
**DECEMBER 31, 2005**

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

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Tallahassee, Florida

February 9, 2007

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 December 31, 2005, of the financial condition and corporate affairs of:

**STAR CASUALTY INSURANCE COMPANY  
3750 WEST FLAGLER STREET  
MIAMI, FLORIDA 33134**

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, 2003 through December 31, 2005. This examination commenced, with planning at the Office of Insurance Regulation (Office), on November 6, 2006, to November 10, 2006. The fieldwork commenced on November 20, 2006, and was concluded as of February 9, 2007. 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 Company's independent audit reports and certain work papers prepared by the Company's independent certified public accountant (CPA) were reviewed and utilized where applicable within the scope of this examination.

We valued and verified the integrity of the balances of the Company's assets and liabilities as reported in its annual statement as of December 31, 2005, as those balances affect the financial solvency of the Company.

Transactions subsequent to year-end 2005 were reviewed where relevant and deemed significant to the Company's financial condition.

This report of examination is confined to financial statements and comments on matters that involve departures from laws, regulations or rules, or which are deemed to require special explanation or description.

### **Status of Adverse Findings from Prior Examination**

The Company was last examined by representatives of the Office as of December 31, 2002. The following was a summary of adverse findings contained in the Office's prior examination report along with the resulting action taken by the Company.

### **Affiliated Companies**

The Company was party to three management agreements with affiliates, wherein compensation was based on each affiliate's financial performance. The management agreements did not specify the services provided. **Resolution:** The Company complied with SSAP No. 25, paragraph 16 in agreements with affiliated companies by basing compensation on allocation of costs.

The Company failed to include an affiliated company in its holding company registration statement and in Schedule Y of the Annual Statement as of December 31, 2002. **Resolution:** The Company included the affiliate in an amended holding company registration statement filed with the Office on July 17, 2003.

### **Custodial Agreement**

The Company did not have a custodial agreement with Merrill Lynch. **Resolution:** The current custodial agreement complied with Rule 69O-143.042, Florida Administrative Code. The Company will annually request to use Merrill Lynch as a custodian. Rule 69O-143.042, Florida Administrative Code, defines a custodian as a national bank, state bank or trust company.

### **Receivable from Parent, Subsidiary, and Affiliates**

The Company failed to report a short-term unwritten agreement it had with an affiliated company in violation of Section 624.4435, Florida Statutes, and to report such agreements in accordance with NAIC Annual Statement instructions concerning transactions with affiliates. **Subsequent Event:** The Company discontinued the agreement in April 2003.

### **Guaranty Association Assessment**

The Company failed to report an assessment from the Florida Insurance Guaranty Association. The amount should have been reported as an asset for policy surcharge receivable and as a related liability in Taxes, Licenses, and Fees per SSAP No. 35, paragraph 9. **Resolution:** The Company reported assessments correctly in subsequent annual and quarterly statements.

### **Commissions Payable**

The Company incorrectly reported commissions' payable as other expenses. **Resolution:** The Company correctly reported commissions payable in subsequent annual and quarterly statements.

### **Payable to Parent, Subsidiary, and Affiliates**

The Company included an amount due to an affiliate in other expenses. **Resolution:** The Company correctly reported affiliated payables in accordance with NAIC Annual Statement Instructions in subsequent annual and quarterly statements.

## **HISTORY**

### **General**

The Company was incorporated in Florida on August 20, 1987 and commenced business on July 25, 1988 as Star Casualty Insurance Company. The Company was a member of an insurance holding company system as defined by Rule 69O-143.045(3), Florida Administrative Code.

In accordance with Section 624.401(1), Florida Statutes, the Company was authorized to transact the following insurance coverage in Florida on December 31, 2005:

Private Passenger Auto Liability

Private Passenger Auto Physical Damage

The articles of incorporation and the bylaws were not amended during the period covered by this examination.

## Capital Stock

As of December 31, 2005, the Company's capitalization was as follows:

Number of authorized common capital shares	750,000
Number of shares issued and outstanding	750,000
Total common capital stock	\$750,000
Par value per share	\$1.00

Nicolas Estrella, who owned 100% of the issued and outstanding capital stock, maintained control of the Company.

## 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 Statement.

	2005	2004	2003
Premiums Earned	19,290,081	18,733,634	14,366,438
Net Underwriting Gain/(Loss)	2,673,786	3,324,086	(1,280,770)
Net Income	2,744,957	2,638,034	(912,099)
Total Assets	29,831,253	28,290,404	21,969,160
Total Liabilities	20,647,038	20,987,771	17,261,771
Surplus As Regards Policyholders	9,184,215	7,302,633	4,707,389

## Dividends to Stockholders

The Company did not declare or pay dividends to its stockholders in 2003, 2004, and 2005.

## 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, 2005, were:

### Directors

<b>Name and Location</b>	<b>Principal Occupation</b>
Nicolas Estrella Key Biscayne, Florida	Owner, Star Casualty Insurance Co.
Josefina Estrella Miami, Florida	Teacher
Maria Remudo Miami, Florida	Manager of Agency Support, Star Casualty Insurance Co.
Richard Estrella Miami, Florida	VP of Estrella Insurance Agency
Lidia Hernandez Miami, Florida	Manager of Claims, Star Casualty Insurance Co.

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

### Senior Officers

<b>Name</b>	<b>Title</b>
Paul G. Gabe Jr.	President
Lidia Hernandez	Vice President
Donald Moser	Vice President
Richard Estrella	Secretary
Alejandro Zajac	Treasurer

The Company's board appointed several internal committees in accordance with Section 607.0825, Florida Statutes. The following were the principal internal board committees and their members as of December 31, 2005:

<b>Executive Committee</b>	<b>Audit Committee</b>	<b>Investment Committee</b>
Nicolas Estrella <sup>1</sup>	Maria Remudo <sup>1</sup>	Nicolas Estrella <sup>1</sup>
Josefina Estrella	Richard Estrella	Josefina Estrella
Maria Remudo	Lidia Hernandez	Maria Remudo
Richard Estrella		Richard Estrella
Lidia Hernandez		Lidia Hernandez
<sup>1</sup> Chairperson		

### **Conflict of Interest Procedure**

The Company adopted a policy statement requiring annual disclosure of conflicts of interest, in accordance with the NAIC Financial Condition Examiners Handbook. No exceptions were noted during this examination period.

### **Corporate Records**

The recorded minutes of the shareholder, Board of Directors, and certain internal committees 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.

The minutes confirmed that the prior examination report was reviewed by the Board of Directors.

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

The Company reported no acquisitions, mergers, disposals, dissolutions, purchases, or sales through reinsurance.

## **Surplus Debentures**

On June 26, 1988, the sole shareholder of the Company entered into a surplus note agreement with the Company in the amount of \$1,175,000 with a 12% annual interest rate, with the approval of the Office. On July 31, 2002, the sole shareholder of the Company executed another surplus note for \$1,000,000 with an annual interest rate of 7%, with the approval of the Office. Pursuant to the second note, no payment of principal or interest may be made without prior approval of the Office, which was in compliance with Section 628.401, Florida Statutes. During the year 2005, the Company paid the interest and principal to retire the first surplus note in the amount of \$1,207,063.

**Subsequent Event:** In 2006, the Company paid the interest and principal to retire the second surplus note in the amount of \$1,022,294. The Company had no remaining surplus notes outstanding.

## **AFFILIATED COMPANIES**

The latest holding company registration statement was filed with the State of Florida on December 31, 2006, as required by Section 628.801, Florida Statutes, and Rule 69O-143.046, Florida Administrative Code.

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

### **Cost Sharing Agreement**

The Company and its affiliates, Centrex Premium Finance Corp., Estrella Insurance Inc., Value Underwriters Inc., Penta Insurance Adjusters, Inc., and Estrella General Agency, Inc., had a cost sharing agreement in which each company agreed to pay a fair portion of their expenses in order to receive a fair allocation of their expenditures according to the agreement.

### **Claims Adjusting Agreement**

The Company and its affiliate, Penta Insurance Adjusters, Inc., had an agreement in which Penta Insurance Adjusters Inc. functioned as the Company's claims department, and provided full claims handling for all reported comprehensive general liability losses, property losses and automobile losses.

### **Managing General Agency Agreement**

The Company and its affiliate, Value Underwriters Inc., had a managing general agency agreement in which the Company retained Value Underwriters, Inc. to manage its insurance operations and availed itself of the experience, sources of information, advice, assistance, and

certain facilities of the manager. The manager undertook the duties and responsibilities set forth on behalf of, and subject to, the supervision of the Company and its Board of Directors.

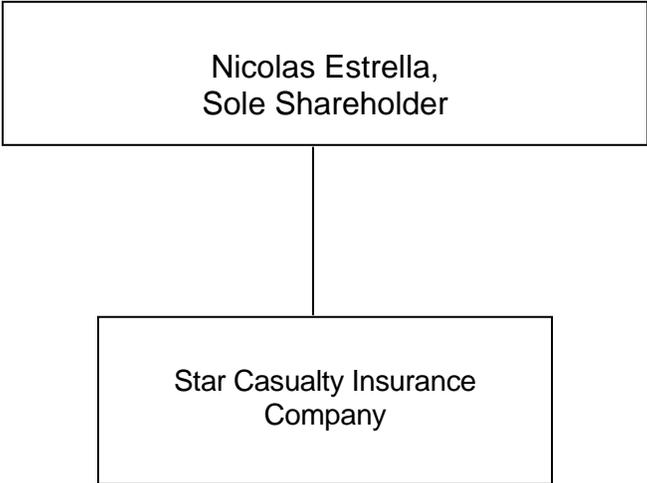
### **Producer's Agreement**

The Company and its affiliate, Estrella Insurance Agency, Inc., had a producer's agreement in which the Company gave the agent the authority to solicit, provide quotes, receive applications, bind coverage, and collect, receive, and receipt for premiums for insurance products specified in the Company's underwriting guidelines in the State of Florida.

A simplified organizational chart as of December 31, 2005 is shown below. Schedule Y of the Company's 2005 annual statement provided a list of all related companies.

**Star Casualty Insurance Company  
Organizational Chart**

**DECEMBER 31, 2005**



## **FIDELITY BOND AND OTHER INSURANCE**

The Company maintained fidelity bond coverage of \$250,000 with a deductible of \$10,000, which did not adequately cover the suggested minimum amount of coverage for the Company as recommended by the NAIC.

The Company maintained an insurance policy which covered the building and its contents.

**Subsequent Event:** The Company increased its fidelity bond coverage to \$300,000 which adequately covered the suggested minimum amount of coverage for the Company as recommended by the NAIC.

## **PENSION, STOCK OWNERSHIP AND INSURANCE PLANS**

The Company had a 401K Plan for employees. However, this plan was discontinued in December 2006 due to low participation by the employees. The provision was made by the Company in the annual statement for the Company's obligations under this plan.

## **STATUTORY DEPOSITS**

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

<b>STATE</b>	<b>DESCRIPTION</b>	<b>RATE</b>	<b>MATURITY DATE</b>	<b>PAR VALUE</b>	<b>MARKET VALUE</b>
FL	CD	3.15%	11/08/06	\$ 30,000	\$ 30,000
FL	CD	3.44%	12/30/06	100,000	100,000
FL	CD	3.25%	06/21/06	150,000	150,000
FL	USTN	2.50%	05/31/06	330,000	327,822
TOTAL FL DEPOSITS				\$ 610,000	\$ 607,822
TOTAL SPECIAL DEPOSITS				\$ 610,000	\$ 607,822

## **INSURANCE PRODUCTS AND RELATED PRACTICES**

### **Territory**

The Company was authorized to transact insurance in the State of Florida only, in accordance with Section 624.401, Florida Statutes. The Company's marketing efforts have been concentrated on marketing through independent agents. Until February 2005, the Company had been marketing exclusively through Estrella insurance agencies and its franchises. After that date, the Company expanded its marketing to include non-affiliated agencies throughout the State of Florida.

### **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 626.954(1)(i)3,a, Florida Statutes.

## **REINSURANCE**

The reinsurance contract was reviewed by the Company's appointed actuary and was utilized in determining the ultimate loss opinion.

The above mentioned contract 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 risk.

### **Ceded**

The Company ceded risk on a catastrophe excess of loss basis to Lloyd's of London through Guy Carpenter, the reinsurance intermediary.

## **ACCOUNTS AND RECORDS**

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

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

An independent CPA audited the Company's statutory basis financial statements annually for the years 2003, 2004 and 2005, 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 and non-affiliates had the following agreements:

### **Custodial Agreement**

The Company had a custodial agreement with Merrill Lynch dated January 17, 1995. There were also two addendums dated May 29, 1998 and November 26, 2003. The agreement was in accordance with Rule 69O-143.042, Florida Administrative Code.

### **Payroll Service Agreement**

The Company entered into a payroll service agreement with Paychex, Inc. on May 1, 2005. The agreement provided that Paychex, Inc. would perform all of the payroll functions of the Company.

### **Independent Auditor Agreement**

The Company had an agreement with Dixon Hughes PLLC, CPA, to perform an audit of its GAAP and Statutory financial statements for the years 2003, 2004, and 2005.

### **Independent Actuary Agreement**

The Company had an agreement with Butler, Dunlap, and Lundquist, for the purpose of providing independent actuarial analysis of the loss and loss expense reserve to be reported by the Company in its financial statements.

## **Risk-Based Capital**

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

## **Information Technology (IT) Report**

Tracy Gates of Highland Clark, LLC performed a computer systems evaluation on the Company.

## **FINANCIAL STATEMENTS PER EXAMINATION**

The following pages contain financial statements showing the Company's financial position as of December 31, 2005, 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."

**Star Casualty Insurance Company  
Assets**

**December 31, 2005**

	<b>Per Company</b>	<b>Examination Adjustments</b>	<b>Per Examination</b>
Bonds	\$ 3,014,366		\$ 3,014,366
Stocks:			
Common	209,367		209,367
Cash and Short-term Investments	19,405,535		19,405,535
Agents' Balances:			
Uncollected premium	410,795		410,795
Deferred premium	5,724,992		5,724,992
Net deferred tax asset	709,567		709,567
EDP Equipment	26,026		26,026
Interest and dividend income due & accrued	24,814		24,814
Receivable from parents, subsidiaries and affiliates	305,791		305,791
Totals	\$ 29,831,253	\$ -	\$ 29,831,253

**Star Casualty Insurance Company  
Liabilities, Surplus and Other Funds**

**December 31, 2005**

<b>Liabilities</b>	<b>Per Company</b>	<b>Examination Adjustments</b>	<b>Per Examination</b>
Losses	\$8,045,945		\$8,045,945
Loss adjustment expenses	3,143,457		3,143,457
Commissions payable	567,472		567,472
Other expenses	284,459		284,459
Taxes, licenses and fees	88,250		88,250
Current federal and foreign income taxes	326,000		326,000
Unearned premium	7,026,920		7,026,920
Drafts outstanding	943,182		943,182
Payable to parent, subsidiaries and affiliates	<u>221,353</u>		<u>221,353</u>
Total Liabilities	\$20,647,038		\$20,647,038
Common capital stock	\$750,000		\$750,000
Surplus note	1,000,000		1,000,000
Gross paid in and contributed surplus	1,662,325		1,662,325
Unassigned funds (surplus)	<u>5,771,890</u>		<u>5,771,890</u>
Surplus as regards policyholders	<u>\$9,184,215</u>		<u>\$9,184,215</u>
Total liabilities, surplus and other funds	<u>\$29,831,253</u>	<u>\$0</u>	<u>\$29,831,253</u>

**Star Casualty Insurance Company  
Statement of Income**

**December 31, 2005**

	<b>Underwriting Income</b>	
Premiums earned		\$19,290,081
DEDUCTIONS:		
Losses incurred		7,771,365
Loss expenses incurred		3,385,108
Other underwriting expenses incurred		5,459,822
Aggregate write-ins for underwriting deductions		0
Total underwriting deductions		<u>\$16,616,295</u>
Net underwriting gain or (loss)		\$2,673,786
	<b>Investment Income</b>	
Net investment income earned		\$260,450
Net realized capital gains or (losses)		<u>(2,745)</u>
Net investment gain or (loss)		\$257,705
	<b>Other Income</b>	
Net gain or (loss) from agents' or premium balances charged off		\$0
Finance and service charges not included in premiums		1,058,882
Aggregate write-ins for miscellaneous income		<u>6,868</u>
Total other income		\$1,065,750
Net income before dividends to policyholders and before federal & foreign income taxes		\$3,997,241
Dividends to policyholders		<u>0</u>
Net Income, after dividends to policyholders, but before federal & foreign income taxes		\$3,997,241
Federal & foreign income taxes		<u>1,252,284</u>
Net Income		\$2,744,957
	<b>Capital and Surplus Account</b>	
Surplus as regards policyholders, December 31 prior year		\$7,302,633
	<b>Gains and (Losses) in Surplus</b>	
Net Income		\$2,744,957
Net unrealized capital gains or losses		(4,993)
Change in Net Deferred income Tax		(53,555)
Change in non-admitted assets		370,173
Change in provision for reinsurance		0
Change in Surplus Notes		(1,175,000)
Examination Adjustment		<u>0</u>
Change in surplus as regards policyholders for the year		\$1,881,582
Surplus as regards policyholders, December 31 current year		<u><u>\$9,184,215</u></u>

## COMMENTS ON FINANCIAL STATEMENTS

### Liabilities

**Losses and Loss Adjustment Expenses** \$11,189,402

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, 2005, 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.

### CAPITAL AND SURPLUS

The Company met the surplus requirement for capital and surplus.

A comparative analysis of changes in surplus is shown below.

**Star Casualty Insurance Company  
Comparative Analysis of Changes in Surplus**

**December 31, 2005**

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, 2005, Annual Statement	\$	9,184,215
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	<u>PER COMPANY</u>	<u>PER EXAM</u>	<u>INCREASE (DECREASE) IN SURPLUS</u>
ASSETS:			
No adjustments			
LIABILITIES:			
No adjustments			
Net Change in Surplus:			0
Surplus as Regards Policyholders December 31, 2005, Per Examination			\$ 9,184,215

## **SUMMARY OF FINDINGS**

### **Compliance with previous directives**

The Company has taken the necessary actions to comply with the comments made in the 2002 examination report issued by the Office.

### **Current examination comments and corrective action**

This examination found no material findings as of December 31, 2005.

## CONCLUSION

The customary insurance examination practices and procedures as promulgated by the NAIC have been followed in ascertaining the financial condition of **Star Casualty Insurance Company** as of December 31, 2005, consistent with the insurance laws of the State of Florida.

Per examination findings, the Company's Surplus as regards policyholders was \$9,184,215, which was in compliance with Section 624.408, Florida Statutes.

In addition to the undersigned, Michael Hampton, CPA, CFE, DABFA, CFE, CPM, Financial Examiner/Analyst Supervisor, Stephen Feliu, Financial Examiner/Analyst II, and Joe Boor, FCAS, Office Actuary, participated in the examination. We also recognize the participation of Mr. Tracy Gates, CPA, CISA of Highland Clark, LLC with the examination.

Respectfully submitted,

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Maurice Fuller  
Financial Examiner/Analyst II  
Florida Office of Insurance Regulation