

REPORT ON EXAMINATION
OF
AMERITRUST INSURANCE
CORPORATION
SARASOTA, FLORIDA

AS OF
DECEMBER 31, 2002

BY THE
OFFICE OF INSURANCE REGULATION

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Tallahassee, Florida
December 5, 2003

Kevin M. McCarty
Director
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 (FS), 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, 2002, of the financial condition and corporate affairs of:

**AMERITRUST INSURANCE CORPORATION
7250 S. BENEVA ROAD
SARASOTA, FLORIDA 34238**

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, 2000 through December 31, 2002. The Company was last examined by representatives of the Florida Office of Insurance Regulation (Office) as of December 31, 1999. This examination commenced, with planning at the Office, on September 2, 2003, to September 5, 2003. The fieldwork commenced on September 8, 2003, and was concluded as of December 5, 2003. 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 Examiners Handbook, Accounting Practices and Procedures Manual and annual statement instructions promulgated by the NAIC as adopted by Rules 4-137.001(4) and 4-138.001, Florida Administrative Code (FAC), 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 A.M. Best Report, 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/or verified the amounts of the Company's assets and liabilities as reported by the Company in its annual statement as of December 31, 2002. Transactions subsequent to year-end 2002 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.

Based on the review of the Company's control environment and the materiality level set for this examination, reliance was placed on work performed by the Company's CPAs after verifying the statutory requirements for the following accounts:

Federal Income Taxes Recoverable
Federal Income Taxes Payable

Status of Adverse Findings from Prior Examination

The following is a summary of significant adverse findings contained in the Office's prior examination report as of December 31, 1999, along with resulting action taken by the Company in connection therewith.

Affiliated Companies

The Company entered into a Management Services/Managing General Agency Agreement with its affiliate, Florida Preferred Administrators, Inc. The agreement did not reflect the correct name of its agent, Florida Preferred Administrators, Inc. **Resolution:** The Company amended its agreement effective July 1, 2001 to reflect the name change of the MGA.

Custodial Agreement

The Company utilized the services of SouthTrust Bank, N.A. and Comerica Bank for the safekeeping of its securities. However, the terms of the agreements were not in accordance with Rule 4-143.042, FAC. **Resolution:** The custodial agreement with SouthTrust Bank, N.A. effective July 24, 2001, contained the proper safeguards and controls indemnifying the Company. The Company no longer uses Comerica Bank as its custodian.

HISTORY

General

The Company was incorporated in Florida on April 18, 1996 and commenced business on June 1, 1996 as Ameritrust Insurance Corporation.

In accordance with Section 624.401(1), FS, the Company was authorized to transact worker's compensation insurance coverage in Florida on December 31, 2002:

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

Capital Stock

As of December 31, 2002, the Company's capitalization was as follows:

Number of authorized common capital shares	100
Number of shares issued and outstanding	100
Total common capital stock	\$100
Par value per share	\$1.00

Control of the Company was maintained by its parent, Star Insurance Company (Star), a Michigan domiciled Insurer, who owned 100 percent of the stock issued by the Company, and, in turn, was 100 percent owned by Meadowbrook Insurance Group, Inc, a Michigan corporation.

Profitability of Company

With earned premiums of \$16,189,588 and \$8,556,568 for 2002 and 2001 respectively, the Company reported a net underwriting loss of (\$979,593) and an after tax loss of (\$400,736) in 2002. In 2001, the Company reported a net underwriting gain of \$1,246,138 and after tax income of \$1,792,699. The Company indicated that the increase in earned premiums was due primarily to the cancellation of a worker's compensation quota share agreement in December 2001. The Company further indicated that after excluding the reinsurance transaction, earned premiums would have decreased \$4.9 million in 2002 as a result of a decline in written premium of both new and renewal business.

Dividends to Stockholders

In accordance with Section 628.371, FS, the Company declared and paid dividends to its stockholder in 2000, 2001 and 2002 in the amounts of \$493,000, \$5,000,000 and \$1,750,000, respectively.

Management

The annual shareholder meeting for the election of directors was held in accordance with Sections 607.1601 and 628.231, FS. The directors serving as of December 31, 2002, were:

Directors

Name and Location	Principal Occupation
Henry J. Abbott Sarasota, Florida	Sr. Vice President Ameritrust Insurance Corporation
Kenn R. Allen Southfield, Michigan	Sr. Vice President Meadowbrook Insurance Group
Robert S. Cubbin Southfield, Michigan	Chairman Meadowbrook Insurance Group
Joseph C. Henry Southfield, Michigan	CEO Meadowbrook Insurance Group
Karen M. Spaun Southfield, Michigan	Vice President, Treasurer Meadowbrook Insurance Group

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

Senior Officers

Name	Title
Gregory L. Wilde	President
Joseph C. Henry	Chief Executive Officer
Michael G. Costello	Sr. Vice President, General Counsel & Secretary
Karen M. Spaun	Vice President & Treasurer
Henry J. Abbott	Vice President

The Company's ultimate parent, Meadowbrook Insurance Group, Inc. appointed several internal committees as follows: The board of the Company reviews and approves the investment transactions of the Company.

Audit Committee

Bruce E. Thal¹
Robert H. Naftaly
Ralph Milo

¹ Chairman

Finance Committee

David K. Page¹
Joseph S. Dresner
Hugh W. Greenberg
Ralph Milo
Robert H. Naftaly
Bruce E. Thal
Robert W. Sturgis
Merton J. Segal
Robert S. Cubbin

Investment Committee

Joseph S. Dresner¹
David K. Page
Merton J. Segal
Bruce E. Thal

Conflict of Interest Procedure

The Company had adopted a policy statement requiring annual disclosure of conflicts of interest, in accordance with Section 607.0832, FS. No exceptions were noted during this examination period.

Corporate Records

The recorded minutes of the shareholder and Board of Directors meetings 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, FS, including the authorization of investments as required by Section 625.304, FS.

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

There were no acquisitions, mergers, disposals, dissolutions or purchase or sales through reinsurance during the period covered by this examination.

Surplus Debentures

As of December 31, 2002, there were no outstanding surplus debentures of the Company.

AFFILIATED COMPANIES

The Company was a member of an insurance holding company system as defined by Rule 4-143.045(3), FAC. The latest holding company registration statement was filed with the State of Florida on April 26, 2002, as required by Section 628.801, FS, and Rule 4-143.046, FAC.

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

Tax Allocation Agreement

The Company, along with its parent and other affiliated companies filed a consolidated federal income tax return. On December 31, 2002, the method of allocation between the Company and its parent was based on separate tax liability as if the Company had filed a separate tax return.

Management Agreement

The Company maintained a management services agreement with its ultimate parent Meadowbrook Insurance Group Inc. (MIG) on October 17, 2001. MIG provided management services which included but was not limited to: accounting, accounts receivable, accounts payable, reports and records underwriting, investment, claims and reinsurance. Management fees paid to MIG in 2002 totaled \$1,000,000.

MGA Agreement

The Company entered into a Management Services/Managing General Agency Agreement with its affiliate, Florida Preferred Administrators, Inc. (FPA) effective May 1, 1996. The agreement provided that FPA would receive, investigate, reject, adjust, compromise, settle or pay, on behalf of the Company, all claims and any losses and expenses, as well as provide other services as shall be reasonably required. Fees paid to FPA were \$5,212,821, \$4,494,953 and \$2,956,000 in 2000, 2001 and 2002 respectively.

FPA operated as the managing general agent for the Company; however, the agreement did not specify the appropriate underwriting guidelines as provided by Section 626.7451 (6), FS.

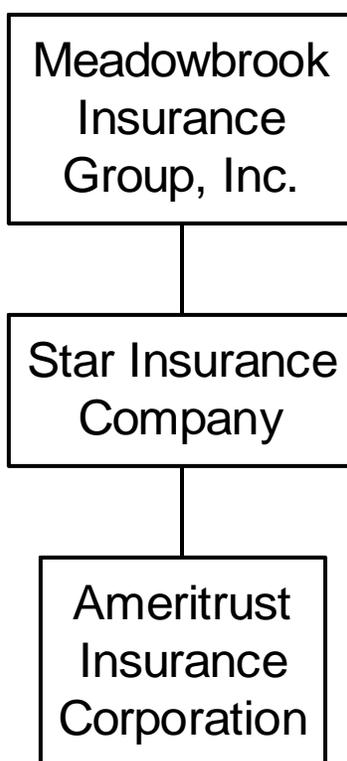
The Company failed to disclose in Note 19 of the 2002 annual statement the aggregate amount of direct premiums written through/produced by the managing general agent as required by NAIC Annual Statement Instructions.

Reinsurance Agreement

The Company entered into a stop loss reinsurance agreement with its parent, Star, effective January 1, 2000. The agreement provided that the reinsurer would pay the Company 100% of the amount of incurred losses that exceeded 60% of the net earned premium of the Company. The Company ceded premiums to Star of \$3,265,061 in 2000, \$1,574,885 in 2001, and \$2,733,015 in 2002.

A simplified organizational chart as of December 31, 2002, reflecting the holding company system, is shown below. Schedule Y of the Company's 2002 annual statement provided a list of all related companies of the holding company group.

**AMERITRUST INSURANCE CORPORATION
ORGANIZATIONAL CHART
DECEMBER 31, 2002**



FIDELITY BOND AND OTHER INSURANCE

The Company and its affiliates maintained fidelity bond coverage up to \$500,000 with a deductible of \$5,000, which adequately covered the suggested minimum amount of coverage as recommended by the NAIC.

PENSION, STOCK OWNERSHIP, AND INSURANCE PLANS

The Company had no employees.

STATUTORY DEPOSITS

The following securities were deposited with the State of Florida as required by Section 624.411, FS, and with various state officials as required or permitted by law:

State	Description	Par Value	Market Value
FL	CD 23482755, 3.92%, 02/29/04	\$ 75,000	\$ 75,000
FL	CD 23482756, 3.92%, 02/29/04	75,000	75,000
FL	CD 23482757, 3.92%, 02/29/04	75,000	75,000
FL	CD, 23482758 3.92%, 02/29/04	<u>75,000</u>	<u>75,000</u>
TOTAL FLORIDA DEPOSITS		\$ 300,000	\$ 300,000
MI	USTNTS, 6.00%, 08/15/09	<u>350,000</u>	<u>406,984</u>
TOTAL OTHER DEPOSITS		\$ 350,000	\$ 406,984
Total Special Deposits		<u>\$ 650,000</u>	<u>\$ 706,984</u>

INSURANCE PRODUCTS AND RELATED PRACTICES

Reliance was placed on the latest market conduct examination, filed January 17, 2002, by the Office to determine the accuracy of premium computation, policy construction, claims handling procedures and use of filed rates and forms. The exceptions noted in the issued report did not affect the solvency of the Company.

Territory and Plan of Operation

The Company was authorized to transact insurance in Florida and Michigan, in accordance with Section 624.401(2), FS. However, the company did not write any insurance business in the State of Michigan during the period covered by this examination.

Treatment of Policyholders

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

REINSURANCE

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

Several of the Company's reinsurance agreements did not specify that reports of premiums and losses be provided no less frequently than on a quarterly basis as required by the NAIC Accounting

Practices and Procedures Manual. Additionally, a few treaties failed to specify that the agreement should constitute the entire contract between the parties.

Assumed

The Company did not assume any insurance business during this examination period.

Ceded

The Company ceded risk on an excess of loss basis to authorized and unauthorized reinsurers. The primary reinsurers were Star, a Michigan domiciled authorized affiliate insurer, and Employers Reinsurance Corporation, an authorized non-affiliated insurer.

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 2000, 2001 and 2002, in accordance with Section 624.424(8), FS. Supporting work papers were prepared by the CPA as required by Rule 4-137.002, FAC.

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 Sarasota, Florida, where this examination was conducted.

The Company and non-affiliates had the following agreements:

Custodial Agreement

The Company utilized the services of SouthTrust Bank. The safekeeping agreement between the Company and SouthTrust Bank contained the appropriate safeguards and controls indemnifying the Company as provided by Rule 4-143.042, FAC.

Independent Auditor Agreement

The Company engaged Thomas Howell Ferguson, P.A. for the purpose of annually auditing and reporting on the statutory basis financial statements at year-end.

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, 2002, 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."

AMERITRUST INSURANCE CORPORATION
Assets

DECEMBER 31, 2002

Classification	Per Company	Examination Adjustments	Per Examination
Bonds	\$24,530,654		\$24,530,654
Cash:			
On deposit	(389,611)		(389,611)
Short-term investments	2,698,086		2,698,086
Agents' Balances:			
Uncollected premium	492,535		492,535
Deferred premium	5,418,822		5,418,822
Accrued retrospective	387,493		387,493
Bills receivable	161,945		161,945
Reinsurance recoverable	776,653		776,653
FIT recoverable	867,838		867,838
Interest and dividend income due & accrued	315,490		315,490
Receivable from PSA	1,375		1,375
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Totals	\$35,261,280	\$0	\$35,261,280
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AMERITRUST INSURANCE CORPORATION
Liabilities, Surplus and Other Funds

DECEMBER 31, 2002

Liabilities	Per Company	Examination Adjustments	Per Examination
Losses	\$10,072,376		\$10,072,376
Loss adjustment expenses	2,806,237		2,806,237
Commissions payable	642,705		642,705
Other expenses	98,198		98,198
Taxes, licenses and fees	720,712		720,712
FIT payable	461,203		461,203
Unearned premium	6,826,754		6,826,754
Advance premiums	527,148		527,148
Ceded reinsurance premiums payable	923,910		923,910
Provision for reinsurance	15,906		15,906
Payable to parent, subsidiaries and affiliates	171,860		171,860
Aggregate write-ins for liabilities	<u>1,346,410</u>		<u>1,346,410</u>
Total Liabilities	\$24,613,419		\$24,613,419
Common capital stock	\$100		100
Gross paid in and contributed surplus	7,999,900		7,999,900
Unassigned funds (surplus)	<u>2,647,861</u>		<u>2,647,861</u>
Surplus as regards policyholders	<u>\$10,647,861</u>		<u>\$10,647,861</u>
Total liabilities, capital and surplus	<u>\$35,261,280</u>	<u>\$0</u>	<u>\$35,261,280</u>

AMERITRUST INSURANCE CORPORATION
Statement of Income
DECEMBER 31, 2002

Underwriting Income

Premiums earned	\$16,189,588
DEDUCTIONS:	
Losses incurred	7,408,011
Loss expenses incurred	2,570,999
Other underwriting expenses incurred	7,190,171
Aggregate write-ins for underwriting deductions	0
Total underwriting deductions	<u>\$17,169,181</u>
Net underwriting gain or (loss)	(\$979,593)

Investment Income

Net investment income earned	\$1,418,489
Net realized capital gains or (losses)	(30,426)
Net investment gain or (loss)	<u>\$1,388,063</u>

Other Income

Net gain or (loss) from agents' or premium balances charged off	(\$35,449)
Finance and service charges not included in premiums	0
Aggregate write-ins for miscellaneous income	15,758
Total other income	<u>(\$19,691)</u>
Net income before dividends to policyholders and before federal & foreign income taxes	\$388,779
Dividends to policyholders	<u>284,251</u>
Net Income, after dividends to policyholders, but before federal & foreign income taxes	\$104,528
Federal & foreign income taxes	<u>505,264</u>
Net Income	(\$400,736)

Capital and Surplus Account

Surplus as regards policyholders, December 31 prior year	\$12,652,837
Gains and (Losses) in Surplus	
Net Income	(\$400,736)
Net unrealized capital gains or losses	0
Change in net deferred income tax	513,098
Change in non-admitted assets	(351,432)
Change in provision for reinsurance	(15,906)
Surplus adjustments: Paid in	0
Dividends to stockholders	(1,750,000)
Aggregate write-ins for gains and losses in surplus	0
Examination Adjustment	0
Change in surplus as regards policyholders for the year	<u>(\$2,004,976)</u>
Surplus as regards policyholders, December 31 current year	<u><u>\$10,647,861</u></u>

COMMENTS ON FINANCIAL STATEMENTS

Assets

Bills Receivable \$161,945

The Company recorded \$161,945 in promissory notes received from policyholders for delinquent and/or past due audit premiums. Although the promissory notes were current and not in default, they were for policies no longer in force, and therefore should have been non-admitted in accordance with Section 625.012 (7), FS, and SSAP 6, which provides that bills receivable for premiums may be admitted to the extent of unearned premium reserves, carried on those policies. Since the amount was below the materiality level of this examination, no financial adjustment was made.

Liabilities

Losses and Loss Adjustment Expenses \$12,878,613

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, 2002, 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.

AMERITRUST INSURANCE CORPORATION
Comparative Analysis of Changes in Surplus

DECEMBER 31, 2002

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, 2002, Annual Statement	\$10,647,861
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	<u>PER</u> <u>COMPANY</u>	<u>PER</u> <u>EXAM</u>	INCREASE (DECREASE) <u>IN SURPLUS</u>
ASSETS:			
LIABILITIES:			
Net Change in Surplus:			0
Surplus as Regards Policyholders December 31, 2002, Per Examination			\$10,647,861

SUMMARY OF FINDINGS

Compliance with previous directives

The Company has taken the necessary actions to comply with the comments made in the 1999 examination report issued by the Office.

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, 2002.

MGA Agreement

The Company's MGA agreement failed to specify appropriate underwriting guidelines as required by Section 626.7451 (6), FS. **The Company is directed to comply with Section 626.7451 (6), FS, and include appropriate underwriting guidelines in the MGA agreement. The Company is to provide documentation of compliance to the Office within 90 days after the report is issued.**

The Company did not properly disclose the aggregate amount of direct premiums written through/produced by the managing general agent as required by NAIC Annual Statement Instructions. **The Company is directed to prepare all future statutory financial statements in accordance with the NAIC Annual Statement Instructions.**

Reinsurance

The Company's reinsurance agreement did not specify that reports of premiums and losses be provided no less frequently than on a quarterly basis nor did the treaty specify that the agreement

should constitute the entire contract between the parties. **The Company is directed to negotiate all future reinsurance treaties such that they contain the required terms in accordance with the NAIC Accounting Practices and Procedures Manual.**

Bills Receivable

The Company inadvertently admitted assets specifically identified in the NAIC Accounting Practices and Procedures Manual as non-admitted. **The Company is directed to correctly report such account balances on all future annual and quarterly statement filings.**

SUBSEQUENT EVENTS

Directors

Joseph Christopher Henry resigned from the board of directors on March 31, 2003, and had not been replaced as of the conclusion of this examination's field work.

Financial Statement Disclosure

The amount of direct premiums written through the MGA was correctly reported on the Company's quarterly statement as of September 30, 2003.

Gross Paid in and Contributed Surplus

The Company received a \$3 Million capital contribution from its parent, Star on September 30, 2003.

CONCLUSION

The customary insurance examination practices and procedures as promulgated by the NAIC have been followed in ascertaining the financial condition of **Ameritrust Insurance Corporation** as of December 31, 2002, consistent with the insurance laws of the State of Florida.

Per examination findings, the Company's surplus as regards policyholders was \$10,647,861, which was in compliance with Section 624.408, FS.

In addition to the undersigned, Xi Luo, Financial Examiner/Analyst I, John C. Berry, Financial Examiner/Analyst Supervisor, and Doug Haseltine, Actuary, participated in the examination.

Respectfully submitted,

Kethessa Carpenter
Financial Specialist
Florida Office of Insurance Regulation