

REPORT ON EXAMINATION
OF
SOUTHERN FIDELITY PROPERTY &
CASUALTY, INC.
TALLAHASSEE, FLORIDA

AS OF
DECEMBER 31, 2013

BY THE
FLORIDA OFFICE OF INSURANCE REGULATION

TABLE OF CONTENTS

LETTER OF TRANSMITTAL	-
SCOPE OF EXAMINATION	1
SUMMARY OF SIGNIFICANT FINDINGS	2
CURRENT EXAM FINDINGS	2
PRIOR EXAM FINDINGS	2
SUBSEQUENT EVENTS	2
HISTORY	3
GENERAL	3
DIVIDENDS TO STOCKHOLDERS.....	4
CAPITAL STOCK AND CAPITAL CONTRIBUTIONS.....	4
SURPLUS NOTES	4
ACQUISITIONS, MERGERS, DISPOSALS, DISSOLUTIONS, AND PURCHASE OR SALES THROUGH REINSURANCE	4
CORPORATE RECORDS	5
CONFLICT OF INTEREST.....	5
MANAGEMENT AND CONTROL	5
MANAGEMENT	5
AFFILIATED COMPANIES	7
ORGANIZATIONAL CHART	7
TAX ALLOCATION AGREEMENT.....	8
MANAGING GENERAL AGENT AGREEMENT	8
MANAGEMENT AGREEMENT	8
POLICY MANAGEMENT SERVICES AGREEMENT	9
FIDELITY BOND AND OTHER INSURANCE	9
PENSION, STOCK OWNERSHIP AND INSURANCE PLANS	9
TERRITORY AND PLAN OF OPERATIONS	10
TREATMENT OF POLICYHOLDERS	10
COMPANY GROWTH	10
PROFITABILITY OF COMPANY	11
LOSS EXPERIENCE	11
REINSURANCE	11
ASSUMED	11
CEDED	12
ACCOUNTS AND RECORDS	13
CUSTODIAL AGREEMENT.....	13
INDEPENDENT AUDITOR AGREEMENT	14
INFORMATION TECHNOLOGY REPORT	14
STATUTORY DEPOSITS	14

FINANCIAL STATEMENTS PER EXAMINATION.....	15
ASSETS.....	16
LIABILITIES, SURPLUS AND OTHER FUNDS.....	17
STATEMENT OF INCOME.....	18
COMPARATIVE ANALYSIS OF CHANGES IN SURPLUS.....	19
COMMENTS ON FINANCIAL STATEMENTS.....	20
LIABILITIES.....	20
CAPITAL AND SURPLUS.....	20
CONCLUSION.....	21

November 7, 2014

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, 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, 2013, of the financial condition and corporate affairs of:

**SOUTHERN FIDELITY PROPERTY & CASUALTY, INC.
2255 KILLEARN CENTER BLVD
TALLAHASSEE, FLORIDA 32309**

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, 2013, through December 31, 2013, and was conducted simultaneously with examinations for Capitol Preferred Insurance Company, Inc. and Southern Fidelity Insurance Company, Inc., which are affiliated through common management pursuant to Section 624.10(1)(b), Florida Statutes. The Company was last examined by representatives of the Florida Office of Insurance Regulation (Office) as of December 31, 2012. This examination commenced with planning at the Office on July 21, 2014, to July 25, 2014. The fieldwork commenced on July 28, 2014, and concluded as of November 07, 2014.

This financial examination was a multi-state 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.

The NAIC Financial Condition Examiners Handbook requires that the examination be planned and performed to evaluate the financial condition and identify prospective risks of the Company by obtaining information about the Company including corporate governance, identifying and assessing inherent risks within the Company, and evaluating system controls and procedures used to mitigate those risks. An examination also includes assessing the principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation and management's compliance with Statutory Accounting Principles and annual statement instructions when applicable to domestic state regulations.

All accounts and activities of the Company were considered in accordance with the risk-focused examination process.

This report of examination is confined to significant adverse findings, a material change in the financial statements or other information of regulatory significance or requiring regulatory action. The report comments on matters that involved departures from laws, regulations or rules, or which were deemed to require special explanation or description.

SUMMARY OF SIGNIFICANT FINDINGS

Current Exam Findings

There were no material findings or exceptions noted during the examination as of December 31, 2013.

Prior Exam Findings

There were no material findings or exceptions noted during the examination as of December 31, 2012.

SUBSEQUENT EVENTS

The Company was approved (in accordance with consent order 144860-13-CO) to take out up to 10,000 policies during the February 2014 Citizens Property Insurance Corporation (Citizens) take-out. In November 2014, the Company participated in an assumption of Citizens policies. The Company was approved for up to a total of 30,000 assumed policies for the November take-out under Consent Order 159622-14-CO.

HISTORY

General

The Company was incorporated in Florida on January 6, 2012, and commenced business on January 12, 2012, as Southern Fidelity Property & Casualty, Inc.

The Company was party to Consent Order 122861-12-CO filed January 6, 2012, regarding the application for the issuance of a Certificate of Authority.

The Company was also party to the following Consent Orders requesting the assumption of selected policies from Citizens.

<u>Consent Order Number</u>	<u>Filing Date</u>	<u>Number of Policies Approved</u>
122964-12-CO	1/18/2012	60,000
124213-12-CO	3/21/2012	20,000
128413-12-CO	9/6/2012	30,000
140064-13-CO	8/23/2013	30,000

The Company was authorized to transact the following insurance coverage in Florida on January 12, 2012 and continued to be authorized as of December 31, 2013:

Homeowners multi peril	Other liability
Fire	Inland marine
Allied lines	

The Company had not written insurance coverage in the previous two years in the lines of business of allied lines, other liability and inland marine. **Subsequent Event:** Effective October 2, 2014, the Company's request to have allied lines, other liability and inland marine removed from its Certificate of Authority (COA) was approved by the Office.

The Articles of Incorporation and the Bylaws were not amended during the period covered by this examination.

Dividends to Stockholders

The Company did not declare or pay any dividends during the period of this examination.

Capital Stock and Capital Contributions

As of December 31, 2013, the Company's capitalization was as follows:

Number of authorized common capital shares	30,000
Number of shares issued and outstanding	20,000
Total common capital stock	\$ 2,000,000
Par value per share	\$ 100

Control of the Company was maintained by its parent, SFPC Holding Company, LLC (Parent), who owned 100% of the stock issued by the Company. The Parent contributed \$18,000,000 in cash to the Company as of December 31, 2013.

Surplus Notes

The Company did not have any surplus notes during the period of this examination.

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

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

CORPORATE RECORDS

The recorded minutes of the Shareholder, Board of Directors (Board) and certain internal committees were reviewed for the period under examination. The recorded minutes of the Board adequately documented its meetings and approval of Company transactions and events, in compliance with the NAIC Financial Condition Examiners Handbook adopted by Rule 69O-138.001, Florida Administrative Code, including the authorization of investments as required by Section 625.304, Florida Statutes.

Conflict of Interest

The Company adopted a policy statement requiring periodic disclosure of conflicts of interest in accordance with the NAIC Financial Condition Examiners Handbook adopted by Rule 69O-138.001, Florida Administrative Code.

MANAGEMENT AND CONTROL

Management

The annual shareholder meeting for the election of directors was held in accordance with Section 628.231, Florida Statutes. Directors serving as of December 31, 2013, were:

Directors

Name and Location

Principal Occupation

James Anthony Graganella
Tallahassee, Florida

President and Chief Executive officer,
Southern Fidelity Property & Casualty, Inc.

Byron Hamelin Wells
Tallahassee, Florida

Vice President, Southern Fidelity Property &
Casualty, Inc.

Keith Edward Martin Tallahassee, Florida	Vice President and Chief Financial Officer, Southern Fidelity Property & Casualty, Inc.
Kristie Beavers Mock Tallahassee, Florida	Secretary, Southern Fidelity Property & Casualty, Inc.
Charles William Whittaker Bainbridge, Georgia	Partner, Dowdy & Whittaker CPA's
Ralph Powell, Jr. Brinson, Georgia	Insurance Executive, Tim Smith & Associates and Financial Services
Timothy Lee Smith Bainbridge, Georgia	Partner, Tim Smith & Associates and Financial Services
John Adams Dowdy, Jr. Bainbridge, Georgia	Partner, Dowdy & Whittaker CPA's

In accordance with the Company's bylaws, the Board appointed the following senior officers:

Senior Officers

Name	Title
James Antony Graganella	President and Chief Executive Officer
Byron Hamelin Wells	Vice President
Keith Edward Martin	Vice President and Treasurer
Kristie Beavers Mock	Secretary

The Company's Board appointed an internal committee. Following was the principal internal Board committee and its members as of December 31, 2013:

Audit Committee

John Adams Dowdy, Jr. ¹
 Timothy Lee Smith
 Charles William Whittaker

¹ Chairman

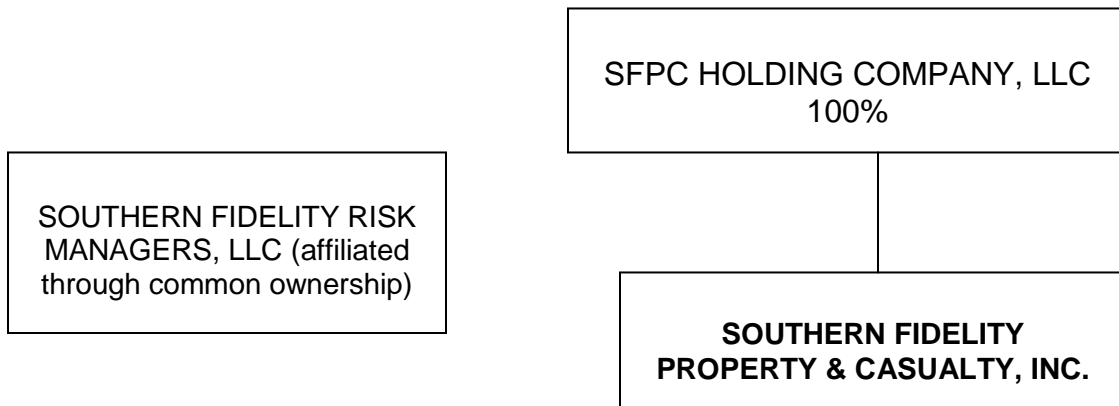
Affiliated Companies

The most recent holding company registration statement was filed with the State of Florida on February 27, 2014, as required by Section 628.801, Florida Statutes.

An organizational chart as of December 31, 2013, reflecting the holding company system, is shown below. Schedule Y of the Company's 2013 annual statement provided a list of all related companies of the holding company group.

SOUTHERN FIDELITY PROPERTY & CASUALTY, INC. ORGANIZATIONAL CHART

DECEMBER 31, 2013



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

Tax Allocation Agreement

The Company, along with its parent, filed a consolidated federal income tax return. On December 31, 2013, the method of allocation between the Company and its parent was based on separate return calculations with current credit for net losses.

Managing General Agent Agreement

The Company entered into a Managing General Agency Agreement with Southern Fidelity Risk Managers, LLC (Agency) on January 6, 2012. The Agency was affiliated by common ownership and common management. The Agency provided claims and policy administration services on behalf of the Company. The Agency received for its services an MGA policy fee of \$25 per policy written by the Company and a commission of 31% of the earned direct premium of the Company. An addendum executed on February 27, 2013, retroactively adjusted the commission percentage from 31% to 27.5% for the calendar year commencing January 1, 2012. The agreement continues in force for a term of three years and will automatically renew for successive three-year periods, unless otherwise terminated within the guidelines of the agreement. Fees incurred under this agreement during 2013 amounted to \$27,815,230.

Management Agreement

The Company entered into a management agreement upon licensure on January 12, 2012, with Preferred Managing Agency, Inc. (Preferred), a party related by common management, along with Agency, whereby Preferred provided assistance in the information and development of policies and

procedures of the Company. The Company did not incur fees directly under these agreements; fees were incurred by the Agency.

Policy Management Services Agreement

The Company entered into a policy management services agreement upon licensure on January 12, 2012, with Preferred, a party related by common management, along with Agency, whereby Preferred provided various policy administration services, including premium billing and collection. The Company did not incur fees directly under these agreements; fees were incurred by the Agency.

FIDELITY BOND AND OTHER INSURANCE

The Company maintained fidelity bond coverage up to \$3,000,000 with a deductible of \$25,000, which reached the suggested minimum as recommended by the NAIC.

The Company also maintained management liability insurance and professional liability insurance with coverage with limits of \$2,000,000 and deductibles ranging from \$0 to \$250,000, as well as commercial umbrella liability coverages.

PENSION, STOCK OWNERSHIP AND INSURANCE PLANS

There were not any pension, stock ownership or insurance plans in place at the Company during the period of this examination.

TERRITORY AND PLAN OF OPERATIONS

The Company was authorized to transact insurance only in 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 626.9541(1) (i) 3a, Florida Statutes.

COMPANY GROWTH

Calendar year 2013 was the Company's second year of operations. All premium revenues came from the assumptions of policies from Citizens in 2012 and 2013. Net underwriting gain decreased in 2013, but net income increased due to increased net investment gains. Surplus grew approximately 8.6% over the examination period.

Profitability of Company

The following table shows the profitability trend (in dollars) of the Company for the period of operations, as reported in the filed annual statements.

	2012	2013
Premiums Earned	34,357,871	54,846,551
Net Underwriting Gain/(Loss)	3,373,897	1,857,834
Net Income	278,747	1,707,743
Total Assets	78,819,964	89,645,769
Total Liabilities	56,324,944	65,227,367
Surplus As Regards Policyholders	22,495,020	24,418,402

LOSS EXPERIENCE

The year ending December 31, 2013 was the Company's second year of operations. The one-year net loss development at the end of the current examination period was favorable at \$552 thousand.

REINSURANCE

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

Assumed

The Company assumed policies during 2013 under a policy assumption agreement with Citizens.

Ceded

As of December 31, 2013, the Company's ceded reinsurance program consisted of catastrophe and per risk excess of loss reinsurance provided by agreements with various commercial reinsurers through reinsurance intermediaries Towers Watson and Aon Benfield. The Company also participated in the Florida Hurricane Catastrophe Fund (FHCF).

The Company's per risk excess reinsurance agreement provided coverage of \$1,500,000 in excess of \$500,000 on each loss, subject to a per loss occurrence limit of \$1,500,000.

The Company had the following catastrophe excess of loss coverage through commercial reinsurers and the FHCF as of December 31, 2013, resulting in coverage of ultimate net losses of \$222,705,060 for the first event:

- First Catastrophe Excess of Loss Reinsurance - \$39,909,554 in private reinsurance coverage with a retention limit of \$3,000,000
- Second Catastrophe Excess of Loss Reinsurance - \$43,855,929 in private reinsurance coverage with a retention limit \$42,909,554
- Florida Catastrophe Hurricane Fund - \$99,030,023 payout limit with an attachment point of \$40,188,877
- Third Catastrophe Excess of Loss Reinsurance - \$39,909,554 in private reinsurance coverage with a retention limit of \$86,765,483

The Company reinsured second and third events with retention of \$2,000,000 each, and forth event had a retention limit of \$3,000,000.

The Company executed reinsurance premiums protection agreements to reinsure the reinstated premium payment obligations which accrued to the Company under the commercial catastrophe excess of loss agreements. The coverage was limited to 100% of the original contracted reinsurance placement.

For the third and fourth event coverage, the Company reinsured up to \$83,765,483 in coverage for each event.

There were no ceded incurred losses during the year ended December 31, 2013.

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

ACCOUNTS AND RECORDS

The Company maintained its principal operational offices in Tallahassee, Florida. The Company's accounting records were maintained on a computerized system.

The Company and non-affiliates had the following agreements:

Custodial Agreement

The Company maintained custodial agreements with Merrill Lynch, Pierce, Fenner & Smith Incorporated executed on February 2, 2012 and Branch Banking and Trust Company executed on October 13, 2012. The agreements were in compliance with Rule 69O-143.042, Florida Administrative Code.

Independent Auditor Agreement

An independent CPA audited the Company’s statutory basis financial statements annually 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

Scott Langstein, CISA, IT Manager, of Cerebres, LLC performed an evaluation of the information technology and computer systems of the Company. Results of the evaluation were noted in the Information Technology Report provided to the Company.

STATUTORY DEPOSITS

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

STATE	Description	Par Value	Market Value
FL	Cash	<u>\$ 300,000</u>	<u>\$ 300,000</u>
TOTAL FLORIDA DEPOSITS		<u><u>\$ 300,000</u></u>	<u><u>\$ 300,000</u></u>

FINANCIAL STATEMENTS PER EXAMINATION

The following pages contain financial statements showing the Company's financial position as of December 31, 2013, 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."

SOUTHERN FIDELITY PROPERTY & CASUALTY, INC.

Assets

DECEMBER 31, 2013

	Per Company	Examination Adjustments	Per Examination
Bonds	\$39,481,490		\$39,481,490
Cash and short-term investments	42,836,568		42,836,568
Current federal/foreign income tax recoverable	793,921		793,921
Agents' balances:			
Uncollected premium	75,990		75,990
Deferred premium	3,601,017		3,601,017
Net deferred tax asset	2,477,835		2,477,835
Interest and dividend income due & accrued	378,948		378,948
	<hr/>		
Totals	\$89,645,769	\$0	\$89,645,769
	<hr/> <hr/>		

SOUTHERN FIDELITY PROPERTY & CASUALTY, INC.
Liabilities, Surplus and Other Funds

DECEMBER 31, 2013

	Per Company	Examination Adjustments	Per Examination
Losses	\$11,117,605		\$11,117,605
Loss adjustment expenses	1,116,116		1,116,116
Commissions payable	831,647		831,647
Other expenses	40,600		40,600
Taxes, licenses and fees	1,061,511		1,061,511
Unearned premium	34,926,071		34,926,071
Advance premium	2,383,402		2,383,402
Ceded reinsurance premiums payable	11,844,518		11,844,518
Amounts withheld or retained	21,410		21,410
Provision for reinsurance	44,000		44,000
Aggregate write-ins for liabilities	1,840,487		1,840,487
Total Liabilities	\$65,227,367	\$0	\$65,227,367
Common capital stock	\$2,000,000		\$2,000,000
Gross paid in and contributed surplus	18,000,000		18,000,000
Unassigned funds (surplus)	4,418,402		4,418,402
Surplus as regards policyholders	\$24,418,402	\$0	\$24,418,402
Total liabilities, surplus and other funds	\$89,645,769	\$0	\$89,645,769

SOUTHERN FIDELITY PROPERTY & CASUALTY, INC.
Statement of Income

DECEMBER 31, 2013

Underwriting Income		
Premiums earned		\$54,846,551
Deductions:		
Losses incurred		\$22,412,162
Loss expenses incurred		2,866,860
Other underwriting expenses incurred		27,709,695
Aggregate write-ins for underwriting deductions		0
Total underwriting deductions		<u>\$52,988,717</u>
Net underwriting gain		\$1,857,834
Investment Income		
Net investment income earned		\$1,090,744
Net realized capital gains or (losses)		0
Net investment gain		<u>\$1,090,744</u>
Other Income		
Net loss from agents' or premium balances charged off		(\$15,345)
Finance and service charges not included in premiums		112,369
Aggregate write-ins for miscellaneous income		0
Total other income		<u>\$97,024</u>
Net income before dividends to policyholders and before federal & foreign income taxes		\$3,045,602
Dividends to policyholders		0
Net Income, after dividends to policyholders, but before federal & foreign income taxes		\$3,045,602
Federal & foreign income taxes		<u>1,337,859</u>
Net Income		<u><u>\$1,707,743</u></u>
Capital and Surplus Account		
Surplus as regards policyholders, December 31 prior year		\$22,495,020
Net Income		\$1,707,743
Change in net deferred income tax		284,871
Change in non-admitted assets		(25,232)
Change in provision for reinsurance		(44,000)
Change in excess statutory over statement reserves		0
Surplus adjustments: Paid in		0
Aggregate write-ins for gains and losses in surplus		0
Examination Adjustment		0
Change in surplus as regards policyholders for the year		<u>\$1,923,382</u>
Surplus as regards policyholders, December 31 current year		<u><u>\$24,418,402</u></u>

A comparative analysis of changes in surplus is shown below.

SOUTHERN FIDELITY PROPERTY & CASUALTY, INC.
Comparative Analysis of Changes in Surplus

DECEMBER 31, 2013

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
December 31, 2013, per Annual Statement \$24,418,402

	<u>PER COMPANY</u>	<u>PER EXAM</u>	<u>INCREASE (DECREASE) IN SURPLUS</u>
ASSETS: No adjustment.			
LIABILITIES: No adjustment.			
Net change in surplus:			<u>0</u>
Surplus as regards policyholders December 31, 2013, Per Examination			<u><u>\$24,418,402</u></u>

COMMENTS ON FINANCIAL STATEMENTS

Liabilities

Losses and Loss Adjustment Expenses \$12,233,721

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, 2013, made a reasonable provision for all unpaid loss and loss expense obligations of the Company under the terms of its policies and agreements.

The Office consulting actuaries, Greg Wilson, FCAS, MAAA, and Patrick Glenn, ACAS, ASA, MAAA, of Lewis & Ellis, Inc., reviewed the loss and loss adjustment expense work papers provided by the Company and they were in concurrence with this opinion.

Capital and Surplus

The amount of capital and surplus reported by the Company of \$24,418,402 exceeded the minimum of \$6,327,220 required by Section 624.408, Florida Statutes.

CONCLUSION

The insurance examination practices and procedures as promulgated by the NAIC have been followed in ascertaining the financial condition of **Southern Fidelity Property & Casualty, Inc.** as of December 31, 2013, consistent with the insurance laws of the State of Florida.

Per examination findings, the Company's surplus as regards policyholders was \$24,418,402, which exceeded the minimum of \$6,327,220 required by Section 624.408, Florida Statutes.

In addition to the undersigned, Patricia Casey Davis, CFE, CPA, INSRIS, Exam Manager; Sarah Lucibello, CPA, CFE, Examiner-In-Charge, Lewis and Ellis, Inc., Amy Carter, AFE, CPA, Participating Examiner, Lewis and Ellis, Inc., David Palmer, CFE, Participating Examiner, Lewis and Ellis, Inc., and Kate Bolbas, CPA, CFE, Participating Examiner, Lewis and Ellis, Inc. participated in the examination. Greg Wilson, FCAS, MAAA, consulting actuary of Lewis & Ellis, Inc., Patrick Glenn, ACAS, ASA, MAAA, consulting actuary of Lewis & Ellis, Inc., and Scott Langstein, CISA, IT Manager of Cerebres, LLC also participated in the examination. In addition, Mikhael Goldgisser, Reinsurance Financial Specialist, of the Office participated in the examination.

Respectfully submitted,

Robin Brown, CFE
Chief Examiner
Florida Office of Insurance Regulation