

REPORT ON EXAMINATION
OF
STAR CASUALTY INSURANCE
COMPANY
MIAMI, FLORIDA

AS OF
DECEMBER 31, 2010

BY THE
FLORIDA OFFICE OF INSURANCE REGULATION

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TALLAHASSEE, FLORIDA

April 16, 2012

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Dear Sirs:

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 of December 31, 2010, of the financial condition and corporate affairs of:

**STAR CASUALTY INSURANCE COMPANY
5539 SW 8th STREET NORTH, SUITE 203
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, 2006, through December 31, 2010. The Company was last examined by representatives of the Florida Office of Insurance Regulation (Office) as of December 31, 2005. This examination commenced with planning at the Office, from December 13, 2011, to December 15, 2011. The fieldwork commenced on December 19, 2011, and was concluded as of April 16, 2012.

This financial examination was a multi-state 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.

The 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.

Transactions subsequent to year-end 2010 were reviewed where relevant and deemed significant to the Company's financial condition.

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

SUMMARY OF SIGNIFICANT FINDINGS

Current Exam Findings

The findings noted during this examination period have been resolved by the Company subsequent to the examination date. However, the findings or exceptions are discussed in detail in the body of the examination report.

Prior Examination Findings

There were no material findings or exceptions noted during the previous examination as of December 31, 2005.

HISTORY

General

The Company was incorporated on August 20, 1987, as a stock property and casualty insurance company under the applicable provisions of the Florida Statutes. The Company commenced business on July 25, 1988.

The Company was authorized to write private passenger auto liability, auto physical damage and other liability insurance coverage throughout the State of Florida, where approximately 75%

of its business is produced. It is also licensed to write similar auto coverages in Kentucky, Tennessee, Georgia, and Arkansas and is actively pursuing business in those jurisdictions.

Capital Stock and Capital Contributions

As of December 31, 2010, 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	\$1,005,000
Par value per share	\$1.34

Control of the Company was maintained by its sole stockholder Nicolas Estrella, Sr. , who owned 100 percent of the stock issued by the Company. That stockholder also owns affiliated companies that were parties to various service and cost sharing agreements.

Surplus Debentures

The Company did not have any surplus debentures at examination date. The Company paid off a \$1,000,000 surplus note in 2006.

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

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

CORPORATE RECORDS

The recorded minutes of the shareholder and Board of Directors (Board) were reviewed for the period under examination. With noted exceptions, 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.

Conflict of Interest

The Company adopted a policy statement requiring annual 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

In lieu of the annual shareholder meeting for the election of directors, the sole stockholder had special joint meetings with the Board to elect the directors of the Company. Those directors designated and serving as of December 31, 2010, were:

Directors

Name and Location	Principal Occupation
Nicolas Estrella Sr. Key Biscayne, Florida	Sole Stockholder of the Company and Owner of all Affiliates
James Paul Kennedy Marietta, Georgia	Retired Insurance Executive
Amanda Josefina Estrella Key Biscayne, Florida	Student, New York University
Nicolas Estrella Jr. Key Biscayne, Florida	Administrator/Manager – Estrella Insurance Inc.
Paul Gerard Gabe Jr. Weston, Florida	CEO, President and Secretary of the Company
Jose Evelio Estrella Miami Beach, Florida	Vice President of the Company

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

Senior Officers

Name	Title
Paul Gerard Gabe Jr.	CEO, President and Secretary
Alejandro Ruben Zajac	Treasurer
Jose Evelio Estrella	Vice President
Francis Walter Brill	Vice President - Claims

The Company established an audit committee in accordance with Section 624.424 (8) (c), Florida Statutes. The Audit Committee consisted of the following members:

Paul Gerard Gabe Jr.
Jose Evelio Estrella
Francis Walter Brill

Affiliated Companies

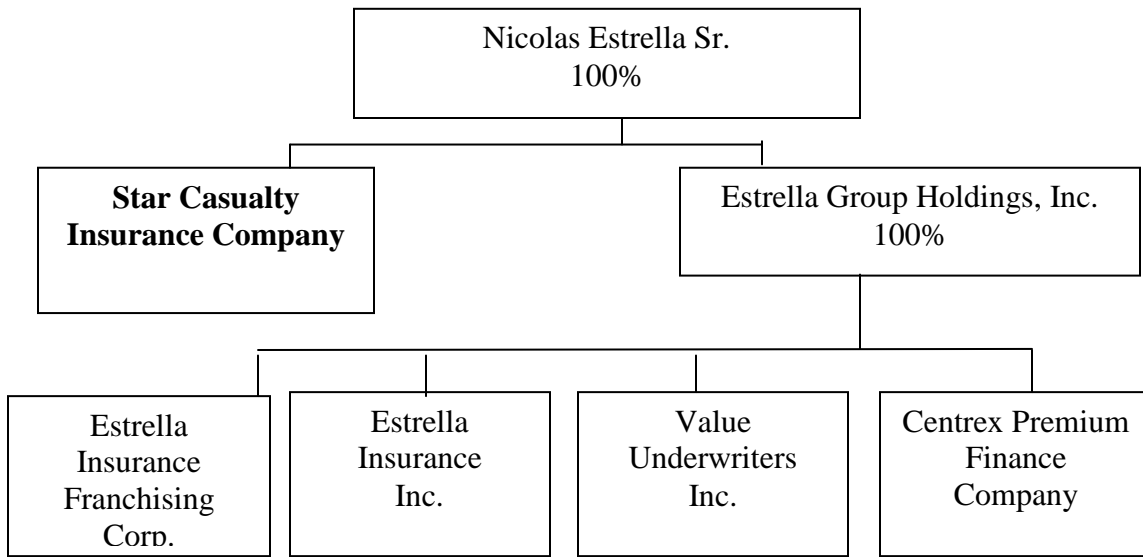
The latest holding company registration statement was filed with the State of Florida on February 11, 2011, as required by Section 628.801, Florida Statutes, and Rule 69O-143.046, Florida Administrative Code.

A simplified organizational chart as of December 31, 2010, reflecting the holding company system is shown below.

STAR CASUALTY INSURANCE COMPANY

ORGANIZATIONAL CHART

DECEMBER 31, 2010



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

Managing General Agency Agreement

Value Underwriters, Inc. agreement was amended and restated January 3, 2006. The Company and its affiliate 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.

Cost Sharing Agreement

Value Underwriters, Inc., Centrex Premium Finance, Estrella Insurance, Inc., Penta Insurance Adjusters, Inc., and Estrella General Agency, Inc. agreements, with an inception date of May 1, 2010, provided for an allocation of office and salary expenses in cases where an affiliate paid for expenses incurred for costs that pertained to another affiliate or affiliates.

Claims Handling Agreement

Penta Insurance Adjusters, Inc. agreement, with an inception date of March 5, 2010, stated that the affiliate will function as the claims department for the Company. In return, the Company paid a fee based on a schedule in the agreement that is linked to the type of claim being settled.

Producers Agreement

Estrella Insurance, Inc. agreement, with an inception date of January 3, 2006, gave the agency the right to solicit, provide quotes, receive applications, bind coverage, and collect, receive, and issue receipts for premiums. In return, the Company paid the agency a commission on policies and

renewals based on applicable commission schedules in effect as of the inception date of each policy or renewal.

FIDELITY BOND AND OTHER INSURANCE

The Company maintained fidelity bond coverage with an aggregate limit of liability of \$250,000. The Company was named as the insured in the policy and the amounts exceed the NAIC recommended minimum fidelity coverage.

PENSION, STOCK OWNERSHIP AND INSURANCE PLANS

The Company adopted a qualified 401 K retirement plan in 1999 covering substantially all employees subject to certain service requirements. No matching contributions were made by the Company. This plan was terminated effective December 31, 2006. At examination date, the Company stated that it was not offering any pension plans to any employees. Insurance coverage was being maintained in the normal course of business.

TERRITORY AND PLAN OF OPERATIONS

The Company was authorized to transact insurance in the following states

Florida
Georgia

Arkansas
Tennessee

Kentucky

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

The Company, during the period under examination, fluctuated in earned premiums, losses, and other asset, liability, surplus and income accounts. The Company reported net underwriting losses for the years 2008 through 2010 totaling \$10,983,070. The Company explained these material fluctuations and losses as being a result of reducing exposures in certain high risk areas and attempting to grow in geographically diverse areas within the five states in which it is licensed.

Profitability of Company

The following table shows the profitability/loss trend of the Company for the period of examination, as reported in the filed annual statement.

	2010	2009	2008	2007	2006
Premiums Earned	9,423,081	9,648,725	5,886,858	16,490,730	18,851,688
Net Underwriting Gain/(Loss)	(3,572,864)	(4,882,627)	(2,527,579)	47,332	4,314,396
Net Income	(2,314,745)	(2,632,652)	(920,504)	1,487,646	4,086,046
Total Assets	18,946,144	18,650,075	19,389,980	26,088,740	29,568,167
Total Liabilities	11,917,753	9,357,794	7,763,337	13,809,390	17,755,123
Surplus As Regards Policyholders	7,028,391	9,292,281	11,626,643	12,279,350	11,813,044

LOSS EXPERIENCE

During the current examination period, the Company showed favorable loss development. The one-year net loss development at the end of the current examination period was favorable at \$786,000. The two-year loss development was also favorable at \$1,353,000.

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 no reinsurance during the period of this examination.

Ceded

The Company participated in quota share and excess of loss reinsurance programs with General Reinsurance Corporation. The Company ceded 40% of its business and received a ceding commission of 26.5% (was 36.5% through March 31, 2010) on an earned basis.

The Company also participated in excess of loss per policy and extra contractual liability programs, also with General Reinsurance Corporation. Both excess of loss contracts have a 36% ceding commission rate in effect. The per occurrence figures were computed net of quota share and the per policy amounts were subtracted from the balances as well.

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 Miami, Florida.

An independent CPA audited the Company's statutory basis financial statements annually for the years under examination, 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 utilized software by Modotech, Inc. to process all transactions by the Company. A Modotech, Inc. computer system was utilized to handle hardware requirements for policy issuance, premium collections, general ledger accounting, and claims record keeping. The software IT Policy Management System (managed by Modotech, Inc.) was utilized for all reporting regarding general ledger and accounts payable information.

The Company and non-affiliates had the following agreements:

Custodial Agreement

The Company had two custodial agreements, one with Merrill Lynch, Fenner & Smith Incorporated (Merrill Lynch) and one with US Bank. Both custodians met the requirements of custodian as defined by Rule 69O-143.041, Florida Administrative Code.

The custodial agreement with Merrill Lynch did not contain clause (o) of Rule 69O-143.042, Florida Administrative Code, which requires the custodian to provide written notification to the Florida Office of Insurance Regulation if the custodial agreement with the insurer has been terminated or if 100% of the account assets in any one custody account have been withdrawn.

Subsequent event: The Company filed a Custodial Agreement Addendum to the Merrill Lynch custodial agreement dated April 4, 2012 which addressed the above issues. The custodial agreement is now in compliance with Rule 69O-143.043, Florida Administrative Code.

Independent Auditor Agreement

The Company contracted with an external independent CPA firm to perform the annual audit of its financial statements as required by Rule 69O-137.002 (7) (c), Florida Administrative Code.

INFORMATION TECHNOLOGY REPORT

Paul Berkebile, CISA, CFSA, CRISC, and Claude B. Granese, CPA, IT specialists from INS Services, Inc. performed an evaluation of the information technology and computer systems of the Company. Results of the evaluation were contained 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, and the State of Alabama:

<u>STATE</u>	<u>Description</u>	<u>Par Value</u>	<u>Market Value</u>
FLORIDA	Cash	\$ 30,000	\$ 30,000
	Certificates of Deposit	<u>770,000</u>	<u>770,000</u>
TOTAL FLORIDA DEPOSITS		<u>\$1,000,000</u>	<u>\$1,000,000</u>
ALABAMA	Industrial & Misc. Bond	\$ 25,000	\$ 25,005
TOTAL SPECIAL DEPOSITS		<u>\$1,025,000</u>	<u>\$1,025,005</u>

FINANCIAL STATEMENTS PER EXAMINATION

The following pages contain financial statements showing the Company's financial position as of December 31, 2010, 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, 2010

Classification	Per Company	Examination Adjustments	Per Examination
Bonds	\$ 2,725,753	\$	\$ 2,725,753
Real estate: Properties occupied by the Company	2,334,112		2,334,112
Cash and short-term investments	7,931,204		7,931,204
Investment income due & accrued	8,294		8,294
Premiums and considerations: Uncollected premiums and agents' balances in course of collection	506,617		506,617
Deferred premiums, agents' balances and installments booked but deferred and not yet due	3,449,293		3,449,293
Reinsurance: Amounts recoverable from reinsurers	1,584,361		1,584,361
Electronic data processing equipment and software	48,244		48,244
Receivables from parent, subsidiaries & affiliates	315,212		315,212
Aggregate write-ins for other than invested assets	43,054		43,054
Totals	<u>\$ 18,946,144</u>		<u>\$ 18,946,144</u>

STAR CASUALTY INSURANCE COMPANY
Liabilities, Surplus and Other Funds

DECEMBER 31, 2010

Liabilities	Per Company	Examination Adjustments	Per Examination
Losses	\$ 3,746,353		\$ 3,746,353
Loss adjustment expenses	613,447		613,447
Commissions payable, contingent commissions & other similar charges	194,377		194,377
Other expenses	250,642		250,642
Taxes, licenses and fees	12,085		12,085
Advance premium	2,535,818		2,535,818
Ceded reinsurance premiums payable	2,920,989		2,920,989
Drafts outstanding	1,607,092		1,607,092
Payable to parent, subsidiaries and affiliates	36,950		36,950
Total liabilities	\$ 11,917,753		\$ 11,917,753
Common capital stock	\$1,005,000		\$1,005,000
Gross paid in and contributed surplus	1,407,325		1,407,325
Unassigned funds (surplus)	4,616,066		4,616,066
Surplus as regards policyholders	\$ 7,028,391		\$ 7,028,391
Total liabilities, capital and surplus	\$ 18,946,144		\$18,946,144

STAR CASUALTY INSURANCE COMPANY
Statement of Income

DECEMBER 31, 2010

Underwriting Income	
Premiums earned	\$ 9,423,081
DEDUCTIONS:	
Losses incurred	\$ 7,933,699
Loss adjustment expenses incurred	2,081,002
Other underwriting expenses incurred	2,981,244
Total underwriting deductions	<u>\$ 12,995,945</u>
 Net underwriting gain or (loss)	 \$ (3,572,864)
Investment Income	
Net investment income earned	\$ 86,178
Net realized capital gains or (losses)	
Net investment gain or (loss)	<u>\$ 86,178</u>
Other Income	
Net gain or (loss) from agents' or premium balances charged off	\$ (148,852)
Finance and service charges not included in premiums	1,326,512
Aggregate write-ins for miscellaneous income	0
Total other income	<u>\$ 1,177,660</u>
 Net income before dividends to policyholders and before federal & foreign income taxes	 \$ (2,309,026)
Dividends to policyholders	<u>0</u>
Net Income, after dividends to policyholders, but before federal & foreign income taxes	\$ (2,309,026)
Federal & foreign income taxes	<u>5,719</u>
 Net Income	 <u><u>\$ (2,314,745)</u></u>
Capital and Surplus Account	
Surplus as regards policyholders, December 31 prior year	\$ 9,292,281
Gains and (Losses) in Surplus	
Net Income	\$ (2,314,745)
Net unrealized capital gains or losses	
Change in net deferred income taxes	53,057
Change in non-admitted assets	(2,202)
Change in provision for reinsurance	
Change in surplus as regards policyholders for the year	<u>\$ (2,263,890)</u>
 Surplus as regards policyholders, December 31 current year	 <u><u>\$ 7,028,391</u></u>

A comparative analysis of changes in surplus is shown below.

STAR CASUALTY INSURANCE COMPANY
Comparative Analysis of Changes in Surplus

DECEMBER 31, 2010

Surplus as Regards Policyholders as of December 31, 2010 per Annual Statement		<u>\$ 7,028,391</u>
	Per Company Per Examination	Increase (Decrease) in Surplus
 ASSETS:		
No Adjustment		
 LIABILITIES:		
No Adjustment		
 Net Change in Surplus		
		<u>_____</u>
Surplus as Regards Policyholders as of December 31, 2010 per Examination		<u><u>\$ 7,028,391</u></u>

COMMENTS ON FINANCIAL STATEMENTS

Liabilities

Losses and Loss Adjustment Expenses \$4,359,800

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, 2010, made a reasonable provision for all unpaid loss and loss expense obligations of the Company under the terms of its policies and agreements. INS Consultants, Inc. (INS) was retained by the Office to conduct an independent review of the Company's loss and loss adjustment expense (LAE) reserves as of December 31, 2010, in conjunction with the financial examination.

The INS actuary reviewed the loss and loss adjustment expense work papers provided by the Company's outside actuarial firm and was in concurrence with their opinion.

Capital and Surplus

The amount of Capital and Surplus reported by the Company of \$7,028,391, exceeded the minimum of \$4,000,000 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 **Star Casualty Insurance Company** as of December 31, 2010, consistent with the insurance laws of the State of Florida.

Per examination findings, the Company's surplus as regards policyholders was \$7,028,391 which exceed the minimum of \$4,000,000 required by Section 624.408, Florida Statutes.

In addition to the undersigned, Hails W. Taylor, CFE, Senior Insurance Examiner, INS Regulatory Insurance Services, Inc.; Gary Farmer, Financial Examiner/Analyst Supervisor; Sara Baylock, Reinsurance/Financial Specialist, of the Office participated in the examination and Tracy Gates, CPA, CISA, as consulting examination manager. We also recognize James R. Neidermyer, FCAS, MAAA and David J. Macesic, ACAS, MAAA, actuaries from INS Consultants, Inc., along with Paul Berkebile, CISA, CFSA, CRISC and Claude B. Granese, CPA, IT Specialists from INS Services, Inc. who participated in the examination.

Respectfully submitted,

Mary M. James, CFE, CPM
Chief Examiner
Florida Office of Insurance Regulation