

**REPORT ON EXAMINATION**  
**OF**  
**TOWER HILL SELECT INSURANCE**  
**COMPANY**  
**GAINESVILLE, FLORIDA**

**AS OF**  
**DECEMBER 31, 2009**

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

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**TALLAHASSEE, FLORIDA**

March 4, 2011

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, 2009, of the financial condition and corporate affairs of:

**TOWER HILL SELECT INSURANCE COMPANY  
7201 N.W. 11<sup>TH</sup> PLACE  
GAINESVILLE, FLORIDA 32605**

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, 2008, through December 31, 2009. The Company was last examined by representatives of the Florida Office of Insurance Regulation (Office) as of December 31, 2007. This examination commenced with planning at the Office on December 13, 2010, to December 17, 2010. The fieldwork commenced on December 20, 2010, and concluded as of March 4, 2011.

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.

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.

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**

The following is a summary of material adverse findings, significant non-compliance findings, or material changes in the financial statements noted during this examination.

### **Reinsurance**

1. Pursuant to Rule 69O-144.005(6), Florida Administrative Code, letters of credit from reinsurers must contain certain clauses and language. The letters of credit from the following reinsurers did not contain all the required clauses or language:

- Glencoe Insurance Ltd.
- Renaissance Reinsurance, Ltd.

The specific missing clauses and language were communicated to the Company with the exception memorandum.

Subsequent Event: On June 17, 2011, the Company notified the Office that these two Letters of Credit were no longer in effect.

## **Prior Exam Findings**

There were no findings, exceptions, or corrective action to be taken by the Company for the examination as of December 31, 2007.

## **HISTORY**

### **General**

The Company is a domestic property and casualty, stock company licensed to write insurance only in Florida. It was incorporated on April 16, 2004, and commenced writing business on June 24, 2004. The Company was authorized to transact the following insurance coverage in Florida on December 31, 2009:

Fire  
Homeowners' Multiple Peril  
Inland Marine  
Allied Lines

The Company assumed premium related to Commercial Multiple Peril without being authorized to write that line of business in violation of Section 624.401(1), Florida Statutes.

### **Dividends to Stockholders**

In accordance with Section 628.371, Florida Statutes, the Company declared and paid dividends to its stockholder in 2009 and 2008, of \$1,650,000 and \$5,600,000, respectively.

### **Capital Stock and Capital Contributions**

As of December 31, 2009, the Company's capitalization was as follows:

Number of authorized common capital shares	100,000
Number of shares issued and outstanding	100,000
Total common capital stock	\$100,000
Par value per share	\$1.00

Control of the Company was maintained by its parent, Tower Hill Holdings, Inc, which owned 100% of the stock issued by the Company, which in turn was owned 57% by William J. Shively (retains 57% voting control) and Patricia Shively (non-voting), 29% by Renaissance Re Ventures, Ltd. and 14% by Benfield Investment Holdings, Ltd.

### **Surplus Debentures**

The Company did not have any surplus debentures as of December 31, 2009.

### **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 of examination.

## **CORPORATE RECORDS**

The recorded minutes of the shareholder, Board of Directors (Board), and certain internal committees were reviewed for the period under examination.

### **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

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, 2009, were:

### Directors

<b>Name and Location</b>	<b>Principal Occupation</b>
William J. Shively Lexington, Kentucky	Chief Executive Officer Tower Hill Insurance Group, LLC
Donald C. Matz, Jr. Gainesville, Florida	President Tower Hill Insurance Group, LLC
Joel P. Curran Gainesville, Florida	Chief Underwriting Officer Tower Hill Insurance Group, LLC
Keyton Benson, Sr. Gainesville, Florida	Chief Marketing Officer Tower Hill Insurance Group, LLC
James N. Smith St. Petersburg, Florida	Retired

**Subsequent Event:** On June 22, 2010, the Board appointed G. Gregory King of Fort Myers, Florida, as a director.

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

### Senior Officers

<b>Name</b>	<b>Title</b>
William J. Shively	Chief Executive Officer
Donald C. Matz, Jr.	President, Chief Operating Officer
Joel P. Curran	Vice President, Secretary
Keyton Benson, Sr.	Vice President, Treasurer

The Company's Board appointed an internal committee in accordance with Section 607.0825, Florida Statutes. Following was the principal internal board committee and its members as of December 31, 2009

#### **Audit Committee**

James N. Smith<sup>1</sup>  
Timothy J. Meenan  
Joel P. Curran

<sup>1</sup> Chairman

#### **Affiliated Companies**

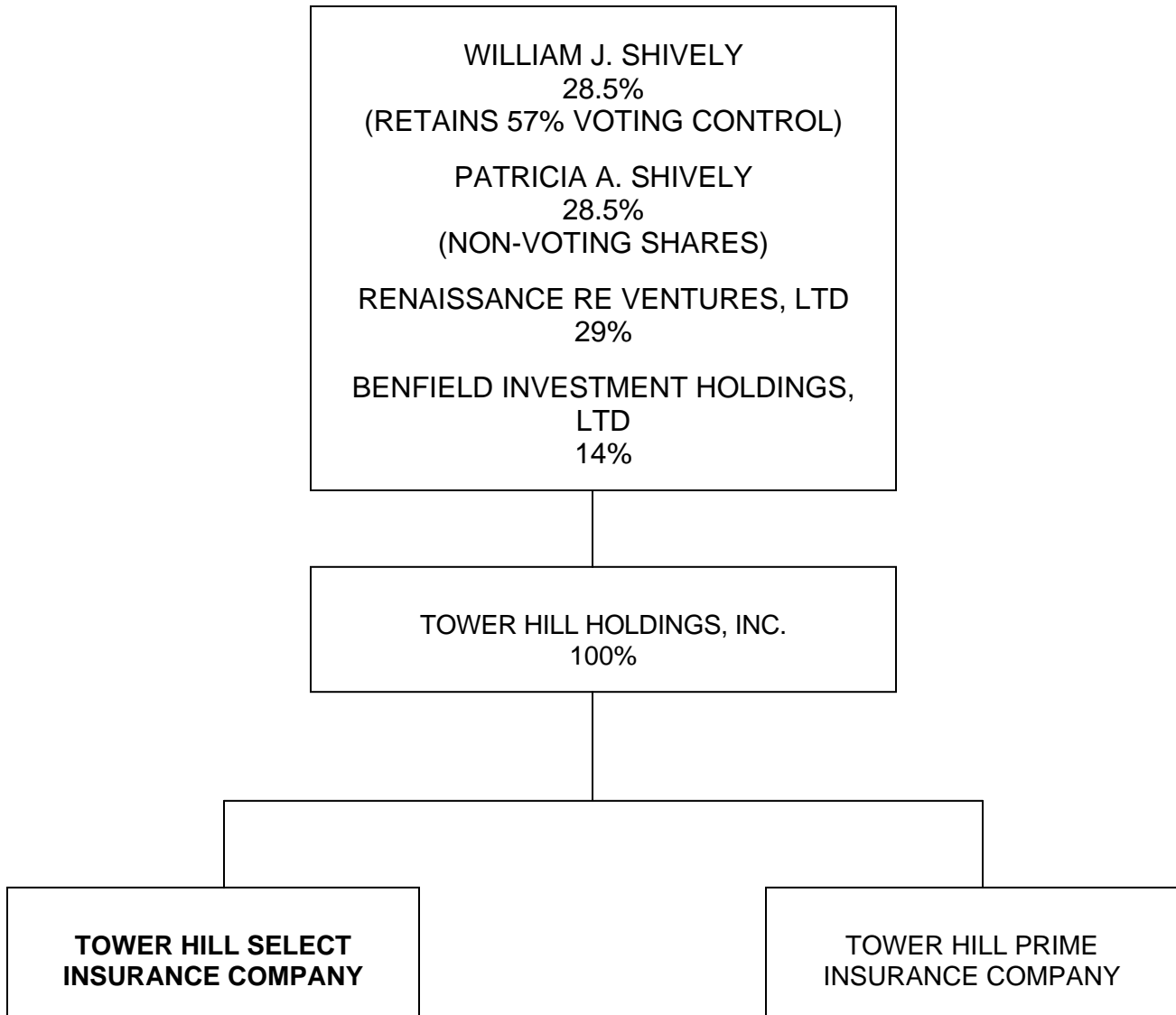
The Company was a member of an insurance holding company system as defined by Rule 69O-143.045(3), Florida Administrative Code. The latest holding company registration statement was filed with the State of Florida on November 15, 2010, as required by Section 628.801, Florida Statutes, and Rule 69O-143.046, Florida Administrative Code.

A simplified organizational chart as of December 31, 2009, reflecting the holding company system, is shown below. Schedule Y of the Company's 2009 annual statement provided a list of all related companies of the holding company group.

# TOWER HILL SELECT INSURANCE COMPANY

## Organizational Chart

DECEMBER 31, 2009



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

### **Tax Allocation Agreement**

The Company, along with its parent, Tower Hill Holdings, Inc. (Holdings), filed a consolidated federal income tax return. On December 31, 2009, the method of allocation between the Company and its parent was on a separate-entity basis. Income tax provisions were allocated to the respective companies based on their contribution to consolidated taxable income.

### **Management Agreement**

The Company entered into a Management Agreement with Holdings, on April 6, 2005, to provide certain management services including, executive management, reinsurance assistance, legal counsel, financial management, and other such services. The agreement continues in force for a term of five years and will automatically renew for successive five-year periods, unless otherwise terminated within the guidelines of the agreement. The management fee paid by the Company each month was equal to 2.0% of written premium on new and renewed business. Fees incurred under this agreement during 2009 amounted to \$1,372,772.

### **General Agency Agreement**

The Company entered into a General Agency Agreement (GA) with its affiliate, Tower Hill Insurance Group, LLC, on January 1, 2008. Services provided by the GA included, but were not limited to, marketing, underwriting, policy issue, premium billing and policy service. The agreement continues in force for a term of five years and will automatically renew for successive five-year periods, unless otherwise terminated within the guidelines of the agreement. Fees under this agreement were based on 22.5% of direct written and included the \$25 policy fee. Fees incurred under this agreement during 2009, amounted to \$55,131,945.

### **Claims Service Agreement**

The Company entered into a Claims Service Agreement with its affiliate, Tower Hill Claims Service, Inc., on January 1, 2008. Pursuant to the agreement, Tower Hill Claims Service Inc. was authorized to process, investigate, evaluate, adjust and negotiate settlements of all claims. The agreement continues in force for a term of five years and will automatically renew for successive five-year periods, unless otherwise terminated within the guidelines of the agreement. Claims administration fees were calculated according to a fee schedule based on size of claim. Fees incurred under this agreement during 2009, amounted to \$1,304,844.

### **Reinsurance Pooling Agreement**

The Company entered into a Reinsurance Pooling Agreement with its affiliate, Tower Hill Prime Insurance Company, on June 1, 2009, with the expectation of reducing administrative and management expenses and providing a broader distribution of risk by lines of business and territory. Pursuant to terms of the agreement, the quota-share percentage participation was 35% to the Company and 65% to Tower Hill Prime Insurance Company. Effective with the agreement, there was an initial portfolio transfer of net underwriting liabilities in order to reflect the quota-share percentage for each participant as provided for in the agreement. All underwriting business of the companies was subject to the pooling agreement.

**Subsequent Event:** The Reinsurance Pooling Agreement was terminated as of June 1, 2010.

## **FIDELITY BOND AND OTHER INSURANCE**

The Company maintained fidelity bond coverage up to \$3,100,000 with a deductible of \$50,000, which reached the suggested minimum as recommended by the NAIC. The Company also maintained professional liability coverage, with an aggregate limit of \$1,000,000 with a deductible of \$250,000; directors and officers (D&O) coverage, with an aggregate limit of \$3,000,000 with a deductible of \$25,000; as well as worker's compensation, general liability and umbrella coverage.

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

The Company did not have any pension stock ownership or employee insurance plans.

## **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

In response to recent years' losses resulting from the active hurricane seasons of 2004 and 2005, the Company aggressively reduced policy counts to temper its overall exposure to weather-related events, while implementing various rate actions. In addition, various capital initiatives in recent years by the parent company have been implemented.

The Company's surplus decreased 28.6% over the period of examination. The decrease was primarily due to the one-time commission expense from non-renewing a quota share contract. Assets have remained invested in cash and short-term investments, 100% of which are rated Class 1, Highest Quality, by the NAIC. The net loss from operations reported for 2009 was due to the combination of reduced direct writings, the higher cost of catastrophe reinsurance protection and the one-time ceded commission expense from the non-renewal of a quota share contract.

### 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 statements.

	2009	2008
Premiums Earned	24,902,998	25,288,220
Net Underwriting Gain/(Loss)	(8,984,105)	1,224,038
Net Income	(9,278,513)	2,229,473
Total Assets	62,909,569	46,599,187
Total Liabilities	46,737,872	23,944,511
Surplus As Regards Policyholders	16,171,697	22,654,676

## **LOSS EXPERIENCE**

There was not any significant change in the Company's loss experience.

## **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**

All assumptions were related to the Reinsurance Pooling Agreement with the Company's affiliate, Tower Hill Prime Insurance Company, as noted above. Pursuant to terms of the agreement, the quota-share percentage participation was 35% to the Company and 65% to Tower Hill Prime Insurance Company.

### **Ceded**

In addition to the cessions related to the Reinsurance Pooling Agreement, the Company ceded risk on a per risk excess of loss and per occurrence catastrophe basis to the Florida Hurricane Catastrophe Fund (FHCF) and various affiliated and non-affiliated reinsurers. For the year ended December 31, 2009, the commercial excess of loss treaties generally provided coverage on ultimate net losses of \$278,300,000 in excess of \$1 million per occurrence, not to exceed \$510,400,000 for all occurrences. The FHCF provided coverage for 90% of the losses from qualifying catastrophic events in excess of \$43,300,000, up to a maximum of \$114,500,000.

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



**Subsequent Event:** The Company entered into a new quota-share reinsurance agreement effective on June 1, 2010 with various participants. Under the new quota share agreement, the Company cedes 32.50% of new, renewal, and in-force business while retaining 67.50%.

## **ACCOUNTS AND RECORDS**

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

An independent CPA audited the Company's statutory basis financial statements annually for the years 2008 and 2009, 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 maintained a custodial agreement with US Bank entered into on July 17, 2006. The agreement in compliance with Rule 69O-143.042, Florida Administrative Code.

### **Asset Management Agreement**

The Company maintained an asset management agreement with Conning Asset Management Company (Conning) entered into on February 15, 2002. Pursuant to the agreement, Conning provided investment advisory and portfolio management services in accordance with the investment guidelines of the Company.

## Independent Auditor Agreement

The Company contracted with KPMG, LLP, to perform the annual audit of its financial statements as required by Rule 690-137.002 (7) (c), Florida Administrative Code.

## INFORMATION TECHNOLOGY REPORT

INS Services, Inc. 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, as required or permitted by law:

STATE	Description	Par Value	Market Value
FL	Cash	\$ <u>300,654</u>	\$ <u>300,654</u>
TOTAL SPECIAL DEPOSITS		<u>\$300,654</u>	<u>\$300,654</u>

## FINANCIAL STATEMENTS PER EXAMINATION

The following pages contain financial statements showing the Company's financial position as of December 31, 2009, and the results of its operations for the year then ended as determined by this examination. Adjustments made as a result of the examination are noted in the section of this report captioned, "Comparative Analysis of Changes in Surplus."

**Tower Hill Select Insurance Company  
Assets**

**DECEMBER 31, 2009**

	<b>Per Company</b>	<b>Examination Adjustments</b>	<b>Per Examination</b>
Cash and Short-Term Investments	\$45,539,233		\$45,539,233
Investment income due and accrued	5,627		5,627
Agents' Balances:			
Uncollected premium	8,011,543		8,011,543
Reinsurance:			
Reinsurance recoverable	4,333,112		4,333,112
Funds held	467,576		467,576
Current federal and foreign income tax recoverable and interest thereon		2,273,500	2,273,500
Net deferred tax asset	3,674,300	(2,273,500)	1,400,800
Guaranty funds receivable or on deposit	714,452		0 714,452
Aggregate write-in for other than invested assets	163,726		0 163,726
	<hr/>		
Totals	<u>\$62,909,569</u>	<u>\$0</u>	<u>\$62,909,569</u>

**Tower Hill Select Insurance Company  
Liabilities, Surplus and Other Funds**

**DECEMBER 31, 2009**

	Per Company	Examination Adjustments	Per Examination
Losses	\$7,969,687		\$7,969,687
Reinsurance payable	1,440,015		1,440,015
Loss adjustment expenses	609,490		609,490
Other expenses	48,204		48,204
Taxes, licenses and fees	143,594		143,594
Unearned premium	18,183,527		18,183,527
Ceded reinsurance premiums payable	17,931,700		17,931,700
Funds held by company under reinsurance treaties	11,737		11,737
Amounts withheld	262,489		262,489
Payable to parent, subsidiaries and affiliates	137,429		137,429
<b>Total Liabilities</b>	<b>\$46,737,872</b>	<b>\$0</b>	<b>\$46,737,872</b>
Common capital stock	\$100,000		\$100,000
Gross paid in and contributed surplus	22,300,000		22,300,000
Unassigned funds (surplus)	(6,228,303)		(6,228,303)
Surplus as regards policyholders	\$16,171,697	\$0	\$16,171,697
<b>Total liabilities, surplus and other funds</b>	<b>\$62,909,569</b>	<b>\$0</b>	<b>\$62,909,569</b>

**Tower Hill Select Insurance Company  
Statement of Income**

**DECEMBER 31, 2009**

**Underwriting Income**

Premiums earned		\$24,902,998
	<b>Deductions:</b>	
Losses incurred		\$15,050,579
Loss expenses incurred		1,936,260
Other underwriting expenses incurred		16,900,264
Total underwriting deductions		<u>\$33,887,103</u>
Net underwriting gain or (loss)		(\$8,984,105)

**Investment Income**

Net investment income earned		\$16,600
Net investment gain or (loss)		<u>\$16,600</u>

**Other Income**

Total other income		<u>\$0</u>
Net income before dividends to policyholders and before federal & foreign income taxes		(\$8,967,504)
Dividends to policyholders		<u>0</u>
Net Income, after dividends to policyholders, but before federal & foreign income taxes		(\$8,967,504)
Federal & foreign income taxes		<u>(311,009)</u>
Net Income		<u><u>(\$9,278,513)</u></u>

**Capital and Surplus Account**

Surplus as regards policyholders, December 31 prior year		\$22,654,676
Net Income		(\$9,278,513)
Change in net deferred income tax		3,390,000
Change in non-admitted assets		(344,466)
Surplus adjustments: Paid in		1,400,000
Dividends to stockholder		(1,650,000)
Change in surplus as regards policyholders for the year		<u>(\$6,482,979)</u>
Surplus as regards policyholders, December 31 current year		<u><u>\$16,171,697</u></u>

A comparative analysis of changes in surplus is shown below.

**Tower Hill Select Insurance Company  
Comparative Analysis of Changes In Surplus**

**DECEMBER 31, 2009**

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, 2009, per Annual Statement \$16,171,697

	<u>PER COMPANY</u>	<u>PER EXAM</u>	<u>INCREASE (DECREASE) IN SURPLUS</u>
<b>ASSETS:</b>			
Current federal and foreign income tax recoverable	\$0	\$2,273,500	\$2,273,500
Net deferred tax asset	3,674,300	1,400,800	(2,273,500)
<b>LIABILITIES:</b>			
No Adjustment			
 Net Change in Surplus:			<u>0</u>
 Surplus as Regards Policyholders December 31, 2009, Per Examination			<u>\$16,171,697</u>

## COMMENTS ON FINANCIAL STATEMENTS

### Assets

<b>Current Federal and Foreign Income Tax Recoverable</b>	<u>\$2,273,500</u>
<b>Net Deferred Tax Asset</b>	<u>\$1,400,800</u>

In 2009, the Company generated a net operating loss (NOL) for federal income tax reporting. In recording this NOL, the Company recorded it as a deferred tax asset and did not record the income tax benefit through the statement of operations. The recording of the deferred tax asset had the effect of crediting surplus for the benefit; however, no benefit to net income was recorded. The adjustments identified above reduce the reported net deferred tax asset and record a current federal and foreign income tax recoverable. There was no effect on surplus as a result of these adjustments.

**Subsequent event:** During the first quarter of 2010, the Company posted the adjustments identified above.

### Liabilities

<b>Losses and Loss Adjustment Expenses</b>	<u>\$8,579,177</u>
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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, 2009, 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 engaged an independent actuarial firm, INS Consultants, Inc., to review the reserves for loss and loss adjustment expenses carried in the Company's balance sheet as of December 31, 2009, and was in concurrence with this opinion.

### **Capital and Surplus**

The amount reported by the Company of \$16,171,697, exceeded the minimum of \$4,673,787 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 **Tower Hill Select Insurance Company** as of December 31, 2009, consistent with the insurance laws of the State of Florida.

Per examination findings, the Company's Surplus as regards policyholders was \$16,171,697, which exceeded the minimum of \$4,673,787 required by Section 624.408, Florida Statutes.

In addition to the undersigned, John V. Normile, CFE, Examiner-In-Charge; J. Matthew Perkins, CFE; Bill W. Holmes, CFE; and Don Gaskill, CFE; Participating Examiners; and Patricia Casey Davis, CPA, CFE, Manager of INS Regulatory Insurance Services, Inc. participated in the examination. James Boswell, Systems Specialist; Michael W. Morrow, ACAS, MAAA, and Robert Gardner, FCAS, MAAA, consulting actuaries of INS Consultants, Inc.; Claude Granese, CPA, Director of Finance and Quality Control of INS Services, Inc.; and Fidel S. Gonzalez, Financial Examiner/Analyst Supervisor of the Office also participated in the examination.

Respectfully submitted,

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