

Florida Select Insurance Company

Insolvency Report

Buttner Hammock & Company, P.A.
October 19, 2012

Florida Select Insurance Company

Insolvency Report

Receivership Information/Reference:

Name of Receivership	Florida Select Insurance Company
Receivership Number	511
Date of Receivership	June 30, 2006
Date of Rehabilitation	June 30, 2006
Date of Liquidation	Pending
Guarantee Association	Florida Insurance Guarantee Association and South Carolina Insurance Guarantee Association

Scope: As provided in the Provider Contract dated October 15, 2007 between the “Receiver of The Estate of Florida Select Insurance Company” (the Receiver being the Florida Department of Financial Services, Division of Rehabilitation and Liquidation), hereinafter referred to as “Receiver,” and Buttner Hammock & Company, P.A. (“BHC”) Section 5 states, in part:

5. SCOPE OF WORK.

5.1.5 “Provider to provide a written Receivership Report to the Receiver consistent with the requirements and formal set forth in Attachment A of this Contract.

Attachment A of the contract is the “Insolvency Report Formal/Scope – Revised May 2007.

The authority under which the insolvency report is written is Section 631.398, Florida Statutes which states as follows:

The 2007 Florida Statutes

Title XXXVII

Chapter 631

Insurance Insurer Insolvency; Guaranty of Payment

631.398 Prevention of insolvencies.—To aid in the detection of prevention of insurer insolvencies or impairments:

(1) Any member insurer; agent, employee, or member of the board of directors; or representative of any insurance guaranty association may make reports and recommendations to the department or office upon any matter germane to the solvency, liquidation, rehabilitation, or conversation of any member insurer or germane to the solvency of any company seeking to do an insurance business in this state. Such reports and recommendations are confidential and exempt from the provisions of s. 119.07(1) until the termination of a delinquency proceeding.

(2) The office shall:

(a) Report to the board of directors of the appropriate insurance guaranty association when it has reasonable cause to believe from any

examination, whether completed or in process, of any member insurer that such insurer may be an impaired or insolvent insurer.

(b) Seek the advice and recommendations of the board of directors of the appropriate insurance guaranty association concerning any matter affecting the duties and responsibilities of the office in relation to the financial condition of member companies and companies seeking admission to transact insurance business in this state.

(3) The department shall, no later than the conclusion of any domestic insurer insolvency proceeding, prepare a summary report containing such information as is in its possession relating to the history and causes of such insolvency, including a statement of the business practices of such insurer which led to such insolvency.

History – ss. 28, 39, ch. 83-38; ss. 187, 188, ch. 91-108; s. 4, ch. 91-429; ss. 2, 6, ch. 93-118; s. 385, ch. 96-406; s. 1351, ch. 2003-261.

The location and dates of our review of files in the RECEIVER's possession were as follows:

- October 2007 – February 2008: Review of Receiver's files in Jacksonville, Florida by Michael Hammock, CPA.
- April 19-20, 2012: Review of Receiver's files at 2020 Capital Circle SE, Tallahassee, Florida by Michael Hammock, CPA.

Business: Historical information related to Florida Select Insurance Company (“Florida Select”) follows:

1. Date and location of Incorporation: Florida Select was originally incorporated in the State of Florida on May 29, 1996 and commenced business on August 16, 1996.
2. Date Company began doing business in Florida: As far as can be determined, Florida Select is presumed to have begun doing business in Florida August 16, 1996.
3. Lines of Business: Florida Select was a Florida for-profit engaged in the marketing and writing of homeowners multi-peril insurance coverage.
4. Certificates of Authority: Florida Select held a license in the States of Florida, South Carolina, Texas, and Virginia.
5. Geographic Areas: Florida Select’s geographic area of insurance coverage for the year ended December 31, 2006 follows:

<u>State</u>	<u>Percent of Premiums</u>
Florida	88%
South Carolina	<u>12%</u>
Total	<u>100%</u>

6. Operating Results: Florida Select's operating results according to Florida Select's 2006 Annual Statement follows:

	<u>Premiums Earned</u>	<u>Underwriting Deductions</u>	<u>Underwriting Gain (Loss)</u>	<u>Net Income (Loss)</u>
2002	\$ 2,559,934	\$ 2,540,289	\$ (19,645)	\$ 2,963,195
2003	\$ 1,876,825	\$ 1,983,892	\$ (107,067)	\$ 868,947
2004	\$ 1,538,762	\$ 1,757,266	\$ (218,504)	\$ 564,278
2005	\$ 1,841,406	\$ 1,996,142	\$ (154,736)	\$ 528,428
2006	\$ 32,488,191	\$ 33,727,784	\$ (1,239,593)	\$ (1,804,681)

7. Ownership:

- Florida Select was a wholly owned subsidiary of Florida Select Insurance Holdings, Inc., which is a wholly owned subsidiary of Vesta Fire Insurance Corporation, which is a wholly owned subsidiary of Vesta Insurance Group, Inc.

The 2005 Annual Statement of Florida Select listed the following officers and trustees:

Officers (March 31, 2006):

- David Wayne Lacefield, President
- Fred Herbert Wright, Treasurer
- Robert Joseph McLaughlin, Jr., Secretary
- Stephen Philip Russell, Actuary
- Russell Key Crouch, Vice President, Special Services
- Kerry Wayne Ford, Vice President, Operations
- Danny Eugene Laffey, Vice President, Information Systems
- Charles David Emery, Chief Claims Officer
- Norman Winn Gayle III, Chief Executive Officer

- Bruce W. Heen, Vice President, Accounting and Treasurer
- Teresa S. McCoy, Vice President, Underwriting
- Bobby Leo Nolen, Executive Vice President

Officers (December 31, 2006):

- Michael Svaldi, Deputy Receiver

Directors (2005):

- John Watkins McCullough
- James Robert Watje
- David Wayne Lacefield
- Fred Herbert Wright
- Bobby Leo Nolen

Directors (2006):

- Michael Svaldi, Deputy Receiver

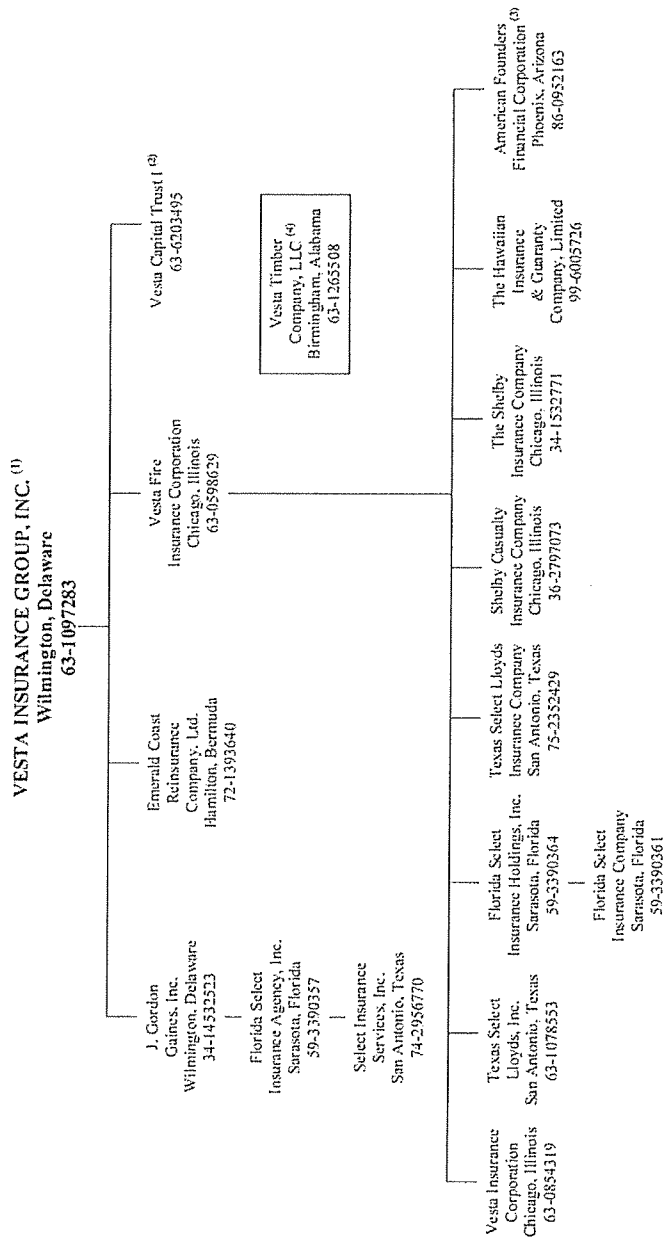
Affiliates: See Organizational Chart

9. Organizational Chart:

ANNUAL STATEMENT FOR THE YEAR 2005 OF THE FLORIDA SELECT INSURANCE COMPANY

SCHEDULE Y - INFORMATION CONCERNING ACTIVITIES OF INSURER MEMBERS OF A HOLDING COMPANY GROUP

PART 1 - ORGANIZATIONAL CHART



⁽¹⁾ No person owns 10% or more of Vesta's common stock.
⁽²⁾ Vesta Capital Trust I is a Delaware limited liability trust whose sole asset is a \$100 million debenture purchased from Vesta in January 1997.
⁽³⁾ Vesta contributed 1% of the Trust's initial capital in January 1997 and the Trust's common securities. Passive, unaffiliated investors owned the remaining 99% of the Trust's initial capital in January 1997. The Trust's common securities are traded on the New York Stock Exchange.
⁽⁴⁾ Acquired 100% of the voting power of American Founders Financial Corporation in February 2003.
⁽⁵⁾ Vesta Timber Company, LLC is owned by Vesta Fire Insurance Corporation (66.17%), The Hawaiian Insurance & Guaranty Company, Ltd. (3.40%), Shelby Casualty Insurance Company (15.46%), and The Shelby Insurance Company (11.77%).

Management: People involved with the management of Florida Select as of the date of rehabilitation include:

- David Wayne Lacefield, President
- Fred Herbert Wright, Treasurer
- Robert Joseph McLaughlin, Jr., Secretary
- Stephen Philip Russell, Actuary
- Russell Key Crouch, Vice President, Special Services
- Kerry Wayne Ford, Vice President, Operations
- Danny Eugene Laffey, Vice President, Information Systems
- Charles David Emery, Chief Claims Officer
- Norman Winn Gayle III, Chief Executive Officer
- Bruce W. Heen, Vice President, Accounting and Treasurer
- Teresa S. McCoy, Vice President, Underwriting
- Bobby Leo Nolen, Executive Vice President

Background and Events of Impact:

In 2006, Florida Select was experiencing difficulty in obtaining a Property Catastrophe Excess of Loss Reinsurance Contract (CAT Contract) to cover the risk associated with their outstanding policies. This was a factor that resulted in the receivership noted below. In addition, the Florida Office of Insurance Regulation (“OIR”) was concerned about the perceived weakness of Vesta Insurance Group, Inc. and did not allow Florida Select to record reinsurance receivable ceded to its parent.

The DFS was concerned that Florida Select was impaired due to its surplus as regards policyholders was under the minimum amount mandated by § 624.408(1)(a) Florida Statutes.

On June 28, 2006, the 126th District Court of Travis County, Texas appointed the Texas Department of Insurance as Rehabilitator of Florida Select's Texas affiliates identified below.

On June 29, 2006, the Directors of Florida Select approved a Joint Resolution of the President, Directors, and Majority Shareholders that consented to the entry of an Order Appointing the Florida Department of Financial Services as Receiver for Rehabilitation or for Liquidation.

On June 30, 2006, the Receiver filed its Petition for Order Appointing the Florida Department of Financial Services as Receiver for Purpose of Rehabilitation, Injunction and Notice of Automatic Stay with the Circuit Court, Second Judicial Circuit, Leon County, Florida.

On June 30, 2006, the Circuit Court, Second Judicial Circuit, Leon County, Florida, entered the Consent Order Appointing the Florida Department of Financial Services as Receiver of Florida Select for Purposes of Rehabilitation, Injunction and Notice of Automatic Stay.

On August 1, 2006, Vesta Fire Insurance Corporation ("Vesta Fire") was placed in receivership for purposes of liquidation by the Texas Department of Insurance (Texas Receiver). Vesta Fire owned 100% of Florida Select.

In addition, on August 1, 2006, other Florida Select affiliates including Vesta Insurance Corporation, Shelby Casualty Corporation, Shelby Insurance Company, Texas Select, Lloyds Insurance Company, and Select Insurance Services, Inc. were ordered into liquidation by the Texas Department of Insurance.

On August 8, 2006, Vesta Insurance Group, Inc. (“VIG”) entered Chapter 11 Bankruptcy proceedings. VIG owned 100% of Vesta Fire.

On August 21, 2006, the Hawaiian Insurance and Guaranty Company, Limited (“HIG”) (a Florida Select affiliate) was placed in receivership for purposes of liquidation by order of the First Circuit Court in and for the State of Hawaii.

Upon appointment, the Florida Receiver explored all available options in its efforts to ensure that Florida Select’s Florida policyholders (approximately 70,000) would be safeguarded from risk throughout the 2006 hurricane season and the course of the receivership. The alternatives reviewed included, but were not limited to, the potential purchase of the Florida Select company by another authorized insurer, as well as the potential assumption of the Florida Select policies in the state of Florida by another authorized insurer.

Despite these repeated efforts by the Receiver, no companies presented an offer to purchase Florida Select. Additionally, the financial status of the company resulted in there being insufficient capital on hand to complete an assumption of the Florida book of business. Consequently, the Receiver had no viable alternative but to continue its efforts to procure a Catastrophe Reinsurance Contract (“CAT”) to ensure the Florida policyholders were protected during the 2006 hurricane season.

The Receiver made extensive efforts to procure a CAT contract on its own. However, the financial condition and receivership status of the company resulted in any potential coverage costing in excess of \$20,000,000. That figure was cost prohibitive to the receivership and would have necessitated the imminent liquidation of the company.

During this same period of time, the Receiver entered discussions with Southern Fidelity Insurance Company (“Southern Fidelity”) regarding the efforts to safeguard Florida Select policyholders.

In discussions between the parties, Southern Fidelity was able to coordinate the arrangement of a CAT Contract for the benefit of Florida Select policyholders in the state of Florida at a substantial cost savings to the receivership. Consequently, the Receiver and Southern Fidelity entered into a Memorandum of Understanding which enabled the Receiver to secure the CAT Contract coverage and ensure policyholder risks were covered throughout the 2006 hurricane season. The premium due for the CAT Contract procured by Southern Fidelity was approximately \$12,360,200.

As part of its duties, the Receiver continued to assess the financial ability of Florida Select to renew policies ongoing coverage to existing policyholders. The Receiver was also cognizant of the fact that if Florida Select continued to have in-force policies as of June 1, 2007, a substantial premium of several million dollars would be due from Florida Select to the Florida Hurricane Catastrophe Fund (“FHCF”). In addition, the Receiver would have needed to procure additional CAT Contract coverage for the 2007 hurricane season to protect the policyholders of Florida

Select in the state of Florida. The cost for such coverage was unknown, but would most certainly have exceeded the premium paid for the coverage outlined above.

Based upon the financial circumstances of the company, the uncertainty of continuing cash flows to the company necessary to cover future costs, and the need to ensure the policyholders of Florida Select were protected, the Receiver recommended that the Court direct it to stop renewing policies and authorize it to non-renew or cancel policies of the Florida Select book of business in the state of Florida.

Upon appointment, the Florida Receiver, working with the South Carolina Department of Insurance, began efforts to identify an insurer willing to assume the Florida and South Carolina policies in order to cover the risk and prevent an uninsured loss by the policyholders.

On October 4, 2006, the South Carolina Department of Insurance approved the Assumption Agreement between Florida Select (in rehabilitation) and Capital Preferred Insurance Company for the South Carolina policies.

On October 4, 2006, the Florida Office of Insurance Regulations approved the Assumption Agreement between Florida Select (in rehabilitation) and Capital Preferred for approximately 14,000 South Carolina policies.

On October 4, 2006, the Circuit Court, Second Judicial Circuit, Leon County, Florida, approved the Motion for Order approving the Assumption Agreement between Florida Select and Capital Preferred Insurance Company

Under the Assumption Agreement, Capital Preferred assumed the South Carolina policies and the responsibility for payment of any claims under those policies which occurred on or after September 15, 2006.

On October 10, 2006, the Receiver informed the South Carolina policyholders and agents/brokers of the assumption of the South Carolina policies by Capital Preferred.

On December 12, 2006, the Circuit Court, Second Judicial Circuit, Leon County, Florida, approved the Receiver's Motion for Order Approving Plan for Transition of Florida Select Policies. Under this Order, the Receiver would work to:

- Finalize the issuance of non renewal or cancellations of Florida Select policies.
- Issue a check to Florida policyholders representing their return premium that had not been earned by Florida Select. Approximately 51,000 checks totaling over \$26.97 million were to be issued.
- Offered insurance coverage by Southern Fidelity Insurance Company.
- Informed the Florida policyholders that they were free to contact their agent to review other coverage options.

On May 4, 2007, the Florida Court approved the Receiver's Motion for Order Approving Plan for Transitions and Cancellation of Remaining Florida Select Policies.

On November 28, 2007, the Circuit Court, Second Judicial Circuit, Leon County, Florida, entered the Order Approving the Receiver's Motion for Approval of Stipulated Agreement.

As a result of the approval of the Stipulated Agreement by the respective receivership courts, the following distributions were able to be made to the Collective Estates:

- a. The sum of \$2,000,000 was distributed from the Escrow Account to the Florida Receiver for the receivership of Florida Select;
- b. The sum of \$2,000,000 was distributed from the Escrow Account to the Hawaii Liquidator for the receivership of HIG; and
- c. The sum of \$10,000,000 was distributed from the Escrow Account to the Texas Liquidator for the five Texas Companies in receivership;
- d. The sum of \$16,000,000 will be distributed from the Escrow Account to the Hawaii Liquidator for the receivership of HIG;
- e. The sum of \$13,500,000 will be distributed from the Escrow Account to the Florida Receiver for the receivership of Florida Select;
- f. The balance of funds remaining in the Escrow Account will be allocated between or among the Texas Companies in receivership;
- g. The Texas Receiver agrees to reserve an amount totaling \$6,500,000 as a restricted asset on Vesta Fire books and records for the benefit of Florida Select. These funds are subject to release to Florida by Texas under certain conditions.

The Stipulated Agreement was subsequently approved by the respective receivership courts in Texas and Hawaii.

On June 27, 2008, the Receiver engaged an expert to provide accounting services including:

- Determine the amount due to Florida Select as of June 30, 2006 by unaffiliated reinsurers for ceded unearned premiums.
- Determine the amount due to Florida Select for ceded reserve benefits by Vesta Fire.
- Determine the amount due to Florida Select for ceded reserve benefits by unaffiliated reinsurers.
- Determine the amount of intercompany balances due to or payable by Florida Select to or from Florida Select's parent or another affiliated entity.

On February 13, 2008, the accounting expert issued a report stating that Florida Select was owed \$29,679,175 as of September 30, 2007 which is comprised of unearned premiums at June 30, 2006, amounts related to the commutation of a net quota share reinsurance treaty as of June 30, 2006, paid losses and loss adjustment expense related to the Vesta Agreement and Catastrophe Excess of Loss Reinsurance Agreements. In addition, the accounting expert noted that Florida Select was owed \$32,129,492 by the Florida Hurricane Catastrophe Fund for paid losses and ceded losses for 2006 and 2007.

On January 23, 2009, the Florida Court approved the Motion for Approval of Settlement and Release Agreement between the Receiver of Florida Select and the Insurance Commissioners of the State of Hawaii and Texas.

On February 6, 2009, the Receiver's Motion for Approval of Settlement Agreement with Florida Select Insurance Agency, Inc. ("FSIA") was approved by the Circuit Court, Second Judicial Circuit, In and For Leon County, Florida. FSIA asserted certain claims against Florida Select as party to a Managing General Agency Agreement. The Settlement Agreement required the Receiver to pay \$743,370 compared to a demand of approximately \$3 million.

On June 24, 2009, the Motion for Approval of Settlement Agreement Regarding Amounts Due to Florida Select by the Florida Hurricane Catastrophe Fund ("FHCA") with the State Board of Administration of Florida ("SBA") was approved by the Circuit Court of the Second Judicial Circuit, In and For Leon County, Florida. The SBA and Receiver agreed to release, acquit, and forever discharge each other from all manner of claim, in whole or in part, as it pertains to the 2004 and 2005 Contract years of Florida Select.

On October 13, 2009, the Receiver's Status Report and Motion for Plan of Rehabilitation was approved by the Circuit Court of the Second Judicial Circuit, In and For Leon County, Florida.

On October 13, 2009, the Circuit Court of the Second Judicial Circuit, In and For Leon County, Florida, approved a Plan of Rehabilitation for Florida Select that:

- 1) Established a Claim Filing Deadline Bar Date of 180 days under Chapter 631, Florida Statutes that stated that any claim filed after the 180 days would be deemed denied and barred unless otherwise ordered by the court.
- 2) Maintained that Florida Select remain in rehabilitation status.

On September 23, 2011, the Florida Secretary of State administratively dissolved Florida Select.

“The Computer Science Corporation Litigation”

While serving as the Receiver, the Computer Science Corporation (“CSC”) requested payment of invoices totaling \$1.528 million for services rendered to Florida Select.

On March 24, 2008, the Circuit Court, Second Judicial Circuit, Leon County, Florida, entered its Order Denying Petition to Enforce Ratified and Assumed Contract which denied CSC from collection of the \$1.528 million.

On April 1, 2008, the Circuit Court, Second Judicial Circuit, Leon County, Florida, issued a Final Judgment as to Petition of Computer Science Corporation which was subsequently appealed by CSC to the First District Court of Appeals.

On February 20, 2009, the First District Court of Appeals affirmed the lower court’s Final Judgment.

On April 2, 2009, a subsequent motion by CSC for rehearing, rehearing en banc and written opinion was denied by the First District Court of Appeals. The claim by CSC for payment of \$1.528 million by the Receiver was resolved and closed without payment.

“Unearned Commissions”

During the course of the receivership, the Receiver recovered \$1,028,300.00 of \$1,188,565 in outstanding unearned commission from agents that were associated with the cancellation of Florida Select policies by the Receiver.

Underwriting Results:

According to Florida Select's Annual Statements the company experienced the following underwriting results for the years 2002, 2003, 2004, 2005, and 2006:

	<u>Premiums Earned</u>	<u>Underwriting Deductions</u>	<u>Underwriting Gain (Loss)</u>	<u>Net Income (Loss)</u>
2002	\$ 2,559,934	\$ 2,540,289	\$ (19,645)	\$ 2,963,195
2003	\$ 1,876,825	\$ 1,983,892	\$ (107,067)	\$ 868,947
2004	\$ 1,538,762	\$ 1,757,266	\$ (218,504)	\$ 564,278
2005	\$ 1,841,406	\$ 1,996,142	\$ (154,736)	\$ 528,428
2006	\$ 32,488,191	\$ 33,727,784	\$ (1,239,593)	\$ (1,804,681)

As noted, Florida Select incurred underwriting losses.

Reinsurance:

The Florida Select reinsurance program consisted of the following coverages:

- Participation in the Florida Hurricane Catastrophe Fund ("FHCF");
- Excess of loss coverages (multiple layers) with unaffiliated reinsurers that coordinated with the FHCF coverage;
- Quota share reinsurance with unaffiliated reinsurers for losses not covered by the FHCF, excess of loss coverages and any other inuring reinsurance; and
- Pro rata reinsurance agreement between Vesta Fire and Florida Select (the "Vesta Agreement").

Vesta Agreement

To summarize, the Vesta Agreement ceded to Vesta 100% of Florida Select's remaining premiums and losses not otherwise ceded to the afore-described FHCF and the unaffiliated excess of loss reinsurers and quota share reinsurers. In addition, the Vesta Agreement also ceded the net loss and allocated loss adjustment expense ("ALAE") reserves, including IBNR, as of December 31, 2000. Therefore, beginning January 1, 2001 Florida Select ceded 100% of its premiums and losses directly to a combination of unaffiliated reinsurers with the remainder ceded to Vesta Fire in accordance with the Vesta Agreement.

The following were selected terms and conditions in the Vesta Agreement:

- Effective January 1, 2001, continuous until December 31, 2003.
- Ceded 100% of net written premiums (gross premiums less inuring reinsurance premiums).
- Ceded 100% of the net case and IBNR loss ALAE reserves as of December 31, 2000.
- Provided for Vesta Fire to pay a 30% ceding commission to Florida Select.
- Reinsured a pro rata participation of 100% of the ultimate net loss resulting from any loss or losses occurring during the term of this agreement under any and all policies inforce, issued, renewed or assumed after the effective date and any unpaid losses outstanding at the effective date on policies written, inforce, issued, renewed or assumed prior to the effective date and classified as homeowners or dwelling fire business, including ancillary coverages.

The Vesta Agreement was scheduled to terminate on December 31, 2003; however, subsequent to December 31, 2003, Vesta Fire and Florida Select continued to operate in a manner consistent with the terms of the Vesta Agreement.

Furthermore, in March 2006 Vesta Fire prospectively terminated the Vesta Agreement effective February 1, 2006 and returned to Florida Select the unearned premiums as of the effective date of the termination.

As noted above, Vesta Fire owned 100% of Florida Select and, on August 1, 2006, Vesta Fire was placed in receivership for purposes of liquidation by the Texas Department of Insurance.

The financial difficulties of Vesta Fire and the inability to honor the Vesta Agreement was a prime factor in the insolvency of Florida Select.

Florida Hurricane Catastrophe Fund ("FHCF")

Florida Select participated in the Florida Hurricane Catastrophe Fund as follows:

<u>Policy Year</u>	<u>Participation %</u>	<u>FHCF Attachment</u>	<u>FHCF Maximum Payment</u>
6/1/04 to 5/30/05	90%	\$22,779,879	\$76,053,933
6/1/05 to 5/30/06	90%	\$21,765,911	\$70,589,644
6/1/06 to 5/30/07	90%	\$25,137,380	\$67,190,798

Catastrophe Excess of Loss Treaties

Florida Select also participated as a named party (with Vesta Fire and other Vesta subsidiaries) in Catastrophe Excess of Loss reinsurance treaties as follows:

Policy year July 1, 2004 to June 30, 2005:

Layer 1	\$7.5 million	XS	\$15 million
Layer 2	\$17.5 million	XS	\$22.5 million
Layer 3	\$30 million	XS	\$40 million
Layer 4	\$40 million	XS	\$70 million

Policy year July 1, 2005 to June 30, 2006:

Layer 1	\$15 million	XS	\$20 million
Layer 2	\$25 million	XS	\$35 million
Layer 3	\$40 million	XS	\$60 million
Layer 4	\$50 million	XS	\$100 million

Based on review of the documents, the 2004 Layer 1 was only 25.5 % subscribed and the 2005 Layer 1 was only 90% subscribed and that any losses relating to any undersubscribed layers would become losses attributed to the net account coverage recoverable under the Quota Share Reinsurance Treaties discussed later herein.

Florida Select had no excess of loss coverage in place for the period July 1, 2006 through August 1, 2006. The Receiver facilitated the purchase of excess of loss coverage for the period September 1, 2006 to June 1, 2007.

Quota Share Reinsurance Agreements

Historically Florida Select entered into Quota Share Net Account Cover reinsurance agreements with unaffiliated third party reinsurers to reinsure loss exposures not subject to other reinsurers, such as the excess of loss reinsurers and the FHCF, with the remaining exposure ceded to Vesta under the Vesta Agreement. Such net account covers are common in the industry and provide reinsurance for the amount below the attachment point for the excess of loss treaties (\$15 million of the July 1, 2004 to June 30, 2005 year and \$20 million for the July 1, 2005 to June 30, 2006 year).

The unaffiliated quota share agreements for the periods prior to July 1, 2005 were commuted on a cut off basis and Florida Select assumed the reserves previously ceded to those reinsurers. Therefore, Florida Select was responsible for any adverse development on losses occurring prior to July 1, 2005. However, Vesta Fire assumed the risk for such adverse loss development under the Vesta Agreement.

For the period July 1, 2005 to November 30, 2005, unaffiliated reinsurers assumed a 50% quota share of the net account coverage with the remaining 50% ceded to Vesta Fire under the Vesta Agreement. From December 1, 2005 to January 31, 2006, unaffiliated reinsurers assumed 75% of the net account coverage with the remaining 25% ceded to Vesta Fire under the Vesta Agreement.

As described previously herein, as of February 1, 2006 Vesta Fire terminated the net account coverage under the Vesta Agreement and made a payment to Florida Select of the unearned premiums as of that date. However, the unaffiliated reinsurers continued to participate at a 75%

quota share through June 30, 2006. The unaffiliated quota share agreements were not renewed after June 30, 2006.

Thus for the period February 1, 2006 to June 30, 2006 Florida Select was uninsured for 25% of the net account exposure and for periods subsequent to June 30, 2006 the Receiver had no quota share coverage in place.

Financial:

Operations:

Florida Select was required to maintain a minimum statutory surplus in accordance with § 624.408(1)(a) Florida Statutes. The minimum surplus was \$4 million. A comparison of such reported amounts is summarized in the following table.

<u>Policyholders' Surplus (Deficit)</u>	
<u>December 31</u>	<u>As Reported</u>
2002	\$17,786,529
2003	\$18,829,072
2004	\$17,800,614
2005	\$19,748,537
2006	\$ (713,010)

Conclusion:

Florida Select was engaged in the writing of insurance coverage for homeowners multi-peril coverage. Florida Select's offices were located Sarasota, Florida. Florida Select wrote insurance coverage in Florida and in South Carolina and was a wholly owned subsidiary of Vesta Fire.

Florida Select was statutorily insolvent in 2006 and perhaps earlier. The decline in statutory surplus was primarily due to the following:

- The financial instability of its parent, Vesta Fire.
- The inability of Vesta Fire to fund and comply with the terms of the reinsurance contract with Florida Select.
- Florida Select's inability to obtain a Property Catastrophe Excess of Loss Reinsurance Contract to cover the risk associated with the outstanding policies of Florida Select in order to safeguard policyholders.

These factors impacted the solvency of Florida Select and, Florida Select could not maintain the minimum surplus as regards policyholders mandated by § 624.408(1)(a) Florida Statutes.

References:

- Florida Select's 2005-2006 Annual Statements
- Consent Order Appointing the Florida Department of Insurance as Receiver for Purposes of Rehabilitation, Injunction and Notice of Automatic Stay, signed and dated June 30, 2006.
- Files maintained by the Department of Financial Services, Division of Rehabilitation and Liquidation.

- The Assumption Agreement between Florida Select (in rehabilitation) and Capital Preferred Insurance Company.
 - The Motion for Order Approving the Assumption Agreement, dated October 4, 2006.
 - The Order approving the Receiver's Motion for Order Approving Plan for Transition and Cancellation or Remaining Florida Select Policies.
 - The Stipulation Agreement, dated November 28, 2007.
 - The Motion for Approval of Settlement and Release Agreement between the Receiver, Florida Select, and the Insurance Commissioners of Hawaii and Texas, dated January 23, 2009.
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