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**STATE OF ALABAMA
DEPARTMENT OF INSURANCE
MONTGOMERY, ALABAMA**

REPORT ON EXAMINATION

as of

DECEMBER 31, 2001

of

**SOUTHERN GUARANTY INSURANCE
COMPANY**

MONTGOMERY, ALABAMA

PARTICIPATION:

Alabama

EXAMINATION AFFIDAVIT

**STATE OF ALABAMA
COUNTY OF MONTGOMERY**

Rex H. Newborn being first duly sworn, upon his oath deposes and says:

That he is an examiner appointed by the Commissioner of Insurance for the State of Alabama;

That an examination was made of the affairs and financial condition of Southern Guaranty Insurance Company for the period of January 1, 1997 through December 31, 2001;

That the following 35 pages constitute the report thereon to the Commissioner of Insurance of the State of Alabama;

And, that the statements, exhibits, and data therein contained are true and correct to the best of his knowledge and belief.



Rex H. Newborn
Examiner-in-charge

Subscribed and sworn to before the undersigned authority this 13th day of November 2002.



(Signature of Notary Public)

Melissa D WATSON _____, Notary Public
Printed name

in and for the State of Alabama

My commission expires _____ My commission expires 4/24/06.

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Montgomery, Alabama
October 30, 2002

Honorable Diane Koken
Chairman, Examination Oversight Committee
Commissioner, Pennsylvania Insurance Department
1326 Strawberry Square
Harrisburg, Pennsylvania 17120

Honorable Alfred W. Gross
Secretary Southeastern Zone
Commissioner, Virginia Bureau of Insurance
P.O. Box 1157
Richmond, Virginia 23218

Honorable D. David Parsons
Commissioner of Insurance
State of Alabama
Post Office Box 303350
Montgomery, Alabama 36130-3350

Dear Commissioner Parsons:

Pursuant to your instructions and in compliance with the statutory requirements of the State of Alabama and the resolutions adopted by the National Association of Insurance Commissioners, an examination has been made of the affairs and condition of

**Southern Guaranty Insurance Company
Montgomery, Alabama**

as of December 31, 2001, at its home office located at 2545 Taylor Road, Montgomery, Alabama 36117. The report of examination is submitted herewith.

Where the term, Company, appears herein without qualification, it is synonymous with Southern Guaranty Insurance Company.

SCOPE OF EXAMINATION

The examination reported herein covers the period from December 31, 1996 through December 31, 2001, and has been conducted by examiners representing the Alabama Department of Insurance. Events subsequent to December 31, 2001, have been reviewed as required and are reported herein as deemed appropriate.

The Company has been examined in accordance with the statutory requirements of the Alabama Insurance Code and the regulations and bulletins of the Alabama Department of Insurance; in accordance with the applicable guidelines and procedures of the NAIC; and in accordance with generally accepted examination standards.

The examination included a general review of the Company's operations, administrative practices and compliance with statutes and regulations. Income and disbursement items were tested for selected periods. Assets were verified and valued and all known liabilities were established or estimated as of December 31, 2001, as shown in the financial statements contained herein.

In compliance with requirements of the Alabama Department of Insurance, the President and Treasurer of the Company executed a letter of representation certifying that the Company had valid title to all its reported assets, and that it did not have unreported liabilities as of December 31, 2001.

Within this report, discussion of the Company's accounts has been confined to those items for which a material change in the financial statements has been noted or for which comments and/or recommendations have been made.

ORGANIZATION AND HISTORY

The Company's charter derives from the incorporation of the United Security Fire Insurance Company (USFIC) in Birmingham, Alabama on July 19, 1963. Existing records indicate that USFIC was dormant until 1968, when it merged with Southern Guaranty Insurance Company of Mississippi (SGIC), effective January 1, 1968.

The merger effected the redomestication of SGIC to Alabama under the Certificate of Incorporation of USFIC. The name, By-Laws and business of SGIC were retained by the surviving corporation; and, the Certificate of Incorporation was amended to authorize 1,000,000 shares of one-dollar par value common stock. The home office of the Company was moved to Montgomery, Alabama, and has remained in Montgomery through the date of this report.

Subsequent to the merger, the Company's paid up capital amounted to \$400,000, consisting of 400,000 shares of one-dollar par value common stock, derived from the conversion of the issued and outstanding common stock of SGIC. Approximately 80%

of said capital stock was owned by Alabama Farm Bureau Mutual Casualty Insurance Company, Inc. Stock dividends in 1972 and 1977 increased the Company's paid up capital to \$500,000 and \$600,000, respectively.

During 1980, Fireman's Fund Insurance Company (FFIC), Novato, California acquired 100% ownership of the Company. Paid up capital was increased to \$1,000,000, in 1981. Also in 1981, the Company formed two wholly-owned subsidiaries: Southern Guaranty Insurance Company of Georgia (SGGA), and Southern Fund Insurance Corporation (SFIC), an Alabama corporation.

On July 1, 1988 the Company was acquired by Winterthur U.S. Holdings, Inc. (WUSH), a Delaware corporation ultimately controlled by Winterthur Swiss Insurance Company, Winterthur, Switzerland.

In 1989, the Company's authorized common stock was increased to 5,000,000 shares, and paid up capital was increased to \$1,250,000, by means of a stock dividend funded from unassigned surplus. By the same method, paid up capital was increased to \$1,500,000 in 1990, and to \$2,000,000 in 1994. As of December 31, 1996, the Company's capital stock consisted of 2,000,000 shares of one-dollar par value common stock, issued and outstanding and owned by WUSH.

In April of 1995, the Company acquired 100% ownership of Jefferson Pilot Fire and Casualty Company (JPFC), Greensboro, North Carolina and its wholly-owned subsidiary, Southern Fire and Casualty Company (SFCC), a Tennessee chartered company. Subsequently, the name of JPFC was changed to Southern Pilot Insurance Company (SPIC). From 1994 through 1996, the Company received \$55,000,000 in surplus contributions from its parent company. The amount of the surplus contributions approximated the cost of the acquisition of JPFC.

In September of 1995, the Company sold SFIC to Blue Ridge Insurance Company (BRIC), Simsbury, Connecticut. BRIC is affiliated with the Company through the WUSH holding company system, but there is no direct ownership relationship between BRIC and the Company.

On December 15, 1997, Credit Suisse Group, Switzerland, acquired Winterthur Swiss Insurance Company (WSIC) and became the entity with ultimate control of the Company. WSIC is the parent of Winterthur U.S. Holdings, Inc., which owns 100% of the Company.

During the examination period the Company entered into 100% quota share reinsurance agreements with its wholly-owned subsidiary, Southern Pilot Insurance Company (SPIC), and Southern Fire and Casualty Company (SFCC), the wholly-owned subsidiary of SPIC. As a result of this reinsurance, and in order to off-set liabilities assumed, the Company received approximately \$37,000,000 in assets.

GROWTH OF THE COMPANY

The following schedule presents financial data, which reflect the growth of the Company for the years indicated:

<i>Year</i>	<i>Gross Premiums Written</i>	<i>Admitted Assets</i>	<i>Liabilities</i>	<i>Policyholders' Surplus</i>
1996	110,937,287	196,959,526	115,028,244	81,931,282
1997	118,390,449	208,908,253	123,510,787	85,397,466
1998	113,444,869	209,133,187	121,088,227	88,044,960
1999	138,968,664	246,613,812	157,566,771	89,047,041
2000	133,717,534	251,203,660	160,482,197	90,721,463
2001	142,810,472	257,874,860	165,813,164	92,061,696

Data for the years 1996 and 2001 are per examination. Data for the remaining years, were obtained from the Company's Annual Statements.

TERRITORY

As of December 31, 2001, the Company was licensed to transact insurance business in the following jurisdictions:

Alabama	Arkansas
Florida	Georgia
Mississippi	North Carolina
South Carolina	Tennessee

The Certificates of Authority from the respective jurisdictions were inspected and found to be in effect at December 31, 2001.

STATUTORY DEPOSITS

In compliance with statutory requirements for transacting insurance business in the respective jurisdictions, the Company had the following securities on deposit at December 31, 2001:

(continued next page)

Deposits Held for the Benefit of Policyholders, Claimants and Creditors of the Company:

	<u>Par Value</u>	<u>Statement Value</u>	<u>Market Value</u>
<u>Alabama</u>			
SouthTrust Bank, U. S. Treas. Note, 5.50%, due 8/15/2028	\$1,200,000	\$1,222,250	\$1,162,500
<u>Arkansas</u>			
Regions Bank, U. S. Treas. Note, 6.25%, due 2/15/2007	250,000	273,491	270,158
<u>Georgia</u>			
Wachovia Bank, U. S. Treas. Note, 6.25%, due 2/15/2007	200,000	218,793	216,126
<u>North Carolina</u>			
Wachovia Bank, U. S. Treas. Note, 7.25%, due 5/15/2004	100,000	99,831	108,719
<u>Tennessee</u>			
SouthTrust Bank, FFCB, 5.24%, due 10/1/2008	2,000,000	1,998,810	1,982,160
SouthTrust Bank, U. S. Treas. Note, 6.125%, due 8/15/2007	3,000,000	3,326,078	3,227,820
SouthTrust Bank, U. S. Treas. Note, 6.00%, due 8/15/2009	9,000,000	10,033,085	9,593,460
SouthTrust Bank, U. S. Treas. Note, 5.625%, due 5/15/2008	<u>3,300,000</u>	<u>3,584,316</u>	<u>3,458,829</u>
Totals	<u>\$19,050,000</u>	<u>\$20,756,654</u>	<u>\$20,019,772</u>

All statutory deposits were confirmed as of December 31, 2001, by written correspondence with the respective custodians.

HOLDING COMPANY AND AFFILIATES

Holding Company Registration and Reporting

The Company is deemed to be subject to the Alabama Insurance Holding Company Regulatory Act of 1973, as defined in Section 27-29-1, *Code of Alabama*, 1975. The Company is responsible for holding company registration and periodic informational filings with Alabama Department of Insurance, in accordance with Section 27-29-4, *Code of Alabama*, 1975, and Alabama Department of Insurance *Regulation Number 55*.

Holding Company filings and amendments to registration statements made on behalf of the Company and its affiliates, for the years under examination, were reviewed. Said

filings and amendments were found to be substantially complete and to reflect the required disclosures.

Organization Chart

The chart on the following page depicts the insurance holding company system with which the Company was affiliated as of December 31, 2001.

(Continued next page)

Agreements with Affiliates

At December 31, 2001, the following agreements (exclusive of reinsurance agreements) were in effect between the Company and certain of its affiliates. The Company has 100% reinsurance agreements with its three downstream affiliates. See "Reinsurance Assumed" for further discussion.

Management Agreement – Southern Guaranty Insurance Company of Georgia (SGGA)

The Company has had an agreement in effect since 1981 to provide SGGA with the facilities, materials and services necessary to transact the business of insurance. In consideration for such services, the Company receives a fee equal to 3% of the premium entered into the statistical records of SGGA. The Company also agrees to provide administrative and clerical investment functions to SGGA in return for a quarterly fee of .25% of SGGA's average invested assets held during the respective quarter.

This agreement was amended on December 29, 1989 to expand on certain provisions contained in the original agreement. The Company agrees to provide SGGA with the facilities, materials and experienced personnel necessary to manage its unallocated claims adjustment service. In consideration for such services, SGGA agrees to pay the Company an amount equal to the expenses incurred which may include, but is not limited to, the actual cost of the Georgia claims office, plus a reasonable allocation of corporate claims and other overhead expenses.

On February 12, 1996, the agreement was amended to provide assurance to SGGA that it can continue operation in the event that the Company is unable to continue to manage SGGA. The specific terms of the amendment deal with, in the event of termination of the agreement, the Company's continued maintenance of records and record keeping functions until SGGA can assume such functions on its own behalf.

Premium Finance Management Agreement – SGGA

The Company entered into an agreement with SGGA, effective December 31, 1990, to provide SGGA with the facilities, materials, and experienced personnel necessary to manage SGGA's premium finance arrangements. In consideration for such services, the Company receives a fee equal to 50% of the finance and service charge income entered into the statistical records of SGGA.

Investment Management Agreement – Southern Fire & Casualty Company (SFCC)

The Company entered into an agreement with SFCC, effective April 1, 1995, to manage SFCC's investment portfolio and to buy and sell stocks, bonds, warrants, options, debentures and other securities for SFCC. In return for its services, the Company receives an annual fee equal to one-tenth of 1% of SFCC's average invested assets held

during the year due and payable within forty-five days after the close of each calendar year. In the event that the expense incurred by the Company exceeds the specified fee, both parties agree that the excess amount would be determined and paid by SFCC to the Company annually.

Investment Management Agreement – Southern Pilot Insurance Company (SPIC)

The terms of this agreement are essentially the same as per the investment management agreement with SFCC.

Expense Allocation Agreement – SPIC, SGGGA, SFCC

The Company, SPIC, SGGGA, and SFCC entered into an expense allocation arrangement, effective January 1, 1998, whereby each company would bear its proportionate share of "Other Underwriting Expenses" (Annual Statement Underwriting & Investment Exhibit Part 4 – Expenses, Column 2, lines 3 through 17 and 21), collectively incurred by the companies, based upon the percentage share that each company's direct premiums bear to the total direct premiums for all the companies. These expenses would not include net commission and brokerage, and taxes, licenses and fees that are specific to each company.

Additionally, the companies entered into an expense allocation arrangement effective January 1, 1998, whereby each company would bear its proportionate share of "Unallocated Loss Adjustment Expenses" (Annual Statement Underwriting & Investment Exhibit Part 4 – Expenses, Column 1, lines 3 through 17 and 21), collectively incurred by the companies, based upon the relationship that each company's direct incurred loss, as might be adjusted, bears to total direct incurred loss of the companies.

Management Services Agreement – SFCC

The Company agreed to provide executive, management and/or other personnel, facilities, services, equipment and supplies to SFCC sufficient to conduct its operations.

In order to assure SFCC of continued operations in the event that the Company, for whatever reason, is unable to continue providing other management services under the agreement, the Company agrees to provide SFCC with continued access to and processing of their computer records until such time as arrangements can be made for the records to be transferred to a system which can process the records for SFCC.

Management Services Agreement – SPIC

The terms of the management services agreement are substantially the same as the Company's management services agreement with SFCC.

Lease Agreement – SPIC

The Company entered into a lease agreement, effective November 1, 1996, with SPIC. The Company agrees to lease to SPIC, office space comprised of the entire first and second floors of the Southern Pilot Building, located at 717 Green Valley Road, Greensboro, North Carolina. The lease term was for a period of six years with an annual rent of \$420,000 payable in monthly installments of \$35,000. In addition to the annual rent, SPIC agreed to pay the Company for expenses of maintenance, upkeep, taxes, fees, etc. applicable to land and building known as the Green Valley Office Park. This lease was terminated effective December 31, 1999. As of the date of this report, SPIC continued to occupy the aforesaid facilities under the terms of the "Management Services Agreement" previously discussed.

Lease Agreement – SGGA

The Company entered into a lease agreement, effective August 1, 1990, with SGGA. The Company agreed to lease a 5,604 square foot building located at 1922 Northlake Parkway, Tucker, Georgia. The initial lease was for a period of ten years beginning October 1, 1990 and terminating on September 30, 1999. The Company agreed to pay SGGA annual rent of \$60,000 payable in monthly installments of \$5,000. The Company agreed to pay all taxes, assessments and insurance. The Company also agreed to pay and hold SGGA free and harmless from bills or assessments for light, heat, water, gas, sewer rentals or charges and any other expenses arising out of or incidental to the occupancy of the leased premises. The Company agreed to repair and restore all improvements on the premises following any damage, loss or destruction of the premises.

The agreement was renewed for another ten-year term on August 19, 1999.

Tax Allocation Agreement – Winterthur U. S. Holdings, Inc. (WUSH) and Subsidiaries

The Company's federal income tax returns are consolidated with Winterthur U. S. Holdings, Inc. and its subsidiaries, under a Tax Allocation Agreement, effective since July, 1988.

Termination of the agreement, relative to a given subsidiary, is subject to U. S. Treasury Regulations and the approval of the Commissioner of Internal Revenue. Otherwise, termination may occur by written agreement of the parties, if the subsidiary's affiliation ceases for any reason or if the subsidiary is not included in the consolidated return for any taxable year.

Dividends to Stockholders

During the period under examination the following cash dividends were paid to stockholders:

<u>Year</u>	<u>Dividends Paid</u>
1997	\$3,000,000
1998	\$ 750,000
1999	\$3,000,000
2000	\$5,000,000
2001	\$5,000,000

Dividends paid appeared to be in accordance with Alabama statutes and regulations.

CORPORATE RECORDS

The Company's Articles of Incorporation, By-Laws and amendments thereto were inspected and found to provide for operation of the Company in accordance with Alabama statutes and regulations and with accepted corporate practices.

Minutes of the meetings of the stockholders, board of directors and committees of the Company, from December 31, 1996 through the most recent meetings recorded, were reviewed. The minutes appeared to be complete and to adequately document the actions of the respective governing bodies.

MANAGEMENT AND CONTROL

Stockholder

The sole stockholder of the Company is Winterthur U. S. Holdings, Inc., a Delaware corporation. The ultimate controlling entity is Credit Suisse Group of Switzerland.

Board of Directors

The Company's By-Laws provide that its property and business shall be managed by a board of directors consisting of not less than five nor more than twelve persons, at least one-third of whom shall be residents of Alabama. Directors are elected at the annual meeting of the stockholder and serve until their successors are elected and qualified.

The following (on the following page) directors were elected by the stockholder and were serving at December 31, 2001:

<u>Director/Residence</u>	<u>Principal Occupation</u>
Jimmy Larry Ridling Pike Road, Alabama	Chairman of the Board, President, and CEO, Company
Henry Pearce Draughon, Jr. Montgomery, Alabama	Senior Vice President, General Counsel, and Secretary, Company
Guy Francis Green, Jr. Pike Road, Alabama	Senior Vice President and Regional Executive, Company
Charles Lee Keith Montgomery, Alabama	Senior Vice President and Chief Investment Officer, Company
Roger Melvin Droste Montgomery, Alabama	Senior Vice President and Senior Home Office Underwriting/Marketing Executive, Company

Committees

The following committees were appointed by the board of directors and were serving at December 31, 2001:

<u>Committee</u>	<u>Members</u>
Executive Committee	Jimmy Larry Ridling Guy Francis Green, Jr. Henry Pearce Draughon, Jr.
Benefits Committee	Guy Francis Green, Jr. Henry Pearce Draughon, Jr. Carlene Winifred Payne Charles Lee Keith
Human Resource Committee	Jimmy Larry Ridling Guy Francis Green, Jr. Carlene Winifred Payne
Underwriting Committee	Roger Melvin Droste Jimmy Larry Ridling Guy Francis Green, Jr. Ben Maurice Spillers

(continued next page)

Reserve Committee

Jimmy Larry Ridling
Guy Francis Green, Jr.
Henry Pearce Draughon, Jr.
Roger Melvin Droste
Ben Maurice Spillers

Officers

The Company's By-Laws provide that its principal officers shall be a chairman of the board, a president, a secretary, a treasurer and such other officers as the board of directors may determine, and for such terms, authority and duties as may be determined by the appointment. Any two or more offices may be held by the same person, except the offices of president and secretary.

The following officers were elected by the board of directors, and were serving at December 31, 2001:

Jimmy Larry Ridling	President and Chief Executive Officer
Sharon Eleais Brown	Vice President – Administration and Centralized Services
Stephen Hart Cone	Vice President and Regional Personal Lines Executive
Larry Fay Criswell	Vice President and Regional Claims Executive
Lewis Pitts Culpepper, Jr.	Vice President and Regional Marketing Executive
Henry Pearce Draughon, Jr.	Senior Vice President and General Counsel and Secretary
Roger Melvin Droste	Senior Vice President and Senior Home Office Underwriting/Marketing Executive
Guy Francis Green, Jr.	Senior Vice President and Regional Executive
Ronnie Dale Hinton	Vice President and Information Services Executive
Jack Steven Hooks	Vice President and Regional Claims Executive
Charles Lee Keith	Senior Vice President and Chief Investment Officer
Dale Luther Kocher	Vice President and Regional Marketing Executive
Walter Rushing Meriwether	Vice President – Financial & Regulatory Reporting, Treasurer and Assistant Secretary
Carlene Winifred Payne	Vice President – Human Resources
Michael Francis Roberts	Vice President and Regional Personal Lines Executive
Bert Charles Shephard	Vice President and Regional Commercial Lines Executive
Ben Maurice Spillers	Senior Vice President and Regional Executive
Gerald Edward Willis	Vice President and Regional Commercial Lines Executive

Conflict of Interest

The Company requires that its directors, officers and key personnel execute conflict of interest statements annually. These statements provide for disclosure, to the board of directors, of any conflicts or potential conflicts which might exist between the interest of the Company and the interest of the signatories.

Conflict of interest statements relative to the years under examination were signed by all subject personnel. No conflicts or potential conflicts of a material nature were disclosed, and none were indicated by examination findings.

FIDELITY BOND AND OTHER INSURANCE

The Company was insured under a financial institution bond issued by National Union Fire Insurance Company of Pittsburgh, Pennsylvania at December 31, 2001. The fidelity bond coverage was found to be in excess of the NAIC's suggested minimum amount. The policy provided coverage for loss resulting directly from dishonest or fraudulent acts committed by employees, officers, or directors.

In addition to the above, the Company had the following coverages in effect at December 31, 2001, under policies issued directly to the Company or as a named insured under policies issued to an affiliate.

- Professional Liability
- Boiler and Machinery
- Commercial Property
- General Liability
- Inland Marine
- Commercial Umbrella
- Worker's Compensation and Employer's Liability
- Business Automobile Insurance

The coverages and limits of the Company's insurance were reviewed and were deemed to adequately protect the Company's interest.

EMPLOYEE AND AGENTS' WELFARE

The Company utilizes only independent agents and provides no benefits for agents. Benefits provided by the Company to its employees included the following at December 31, 2001:

(continued next page)

- Health and life insurance
- Short and long-term disability
- Paid vacation, sick leave and holidays
- Deferred compensation plan
- Defined benefit retirement plan
- Incentive compensation plan
- Incentive savings plan (401K plan)
- Pension restoration plan

Benefits provided by the Company appeared to be in accordance with usual practices within the insurance industry.

REINSURANCE

Reinsurance Assumed

The Company reinsures 100% of the business of its three downstream affiliates. The reinsurance agreements are described as follows.

The Company has had a reinsurance agreement with its wholly-owned subsidiary, Southern Guaranty Insurance Company of Georgia (SGGA) since 1981. Said reinsurance agreement provides for the Company to receive 100% of the premiums and assume 100% of the liabilities on all business written by SGGA. Liabilities are to include, but are not limited to, direct losses incurred, including IBNR reserves, direct loss adjustment expenses incurred and any unallocated claims adjustment service fees charged by the Company under separate Agreement on those policies of insurance issued by SGGA. In return, SGGA receives a 3.25% override commission. Either party may terminate the agreement upon 120 days notice, but in the event of termination, no return of override commissions will be made. The contract contains the usual provisions relating to insolvency. The Company also provides management services to SGGA. See "Holding Company and Affiliates," subsection "Agreements with Affiliates," for further discussion on this topic.

Effective January 1, 1999, the Company entered into a quota-share agreement with its wholly-owned subsidiary, Southern Pilot Insurance Company (SPIC) whereby the Company shall assume 100% of SPIC's liabilities and obligations arising out of or in connection with the Covered Business. This includes the assumption by the Company reserves for unpaid losses (including incurred but not reported and loss adjustment reserves) of SPIC arising out of policies of insurance issued or assumed by SPIC prior to the effective date of this Agreement.

Effective January 1, 2000, the Company entered into a quota-share agreement with Southern Fire & Casualty Company (SFCC), a wholly-owned subsidiary of SPIC, which is

substantially the same as the agreement between the Company and SPIC, described above.

The Company also participates in several assigned risk pools. The amounts of premiums and liabilities assumed from these pools were not material, except as respects the assumptions from the National Workers Compensation Reinsurance Pool (NWCRP) and North Carolina Reinsurance Facility (NCRF). At December 31, 2001, premiums assumed from NWCRP amounted to \$253,000 and losses and loss adjustment expense reserves amounted to \$6,561,000 and premiums assumed from NCRF amounted to \$2,284,000 and losses and loss adjustment expense reserves amounted to \$1,157,000.

Reinsurance Ceded

The Company's catastrophe and property excess of loss reinsurance is primarily administered through an intermediary, Guy Carpenter & Company, Inc., San Francisco, California. The reinsurance agreements are reviewed annually by the Company and revised and/or renewed in accordance with the reinsurance requirements of the Company. All of the agreements for reinsurance were effective January 1, 2001 for a term of one year.

All of the agreements for ceded reinsurance were reviewed as to insolvency provisions and found to comply with statutory requirements. Subscribing reinsurers were reviewed as to financial condition and status as authorized reinsurers in Alabama, or adequate deposits or letters of credit securing reinsurance in unauthorized companies. Winterthur Swiss Insurance Company (WSIC), Winterthur, Switzerland, is affiliated with the Company by common ownership. WSIC subscribes to a significant portion of the Company's property per risk and property catastrophe reinsurance ceded. The reinsurance coverages and subscribing reinsurers are described as follows:

First Property Per Risk Excess of Loss

Business covered – all business classified by the Company as property insurance

Retention - \$250,000 per risk

Limits – \$250,000 excess of \$250,000

Subscribing reinsurers and percentage of participation:

St. Paul Reinsurance	50.00%
WSIC	<u>50.00%</u>
Total	100.00%

Second Property Per Risk Excess of Loss

Business covered – all business classified by the Company as property insurance

Retention - \$500,000 per risk

Limits – \$1,500,000 excess of \$500,000

Subscribing reinsurers and percentage of participation:

NAC Re	20.00%
St. Paul Reinsurance	50.00%
WSIC	<u>30.00%</u>
Total	100.00%

Third Property Per Risk Excess of Loss

Business covered – all business classified by the Company as property insurance

Retention - \$2,000,000 per risk

Limits - \$3,000,000 excess of \$2,000,000

Subscribing reinsurers and percentage of participation:

NAC Re	20.00%
St. Paul Reinsurance	50.00%
WSIC	<u>30.00%</u>
Total	100.00%

First Casualty Excess of Loss

Business covered – all business classified by the Company as liability

Retention - \$300,000 per risk

Limits - \$200,000 excess of \$300,000

Contingent commissions – 33.3% of all the net profit accruing to the Corporation

Subscribing reinsurers and percentage of participation:

Employer's Re	100.00%
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Second Casualty Excess of Loss

Business covered - all business classified by the Company as liability

Retention - \$500,000 per risk

Limits - \$500,000 excess of \$500,000

Subscribing reinsurers and percentage of participation:

Employer's Re	100.00%
---------------	---------

Third Casualty Excess of Loss

Business covered – all business classified by the Company as liability

Retention - \$1,000,000 per risk

Limits - \$1,000,000 excess of \$1,000,000

Subscribing reinsurers and percentage of participation:

PMA Reinsurance	50.00%
Partner Re	<u>50.00%</u>
Total	100.00%

Fourth Casualty Excess of Loss

Business covered – all business classified by the Company as liability

Retention - \$2,000,000 per risk

Limits - \$3,000,000 excess of \$2,000,000, maximum worker's compensation limit of \$5,000,000 per claimant

Subscribing reinsurers and percentages of participation:

PMA	50.00%
Partner Re	<u>50.00%</u>
Total	100.00%

First Property Catastrophe Excess of Loss

Business covered – all business classified by the Company as property insurance

Retention - \$2,500,000 per risk

Limits – \$2,500,000 excess of \$2,500,000

Subscribing reinsurers and percentage of participation:

Tempest Re	70.00%
WSIC	<u>30.00%</u>
Total	100.00%

Second Property Catastrophe Excess of Loss

Business covered – all business classified by the Company as property insurance

Retention - \$5,000,000 per risk

Limits – \$5,000,000 excess of \$5,000,000

Subscribing reinsurers and percentage of participation:

Tempest Re	65.00%
WSIC	30.00%
Renaissance Re	<u>5.00%</u>
Total	100.00%

Third Property Catastrophe Excess of Loss

Business covered – all business classified by the Company as property insurance

Retention - \$10,000,000 per risk

Limits – \$25,000,000 excess of \$10,000,000

Subscribing reinsurers and percentage of participation:

WSIC	100.00%
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Property Aggregate Catastrophe Excess of Loss

Business covered – all business classified by the Company as property insurance

Deductible - \$3,500,000 in the aggregate

Limits – \$7,500,000 in the aggregate, excess of \$3,500,000

Subscribing reinsurers and percentage of participation:

Tempest Re	70.00%
WSIC	<u>30.00%</u>
Total	100.00%

Commercial Umbrella-Automatic Facultative

Business covered – all business classified by the Company as Commercial and Personal

Retention – 2½% of first \$1,000,000

Limits – 97½% of first \$1,000,000
100% of 2nd to 5th million dollars

Subscribing reinsurers and percentage of participation:

Swiss Re	100.00%
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MARKET CONDUCT

Plan of Operation

The Company markets its products only through independent agents. At December 31, 2001, the Company was marketing its products in Alabama through 55 agencies employing 329 agents appointed to write for the Company.

Southern Guaranty Insurance Company sells commercial lines, personal lines and workmen's compensation insurance in most southeastern states. Small to mid-size commercial accounts are targeted with a comprehensive range of products. The Commercial umbrella is offered with limits up to \$5,000,000. Personal lines offered include primarily automobile and homeowner insurance.

Policy Forms and Underwriting

All the Company's active policy forms and rates in force at December 31, 2001 were found to have been approved by the Alabama Department of Insurance.

Compliance With Agents Licensing Requirements

At December 31, 2001, the Company had 55 licensed independent agencies with 329 appointed agents in Alabama who were receiving commissions from the Company. The examiner reviewed commission payments to agents to assert that the persons receiving commissions from the Company were properly licensed. No discrepancies were found.

Advertising

The Company had no formal advertising program during the examination period. The Company does have a Web page (www.sgic.com), which displays the following links: Company's background, product lines, employment opportunities, agent access and how to locate an agent. The Company's advertising was found to be in compliance with Alabama Insurance Department, *Regulation No. 110*.

Claims Payments Practices

A sample of 94 claims files comprised of claims that were open, closed and closed without payment, was reviewed in order to evaluate the Company's claims payment practices. Claims were reviewed with regard to compliance with policy provisions, timeliness of payment and adequacy of documentation. No noteworthy discrepancies were found in the sample.

Complaints

The examiner reviewed the Company's complaints register. Only ten complaints were reported to the Alabama Department of Insurance, Consumers Division during the examination. This is deemed to be a very low number of complaints in relation to the amount of business written by the Company. The complaints ranged from policy issues to claim loss amounts.

Privacy

The Company's policy is that non-public information involving underwriting, claims handling and fraud prevention is not shared with anyone outside the Company except for that sharing allowed by the exceptions in the Gramm-Leach-Bliley Act (GLBA). The Company does not share any personal information for purposes of marketing. The Company sends a "Notification of Information Practices" (Opt-Out Notice) with all renewals of personal lines and workers compensation policies.

The Company appeared to be in compliance with the privacy requirements of Alabama Department of Insurance, *Regulation No. 122*.

ACCOUNTS AND RECORDS

Internal Accounting Records

The Company's internal controls and information systems were evaluated by observation, by interviewing Company personnel, and by reviewing NAIC Internal Controls and Information Systems questionnaires completed by the Company. The Company's internal controls and controls over its information systems appeared to be sufficient to safeguard Company assets and to generate adequate records of its business. The Company's accounting systems and documentation of its transactions were deemed to be excellent, except for the problems encountered with the closing of accounts, which are discussed in the next report section.

The Company is audited periodically by the internal audit department of its ultimate parent company, Credit Suisse Group. The internal audit reports were made available to the examiners; however, the findings of the internal auditors were not deemed to have a material impact on the examination.

Accelerated Closing of Accounts (Permitted Practices)

The Company's parent, Winterthur U.S. Holdings, Inc. requires the Company to submit year-end financial data in early January of each year. The Company has found it difficult to comply with this requirement if it waits until year-end to close its books. For this reason, the Company has implemented an accelerated closing (cut-off) date.

The Company obtained permission from its regulators, including the Alabama Department of Insurance, to implement an accelerated (20th of the month) closing of its books, beginning with year-end 2000. The related permitted practices letter also stated that the Company would, "... post appropriate premium, loss and loss adjustment expenses, O,A & G expense and premium tax accruals which would be necessary as a result of this accelerated month end closing date." The examiners found this statement to be imprecise in relation to the Company's actual practice. Also, the Company's implementation of the accelerated cut-off appeared to be inconsistent with precise balance sheet accounting.

The examination found that the Company closed its cash operating accounts on December 20, 2001, except for the investment accounts which were closed on December 31, 2001. Premiums on new business were cut off on December 20th, while renewals were not closed until December 31st. Claims payments were cut-off as of

December 20th, but estimated to December 31, for reserve purposes. Case reserves were stated as of December 20, 2001. The Company's bulk and IBNR reserve data was compiled as of November 20, 2001, then estimated to December 31, 2001, while the same data for the year 2000 was cut-off as of December 20, 2000.

In summary, the Company's year-end 2001 account balances were either stated as of the 20th of the month, cut-off as of the 20th then estimated to the end of the accounting period, or closed at the end of the accounting period. As a result of this diversity in cut-off dates, the risk of examination error was deemed to be increased; and, an inordinate amount of time was spent in obtaining explanations of the accounts and in performing additional reconciliation work.

It was also noted that the December 20th cut-off was not disclosed in "Note 1, Summary of Significant Accounting Practices," Notes to the Financial Statements, of the Company's Annual Statements.

External Audit and Actuarial

The Company was audited for each of the years under examination by the certified public accounting firm of KPMG, LLP, Atlanta, Georgia. The audit reports and work papers of the external auditors were made available to the examiners, and have been utilized in the examination to the extent deemed appropriate. The 2001 audit workpapers were not delivered to the examiners until mid June, 2002, and were consequently not available for examination planning purposes.

The Company's reserves were certified, as of December 31, 2001, by George M. Levine, FCAS, MAAA of KPMG LLP, of Hartford, Connecticut.

FINANCIAL STATEMENTS

Financial statements included in this report, which reflect the operations of the Company for the years under examination and financial condition at December 31, 2001, consist of the following:

	<u>Page</u>
Statement of Assets, Liabilities, Surplus and Other Funds	25
Statement of Income	27
Reconciliation of Surplus as Regards Policyholders	28
Capital Gains and Losses	28

THE NOTES IMMEDIATELY FOLLOWING THE FINANCIAL STATEMENTS ARE AN INTEGRAL PART THEREOF.

STATEMENT OF ASSETS, LIABILITIES, SURPLUS AND OTHER FUNDS

For the Period Ended December 31, 2001

ASSETS

	<i>Ledger Assets</i>	<i>Non-Admitted Assets</i>	<i>Admitted Assets</i>
Bonds	\$ 125,613,823		\$ 125,613,823
Preferred stocks	6,000,000		6,000,000
Common stocks	61,783,518		61,783,518
Real estate:			
Occupied by Company	5,202,751		5,202,751
Held for production of income	5,605,325		5,605,325
Held for sale	1,531,777		1,531,777
Cash	10,058,457		10,058,457
Receivable for securities	844,231		844,231
Agents balances or uncollected premiums:			
In course of collection	7,779,569	\$ 1,367,507	6,412,062
Booked but deferred and not yet due	27,637,829		27,637,829
Bills receivable taken for premiums (<i>Note-1</i>)	1,114,878	1,111	1,113,767
Reinsurance recoverables (<i>Note-2</i>)	951,196		951,196
Federal income tax recoverable	11,629,000	11,629,000	
Guaranty funds receivable or on deposit	294,924	294,924	
Data processing equipment	360,451	165,440	195,011
Interest, dividends and real estate income	2,002,733		2,002,733
Receivable from subsidiaries	2,000		2,000
Equities or deposits in pools or associations	2,907,995		2,907,995
Furniture, equipment and supplies	842,720	842,720	
Prepaid expenses	46,913	46,913	
Sundry assets	1,117,445	1,105,060	12,385
Total Assets	\$ 273,327,535	\$ 15,452,675	\$ 257,874,860

STATEMENT OF ASSETS, LIABILITIES, SURPLUS AND OTHER FUNDS (continued)

LIABILITIES SURPLUS AND OTHER FUNDS

Liabilities

Losses (Note-3)	\$ 67,087,228
Loss adjustment expenses (Note-3)	14,573,145
Commissions payable	2,934,262
Other expenses	1,672,063
Taxes, licenses and fees	1,785,025
Unearned premiums	66,456,413
Ceded reinsurance premiums payable	775,738
Funds held by Company under reinsurance treaties	5,932
Amounts withheld or retained for account of others (Note-4)	1,687,640
Provision for reinsurance	66,800
Drafts outstanding	5,165,729
Payable to affiliates	137,920
Pension liabilities, accounts payable and other liabilities	2,728,094
Reserve for self-insurance program	100,000
Accumulated post-benefit obligations other than retirement	<u>637,175</u>
Total liabilities	\$ 165,813,164

Surplus and Other Funds

Common Capital Stock	\$ 2,000,000
Gross paid in and contributed surplus	60,741,690
Unassigned funds (surplus) (Note-5)	<u>29,320,006</u>
Surplus as regards policyholders	<u>92,061,696</u>
Total liabilities, surplus and other funds	<u>\$ 257,874,860</u>

STATEMENT OF INCOME

For the Periods Ended,

	<u>December</u> <u>31, 2001</u>	<u>December</u> <u>31, 2000</u>	<u>December</u> <u>31, 1999</u>	<u>December</u> <u>31, 1998</u>	<u>December</u> <u>31, 1997</u>
Underwriting income:					
Premiums earned	\$ 121,735,781	\$ 112,954,472	\$ 122,099,583	\$ 108,641,782	\$ 107,904,718
Deductions:					
Losses incurred	\$ 71,975,099	\$ 64,099,475	\$ 77,131,449	\$ 75,921,431	\$ 69,245,269
Loss expenses incurred	13,390,228	15,263,414	13,352,426	10,761,284	10,098,448
Other underwriting expenses incurred	42,639,981	40,109,834	39,388,089	32,150,776	29,567,708
Total deductions	\$ 128,005,308	\$ 119,472,723	\$ 129,871,964	\$ 118,833,491	\$ 108,911,425
Net underwriting gain (loss)	\$ (6,269,527)	\$ (6,518,251)	\$ (7,772,381)	\$ (10,191,709)	\$ (1,006,707)
Investment income:					
Net investment income earned	\$ 6,646,215	\$ 8,517,021	\$ 5,212,255	\$ 5,921,192	\$ 5,915,508
Net realized capital gains (losses)	688,554	2,477,957	2,675,053	4,975,889	2,681,733
Net investment gain (loss)	\$ 7,334,769	\$ 10,994,978	\$ 7,887,308	\$ 10,897,081	\$ 8,597,241
Other income:					
Net loss from agent's or premium balances charged off	\$ (61,152)	\$ (299,159)	\$ (8,644)	\$ 9,101	\$ (299,769)
Finance and service charges not included in premiums	947,803	846,721	701,927	738,054	649,309
Total other income	\$ 886,651	\$ 547,562	\$ 693,283	\$ 747,155	\$ 349,540
Net income before dividends and taxes	\$ 1,951,893	\$ 5,024,289	\$ 808,210	\$ 1,452,527	\$ 7,940,074
Federal income taxes incurred	(98,070)	59,361	(75,521)	120,000	149,359
Net income	\$ 2,049,963	\$ 4,964,928	\$ 883,731	\$ 1,332,527	\$ 7,790,715

RECONCILIATION OF SURPLUS AS REGARDS POLICYHOLDERS

For the Periods Ended December 31,

	<u>2001</u>	<u>2000</u>	<u>1999</u>	<u>1998</u>	<u>1997</u>
Surplus as regards policyholders, January 1,	\$ 90,721,463	\$ 89,047,041	\$ 88,044,960	\$ 85,397,466	\$ 81,931,282
Net income	\$ 2,049,963	\$ 4,964,928	\$ 883,731	\$ 1,332,527	\$ 7,790,715
Net unrealized capital gains or (losses)	2,084,915	1,924,778	3,549,891	1,963,895	4,498,795
Change in net deferred income tax	11,629,000				
Change in non-admitted assets	(12,370,045)	82,516	(625,141)	222,072	(786,313)
Change in provision for reinsurance	32,400	358,200	(426,400)	(31,000)	206,987
Change in excess of statutory reserves		(656,000)	620,000	(90,000)	(244,000)
Cumulative effect of changes in accounting principles	2,914,000				
Paid in surplus					
Change in surplus notes		(5,000,000)	(3,000,000)	(750,000)	(5,000,000)
Dividends to stockholders	\$ 1,340,233	\$ 1,674,422	\$ 1,002,081	\$ 2,647,494	\$ 3,466,184
Change in surplus as regards policyholders	\$ 92,061,696	\$ 90,721,463	\$ 89,047,041	\$ 88,044,960	\$ 85,397,466
Surplus as regards policyholders, December 31,	<u>\$ 92,061,696</u>	<u>\$ 90,721,463</u>	<u>\$ 89,047,041</u>	<u>\$ 88,044,960</u>	<u>\$ 85,397,466</u>

CAPITAL GAINS AND LOSSES

For The Year Ended December 31, 2001

	<u>Profit on Sales or Maturities</u>	<u>Loss on Sales or Maturities</u>	<u>Difference Between Book and Admitted Values</u>	<u>Total Gain or (Loss)</u>
U.S. government bonds	\$ 888,322			\$ 888,322
Other bonds (unaffiliated)		(4,071)		(4,071)
Common stocks (unaffiliated)		(235,809)	(773,835)	(1,009,644)
Common stocks of affiliates			2,858,750	2,858,750
Sale of fixed assets	40,112			40,112
Totals	<u>\$ 928,434</u>	<u>\$ (239,880)</u>	<u>\$ 2,084,915</u>	<u>\$ 2,773,469</u>
Net realized capital gains				\$ 688,554
Net unrealized capital losses				\$ 2,084,915

NOTES TO THE FINANCIAL STATEMENTS

Note 1 – Bills Receivable Taken For Premium **\$1,113,767**

The amount of the captioned asset is the same as reported in the Company's 2001 Annual Statement. The amount determined per examination was \$422,310 less. The amount of the difference was deemed to be immaterial and no related change has been made to the financial statements of this report.

The aforesaid difference resulted because the Company calculated the non-admissible portion of its bills receivable as those amounts that were ninety days or more past due. On the other hand, SSAP #6 requires that, "If any installment is past due, the entire bills receivable balance from that policy is non-admitted." The Company's method of calculating the non-admissible portion (amounts ninety days or more past due) yielded a non-admissible amount of \$1,111. The recalculation by the examiner, in accordance with the requirements of SSAP #6 (entire balance of past due accounts) yielded a non-admitted amount of \$423,421.

Note 2 – Reinsurance Recoverables on Loss and Loss Adjustment Expense Payments **\$951,196**

The captioned amount is the same as reported in the Company's 2001 Annual Statement. The amount verified by the examination was \$609,844. The \$341,352 difference was deemed to be immaterial and no related change has been made in the financial statements of this report.

The \$341,352 examination difference was comprised of reported reinsurance recoverables in the amount of \$169,944 due from Employers Reinsurance Company, and \$171,408 due from reinsurance intermediary, Guy Carpenter. Neither of these amounts could be traced to subsequent payments or offsets of balances payable. It is probable that difficulty in verifying these recoverables was due to imprecision in the reinsurers' reporting and/or the Company's accounting for these balances; nevertheless, the asset was unsubstantiated and is not admissible for the purposes of this report.

Note 3 – Losses **\$67,087,228**
Loss Adjustment Expenses **\$14,573,145**

The amounts of the captioned reserve liabilities are the same as reported in the Company's 2001 Annual Statement. Examination of the reserves indicated that the Company's data was complete, and actuarial examination found the amounts reported to be reasonable overall and in some instances conservative. The following discussion

relates to certain discrepancies found in the Company's methods of calculating and/or accounting for the reserves.

The Company's parent requires that it complete its annual reporting in early January. For this reason the Company received permission from the Alabama Department of Insurance to close its books on the 20th of each month and to use December 20th as a year-end cutoff date. See "Accounts and Records" for further discussion.

Most of the Company's year-end 2001 reserves were based on November 20th data adjusted to reflect December 31st. Bulk and IBNR reserves for 2001 for losses and ALAE were calculated from November data. The use of development triangles that were "modified" to reflect that they were estimated from November data produced overstatement of the year 2001 and understatement of all other accident years. The impact was minimal for short-tailed lines of business, but more prominent for longer tailed lines. Several adjustments were made to compensate for the early close and the forty-two days of development between November 20th and December 31, 2001. The actuarial examiner considered some of the adjustments to be unnecessary; and, the resulting bulk and IBNR reserves were deemed to be reasonably conservative.

Booked case loss reserves were taken from the December 20th year-end cutoff date. The Company did not set case reserves for loss adjustment expenses. The loss adjustment expense reserves were calculated using methodology similar to that employed in calculating the loss reserves, with equivalent results. Also, reserves were booked gross of approximately \$827,000 of anticipated salvage and subrogation as is required by Alabama statutes.

The actuarial examiner noted some reconciliation problems between the Company's actuarial reserve study data and Annual Statement Schedule P. The gross data was found to reconcile closely to Schedule P while the net data did not reconcile. Two reasons for the lack of reconciliation were identified. First, significant input errors were detected in the Schedule P data reconciliation. Also, the net data (reserve study) consisted of estimated year-end data whereas Schedule P was prepared with actual year-end data.

<u>Note 4 – Amounts Withheld for Account of Others</u>	\$1,687,640
<u>Remittances and Items not Allocated</u>	\$ -0-

The captioned amounts are the same as reported in the Company's 2001 Annual Statement. However, it was found that \$896,534 of the amount reported as "Amounts Withheld for Account of Others" should have been reported as "Remittances and Items not Allocated." No changes have been made to the financial statements of this report because the amounts involved are not material and the misclassification has no effect on the Company's surplus.

The \$896,534 amount that was found to be misclassified in "Amounts Withheld for the Account of Others" consisted of premium suspense and unapplied cash items. In accordance with NAIC Annual Statement Instructions these suspense items, which are usually the property of the Company but are in suspense pending their booking to the proper accounts, are properly reported as "Remittances and Items not Allocated." The "Amounts Withheld for Account of Others" line item is designated for employee withholdings and other amounts that usually do not belong to the Company, but are temporarily in the Company's custody.

It appears that the "Remittances and Items not Allocated," line item was not added to the NAIC Property and Casualty Annual Statement convention blank until 1998 and the Company did not recognize the change.

Note 5 – Unassigned Funds (surplus)

\$92,061,696

The amount of unassigned funds per examination is the same as reported in the Company's 2001 Annual Statement. Variances in account balances determined by the examination were deemed to be immaterial in the aggregate amount.

CONTINGENT LIABILITIES AND PENDING LITIGATION

Examination for contingent liabilities and pending litigation included review of the Company's annual statement disclosures, minutes of the corporate governing bodies, pending claims, and the usual examination of the accounts for unrecorded items. No material unreported contingencies were noted and all pending litigation against the Company appeared to be within the ordinary course of its business, except as discussed in "Subsequent Events," which follows this section.

The Company's President and its Treasurer executed a letter of representation attesting to the non-existence of unreported liabilities and contingencies as of December 31, 2001.

SUBSEQUENT EVENTS

The review of events subsequent to December 31, 2001 and up to the date of this report included: review of the Company's 2002 Quarterly Statements; review of certain receipts and disbursements through March 31, 2002; review of corporate records through September of 2002; and, inquiries of Company management. No significant subsequent events were disclosed by this review.

Company officials notified the examiners of two subsequent events that were not known at the time of the 2001 Annual Statement filing. These events were found to be disclosed in subsequent quarterly filings, as follows.

In its September 30, 2002 Quarterly Statement the Company disclosed that it was named in a class action lawsuit filed in the State of Georgia in 2002. Said lawsuit alleges damages as a result of diminished value with regard to certain Georgia automobile physical damage claims previously settled by the Company during the period 1996 through 2001. "Diminished value" relates to the decline in market value of an automobile as a result of its having been wrecked, and the assertion by the plaintiffs is that the insurer should pay for this diminished value as part of the claim. The Company has estimated its ultimate liability regarding this lawsuit at \$1,300,000 and has recorded this amount as an "other underwriting expense" in the September 30, 2002 Quarterly Statement. This \$1,300,000 amount is not material for the purposes of this report.

In its June 30, 2002 Quarterly Statement, the Company reported a permanent impairment in the amount of \$3,567,000 to certain of its common stocks. This action was taken in compliance with SSAP No. 30. The \$3,567,000 amount is material for the purposes of this report. Nevertheless, the Company's surplus at December 31, 2001 was more than \$92,000,000; and, the impact of all subsequent events and contingencies determined by this examination would appear to minimal.

COMPLIANCE WITH PREVIOUS RECOMMENDATIONS

It appears that the Company has complied with all recommendations made as a result of the examination report as of December 31, 1996.

COMMENTS AND RECOMMENDATIONS

Accounts and Records – Page 21

In 2000, the Company obtained permission from its regulators, in the states in which it operates, to close its accounts on December 20th for year-end reporting and on the 20th of each month for interim accounting purposes. It appears that the Company has not strictly followed what was proposed in the permitted practices writing.

It is recommended that the Company review its practices regarding the year-end closing of its accounts, using a December 20th cut-off date for some accounts and the usual December 31st cut-off date for other accounts. Also, some accounts were cut-off at December 20th and estimated to December 31st. These practices created additional audit and reconciliation work for the examiners. The actuarial examiner also noted that

the Company's reserve data was cut-off on November 20th and estimated to December 31st.

It was also noted that the December 20th cut-off was not disclosed in "Note 1, Summary of Significant Accounting Practices," Notes to the Financial Statements, in the Company's pertinent Annual Statements. It is recommended that this disclosure be made in all future statutory financial statements.

It is recommended that the Company define, precisely, what practices it intends to follow regarding its accounting cut-off dates, and resubmit those practices to the Alabama Department of Insurance for approval. If the current practices continue to be permitted, it is recommended that the Company keep detailed reconciliation workpapers that will allow examiners to determine the value of all account balances as of one particular date.

Note 1 – Bills Receivable Taken for Premium – Page 29

It is recommended that the Company calculate the non-admissible portion of its bills receivable taken for premium in accordance with SSAP #6. The entire balance of past due accounts must be non-admitted, rather than only the amount that is more than ninety days past due.

Note 2 – Reinsurance Recoverables on Loss and Loss Adjustment Expense Payments – Page 29

It is recommended that the Company not admit any reinsurance recoverables that cannot be substantiated by subsequent examination of Company records.

Note 3 – Losses and Loss Adjustment Expenses – Page 29

It is recommended that the Company work with its consulting actuary to improve the process of using an early cut-off date for estimating year-end reserves.

It is recommended that the Company's consulting actuary conduct the required reconciliation of reserving data to Annual Statement, Schedule P in conjunction with issuing future reserve opinions. This reserve study should address all inconsistencies and issues by the reconciliation.

Note 4 – Amounts Withheld for Account of Others / Remittances and Items not Allocated – Page 30

It is recommended that the Company reports its suspense items under the Annual Statement caption, "Remittances and Items not Allocated," in accordance with NAIC, *Annual Statement Instructions*.

CONCLUSION

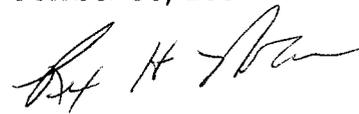
Acknowledgement is hereby made of the courtesy and cooperation extended by representatives of **Southern Guaranty Insurance Company** during this examination.

The customary examination procedures, as recommended by the National Association of Insurance Commissioners, have been followed to the extent appropriate in connection with the verification and valuation of assets and the determination of liabilities set forth in this report.

Examination findings indicated that the Company was in sound financial condition as of December 31, 2001.

In addition to the undersigned, the following persons represented the Alabama Department of Insurance as participants in this examination: Thomas W. Salo, Palmer W. Nelson, Theophilos C. Goodin, examiners; Glenn Taylor, ACAS, MAAA, and Randall D. Ross, actuarial consultants.

Respectfully submitted,
October 30, 2002



Rex H. Newborn, CFE
Examiner-in-Charge
Alabama Department of Insurance



DON SIEGELMAN
GOVERNOR

STATE OF ALABAMA
DEPARTMENT OF INSURANCE
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JOHN S. ROBISON
GENERAL COUNSEL
MICHAEL A. BOWNES
RECEIVER
DENISE B. AZAR
LICENSING MANAGER
JIMMY W. GUNN

February 14, 2002

Mr. Jim L. Riddling
President
Southern Guaranty Insurance Company
2545 Taylor Road
P. O. Box 235004
Montgomery, AL 36123-5004

Re: Financial Examination As Of December 31, 2001

Dear Mr. Riddling:

This letter is to inform you of a financial examination of your company called by the Alabama Department of Insurance and to authorize Rex Newborn, CFE, Examiner, to conduct the examination. This authorization is pursuant to the instructions of Alabama Insurance Commissioner, D. David Parsons, and in compliance with the statutory requirements of the State of Alabama and resolutions adopted by the National Association of Insurance Commissioners.

Your examination is to commence on or about March 18, 2002, and will be conducted primarily in your offices. The expected duration of the examination is approximately three months. Preliminary planning of your examination will first begin in the offices of the Alabama Department of Insurance. The examiner will arrive in your offices on or after this date. You will be contacted by Mr. Newborn regarding the exact arrival date at your offices.

The Alabama Insurance Department has adopted work policies and rules governing work hours, leave and unacceptable conduct including sexual harassment. If you have any question about our examiner's conduct at your offices, please contact me immediately.

As part of your examination, the enclosed internal control and information systems questionnaire is required to be completed for review by our examiner. Please complete and return the questionnaire to this Department within 30 days, addressed to the attention of the Examiners' Division. The questions may be answered on the questionnaire itself or on a separate sheet if additional explanation is required. If possible, your CPA's workpapers and a representative of your CPA firm should be available the week of March 18, 2002, for review at your offices.

Invoices covering examination fees and related expenses will be submitted to the appropriate company official in accordance with standard Departmental policy. Payment of any examination charges so invoiced are due within two business days following presentation of the invoice.

Sincerely,

Richard L. Ford, CFE
Acting Deputy Commissioner and
Chief Examiner

RLF:dk

Enclosures

cc: Jack M. Brown, CFE
Rex H. Newborn, CFE
Glenda Daniel

EQUAL OPPORTUNITY EMPLOYER

SENDER: COMPLETE THIS SECTION

- Complete items 1, 2, and 3. Also complete item 4 if Restricted Delivery is desired.
- Print your name and address on the reverse so that we can return the card to you.
- Attach this card to the back of the mailpiece, or on the front if space permits.

1. Article Addressed to:

Jim L. Riddling
 President
 Southern Guaranty Insurance Co
 2545 Taylor Road
 P O Box 235004
 Montgomery AL 36123-5004

2. Article Number (Copy from service label)

7099 3400 0015 2327 4770

COMPLETE THIS SECTION ON DELIVERY

A. Received by (Please Print Clearly) B. Date of Delivery

LANNIE PICKSON 2/20/02

C. Signature

[Handwritten Signature]

 Agent AddresseeD. Is delivery address different from item 1? YesIf YES, enter delivery address below: No

3. Service Type

 Certified Mail Express Mail Registered Return Receipt for Merchandise Insured Mail C.O.D.4. Restricted Delivery? (Extra Fee) Yes



DON SIEGELMAN
GOVERNOR

STATE OF ALABAMA
DEPARTMENT OF INSURANCE
201 MONROE STREET, SUITE 1700
POST OFFICE BOX 303351
MONTGOMERY, ALABAMA 36130-3351
TELEPHONE: (334) 269-3550
FACSIMILE: (334) 241-4192
INTERNET: www.aldoi.org

D. DAVID PARSONS
COMMISSIONER
ASSISTANT COMMISSIONER
TREY GRANGER
DEPUTY COMMISSIONER
JAMES R. (JOHNNY) JOHNSON
CHIEF EXAMINER
RICHARD L. FORD
STATE FIRE MARSHAL
JOHN S. ROBISON
GENERAL COUNSEL
MICHAEL A. BOWNES
RECEIVER
DENISE B. AZAR
LICENSING MANAGER
JIMMY W. GUNN

April 15, 2002

Mr. Glen Taylor
Taylor-Walker & Associates, Inc.
Actuarial Consulting Group
P. O. Box 156
40 North Main
Midvale, UT 84047

Re: Examination of Southern Guaranty Insurance Company
As of December 31, 2001

Dear Mr. Taylor:

This letter is to request and authorize your participation in the examination of the above referenced company for the purpose of computing reserves and making other valuations in your usual manner.

The examination will begin on April 15, 2002. The examination for this company is being conducted in the company's offices at 2545 Taylor Road, Montgomery, AL 36117, and will cover the period ending December 31, 2001. The expected duration of the examination is approximately three months.

The Examiner-in-Charge will be Mr. Rex H. Newborn, CFE. Please contact him at the company after the beginning date to coordinate the scheduling of your portion of this examination. The company telephone number is (334) 270-6000.

If your schedule does not permit you to accept this assignment, please let me know so that other arrangements can be made.

Thank you for your assistance in this matter.

Sincerely,

Richard L. Ford, CFE
Acting Deputy Commissioner and
Chief Examiner

RLF:dk

cc: Jack M. Brown, CFE
Rex H. Newborn, CFE
Glenda Daniel

SENDER: COMPLETE THIS SECTION

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1. Article Addressed to:

Mr. Glen Taylor
 Taylor-Walker & Associates Inc
 Actuarial Consulting Group
 P O Box 156
 40 North Main
 Midvale UT 84047

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C. Signature

X *Paul Bleiker* Agent Addressee

D. Is delivery address different from item 1? Yes

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3. Service Type

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- Registered Return Receipt for Merchandise
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4. Restricted Delivery? (Extra Fee) Yes

2. Article Number (Copy from service label)

7099 3400 0015 2327 6682

PS Form 3811, July 1999.

Domestic Return Receipt

102595-00-M-0952

Don Siegelman
Governor

D. David Parsons
Commissioner



201 Monroe Street, Suite 1700
Montgomery, Alabama 36130
Telephone: (334)269-3550
Facsimile: (334)240-3194

Richard L. Ford
Acting Deputy Commissioner/
Chief Examiner

Johnny Johnson
Deputy Commissioner

John S. Robinson
State Fire Marshall

Michael A. Bownes
General Counsel

Fax

To: Jack Brown, CFE From: Rex Newborn

Fax: Pages: 6

Phone: Date: 6/20/2002

Re: KPMG Workpapers for Southern Guaranty CC:

Urgent For Review Please Comment Please Reply Please Recycle

See attached MEMO

Unless otherwise indicated, the information contained in this facsimile message is CONFIDENTIAL information intended for the use of the individual or entity named above. If the reader of this message is not the recipient or the employee responsible to deliver to intended recipient you are hereby notified that any dissemination, distribution or copying of this communication is strictly prohibited. If you received this communication in error, please immediately notify us by telephone and return the original message to us via U.S. Postal Service at our expense.



**GOVERNOR
DON SIEGELMAN**

**STATE OF ALABAMA
DEPARTMENT OF INSURANCE**

201 Monroe Street, Suite 1700
Post Office Box 303351
Montgomery, Alabama 36130-3351
Telephone: (334) 269-3550
Facsimile: (334) 240-3194

**COMMISSIONER
D. DAVID PARSONS**

**Chief Examiner
Richard L. Ford**

**State Fire Marshal
John S. Robison**

**General Counsel
Michael A. Bownes**

MEMORANDUM

To: Jack Brown, Assistant Chief Examiner
From: Rex Newborn *RN*
Date: June 20, 2002
Re: Attached Communication from KPMG

Please note the penultimate paragraph of the subject letter.

After this examination has concluded, I will not be in a position to provide KPMG with notification should there be any further distribution of information from their workpapers. Therefore, I am not the appropriate person to sign this document.

Since the examination is already well under way, the KPMG workpapers are not expected to contribute much, and cannot be expected to expedite any examination work. Please let me know how you want to proceed.



Date: June 19, 2002
To: Mr. Rex Newborn
c/o Buddy Griffith
(334) 270-6283

Page 1 of 4

Re:

From: Ersula Butler for Caroline de Witt
Tel: 404-222-7187
Fax: 404-222-3431

This is a confidential fax, intended specifically for the individual named above. If you receive it in error, please contact Ersula Butler, 404-222-7187.

Mr. Newborn:

Please sign and return to me via fax. I will forward the workpapers after I receive your signed letter. Additionally, I am forwarding an original to be included with the workpapers. Please return one signed copy as we need your original signature on file.

Thank you,
Ersula





303 Peachtree Street, N.E.
Suite 2000
Atlanta, GA 30308

Telephone 404 222 3000
Fax 404 222 3060

June 19, 2002

Mr. Rex Newborn
Examiner
Alabama Department of Insurance
c/o Southern Guaranty Insurance
2545 Taylor Road
Montgomery, AL 36117

Dear Mr. Newborn:

Your representatives have requested access to our work papers in connection with our audit of the December 31, 2001, statutory financial statements of Southern Guaranty Insurance Company (the "Company"). It is our understanding that the purpose of your request is to facilitate your regulatory examination for the period then ended.

Our audit of the Company's December 31, 2001, financial statements was conducted in accordance with auditing standards generally accepted in the United States of America, the objective of which is to form an opinion as to whether the financial statements, which are the responsibility and representations of management, present fairly, in all material respects, the admitted assets, liabilities, and capital and surplus of the Company in conformity with accounting practices prescribed or permitted by the Department of Insurance of the State of Alabama. Under auditing standards generally accepted in the United States of America, we have the responsibility, within the inherent limitations of the auditing process, to plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether caused by error or fraud. Because of the nature of audit evidence and the characteristics of fraud, the auditor is able to obtain reasonable, but not absolute, assurance that material misstatements are detected. The auditor has no responsibility to plan and perform the audit to obtain reasonable assurance that misstatements, whether caused by errors or fraud, that are not material to the financial statements are detected. In addition, those standards require the independent auditor to plan and perform his or her work with due professional care. Due professional care imposes a responsibility upon each professional within an independent auditor's organization to observe the standards of fieldwork and reporting.

KPMG

Page 3

Alabama containing information derived there from. We further request that written notice be given to our firm before distribution of the information in the work papers (or photocopies thereof) to others, including other governmental agencies, except when such distribution is required by law or regulation.

Any photocopies of our work papers we agree to provide you will be identified as "Confidential Treatment Requested by KPMG LLP, 303 Peachtree Street, Suite 2000, Atlanta, Georgia 30308."

Very truly yours,

KPMG LLP



Michael J. Grillaert
Partner

ACKNOWLEDGED BY:

By _____ Date _____
Authorized Signature and Title

Regulatory agency

cc:

Southern Guaranty Insurance Company



The concept of selective testing of the data being audited, which involves judgment both as to the number of transactions to be audited and as to the areas to be tested, has been generally accepted as a valid and sufficient basis for an auditor to express an opinion on financial statements. Thus, our audit, based on the concept of selective testing, is subject to the inherent risk that material errors or fraud, if they exist, would not be detected. In addition, an audit does not address the possibility that material errors or fraud may occur in the future. Also, our use of professional judgment and the assessment of materiality for the purpose of our audit means that matters may have existed that would have been assessed differently by you.

The work papers were prepared for the purpose of providing the principal support for our report on the Company's December 31, 2001, financial statements and to aid in the conduct and supervision of our audit. The work papers document the procedures performed, the information obtained and the pertinent conclusions reached in the engagements. The audit procedures that we performed were limited to those we considered necessary under generally accepted auditing standards to enable us to formulate and express an opinion on the financial statements taken as a whole. Accordingly, we make no representation as to the sufficiency or appropriateness, for your purposes, of either the information contained in our work papers or our audit procedures. In addition, any notations, comments, and individual conclusions appearing on any of the work papers do not stand alone, and should not be read as an opinion on any individual amounts, accounts, balances or transactions.

Our audits of the Company's December 31, 2001, financial statements were performed for the purpose stated above and have not been planned or conducted in contemplation of your regulatory examination or for the purpose of assessing the Company's compliance with laws and regulations. Therefore, items of possible interest to you may not have been specifically addressed. Accordingly, our audit and the work papers prepared in connection therewith, should not supplant other inquiries and procedures that should be undertaken by the Insurance Department of the State of Alabama for the purpose of monitoring and regulating the financial affairs of the Company. In addition, we have not audited any financial statements of the Company since December 31, 2001 nor have we performed any audit procedures since March 29, 2002, the date of our auditors' report, and significant events or circumstances may have occurred since that date.

The work papers constitute and reflect work performed or information obtained by KPMG LLP in its capacity as independent auditor for the Company. The documents contain trade secrets and confidential commercial and financial information of our firm and the Company that is privileged and confidential, and we expressly reserve all rights with respect to disclosures to third parties. Accordingly, we request confidential treatment under the Freedom of Information Act or similar laws and regulations when requests are made for the work papers or information contained therein or any documents created by the Insurance Department of the State of



DON SIEGELMAN
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D. DAVID PARSONS
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RICHARD L. FORD
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JOHN S. ROBISON
GENERAL COUNSEL
MICHAEL A. BOWNES
RECEIVER
DENISE B. AZAR
LICENSING MANAGER
JIMMY W. GUNN

June 21, 2002

Michael J. Grillaert
KPMG
303 Peachtree Street, N.E.
Suite 2000
Atlanta, GA 30308

Re: Request for CPA Workpapers in December 31, 2001 Financial Examination of
Southern Guraranty Insurance Company

Dear Sir:

We received your June 19, 2002, letter regarding the request for inspection of the workpapers prepared in the referenced examination.

The request to inspect the workpapers is made by your client pursuant to Section 13 of Regulation 100. The letter of qualification your firm provided your insurer client should consent and agree to make available for review by the Commissioner, his designee or his appointed agent, the workpapers prepared in your examination. This agreement and consent is required by Section 12 of Regulation 100. Any copies of your firm's workpapers included in the Department's files will remain confidential to the extent provided under Alabama law.

If you have any questions, please advise.

Sincerely,


Jack M. Brown
Assistant Chief Examiner

cc: Richard Ford
Rex Newborn, Examiner-in-charge



DON SIEGELMAN
GOVERNOR

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GENERAL COUNSEL
MICHAEL A. BOWNES
RECEIVER
DENISE B. AZAR
LICENSING MANAGER
JIMMY W. GUNN

November 15, 2002

CERTIFIED MAIL
RETURN RECEIPT REQUESTED

Mr. Jim L. Riddling
President
Southern Guaranty Insurance Company
2545 Taylor Road
P. O. Box 235004
Montgomery, AL 36123-5004

**RE: Southern Guaranty Insurance Company
Report of Examination as of December 31, 2001**

Dear Mr. Riddling:

Enclosed is a copy of the Report of Examination of the above-cited company as of December 31, 2001. In the event that you have any objections to this report, please advise this Department in writing within twenty (20) days, and a hearing will be scheduled, at which time you may present your arguments regarding any objections.

Unless we hear from you within the above-stated time, the report will be filed as a public document. Once filed, no annual or quarterly statements, or other material reflecting the statutory financial condition of the company may be filed with or accepted by this Department if those statements conflict with any basis of calculation to establish the value of any asset, liability, or capital account in the report.

Sincerely,

Richard L. Ford, CFE
Acting Deputy Commissioner and
Chief Examiner

RLF:dk

Enclosure

cc: Jack M. Brown, CFE
Rex Newborn, CFE
Jill E. Baker

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1. Article Addressed to:

Mr. Jim L. Riddling
 President
 Southern Guaranty Insurance Co
 2545 Taylor Road
 P. O. Box 235004
 Montgomery, AL 36123-5004

COMPLETE THIS SECTION ON DELIVERY

A. Received by (Please Print Clearly)

LIMMIE PICKSON

Date of Delivery

NOV 21 2002

C. Signature

X  Agent AddresseeD. Is delivery address different from item 1? YesIf YES, enter delivery address below: No

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4. Restricted Delivery? (Extra Fee)

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PS Form 3811, July 1999

Domestic Return Receipt

102595-00-M-0952



DON SIEGELMAN
GOVERNOR

STATE OF ALABAMA
DEPARTMENT OF INSURANCE
201 MONROE STREET, SUITE 1700
POST OFFICE BOX 303351
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D. DAVID PARSONS
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RICHARD L. FORD
STATE FIRE MARSHAL
JOHN S. ROBISON
GENERAL COUNSEL
MICHAEL A. BOWNES
LICENSING MANAGER
JIMMY W. GUNN

**BEFORE THE INSURANCE COMMISSIONER
OF THE
STATE OF ALABAMA**

IN THE MATTER OF:)
FINANCIAL CONDITION EXAMINATION OF)
SOUTHERN GUARANTY INSURANCE COMPANY)
AS OF DECEMBER 31, 2001)

ORDER

ON THE 15th day of January, 2003, the above entitled cause came on for consideration by the Insurance Commissioner, pursuant to Regulation 103. The Insurance Commissioner, having fully considered and reviewed the Examination Report together with any written submissions or written rebuttals and any relevant portions of the examiners' workpapers, finds and states as follows, to-wit:

JURISDICTION

1. That the Insurance Commissioner has jurisdiction of this cause, pursuant to the provisions of the Alabama Insurance Code.
2. That Southern Guaranty Insurance Company is a domestic insurer licensed for property and miscellaneous casualty, including official surety bonds, in the State of Alabama.

FINDINGS OF FACT

1. That on October 30, 2002, the verified Financial Condition Examination Report of Southern Guaranty Insurance Company was filed with the Insurance Department.
2. That following receipt of the December 31, 2001 Examination Report, the Company was afforded a reasonable opportunity of not more than twenty (20) days to make a written submission or written rebuttal with respect to any matters contained in the Examination Report.
3. That Regulation 103 provides that within twenty (20) days of the end of the period allowed for the receipt of written submissions or written rebuttals, the Insurance Commissioner shall fully consider and review the report, together with any written submissions or written rebuttals and any relevant portions of the examiners' workpapers and enter an order. The order shall either: (i) adopt the examination report as filed or with modifications or corrections, including an order that the company take actions to cure any violations; (ii) reject the examination report with directions to the examiners to reopen the examination for purposes of obtaining additional data, documentation or information; or (iii) call for an investigatory hearing for purposes of obtaining additional documentation, data, information and testimony.
4. Regulation 103 requires the company to file affidavits executed by each of its directors stating under oath that they have received a copy of the adopted report and related orders within thirty (30) days of the issuance of the adopted report.

CONCLUSIONS OF LAW

1. That the December 31, 2001 Financial Condition Examination Report of Southern Guaranty Insurance Company shall be and hereby is Adopted by the Insurance Commissioner, pursuant to Regulation 103.

ORDER
FINANCIAL CONDITION EXAMINATION
PAGE 3

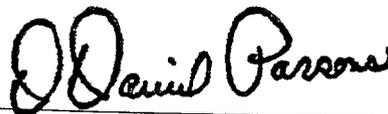
ORDER

IT IS THEREFORE ORDERED by the Commissioner of Insurance as follows:

1. That the December 31, 2001 Financial Condition Examination Report of Southern Guaranty Insurance Company is hereby Adopted.
2. That Southern Guaranty Insurance Company file an affidavit with the Alabama Department of Insurance stating that a copy of the adopted report and related orders were reviewed by the board of directors within thirty (30) days of the issuance of the adopted report.
3. That Southern Guaranty Insurance Company file an affidavit with the Department of Insurance within thirty (30) days of the issuance of the adopted report that the company filed a copy of the adopted report and related orders with all licensing states and the NAIC. An affidavit form is attached.
4. That Southern Guaranty Insurance Company shall comply with the recommendations set forth in the Report of Examination, and that failure by Southern Guaranty Insurance Company to so comply may result in sanctions or administrative action; and further, that Southern Guaranty Insurance Company shall file with the Department of Insurance within thirty (30) days of the order a statement signed by an appropriate official of the company stating the corrective action taken to comply with the recommendations made in the Report of Examination.

WITNESS My Hand and Official Seal this 15th day of January, 2003.

(SEAL)



D. David Parsons
Insurance Commissioner
201 Monroe Street, Ste 1700
Montgomery, Alabama 36130
(334) 269-3550

CERTIFICATION

I, _____, _____ (office) of
_____ Company, do hereby certify that the Report of Examination of
_____ Company as of _____, _____, was filed with all states in
which _____ Company is licensed, and with the office of the National Association of
Insurance Commissioners.

By: _____

Sworn and subscribed before the undersigned authority on the ____ day of _____, 2003.

Seal

Notary

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1. Article Addressed to:

Mr. Jim L. Ridling, President
 Southern Guaranty Insurance Co
 2545 Taylor Road
 P O Box 235004
 Montgomery, AL 36123-5004

2. Article Number (Copy from service label)

7002 2030 0000 9484 2489

PS Form 3811, July 1999

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KEITH HAYES

B. Date of Delivery

1-17-03

C. Signature

x Keith Hayes

 Agent AddresseeD. Is delivery address different from item 1? YesIf YES, enter delivery address below: No

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 Yes

file w/ report

southern guaranty

Walter R. Meriwether
Vice President &
Treasurer

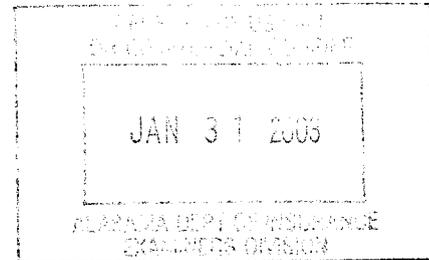
January 27, 2003

Post Office Box 235004
Montgomery, Alabama 36123
Telephone (334) 270-6114
Fax (334) 270-6283
E-mail: Rush.Meriwether@sgic.com

Mr. Richard L. Ford, CFE, CIE
Chief Examiner
State of Alabama, Department of Insurance
P. O. Box 303351
Montgomery, Alabama 36130-3351

VIA CERTIFIED MAIL

Re: Report of Examination, December 31, 2001
Southern Guaranty Insurance Company



Dear Mr. Ford:

In response to the "Comments and Recommendations" contained in the above referenced, we provide the following:

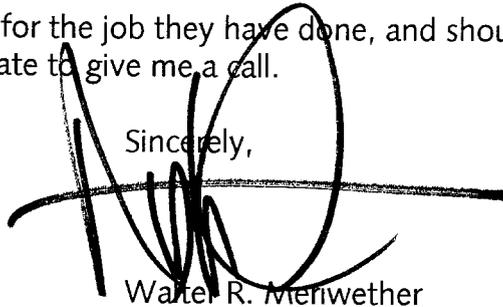
- Accounts and Records – The Company doesn't use the 20th of the month as its month-end and year-end closing dates. Certain system processes (primarily new business and claims handling) are cut off on the 20th of each month with estimates, as deemed appropriate, recorded for the period from the 21st day of the month until month-end. We apologize for any inconvenience we have caused the Alabama Examiners and their Actuaries during this examination. We do feel that this closing process still enables the Company to properly report its financial results in its quarterly and year-end financial statements.
- Bills Receivable Taken for Premium – The Company has taken the actions necessary to calculate the non-admitted portion of its bills receivable in accordance with SSAP #6.
- Reinsurance Recoverables on Loss and Loss Adjustment Expense Payments – The Company's policy is to write-off any uncollectible reinsurance balances when its determined that these balances are uncollectible.
- Losses and Loss Adjustment Expenses – The Company continually works with its consulting Actuary to improve its process of using an early cut-off date for estimating year-end reserves.
- Amounts withheld or Retained by Company for Account of Others/ Remittances and Items Not Allocated. The Company will report its suspense items as "Remittances and Items Not Allocated".

Richard L. Ford
January 27, 2003
Page Two

Additionally, enclosed herewith, you will find my Certification that a certified copy of this Report of Examination was filed with all states in which the Company is licensed, and the N.A.I.C., and that each Director of the Company received and read a copy of this Report.

Thank you and your staff for the job they have done, and should you have any questions, please don't hesitate to give me a call.

Sincerely,

A handwritten signature in black ink, appearing to be 'Walter R. Merwether', written over a horizontal line. The signature is stylized with a large loop and a long horizontal stroke.

Walter R. Merwether

WRM/mal
Enclosure

cc: Jim Ridling

Walter R. Meriwether
Vice President &
Treasurer

Post Office Box 235004
Montgomery, Alabama 36123
Telephone (334) 270-6114
Fax (334) 270-6115

CERTIFICATION

I, Walter Rushing Meriwether, Treasurer of Southern Guaranty Insurance Company, do hereby certify that the Report of Examination of Southern Guaranty Insurance Company as of December 31, 2001, was filed with all states in which Southern Guaranty Insurance Company is licensed, and with the office of the National Association of Insurance Commissioners.

By: _____

Sworn and subscribed before the undersigned authority on the 27th day of

January, 2003.

NOTARY PUBLIC IN THE STATE OF ALABAMA AT LARGE
MY COMMISSION EXPIRES ON 06/30/2005
PLEASE CONTACT ME AT 205-933-1100

Seal