

**REPORT OF
EXAMINATION**

OF

NATIONAL SECURITY FIRE & CASUALTY COMPANY

ELBA, ALABAMA

AS OF

DECEMBER 31, 2018

TABLE OF CONTENTS

EXAMINER'S AFFIDAVIT	iii
SALUTATION	1
SCOPE OF EXAMINATION.....	2
ORGANIZATION AND HISTORY	3
MANAGEMENT AND CONTROL	4
Stockholder.....	4
Board of Directors.....	4
Officers.....	4
Committees.....	5
Conflict of Interest.....	5
CORPORATE RECORDS	5
HOLDING COMPANY AND AFFILIATE MATTERS.....	5
Holding Company.....	5
Dividends to Stockholders.....	6
Management and Service Agreements.....	6
<i>Holding Company Management Service Agreement</i>	6
<i>Agreement for the Allocation of General and Administrative Expenses</i>	6
ORGANIZATIONAL CHART.....	7
FIDELITY BOND AND OTHER INSURANCE	9
EMPLOYEE AND AGENT WELFARE	9
Compliance with 18 U.S.C § 1033	10
MARKET CONDUCT ACTIVITIES	10
Territory	10
Plan of Operation	10
Advertising and Marketing.....	10
Policyholders' Complaints	11
Claims Payment Practices	11
<i>Paid Claims</i>	11
<i>Closed Without Payment/ Denied Claims</i>	11
<i>Closed Litigated Claims</i>	11
Compliance with Producer Licensing Requirements.....	12
<i>Appointment</i>	12
<i>Termination</i>	12
Underwriting and Rating.....	12

<i>Rates and Statistical Reporting</i>	12
<i>Policy Forms</i>	12
<i>Underwriting Practices</i>	13
Privacy Standards	13
SPECIAL DEPOSITS	13
FINANCIAL CONDITION AND GROWTH OF THE COMPANY	14
REINSURANCE.....	14
Ceded Reinsurance.....	14
Unaffiliated	14
<i>Property Catastrophe Excess of Loss Reinsurance Program</i>	14
<i>Reinstatement Premium Protection Reinsurance</i>	16
Affiliated.....	16
<i>Catastrophe Excess of Loss Reinsurance Agreement with Omega One Insurance Company</i>	16
ACCOUNTS AND RECORDS.....	17
Unclaimed Property	17
FINANCIAL STATEMENTS	18
NOTES TO FINANCIAL STATEMENTS	22
Analysis of Changes to Surplus	22
COMMENTS AND RECOMMENDATIONS	22
COMPLIANCE WITH PREVIOUS RECOMMENDATIONS.....	22
CONTINGENT LIABILITIES AND PENDING LITIGATION	23
SUBSEQUENT EVENTS.....	23
CONCLUSION	24

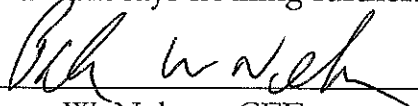
EXAMINER'S AFFIDAVIT

**STATE OF ALABAMA
COUNTY OF COFFEE**

Palmer W. Nelson, CFE, being duly sworn, states as follows:

1. I have the authority to represent Alabama in the examination of National Security Fire & Casualty Company.
2. Alabama is accredited under the National Association of Insurance Commissioners Financial Regulation Standards and Accreditation.
3. I have reviewed the examination workpapers and examination report, and the examination of National Security Fire & Casualty Company was performed in a manner consistent with the standards and procedures required by the State of Alabama.

The affiant says nothing further.



Palmer W. Nelson, CFE

Subscribed and sworn before me by Palmer W. Nelson on the 25th day of October, 2019.

(Seal)


(Signature of Notary Public)

My commission expires _____
MY COMMISSION EXPIRES
February 5, 2023



KAY IVEY
GOVERNOR

JIM L.
RIDLING
COMMISSIONER

STATE OF ALABAMA
DEPARTMENT OF INSURANCE
201 MONROE STREET, SUITE 502
POST OFFICE BOX 303351
MONTGOMERY, ALABAMA 36130-3351
TELEPHONE: (334) 269-3550
FACSIMILE: (334) 241-4192
INTERNET: www.aldoi.gov

DEPUTY COMMISSIONER
JERRY WORKMAN
MARK FOWLER

CHIEF EXAMINER
RICHARD L. FORD

STATE FIRE MARSHAL
SCOTT F. PILGREEN

GENERAL COUNSEL
REYN NORMAN

October 25, 2019

Honorable Jim L. Ridling
Commissioner of Insurance
Alabama Department of Insurance
201 Monroe Street, Suite 502
Montgomery, AL 36104

Dear Commissioner Ridling:

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, a full scope financial and market conduct examination as of December 31, 2018, has been made of

**National Security Fire & Casualty Company
Elba, AL**

at its home office located at 661 East Davis Street Elba, AL 36323. The report of examination is submitted herewith. Where the description "The Company" or "NSFC" appears herein, without qualification, it will be understood to indicate National Security Fire & Casualty Company.

SCOPE OF EXAMINATION

We have performed an examination of National Security Fire & Casualty Company, a multi-state insurance company. The last examination covered the period of January 1, 2010 through December 31, 2013. The current examination covers the period of January 1, 2014 through December 31, 2018.

The examination was conducted in accordance with the NAIC *Financial Condition Examiners Handbook*. The Handbook requires that we plan and perform the examination to evaluate the financial condition, assess corporate governance, identify current and prospective risks of the Company and evaluate system controls and procedures used to mitigate those risks. An examination also includes identifying and evaluating significant risks that could cause an insurer's surplus to be materially misstated both currently and prospectively.

All accounts and activities of the Company were considered in accordance with the risk-focused examination process. This may include assessing significant estimates made by management and evaluating management's compliance with Statutory Accounting Principles. The examination does not attest to the fair presentation of the financial statements included herein. If, during the course of the examination an adjustment is identified, the impact of such adjustment will be documented separately following the Company's financial statements.

This examination report includes significant findings of fact, as mentioned in the *Code of Alabama, 1975*, as amended and general information about the insurer and its financial condition. There may be other items identified during the examination that, due to their nature, are not included within the examination report but separately communicated to other regulators and/or the Company.

The Company's annual statements for each year under examination were compared with or reconciled to the corresponding general ledger account balances.

An examination of the Company's information systems (IS) was conducted concurrently with the financial examination. The IS examination included a review of management and organizational controls, logical and physical security controls, changes in applications controls, system and program development controls, contingency planning controls, service provider controls, operations controls, processing controls, e-commerce controls, and network and internet controls.

A market conduct examination was performed concurrently with the financial examination. The examination included reviews of the Company's territory, plan of

operation, claims payment practices, advertising and marketing, underwriting and rating, policyholders' complaints, compliance with producers licensing requirements, and privacy standards. See the "Market Conduct Activities" section of this report on page 10 for further discussion.

Warren Averett, LLC, was the Company's certified public accountant (CPA) for all years under examination. The examiners reviewed the CPA's workpapers, copies of which were incorporated into the examination as deemed appropriate. The workpapers of the Company's internal audit department were reviewed and considered in the examiner's identification and assessment of risks and controls.

A signed letter of representation was obtained at the conclusion of the examination. In this letter, management attested to having valid title to all assets and to the nonexistence of unrecorded liabilities as of December 31, 2018.

ORGANIZATION AND HISTORY

The Company was incorporated on January 1, 1959, under the laws of the State of Alabama, as a wholly owned subsidiary of National Security Insurance Company.

Various changes in the amounts and par value of the Company's capital stock occurred between the date of incorporation and 1985. From 1985 through 1991, the authorized capital remained 1,500,000 shares of \$1.00 par value common stock of which 1,000,000 shares were issued and outstanding.

On December 31, 1990, all of the Company's outstanding capital stock was contributed to a newly formed holding company, The National Security Group, Inc. (NSG), a Delaware corporation. Simultaneously, an extraordinary cash dividend of \$10,000,000 was declared by the Company's Board of Directors payable to NSG.

On June 30, 1992, the Company paid a stock dividend for 500,000 shares to NSG; thereby increasing the Company's paid up capital to \$1,500,000 consisting of 1,500,000 shares of \$1.00 par value common stock.

During 2005, the Company received a capital contribution of \$6,000,000 from its sole owner, The National Security Group, Inc.

The Company's capital structure at December 31, 2018 consisted of 1,500,000 shares of common stock, issued and outstanding, for a total common stock par value of \$1,500,000. The Company also had \$6,360,000 in gross paid in and contributed

surplus and reported \$26,784,776 of unassigned funds. The Company's total reported capital and surplus at December 31, 2018, was \$34,644,776.

MANAGEMENT AND CONTROL

Stockholder

The Company is a stock corporation with ultimate control vested in its stockholders. At December 31, 2018, 100% of the Company's issued and outstanding common stock was owned by The National Security Group, Inc., a Delaware corporation.

Board of Directors

<u>Director</u>	<u>Residence</u>	<u>Principal Occupation</u>
William Lister Brunson, Jr.	Elba, Alabama	President, National Security Insurance Company and CEO of The National Security Group, Chairman of the Board of National Security Insurance Company, National Security Fire & Casualty Company, and Omega One Insurance Company
Jack Edward Brunson	Elba, Alabama	President, National Security Fire & Casualty Company and Omega One Insurance Company
Brian Richard McLeod	Elba, Alabama	Treasurer and Chief Financial Officer of National Security Insurance Company, National Security Fire & Casualty Company and Omega One Insurance Company
Patricia Bowdoin Henderson	Elba, Alabama	Vice President of National Security Insurance Company

Officers

Officers of the Company elected by the Board of Directors and serving at December 31, 2018 were as follows:

<u>Officer</u>	<u>Title</u>
Jack Edward Brunson	President
Brian Richard McLeod	Treasurer
Tonya Matthews Jones	Secretary
Timothy Richard Wilson	Vice President
Kelly Holland Jackson	Controller
Patricia Bowdoin Henderson	Vice President

Committees

The Company had no committees of the Board during the examination. The Audit Committee of the holding company, The National Security Group, Inc. serves as the audit committee of all insurance companies of the group.

Conflict of Interest

The conflict of interest statements filed by the officers and directors of the Company were reviewed for this examination period. There were no conflicts disclosed.

CORPORATE RECORDS

The Company's Articles of Incorporation, By-Laws, and amendments thereto were inspected during the course of the examination and appeared to provide for the operation of the Company in accordance with usual corporate practices and applicable regulations.

HOLDING COMPANY AND AFFILIATE MATTERS

Holding Company

The Company was subject to the Alabama Insurance Holding Company Regulatory Act, as defined in ALA. CODE § 27-29-1(1975). The Company's sole owner, The National Security Group, Inc. was registered with the Alabama Department of Insurance as registrant of an Insurance Holding Company System.

Appropriate filings required under the Holding Company Act were made from time to time by the registrant. A review of the Company's filings during the period under examination indicated that all required filings were made.

Dividends to Stockholders

The Company paid the following stockholder dividends during the examination period.

Year	Stockholder Dividends
2018	\$0
2017	\$0
2016	\$1,000,000
2015	\$1,500,000
2014	\$1,750,000

Management and Service Agreements

The following agreements between the Company and its affiliates were in effect during the examination period.

Holding Company Management Service Agreement

Effective July 1, 2010, The National Security Group, Inc. (NSG), the Holding Company, entered into a Holding Company Management Service Agreement among and between, National Security Fire and Casualty Company, Omega One Insurance Company and National Security Insurance Company.

The one year term of the Holding Company Management Service Agreement is renewable for successive one year periods until either party terminates or until modified, amended or superseded by a subsequent agreement.

The purpose is to provide remuneration for services provided by the Holding Company on behalf of and/or to the benefit of its subsidiaries. The primary intent of this fee is to cover the operating costs of NSG related to providing additional risk management, board oversight and various other benefits to its subsidiaries. The Holding Company Management Fee is calculated and paid on a monthly basis.

Agreement for the Allocation of General and Administrative Expenses

On December 1, 2011, an Amendment to the Management Agreement for Allocation of General and Administrative Expenses, Adjuster Employees and Income Taxes was filed. A Form D Prior Notice of a Transaction was filed with the Alabama Department of Insurance by The National Security Group, Inc. (NSG) on behalf of

the following Insurance Companies: National Security Insurance Company, National Security Fire & Casualty Company, Omega One Insurance Company, and Natsco, Inc. The amendment provided for allocation of common expenses, adjuster fees and income taxes between NSG and its subsidiaries.

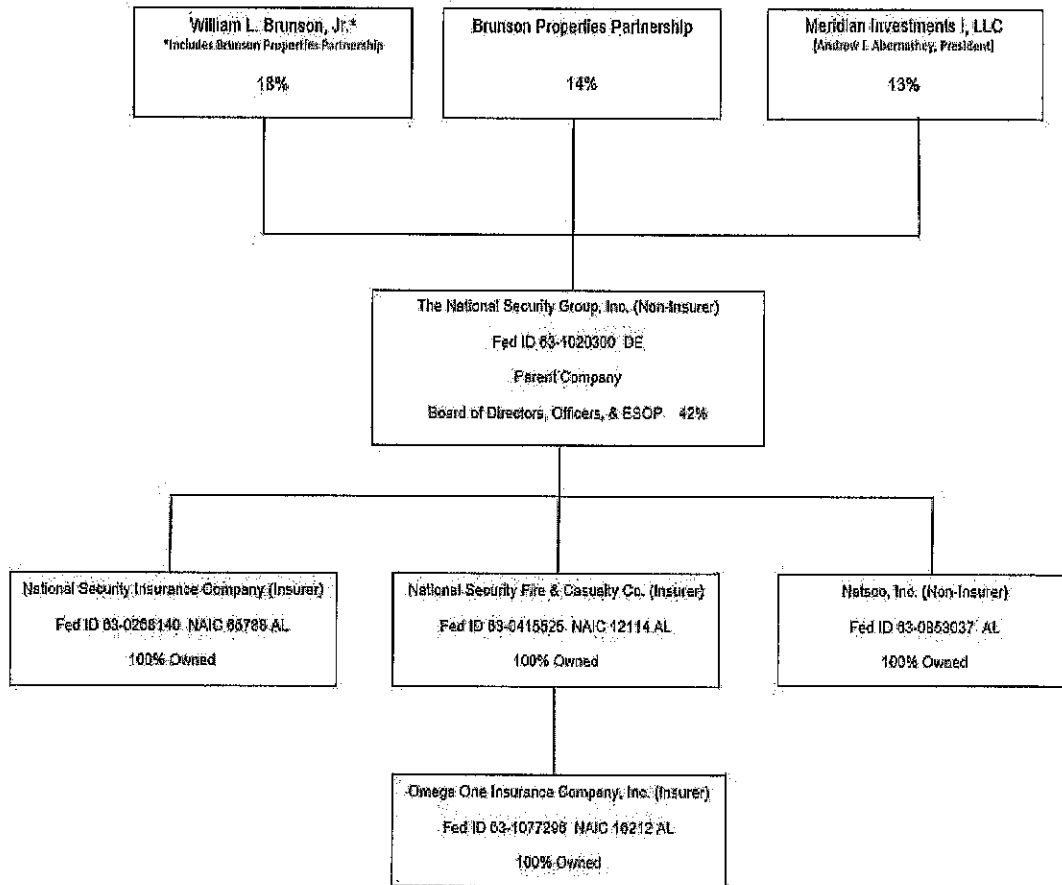
In consideration for the settlement of common expenses, adjuster fees and income taxes between NSG and its subsidiaries, each subsidiary agreed to pay the respective amounts to the respective Company as calculated using the most pertinent means which shall be construed as reimbursement of all direct costs.

This term of the agreement was for one year, renewable for successive one year periods until any party elects to terminate or until modified, amended or superseded by a subsequent agreement.

ORGANIZATIONAL CHART

The following chart presents the affiliations of the entities affiliated with the Company.

Organizational Chart



FIDELITY BONDS AND OTHER INSURANCE

The Company was insured by a Financial Institution Bond issued by Liberty Mutual Insurance Company. The bond was issued to The National Security Group, Inc. and Subsidiaries beginning in May 2018. The amount of the fidelity bond maintained by the Company exceeded the minimum amount suggested in the NAIC

Financial Condition Examiners Handbook.

In addition to the above coverage, the Company was named insured under policies affording the following protections at December 31, 2018:

- Business Auto Coverage with The Cincinnati Insurance Company.
- Commercial Property Coverage with The Cincinnati Insurance Company.
- Commercial General Liability Coverage with The Cincinnati Insurance Company.
- Electronic Data Processing Coverage with The Cincinnati Insurance Company.
- Claims Liability Insurance with National Union Fire Insurance Company of Pittsburgh, PA.
- IT Cyber Security Insurance Coverage with National Union Fire Insurance Company of Pittsburgh, PA.
- System Failure Coverage with National Union Fire Insurance Company of Pittsburgh, PA.

The examiners determined that the Company appeared to have adequate insurance for the hazards and risks to which it was exposed.

EMPLOYEE AND AGENT WELFARE

The Company did not have any employees at December 31, 2018; therefore it had no employee benefit plans. All functions of the Company were performed by employees of National Security Insurance Company via the terms of an administrative services agreement. The Company utilized an independent agent distribution system.

Compliance with 18 U.S.C. § 1033

The examiners reviewed the Company's internal procedures to determine if prospective and current employees or employees of affiliates are in compliance with 18 U.S.C. § 1033, which prohibits persons with certain felony offenses from participating in conducting the business of insurance.

The examiners determined that the Company had adequate procedures and were in compliance with 18 U.S.C. § 1033 and ALA. ADMIN. CODE 482-1-146 (2009) during the exam period.

MARKET CONDUCT ACTIVITIES

Territory

As of December 31, 2018, the Company was licensed to write business in the following states: Alabama, Arkansas, California, Florida, Georgia, Kentucky, Mississippi, Oklahoma, South Carolina, Tennessee, and West Virginia.

The Company wrote business on a surplus lines basis in Louisiana, Idaho, Missouri, and Texas.

Plan of Operation

The Company's primary lines of businesses were Property and Casualty. The types of products written are property, dwelling fire/mobile home, limited homeowners, comprehensive mobile homeowners, dwelling and tenant scheduled options. As of December 31, 2018, the Company's agency force consisted of approximately 800 independent producers with a small staff of home service captive producers.

Advertising and Marketing

The National Security Group, Inc., the holding company, did general corporate advertising with very little specific advertisement of its products. The Company had a limited number of advertisements appearing in insurance periodicals during the examination period. Brochures and advertising materials were distributed to potential customers through the Company's agents.

The Company's website (www.nationalsecuritygroup.com) provided information about its products, access to claim forms that can be submitted over the website,

information to help customers find an agent, information for prospective agents, investor information, and instructions for customers to submit premium payments on-line.

Policyholders' Complaints

The Company had adequate complaint procedures in place for the distribution of complaints, and obtaining and recording responses to those complaints. The examiner reviewed all of the Company's Alabama complaints during the examination period, a total of nine complaints forwarded by the Alabama Department of Insurance. No consumer direct complaints were received by the Company during the examination period. It was determined that the complaints were responded to timely. The Company fully addressed the issues raised by the complainants. The Company properly documented its complaint register in the required format.

Claims Payment Practices

Paid Claims

The examiner selected a sample of 110 Alabama paid claims from the population of 74,061 transactions for the examination period (2014-2018). The sample was reviewed for compliance with the Company's policy provisions, timeliness of payments, and adequacy of documentation. There were no issues noted as a result of the sample review. Each claim in the sample was paid in compliance with ALA. ADMIN. CODE 482-1-125-.07(1)(2003).

Closed Without Payment/Denied Claims

A sample of 110 Alabama denied and closed without payment claims was selected from a population of approximately 1,760 closed without payment or denied claims for the examination period (2014-2018). The sample was reviewed for compliance with the Company's policy provisions and adequacy of documentation. No discrepancies were found as a result of the sample review.

Closed Litigated Claims

The entire population of 63 closed litigated claims during the examination period (2014-2018) was reviewed. No problematic claim handling practices were noted during the review.

Compliance with Producer Licensing Requirements

Appointment

A random sample of 114 transactions was selected from the Alabama written premium transactions that took place during the examination period. The examiners used the NAIC's State Based System and verified that all the producers that produced the business represented in the sample were appropriately licensed and appointed by the Company prior to each producer writing the subject business.

Termination

A random sample of 79 Alabama terminated producers was selected from a population of 97 terminations. The examiners reviewed the producer termination notifications on the State Based System and termination notification letters sent to the producers. The Company did not send a termination notification to one of its terminated producers in accordance with ALA. CODE § 27-7-30.1(a)(1975), which states: "Within 15 days after making the notification required by subsection (e) of Section 27-7-30, the insurer shall mail a copy of the notification to the producer at his or her last known address."

Underwriting and Rating

Rates and Statistical Reporting

The Company reports all written premium, paid and unpaid losses to Independent Statistical Service (ISS). The Company also subscribes to Insurance Services Offices (ISO) and American Association of Insurance Services (AAIS) manuals, forms and symbols. The Company independently filed its changes to AAIS forms with the Departments of Insurance in states the Company wrote business.

Policy Forms

The examination indicated that all of the forms, endorsements and premium rates utilized by the Company in Alabama during the examination period had been properly filed and approved by the Alabama Department of Insurance.

Underwriting Practices

A random sample of 114 Alabama premium transactions was selected from the premium transactions in 2014-2018. The examiners recalculated the premium amounts and verified that the premium was calculated in accordance with the Company's Underwriting guidelines and rates filed with the Department. It was verified that the Company's policies and endorsements were issued to the applicants in a timely manner. The examiners also reviewed a sample of 116 Alabama canceled policies and a sample of 116 rejected applications for insurance for completeness and accuracy and whether notices were sent timely. No discrepancies were noted during the review.

Privacy Standards

The Company's Privacy Notice was reviewed for compliance to ALA. ADMIN. CODE 482-1-122(2001). The Company sent out the notices to policyholders when a policy was written or renewed and annually thereafter. The Company provided notices to its customers that indicated the types of information collected, the way the information is used and the manner that it is collected. The notice also informed the customer that the Company did not disclose any information to any nonaffiliated third parties.

The Company's privacy notice emphasized and explained the Company's policies. The Company's policies followed the guidelines established in ALA. ADMIN. CODE 482-1-122(2001).

The Company does not share customer and/or consumer personal information with any nonaffiliated third parties. The Company had proper controls in place for employees and producers for the disclosure of nonpublic personal financial, health or medical information.

SPECIAL DEPOSITS

At December 31, 2018, as required or permitted by law, the Company maintained deposits with the respective statutory authorities as follows:

State	Book/Adjusted Carrying Value	Fair Value
Alabama	\$1,129,633	\$1,092,496
Georgia	\$50,000	\$51,300

FINANCIAL CONDITION/GROWTH OF THE COMPANY

	<u>2014</u>	<u>2015</u>	<u>2016</u>	<u>2017</u>	<u>2018</u>
Admitted Assets	\$ 73,639,965	\$ 76,405,971	\$ 75,664,706	\$ 73,266,506	\$ 73,957,530
Liabilities	41,325,956	41,960,170	40,422,502	39,078,195	39,312,756
Gross Written Premium	58,925,968	60,422,801	6,113,736	61,497,514	61,006,871
Net Losses Incurred	22,821,769	26,390,572	29,463,439	33,275,289	30,882,182
Net Loss Adjustment					
Expenses Incurred	4,269,033	4,365,806	4,355,208	4,899,789	4,528,963
Common Capital Stock	1,500,000	1,500,000	1,500,000	1,500,000	1,500,000
Gross Paid in and					
Contributed Surplus	6,360,000	6,360,000	6,360,000	6,360,000	6,360,000
Unassigned Funds	24,454,009	26,585,803	27,382,206	26,328,313	26,784,776

REINSURANCE

Ceded Reinsurance

Unaffiliated

Property Catastrophe Excess of Loss Reinsurance Program

As of December 31, 2018, the Company had a property catastrophe agreement that involved three excess layers. The business of the Company's subsidiary, Omega One Insurance Company, was also reinsured under the agreement. The limits, retentions, and reinsurance premiums were applicable to the combined losses and premiums of the Company and its subsidiary. The business reinsured was policies classified as dwelling and commercial fire, allied lines, homeowners (section I only), mobile homes, inland marine, special multi-peril (section I only) and industrial fire in force at the inception of this contract or written or renewed during the term of the contract. The term of the agreement was January 1, 2018 to January 1, 2019, with respect to losses occurring during the contract term.

The retentions and limits were per occurrence. There was an aggregate loss limit for losses from all occurrences within each layer that was twice the per occurrence limit. Each layer began where the previous layer ended leaving no gaps in reinsurance from the first layer to the third. The catastrophe reinsurance program provided reinsurance for \$72.5 million of catastrophe losses from any one occurrence with a retention of \$4 million for any one event. The layers of excess of loss reinsurance were as follows:

- First Layer - \$13.5 million each occurrence, in excess of \$4 million
- Second Layer - \$25 million each occurrence in excess of \$17.5 million
- Third Layer - \$30 million each occurrence in excess of \$42.5 million

Reinsurers and Percentage of Participation:

Participating Reinsurer	1st Layer	2nd Layer	3rd Layer
Allied World Reinsurance Company	7.50%	2.50%	2%
American Standard Insurance Company of Wisconsin	0%	1%	1.75%
Arch Reinsurance Company	0%	5%	5%
Employers Mutual Casualty Company	0%	1.50%	0%
Everest Reinsurance Company	16%	13%	11%
Farm Mutual Reinsurance Plan, Inc.	8%	2.25%	1%
Fidelis Insurance Bermuda Limited	1.50%	1.50%	1.50%
Hamilton Re, Ltd.	0%	1.50%	1.50%
Hanover Rueck SE	2%	1%	0%
Hanover Rueck SE	5%	4.50%	0%
Lloyds London Syndicate 2001	5%	15%	15%
Lloyds London Syndicate 2791	8.75%	0%	0%
Lloyds London Syndicate 2791	3.75%	0%	0%
Lloyds London Syndicate 1729	1.50%	2.50%	6.50%
Lloyds London Syndicate 2014	1%	2%	2%
Lloyds London Syndicate 4444	0%	7%	7%
Lloyds London Syndicate 2010	0%	1%	1%
Lloyds London Syndicate 2007	0%	2%	3.50%
Lloyds London Syndicate 5886	0%	1%	1%
Lloyds London Syndicate 780	0%	1%	1%
Lloyds London Syndicate 3334	0%	0.75%	1%
Lloyds London Syndicate 1225	0%	1%	1%
MS Amlin AG, Bermuda Branch	0%	2%	5%
R+V Versicherung AG	22.50%	22.50%	21%
Renaissance Reinsurance Ltd.	1.50%	0%	1%
Swiss Reinsurance America Corporation	5%	3%	3%
Taiping Reinsurance Company Limited	0%	0%	2.25%
Validus Reinsurance, Ltd.	10%	2.50%	3.50%
Fidelis Underwriting Limited	1%	3%	1.50%

The catastrophe reinsurance was administered by a reinsurance intermediary, Guy Carpenter. Interest and liability agreements with the subscribing reinsurers were a part of the agreement. All communications between the parties were transmitted through the intermediary. Payments by the Company were deemed to constitute

payment to the participating reinsurers. Payments by the reinsurers to the intermediary were deemed to constitute payment to the Company, to the extent that such payments were actually received by the Company. The agreement provided reinsurance for any one occurrence. The agreement had provisions for a reinstatement premium to reinstate the reinsurance subsequent to an occurrence.

The Property Catastrophe Excess of Loss Agreement and the Reinstatement Premium Protection Reinsurance Agreement were replaced by agreements for the subsequent year beginning January 1, 2019 with terms that were substantially the same as the terms of the agreements that were in effect at December 31, 2018.

Reinstatement Premium Protection Reinsurance

The Company and its subsidiary, Omega One Insurance Company, had an agreement for the purpose of indemnifying the Company for reinstatement premiums due under the Company’s Property Catastrophe Excess of Loss Reinsurance Agreement. The term of the agreement was January 1, 2018 to January 1, 2019. The agreement was structured with two excess layers of reinsurance. The reinsurers and the percentage of participation were as follows:

Reinsurer	1 st Layer Participation	2 nd Layer Participation
Everest Reinsurance Company	20%	20%
Farm Mutual Reinsurance Plan, Inc.	5%	10%
Hanover Rueck SE	35%	35%
Lloyds London Syndicate 1729	5%	10%
Validus Reinsurance, Ltd.	35%	25%

Affiliated

Catastrophe Excess of Loss Reinsurance Agreement with Omega One Insurance Company

The Company had a catastrophe reinsurance agreement with its subsidiary, Omega One Insurance Company (Omega) effective February 15, 2015 for a one year term. The agreement has subsequently been renewed each year and the agreement for the term February 15, 2018 to February 15, 2019 was in effect as of the examination date. The agreement may be cancelled by either party giving the other sixty days advance notice of cancellation. The agreement covers the Company’s business known as dwelling fire, allied lines, homeowners (section I only), and mobile home. Under the terms of the agreement, Omega agreed to reinsure catastrophe losses in excess of \$3 million from any one occurrence up to a limit of \$1 million per occurrence. The reinsurance may be reinstated following a catastrophe event by payment of the

reinstatement premium. The aggregate limit for all events under the contract is \$2 million.

ACCOUNTS AND RECORDS

The Company maintained its accounting, premiums and losses data electronically. The Company maintained additional electronic workpapers, reconciliations and statements in its database of imaged records.

The Company's independent audit was performed by Warren Averett, a certified public accounting firm of Birmingham, Alabama.

Unclaimed Property

The Company provided its outstanding checks detail as of December 31, 2018. The Company had five outstanding checks totaling \$7,134.21 payable to Alabama residents with a dormancy period greater than three years. These outstanding checks were unclaimed property per the Alabama Code.

It was determined that the Company did not properly escheat the unclaimed property to the State of Alabama in accordance with ALA. CODE § 35-12-72(1975), which states: "(a) Property is presumed abandoned if it is unclaimed by the apparent owner during the time set forth below for the particular property ... (18) All other property, three years after the owner's right to demand the property or after the obligation to pay or distribute the property arises, whichever first occurs." All Alabama unclaimed property is to be included in the unclaimed property reports in accordance with the reporting procedures described in ALA. CODE § 35-12-76(1975).

FINANCIAL STATEMENTS

The following financial statements are based on the statutory financial statements filed by the Company with the Alabama Department of Insurance and present the financial condition of the Company for the period ending December 31, 2018. The accompanying comments on financial statements reflect any examination adjustments to the amounts reported in the annual statement and should be considered an integral part of the financial statements.

Statement of Assets, Liabilities, Surplus and Other Funds	19
Statement of Income.....	20
Capital and Surplus.....	21

National Security Fire & Casualty Company
Statement of Assets, Liabilities, Surplus and Other Funds
For the Year Ended December 31, 2018

<u>ASSETS</u>	Assets	Non Admitted Assets	Net Admitted Assets
Bonds	\$ 40,166,722	-	\$ 40,166,722
Common stocks	7,699,175	-	7,699,175
Properties held for the production of income	2,557,391	-	2,557,391
Cash (\$...(274,172), Schedule E-Part 1), cash equivalents (\$....0, Schedule E-Part 2) and short-term investments (\$...3,730,159, Schedule DA	3,455,987	-	3,455,987
Other Invested Assets	1,981,803	-	\$ 1,981,803
Subtotals, cash and invested assets	\$ 55,861,078	-	\$ 55,861,078
Investment income due and accrued	192,047	-	192,047
Uncollected premiums and agents' balances	111,778	3,411	108,367
Deferred Premiums, agents' balances and installments booked but deferred and not yet due	11,005,193	-	11,005,193
Amounts recoverable from reinsurers	387,565	20,052	367,513
Current federal and foreign income tax recoverable and interest thereon	363,311	-	363,311
Net deferred tax asset	1,607,444	179,628	1,427,817
Electronic data processing equipment and software	32,394	-	32,394
Furniture and equipment, including health care delivery assets	22,528	22,528	-
Receivables from parent, subsidiaries and affiliates	3	-	3
Aggregate write-ins for other-than-invested assets	4,604,380	4,573	4,599,807
TOTAL ASSETS	\$ 74,187,722	\$ 230,192	\$ 73,957,530
<u>LIABILITIES</u>			
Losses			\$ 6,435,464
Loss adjustment expenses			366,874
Commissions payable, contingent commissions and other similar charges			760,717
Other expenses (excluding taxes, licenses and fees)			953,309
Taxes, licenses and fees (excluding federal and foreign income taxes)			666,034
Unearned premiums			29,171,026
Advance premium			818,466
Ceded reinsurance premiums payable			6,968
Funds held by company under reinsurance treaties			69,307
Provision for reinsurance (including \$...26,000 certified)			33,000
Payable to parent, subsidiaries and affiliates			31,592
TOTAL LIABILITIES			\$ 39,312,757
<u>SURPLUS</u>			
Common capital stock			\$ 1,500,000
Gross paid in and contributed surplus			6,360,000
Unassigned funds (surplus)			26,784,776
Surplus as regards policyholders			\$ 34,644,776
TOTAL LIABILITIES, SURPLUS AND OTHER FUNDS			\$ 73,957,533

**THE NOTES TO THE FINANCIAL STATEMENTS ARE AN INTEGRAL
PART THEREOF**

National Security Fire & Casualty Company
Statement of Income
For the Year Ended December 31, 2018

<u>UNDERWRITING INCOME</u>	2018	2017	2016	2015	2014
Premiums earned	\$ 54,225,645	\$ 54,432,684	\$ 54,553,078	\$ 52,550,280	\$ 50,279,232
DEDUCTIONS					
Losses incurred	30,882,182	33,275,289	29,463,439	26,390,572	22,821,769
Loss adjustment expenses	4,528,963	4,899,789	4,355,208	4,365,806	4,269,033
Other underwriting expenses incurred	19,467,500	19,599,804	19,630,261	19,554,292	18,962,772
Aggregate write-ins for underwriting deductions	2,853	-	-	-	5,782
Total underwriting deductions	<u>\$ 54,881,498</u>	<u>\$ 57,774,882</u>	<u>\$ 53,448,908</u>	<u>\$ 50,310,670</u>	<u>\$ 46,059,356</u>
Net underwriting gain (loss)	<u>\$ (655,853)</u>	<u>\$ (3,342,198)</u>	<u>\$ 1,104,170</u>	<u>\$ 2,239,610</u>	<u>\$ 4,219,876</u>
<u>INVESTMENT INCOME</u>					
Net investment income earned	\$ 1,133,493	\$ 1,007,595	\$ 1,165,944	\$ 1,185,627	\$ 1,151,983
Net realized capital gains (losses less capital gains tax of \$...8,123)	<u>\$ 30,557</u>	<u>\$ 75,211</u>	<u>\$ 167,681</u>	<u>\$ 109,576</u>	<u>\$ (314,552)</u>
Net investment gain (loss)	<u>\$ 1,164,050</u>	<u>\$ 1,082,806</u>	<u>\$ 1,333,625</u>	<u>\$ 1,295,203</u>	<u>\$ 837,431</u>
<u>OTHER INCOME</u>					
Finance and service charges not included premiums	\$ 566,434	\$ 560,412	\$ 576,961	\$ 587,476	\$ 534,047
Aggregate write-ins for miscellaneous items	<u>(342,340)</u>	<u>142,228</u>	<u>(8,630)</u>	<u>(186,170)</u>	<u>3,277,554</u>
Total other income	<u>\$ 224,094</u>	<u>\$ 702,640</u>	<u>\$ 568,331</u>	<u>\$ 401,306</u>	<u>\$ 3,811,601</u>
Net income before dividends to policyholders, after capital gains tax and before all other federal and foreign income taxes	\$ 732,292	\$ (1,556,752)	\$ 3,006,126	\$ 3,936,120	\$ 8,868,908
Net income, after dividends to policyholders, after capital gains tax and before all other federal and foreign income taxes	732,292	(1,556,752)	3,006,126	3,936,120	8,868,908
Federal and foreign income taxes incurred	<u>\$ (53,552)</u>	<u>\$ (635,801)</u>	<u>\$ 945,649</u>	<u>\$ 948,123</u>	<u>\$ 2,278,157</u>
Net income	<u>\$ 785,844</u>	<u>\$ (920,951)</u>	<u>\$ 2,060,477</u>	<u>\$ 2,987,997</u>	<u>\$ 6,590,751</u>

THE NOTES TO THE FINANCIAL STATEMENTS ARE AN INTEGRAL PART THEREOF

National Security Fire & Casualty Company
Capital and Surplus
For the Year Ended December 31, 2018

	2018	2017	2016	2015	2014
Surplus as regards policyholders, December 31 prior year	<u>\$ 34,188,313</u>	<u>\$ 35,242,206</u>	<u>\$ 34,445,803</u>	<u>\$ 32,314,009</u>	<u>\$ 26,317,373</u>
Net income	785,844	(920,951)	2,060,477	2,987,997	6,590,751
Change in net unrealized capital gains or (losses) less capital gains tax of	(277,333)	405,126	93,416	481,338	508,281
Change in net deferred income tax	326	(1,087,907)	(10,496)	373,461	666,993
Change in nonadmitted assets	(66,372)	253,838	(41,993)	(173,002)	(116,389)
Change in provision for reinsurance	14,000	296,000	(305,000)	(38,000)	97,000
Dividends to stockholders	-	-	(1,000,000)	(1,500,000)	(1,750,000)
Change in surplus as regards policyholders for the year	<u>456,465</u>	<u>(1,053,894)</u>	<u>796,404</u>	<u>2,131,794</u>	<u>5,996,636</u>
Surplus as regards policyholders, December 31 current year	<u>\$ 34,644,778</u>	<u>\$ 34,188,312</u>	<u>\$ 35,242,207</u>	<u>\$ 34,445,803</u>	<u>\$ 32,314,009</u>

**THE NOTES TO THE FINANCIAL STATEMENTS ARE AN INTEGRAL
PART THEREOF**

NOTES TO FINANCIAL STATEMENTS

Analysis of Changes to Surplus

No changes were made to surplus.

COMMENTS AND RECOMMENDATIONS

Compliance with Producers Licensing Requirements – Page 12

It is recommended that the Company properly send notifications to the terminated producers' last known address in compliance with ALA. CODE § 27-7-30.1(a)(1975), which states: "Within 15 days after making the notification required by subsection (e) of Section 27-7-30, the insurer shall mail a copy of the notification to the producer at his or her last known address."

Accounts and Records – Page 17

It is recommended that the Company properly identify and escheat all Alabama unclaimed property in accordance with ALA. CODE § 35-12-72(1975), which states, "(a) Property is presumed abandoned if it is unclaimed by the apparent owner during the time set forth below for the particular property ... (18) All other property, three years after the owner's right to demand the property or after the obligation to pay or distribute the property arises, whichever first occurs." All Alabama unclaimed property is to be included in the unclaimed property reports in accordance with the reporting procedures described in ALA. CODE § 35-12-76(1975).

COMPLIANCE WITH PREVIOUS RECOMMENDATIONS

A review was performed to determine if the Company had complied with the recommendations made in the last examination report. The review indicated that the Company had complied with the recommendations contained in the most recent Report of Examination with the exception of the item noted below.

The previous examination report included a recommendation for the Company to identify and escheat all Alabama unclaimed property in accordance with ALA. CODE § 35-12-72 (a)(1975), which states, "Property is presumed abandoned if its unclaimed by the apparent owner during the time set forth below for the particular property ... (18) All other property, three years after the owner's right to demand the property or after the obligation to pay or distribute the property arises, whichever

first occurs.” The examination indicated that the Company did not escheat all Alabama unclaimed property to the Alabama Unclaimed Property Division.

CONTINGENT LIABILITIES AND PENDING LITIGATION

The review of the contingent liabilities and pending litigation included an inspection of representations made by the Company’s managers, a review of the Company’s records and files for the period under examination, and a review of the records subsequent to the examination date. The reviews performed did not identify any items that would have a material effect on the Company’s financial condition in the event of an adverse outcome.

SUBSEQUENT EVENTS

On February 2, 2017, Meridian Investments I, LLC (Meridian), represented by the entity’s principal owner, Andrew Abernathey, was approved to acquire an ownership of 14.9% of The National Security Group, Inc. (NSG), the publicly traded holding company. The Department held a Form A hearing on March 21, 2019. An order was signed March 27, 2019 approving Meridian acquiring an ownership of NSG up to 20.9%.

The review of the events subsequent to December 31, 2018, did not reveal any other items of a material amount or noteworthy in nature.

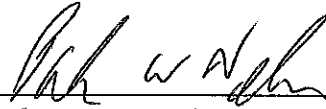
CONCLUSION

Acknowledgement is hereby made of the courtesy and cooperation extended by all persons representing National Security Fire & Casualty Company during the examination.

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

In addition to the undersigned, Theo Goodin, ALMI, MCM, Jacob Grissett, Chemeka Thomas, Charles Turner, CISA, and Kizzy Williams, Examiners; and Brent Sallay, FCAS, MAAA, of Taylor Walker & Associates, Consulting Actuary; all representing the Alabama Department of Insurance, participated in the examination of National Security Fire & Casualty Company.

Respectfully submitted,



Palmer W. Nelson, CFE
Examiner-in-charge
Alabama Department of Insurance