

**Homewise Insurance Company
Insolvency Report
June 30, 2015**

Prepared by:





Receivership information:

| | |
|-----------------------------|-----------------------------------|
| Name of Receivership | Homewise Insurance Company |
| Case number | 2011-CA-003221 |
| Date of Conservation | N/A |
| Date of Rehabilitation | N/A |
| Date of Liquidation | November 18, 2011 |

Scope:

As provided in the Provider Contract between the “Receiver of the Estate of **Homewise Insurance Company**” (the Receiver being the Florida Department of Financial Services, Division of Rehabilitation and Liquidation), 2020 Capital Circle, SE, Alexander Building, 3rd Floor, Tallahassee, Florida 32302, hereinafter referred to as “RECEIVER”, and **Carr, Riggs & Ingram, LLC**, whose address is 1713 Mahan Drive, Tallahassee, FL 32308, hereinafter referred to as “PROVIDER”, effective February 6, 2012, Section 5.3.9, SCOPE OF WORK, states:

5.3.9. Prepare insolvency summary reports ("Insolvency Reports"), pursuant to the requirements of 631.398 (3), Florida Statutes.

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

Chapter 631

INSURER INSOLVENCY; GUARANTY OF PAYMENT

631.398

Prevention of insolvencies.

—

To aid in the detection and prevention of insurer insolvencies or impairments:

(1)

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

(2)

The office shall:

(a)

Report to the board of directors of the appropriate insurance guaranty association when it has reasonable cause to believe from any examination, whether completed or in process, of any member insurer that such insurer may be an impaired or insolvent insurer.

(b)

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

(3)

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

History.

—

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

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

Our review of files in the RECEIVER's possession began in February, 2012 in conjunction with a forensic analysis engagement and continued through January, 2013. Approximately two days were spent reviewing hard copy files in the offices of Florida Department of Financial Services. One day was spent reviewing files at the office of the Company's audit firm. All other review procedures were conducted at the office of the PROVIDER through examination of electronic files provided by the RECEIVER and hard copy documents provided by vendors and banking institutions.

Business

Historical information related to the company is as follows:

Homewise Insurance Company (the Company) (TIC 20-5935917) was incorporated in the State of Florida on April 4, 2005, received its Certificate of Authority on December 5, 2005, and began operations on January 12, 2006.

The Company represented itself as a homeowner's insurer, providing wind-only coverage exclusively in the State of Florida.

According to audited financial statements and tax returns examined, the Company is a wholly-owned subsidiary of Homewise Holdings, Inc. (HHI) and is affiliated with Homewise Management Company (HMC) and Homewise Preferred Insurance Company (HPIC), which are also wholly-owned subsidiaries of HHI.

Operating Results: According to the Company's audited financial statements for the years 2006 through 2010, and for the six-month period ended June 30, 2011, the operating results (statutory basis) of the Company were as follows:

| | Year 2006 | Year 2007 | Year 2008 |
|--------------------------------|--------------|--------------|---------------|
| Premiums earned, net | \$ 4,337,035 | \$ 2,651,949 | \$1,362,358 |
| Net underwriting income (loss) | \$ (981,843) | \$ 433,910 | \$(2,124,153) |
| Net income (loss) | \$ (384,201) | \$ 775,924 | \$(1,043,316) |
| Ending capital/surplus | \$ 9,152,355 | \$ 9,687,400 | \$8,395,814 |
| | | | |

| | Year 2009 | Year 2010 | YTD June 30, 2011 |
|----------------------------------|----------------|----------------|-------------------|
| Premiums earned, net | \$ 4,555,001 | \$ 15,363,099 | \$3,300,326 |
| Net underwriting income (loss) | \$ (1,946,732) | \$ (2,450,755) | \$(13,062,632) |
| Net income (loss) | \$ (2,102,955) | \$ (2,032,047) | \$(13,422,140) |
| Ending capital/surplus (deficit) | \$ 20,262,170 | \$ 18,799,788 | \$(2,084,080) |
| | | | |

Management

The officers and directors of the Company at December 31, 2010 were as follows:

President/CEO – Dale Stephen Hammond

Vice President/CFO – Timothy Lyons Journy

Secretary/General Counsel – Diane Eileen Falcone

Other Directors- Jamiel Andrew Akhtar
 John Baker Gentry Jr.
 Thomas Anthony Lee
 William Edward Rose

Background/Events of Impact

HMC provided nearly all operating and management services for the Company and HPIC, by contracting with outsourced vendors. HMC also paid the salaries and benefits for the executives and managers of the group of affiliated Homewise companies. The Company and HPIC provided the cash to HMC to meet the demands of the outsourcing contracts and the salaries and benefits.

The heavy flow of cash out of HPIC and the Company to HMC weakened both insurance companies and ultimately contributed to their insolvency. It appears that the management company outsourced nearly all management functions and paid nearly \$37 million in fees to service providers and consultants, yet also paid out over \$23 million in salaries and benefits, during the years 2009-2011.

The flow of cash out of HPIC to the Company to the management company was not limited to the management fees. Millions of dollars were also transferred from the insurance companies to the management company and recorded in due to/due from accounts. The fee formula in the MGA agreement became less relevant to the flow of cash because the formula was adjusted by changes in the fee percentage and by forgiveness of fees, which appears to have been subjectively applied. The companies' independent audit firm noted this was done without authorization by the board of directors.

Assuming value was received for the large fees paid to outside service providers and consultants, the purpose of the large amount of salaries and benefits also paid by the management company is unclear.

The year 2009 appears to be the year that HPIC and the Company were significantly weakened with over \$63 million cash outflows to the management company, which was used to pay \$35 million of fees to service providers and consultants, \$22 million in commissions, and \$9 million in salaries and wages. With significant increases in claims losses in 2009-2010, the Company and HPIC could only provide approximately \$25 million in cash to the management company in 2010. Commissions fell to \$17 million and fees paid fell to \$10 million, yet salaries and benefits still remained above \$8 million. Even in 2011, as losses accumulated and cash dwindled, salaries and benefits were over \$6 million.

Loss Reserves

An analysis and investigation of the loss reserve methodologies of HPIC and the Company was performed and revealed that loss reserves for sinkhole claims were often underestimated and that claim payment amounts often substantially exceeded the initially recorded reserves. This was particularly prevalent in 2010 as the financial position of the companies deteriorated.

Loans from Reinsurers

On February 22, 2010, HHI issued secured promissory notes totaling \$13,195,508 to its reinsurance broker and several of its reinsurers in exchange for cash. Subsequently, additional loans were effectuated that brought the total amount of promissory notes to approximately \$15 million.

Concurrent with the issuance of these notes, HHI entered into a note purchase agreement and security agreements with the lenders. As security for the notes, HHI pledged all of its assets, including its ownership interests in all of its subsidiaries and any assets acquired after the effective date of the debt agreements.

These debt agreements had the effect of removing the premiums payable from the books of the insurance companies and placing notes payable on the books of Homewise Holdings, Inc., effectively increasing the surplus position of the insurance companies by the amount of the decrease in premiums payable plus the additional monies borrowed from the lenders, that was injected into the Company and HPIC.

This arrangement resulted in improved financial position reported on the financial statements of the Company and HPIC, but did not improve financial position for the Homewise group of affiliated companies. Since the only source of cash for the service of debt under this arrangement remained the two insurance companies, even greater demand for cash was placed on the Company and HPIC.

Conclusion

In conclusion, the insolvency of Homewise Insurance Company appears to be the result of an excessive outflow of cash from the company to Homewise Management Company for the purposes of paying (1) outsourced service providers, (2) significant executive and management salaries and benefits, and (3) debt service. Financial reporting practices such as under reserving sinkhole claims and moving liabilities from the insurance company to an affiliated company in the Homewise group may have delayed the recognition that the insurance company was approaching insolvency.

References

Exhibit 1 - Audited financial statements, Homewise Insurance Company, Years Ended December 31, 2006 through 2010, and for the six months ended June 30, 2011

Exhibit 2 - Organizational Chart: Homewise Insurance Company and its Affiliates

EXHIBIT I

Statutory Basis Financial Statements
and Other Financial Information

HomeWise Insurance Company

*For the year ended December 31, 2006
with Report of Independent Auditors*

Thomas Howell

 Ferguson P.A.

HomeWise Insurance Company

Statutory Basis Financial Statements
and Other Financial Information

Year ended December 31, 2006

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Report of Independent Auditors

The Board of Directors
HomeWise Insurance Company

We have audited the accompanying statement of admitted assets, liabilities and capital and surplus - statutory basis of the HomeWise Insurance Company (the Company), as of December 31, 2006, and the related statutory basis statements of operations, changes in capital and surplus, and cash flows for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in Note 1, the accompanying statutory basis financial statements have been prepared in conformity with accounting practices prescribed or permitted by the Florida Office of Insurance Regulation, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the admitted assets, liabilities and capital and surplus of HomeWise Insurance Company as of December 31, 2006, and the results of its operations and its cash flows for the year then ended, on the basis of accounting described in Note 1.

Thomas Howell
▲ Ferguson P.A.

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Our audit was made for the purpose of forming an opinion on the statutory basis financial statements taken as a whole. The supplemental disclosures included in other financial information as of and for the year ended December 31, 2006, are presented to comply with the National Association of Insurance Commissioners' *Accounting Practices and Procedures Manual* and are not a required part of the statutory basis financial statements. This other financial information has been subjected to the auditing procedures applied in our audit of the statutory basis financial statements and, in our opinion, is fairly stated in all material respects in relation to the statutory basis financial statements taken as a whole.

This report is intended solely for the use of the Board of Directors and management of HomeWise Insurance Company and state insurance regulatory authorities and should not be used for any other purpose.

Thomas Howell Ferguson P.A.

May 25, 2007

HomeWise Insurance Company

Statement of Admitted Assets, Liabilities and Capital and Surplus - Statutory Basis

December 31, 2006

Admitted assets

Cash and invested assets:

| | |
|--------------------------------|-------------------|
| Short-term investments | \$ 2,058,147 |
| Cash and cash equivalents | <u>20,673,342</u> |
| Total cash and invested assets | 22,731,489 |

| | |
|---|-----------------------------|
| Accrued investment income | 19,518 |
| Premiums receivable | 3,662,727 |
| Reinsurance balances recoverable | 764,564 |
| Electronic data processing equipment, net | 90,815 |
| Receivables from parent and affiliates | 48,217 |
| Net deferred tax asset | 183,011 |
| Federal income taxes recoverable | 780,575 |
| Other assets | <u>104,365</u> |
| Total admitted assets | <u><u>\$ 28,385,281</u></u> |

Liabilities and capital and surplus

Liabilities:

| | |
|--|------------------|
| Loss and loss adjustment expense reserves | \$ 80,702 |
| Unearned premiums, net | 2,663,052 |
| Reinsurance premiums payable | 12,652,500 |
| Accounts payable and accrued expenses | 1,160,934 |
| Payable to affiliates | 1,489,850 |
| Payable to Citizens Property Insurance Corporation | <u>1,185,888</u> |
| Total liabilities | 19,232,926 |

| | |
|---|-----------------------------|
| Capital and surplus | <u>9,152,355</u> |
| Total liabilities and capital and surplus | <u><u>\$ 28,385,281</u></u> |

See accompanying notes.

HomeWise Insurance Company
Statement of Operations - Statutory Basis
Year ended December 31, 2006

| | |
|--|----------------------------|
| Underwriting income: | |
| Premiums earned, net of reinsurance ceded | \$ 4,337,035 |
| Underwriting expenses: | |
| Losses and loss adjustment expenses incurred | 240,555 |
| Underwriting, acquisition, and other expenses incurred | <u>5,078,323</u> |
| Total underwriting expenses | <u>5,318,878</u> |
| Net underwriting loss | (981,843) |
| Net investment income | 638,975 |
| Other income (loss) | <u>(127)</u> |
| Loss before federal income tax expense | (342,995) |
| Federal income tax expense | <u>(41,206)</u> |
| Net loss | <u><u>\$ (384,201)</u></u> |

See accompanying notes.

HomeWise Insurance Company

Statement of Changes in Capital and Surplus - Statutory Basis

Year ended December 31, 2006

| | <u>Common Stock</u> | | <u>Gross Paid-in and Contributed Surplus</u> | | <u>Unassigned Funds</u> | <u>Total</u> |
|-------------------------------------|---------------------|-------------------|--|---------------------|-------------------------|--------------|
| | <u>Shares</u> | <u>Par Value</u> | | | | |
| Balance as of December 31, 2005 | 100,000 | \$ 100,000 | \$ 9,400,000 | \$ 31,287 | \$ 9,531,287 | |
| Change in net deferred income taxes | - | - | - | 183,011 | 183,011 | |
| Change in nonadmitted assets | - | - | - | (177,742) | (177,742) | |
| Net loss | - | - | - | (384,201) | (384,201) | |
| Balance as of December 31, 2006 | <u>100,000</u> | <u>\$ 100,000</u> | <u>\$ 9,400,000</u> | <u>\$ (347,645)</u> | <u>\$ 9,152,355</u> | |

See accompanying notes.

HomeWise Insurance Company
Statement of Cash Flows - Statutory Basis

Year ended December 31, 2006

Operating activities

| | |
|--|-------------------|
| Premiums collected, net of reinsurance | \$ 17,172,332 |
| Net investment income received | 622,074 |
| Losses and loss adjustment expenses paid | (409,917) |
| Underwriting, acquisition, and other expenses paid | (4,504,711) |
| Income taxes paid | <u>(827,303)</u> |
| Net cash provided by operating activities | <u>12,052,475</u> |

Financing and miscellaneous activities

| | |
|---|------------------|
| Other miscellaneous sources | <u>1,142,971</u> |
| Net cash provided by financing and miscellaneous activities | <u>1,142,971</u> |

| | |
|----------------------|------------|
| Net increase in cash | 13,195,446 |
|----------------------|------------|

| | |
|---------------------------|------------------|
| Cash at beginning of year | <u>9,536,043</u> |
|---------------------------|------------------|

| | |
|---------------------|-----------------------------|
| Cash at end of year | <u><u>\$ 22,731,489</u></u> |
|---------------------|-----------------------------|

Cash consists of the following:

| | |
|---------------------------|-----------------------------|
| Cash and cash equivalents | \$ 20,673,342 |
| Short-term investments | <u>2,058,147</u> |
| | <u><u>\$ 22,731,489</u></u> |

See accompanying notes.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

Year ended December 31, 2006

1. Summary of Significant Accounting Policies

Organization and Description of Company

HomeWise Insurance Company (the Company), a wholly-owned subsidiary of HomeWise Holdings, Inc., an insurance holding company, is domiciled in the state of Florida. The Company received its Certificate of Authority on December 5, 2005, and commenced operations on January 12, 2006.

The Company writes wind-only coverage exclusively in the state of Florida, an area that is exposed to damage from hurricanes and severe storms. The Company attempts to mitigate its exposure to losses from storms by purchasing catastrophe reinsurance coverage. However, such a storm, depending on its path and severity, could result in losses to the Company exceeding its reinsurance protection, and could have a material adverse effect on the financial condition and results of operations of the Company.

Basis of Presentation

The accompanying statutory basis financial statements have been prepared in accordance with statutory accounting practices (SAP) prescribed or permitted by the Florida Office of Insurance Regulation (the Office). Such statutory practices require preparation of the financial statements in accordance with the National Association of Insurance Commissioners' (NAIC) *Accounting Practices and Procedures Manual* subject to deviations prescribed by the Office. SAP is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America (GAAP). Such practices vary in certain respects from those under GAAP. The Company's significant accounting practices and the variances from GAAP are summarized below:

- Certain assets designated as "nonadmitted," principally past-due uncollected premiums, prepaid expenses, and other assets not specifically identified as an admitted asset within the *Accounting Practices and Procedures Manual*, are excluded from the accompanying statement of admitted assets, liabilities, and capital and surplus and are charged directly to unassigned surplus. Under GAAP, such assets are included in the balance sheet at net realizable values.
- Loss and loss adjustment expense reserves and unearned premiums ceded to reinsurers have been reported as reductions of the related liabilities rather than as assets as would be required under GAAP.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

1. Summary of Significant Accounting Policies (continued)

Basis of Presentation (continued)

- Cash in the statement of cash flows represent cash, cash equivalents, and short-term investments with remaining maturities of one year or less. Under GAAP, the corresponding caption of cash and cash equivalents includes cash balances and investments with initial maturities of three months or less.
- The costs of acquiring and renewing business are expensed when incurred. Under GAAP, such costs, to the extent recoverable, would be deferred and amortized over the effective period of the related insurance policies.
- Deferred tax assets are limited to 1) the amount of federal income taxes paid in prior years that can be recovered through loss carrybacks for existing temporary differences that reverse by the end of the subsequent calendar year, plus 2) the lesser of the remaining gross deferred tax assets expected to be realized within one year of the financial statement date or 10% of capital and surplus excluding any net deferred tax assets, "electronic data processing" (EDP) equipment and operating software and any net positive goodwill, plus 3) the amount of remaining gross deferred tax assets that can be offset against existing gross deferred tax liabilities. The remaining deferred tax assets are nonadmitted. Deferred taxes do not include amounts for state income taxes. Under GAAP, state income taxes are included in the computation of deferred taxes, a deferred tax asset is recorded for the amount of gross deferred tax assets expected to be realized in future years, and a valuation allowance is established for deferred tax assets not realizable.

Other significant accounting practices are as follows:

Recognition of Premium Revenues

Premiums are recorded as earned on a monthly pro rata basis over the contract period that the related policies are expected to be in force. The portion of premiums not earned at the end of the year is recorded as unearned premiums.

Cash, Cash Equivalents, and Short-term Investments

Cash and cash equivalents includes demand deposits with financial institutions and other highly liquid investments with original maturities of three months or less. Short-term investments are highly liquid investments with remaining maturities of one year or less.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

1. Summary of Significant Accounting Policies (continued)

Concentration of Credit Risk

The Company's financial instruments exposed to concentrations of credit risk consist primarily of its cash and cash equivalents, short-term investments, and premium revenue. The Company maintains its cash and cash equivalents at several quality financial institutions. Bank deposit accounts, at times, may exceed federally insured limits. The Company has not experienced any losses in such accounts. The Company believes it is not exposed to any significant credit risk on cash and cash equivalents.

All investment transactions have credit exposure to the extent that a counterparty may default on an obligation to the Company. Credit risk is a consequence of carrying investment positions. To manage credit risk, the Company focuses primarily on highly liquid debt instruments, reviews the credit strength of all entities in which it invests, limits its exposure in any one investment, and monitors portfolio quality, taking into account credit ratings assigned by recognized credit rating organizations.

Electronic Data Processing (EDP) Equipment

The admitted value of the Company's EDP equipment and operating software is limited to 3% of capital and surplus. The admitted portion is reported at cost, less accumulated depreciation of \$27,631 at December 31, 2006. EDP equipment and operating software is depreciated using the straight-line method over the lesser of its useful life or three years. Other furniture and equipment is recorded as a non-admitted asset and depreciated using the straight-line method over the estimated useful life of seven years. Depreciation expense charged to operations in 2006 was \$37,661.

Reinsurance

The accompanying statutory basis financial statements reflects reserves for premiums and losses and loss adjustment expenses (LAE) net of reinsurance ceded (Note 6). Those reinsurance arrangements allow management to control exposure to potential losses arising from large risks. A significant portion of the reinsurance is effected under a quota share reinsurance contract. Amounts recoverable from reinsurers are estimated in a manner consistent with the loss and LAE reserves associated with the reinsured policies. Reinsurance premiums, losses, and LAE are accounted for on bases consistent with those used in accounting for the original policies issued and the terms of the reinsurance contracts.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

1. Summary of Significant Accounting Policies (continued)

Loss and Loss Adjustment Expense (LAE) Reserves

Loss and LAE reserves represent the estimated ultimate net cost of all unpaid reported and unreported losses and LAE. The reserves for unpaid losses and LAE are estimated using individual case-basis estimates for reported losses and actuarial estimates for losses incurred but not yet reported. Those estimates are subject to the effects of trends in loss severity and frequency. Although considerable variability is inherent in such estimates, management believes that the reserves for losses and LAE are adequate. The estimates are continually reviewed and adjusted as necessary as experience develops or new information becomes known; such adjustments are included in current operations. The ultimate settlement of losses and LAE may vary significantly from the estimated amounts included in the financial statements. The Company does not discount its loss and LAE reserves.

The anticipated effect of inflation is implicitly considered when estimating liabilities for losses and LAE. While anticipated price increases due to inflation are considered in estimating the ultimate claim costs, the increase in average severities of claims is caused by a number of factors that vary with the individual type of policy written. Future average severities are projected based on historical trends adjusted for implemented changes in underwriting standards, policy provisions, and general economic trends. Those anticipated trends are monitored based on actual development and the estimated liabilities are modified if necessary.

Loss and LAE reserves are reported net of reinsurance recoverables for unpaid losses and LAE. Losses and LAE ceded through reinsurance are credited against losses and LAE incurred.

Guaranty Fund and Residual Market Pool Assessments

The Company is subject to assessments by a Florida guaranty fund, a residual market pool, and a state catastrophe reinsurance pool, namely the Florida Insurance Guaranty Association (FIGA), Citizens Property Insurance Corporation (Citizens), and the Florida Hurricane Catastrophe Fund (FHCF), respectively. The activities of this fund and these pools include collecting funds from solvent insurance companies to cover losses resulting from the insolvency or rehabilitation of other insurance companies or deficits generated by FIGA, Citizens and FHCF.

The Company's policy is to recognize its obligation for FIGA, Citizens, and FHCF assessments when the Company has the information available to reasonably estimate its liabilities. FIGA, Citizens, and FHCF assessments are generally available for recoupment from policyholders and as such, amounts assessed are recorded as a recoverable asset. As of December 31, 2006, the Company had no outstanding notices of assessments.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

1. Summary of Significant Accounting Policies (continued)

Income Taxes

The Company calculates its state and federal income tax liabilities based upon the statutory rates in effect during the year.

Use of Estimates

The preparation of statutory basis financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the statutory basis financial statements and the reported amounts of revenues and expenses during the reporting period. Such estimates and assumptions could change in the future as more information becomes known, which could impact the amounts reported and described in the financial statements.

2. Regulatory Requirements and Restrictions

Florida Statutes Section 624.408 requires the Company to maintain minimum capital and surplus of \$4 million and to meet the risk-based capital requirements (see Note 8). Additionally, Florida Statutes Section 624.4095 requires the Company to maintain a ratio of the product of written premiums times 0.90 to surplus of no greater than 10-to-1 for gross written premiums and 4-to-1 for net written premiums. The Company is in compliance with these requirements.

Additionally, the Company is required to maintain an amount on deposit with the state of Florida to secure the payment of claims. A cash deposit in the amount of \$310,371 has been assigned to the Office to satisfy this requirement. This deposit was included in cash and cash equivalents in the accompanying statement of admitted assets, liabilities, and capital and surplus at December 31, 2006.

3. Investments

Short-term investments consist of U.S. Government money market funds that have a maturity of one year or less from the date of purchase and are stated at cost, which approximates fair value.

Major categories of the Company's net investment income are summarized as follows:

| | |
|---|-------------------|
| Cash and cash equivalents | \$ 1,029,790 |
| Short-term investments | <u>65,774</u> |
| | 1,095,564 |
| Investment expenses: | |
| Interest expense on funds held under reinsurance agreements | (435,082) |
| Interest expense on arbitration | (6,981) |
| Bank fees | <u>(14,526)</u> |
| Net investment income | <u>\$ 638,975</u> |

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

4. Premiums Receivable

Premiums receivable includes amounts due from HomeWise Management Company, the Company's managing general agent (MGA), who collects all premiums and remits them to the Company. The Company nonadmits balances due from insureds and deferred installments for which a portion of the receivable is more than 90 days past due and exceeds the related unearned premium. Premiums receivable is charged to bad debt expense in the period determined uncollectible. Recoveries received on amount previously charged off are credited to bad debt expense in the period received.

Premiums receivable at December 31, 2006 consists of the following:

| | |
|---------------------------------|---------------------|
| Premiums receivable, gross | \$ 3,666,143 |
| Nonadmitted premiums receivable | <u>(3,416)</u> |
| Premiums receivable, net | <u>\$ 3,662,727</u> |

5. Loss and Loss Adjustment Expense (LAE) Reserves

The following table provides a reconciliation of the beginning and ending reserve balances for losses and LAE, net of reinsurance recoverables at December 31, 2006.

| | |
|--|-----------------------|
| | <i>(in thousands)</i> |
| Loss and LAE reserves at beginning of year | \$ - |
| Losses and LAE incurred related to: | |
| Current year | 241 |
| Prior years | <u>-</u> |
| | 241 |
| Losses and LAE paid related to: | |
| Current year | 160 |
| Prior years | <u>-</u> |
| | <u>160</u> |
| Loss and LAE reserves at end of year | <u><u>\$ 81</u></u> |

Anticipated reinsurance recoverables on unpaid losses and LAE are approximately \$242,000 at December 31, 2006. Reinsurance recoverables on paid losses and LAE are \$250,000 at December 31, 2006.

6. Reinsurance

Certain premiums and benefits are ceded to other insurance companies under various reinsurance agreements. The reinsurance agreements provide the Company with increased capacity to write larger risks and maintain its exposure to loss within its capital resources. As of December 31, 2006, the Company's reinsurance program consisted of quota share and excess of loss reinsurance for catastrophic events. Following is a summary of the reinsurance coverage.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

6. Reinsurance (continued)

Effective January 4, 2006, the Company entered into a quota share agreement that generally provides coverage for 75% of all losses net of other reinsurance coverages. The reinsurer's maximum liability per occurrence shall be limited to 75% of \$20,000,000, and as respects to any one risk shall be 75% of \$4,000,000. The reinsurer allows the Company a ceding commission percentage equal to that of the Company's acquisition costs. Premiums ceded under the quota share agreement, net of reinsurer's pro rata cost of catastrophe coverages and ceding commissions were \$19,541,734 and \$13,831,937, respectively, for the year December 31, 2006. The ceding commissions have been recorded as a reduction of underwriting, acquisition, and other expenses in the accompanying statement of operations. In addition, the reinsurer shall pay the Company a 15% profit commission on net profit to be determined at the expiration of the contract period, May 31, 2007.

Effective June 1, 2006, the Company executed catastrophe excess of loss agreements in which the coverage is provided by agreements with commercial reinsurers and coverage provided by the FHCF. The excess of loss treaties generally provide coverage on ultimate net losses of approximately \$142,600,000 in excess of \$5,200,000 per occurrence, not to exceed approximately \$158,700,000 for all occurrences. The FHCF provided coverage for 90% of the losses from qualifying catastrophic events in excess of approximately \$34,300,000 up to a maximum of approximately \$142,600,000, plus 100% of qualifying losses in excess of \$2,900,000 (drop down layer) up to a maximum of \$10,000,000. For the year ended December 31, 2006, premiums of \$13,110,945 and \$6,223,942 were ceded under the commercial excess catastrophe agreements and FHCF, respectively.

The FHCF provides coverage for named hurricanes only and provides no coverage after the one time limit is exhausted. Reinsurance premiums for the FHCF are paid on a total insured value basis. In the event of a loss assessment, the Company may recoup the assessments from its policyholders.

Effective June 1, 2006, the Company executed reinsurance premium protection agreements to reinsure the reinstatement premium payment obligations which accrue to the Company under the private catastrophe excess of loss agreements. The coverage is limited to 100% of the original contracted reinsurance placement. Premiums ceded under the reinsurance premium protection agreement were \$7,723,023.

The Company's reinsured risks are treated, to the extent of the reinsurance, as though they are risks for which the Company is not liable. However, the Company remains contingently liable in the event the reinsuring companies do not meet their obligations under these reinsurance contracts. Given the quality of the reinsuring companies, management believes this possibility to be remote. See Note 5 for recoveries due from reinsurers relating to paid and unpaid losses and LAE.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

6. Reinsurance (continued)

For the year ended December 31, 2006, the Company did not commute nor enter into or engage in any loss portfolio transfer for any lines of business.

The effects of reinsurance on premiums written and earned at December 31, 2006, are as follows:

| | <u>Written</u> | <u>Earned</u> |
|------------------|---------------------|---------------------|
| Direct premiums | \$ 37,776,317 | \$ 13,858,975 |
| Assumed premiums | 21,873,836 | 21,496,120 |
| Ceded premiums | <u>(52,650,065)</u> | <u>(31,018,060)</u> |
| Net premiums | <u>\$ 7,000,088</u> | <u>\$ 4,337,035</u> |

At December 31, 2006, no individual reinsurer owed the Company an unsecured amount that was greater than 3% of the Company's surplus.

7. Policy Assumption Agreement

The Company assumed written premiums of \$21,873,836 during 2006 under a policy assumption agreement with Citizens. The Company provides a ceding commission to Citizens of 16% of assumed premiums to cover the acquisition costs incurred by Citizens. Total ceding commissions charged to operations in 2006 were \$3,499,814.

8. Income Taxes

Income before federal income taxes differs from taxable income principally due to differences in loss and LAE reserves and unearned premiums for tax and statutory basis financial reporting purposes.

State income taxes are classified as taxes, licenses, and fees in the NAIC Annual Statement and as underwriting, acquisition, and other expenses on the statement of operations.

A. Components of deferred tax assets (DTAs) and deferred tax liabilities (DTLs) are as follows:

| | |
|-------------------|-------------------|
| Gross DTAs | \$ 252,962 |
| Gross DTLs | <u>(35,370)</u> |
| Net admitted DTAs | 217,592 |
| Nonadmitted DTAs | <u>(34,581)</u> |
| Net admitted DTAs | <u>\$ 183,011</u> |

B. Unrecognized DTLs

There are no unrecognized DTLs.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

8. Income Taxes (continued)

C. Current tax and change in deferred tax:

The provisions for income taxes incurred on earnings were:

| | |
|---------------------------------|------------------|
| Current year income tax expense | \$ 41,206 |
| Prior year over accrual | - |
| Current income taxes incurred | <u>\$ 41,206</u> |

The tax effect of temporary differences at December 31, 2006, that give rise to significant deferred tax assets and deferred tax liabilities are as follows:

| DTAs | <u>Statutory</u> | <u>Tax</u> | <u>Difference</u> | <u>Tax Effect</u> |
|-------------------------|-------------------------|-------------------|--------------------------|--------------------------|
| Unpaid losses and LAE | \$ 80,702 | \$ 75,046 | \$ 5,656 | \$ 1,923 |
| Unearned premiums | 2,663,052 | 2,130,442 | 532,610 | 181,087 |
| Nonadmitted assets | - | 205,742 | 205,742 | <u>69,952</u> |
| Gross DTAs | | | | <u>\$ 252,962</u> |
| DTLs | <u>Statutory</u> | <u>Tax</u> | <u>Difference</u> | <u>Tax Effect</u> |
| Furniture and equipment | \$ - | \$ (87,033) | \$ (87,033) | \$ (29,591) |
| Prepaid expenses | - | (16,998) | (16,998) | <u>(5,779)</u> |
| Gross DTLs | | | | <u>\$ (35,370)</u> |

The change in gross DTAs of \$252,962 and gross DTLs of \$(35,370) is the change in net deferred income taxes before the consideration of nonadmitted DTAs.

D. Reconciliation of federal income tax rate to actual effective rate:

The significant book-to-tax adjustments were as follows:

| | <u>2006</u> | <u>Effective Tax Rate</u> |
|---|---------------------|--------------------------------------|
| Provision computed at statutory rate | \$ (116,618) | (34.00)% |
| Nonadmitted assets | (69,952) | (20.39) |
| Other | <u>10,184</u> | <u>2.96</u> |
| Total | <u>\$ (176,386)</u> | <u>(51.43)%</u> |
| Federal income tax | \$ 41,206 | 12.01 % |
| Change in deferred taxes | <u>(217,592)</u> | <u>(63.44)</u> |
| Statutory income taxes | <u>\$ (176,386)</u> | <u>(51.43)%</u> |

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

8. Income Taxes (continued)

E. Operating loss and tax credit carryforwards:

1. At December 31, 2006, the Company had no unused capital loss carryforwards available to offset against future taxable income.
2. The Company had no unused net operating loss carryforwards available to offset future taxable income at December 31, 2006.
3. The following is income tax expense that is available for recoupment in the event of future net losses:

| <u>Year</u> | <u>Amount</u> |
|-------------|---------------|
| 2006 | \$ 41,206 |

F. Consolidated federal income tax return:

The Company files a consolidated income tax return with the following:

HomeWise Holdings, Inc.

HomeWise Preferred Insurance Company

HomeWise Management Company

9. Capital and Surplus

The Company has authorized 100,000 shares of \$1 par value common stock, of which 100,000 shares are issued and outstanding. The parent company, HomeWise Holdings, Inc., is the sole shareholder.

Property and casualty insurance companies are subject to certain risk-based capital (RBC) requirements as specified by the NAIC. Under those requirements, the amount of capital and surplus maintained by a property and casualty insurance company is to be determined based on the various risk factors related to it. The Company's capital and surplus exceeds the RBC requirements at December 31, 2006.

The maximum amount of dividends that may be paid by property and casualty insurance companies without prior approval of the Office is subject to restrictions relating to statutory surplus and net income. Furthermore, in accordance with the Company's Certificate of Authority Consent Order, during the first three years of operations, it may only pay dividends that are approved in advance by the Office. The Company did not declare or pay any dividends during the year ended December 31, 2006.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

10. Related Party Transactions

The Company is a wholly-owned subsidiary of HomeWise Holdings, Inc. (HHI) and is affiliated with HomeWise Management Company (HMC) and HomeWise Preferred Insurance Company (HPIC), which are also wholly-owned subsidiaries of HHI.

Effective January 1, 2006, the Company entered into a managing general agency agreement with HMC. Pursuant to the agreement, HMC provides to the Company premium billing, claims management and underwriting functions. During 2006, expenses incurred related to this agreement totaled \$12,994,250. As of December 31, 2006, the Company has a net payable due to HMC in the amount of \$1,489,850.

Effective December 5, 2005, the Company entered into a service agreement with HHI. Pursuant to the agreement, HHI provides to the Company capital management services, investor management and relations, and assists with overall general management of the Company. During 2006, expenses incurred related to this agreement totaled \$591,640. As of December 31, 2006, the Company has a receivable due from HHI in the amount of \$40,952.

The Company is also party to a Cost Allocation Agreement with HPIC, HMC, and HHI in which expenses benefiting more than one company are allocated based upon direct allocation or revenue allocation rules, whichever is most appropriate for the expenses. As of December 31, 2006, the Company has a receivable due from HPIC in the amount of \$7,625.

11. Premiums Produced by Managing General Agents or Third Party Administrators

The Company uses a managing general agent, HMC, to write and administer insurance products. HMC has contracted with an unaffiliated service company to provide this function. The total premium produced and serviced through the contract during 2006 is summarized below. The Company retains underwriting authority for all policies issued under these agreements.

| <u>Name and Address</u> | <u>FEI Number</u> | <u>Exclusive Contract</u> | <u>Type of Business Written</u> | <u>Type of Authority Granted</u> | <u>Direct Premium Written</u> |
|--|-------------------|---------------------------|---------------------------------|--|-------------------------------|
| HomeWise Management 18302 Highwoods Preserve Prkwy Suite 110 Tampa, FL 33647 | 20-3395152 | Yes | Wind-only | Premium collection, claims adjustment, binding authority, and underwriting | \$ 37,776,317 |

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

12. Lease Commitments

On September 2, 2005, the Company entered into an operating lease agreement for office space in Tallahassee, Florida, which is effective October 15, 2005, through October 31, 2008.

On May 1, 2006, the Company also entered into an operating lease agreement for office space in Tampa, Florida, which is effective June 1, 2006, through May 31, 2011. The Company has the option to renew the term of the lease for an additional five year period at the prevailing rental rate at that time, provided the Company gives the lessor written notice nine months prior to its intent to renew the lease.

Approximate future lease payments under these operating leases are as follows at December 31, 2006:

| | | |
|------|----|----------------|
| 2007 | \$ | 238,421 |
| 2008 | | 236,969 |
| 2009 | | 175,001 |
| 2010 | | 182,048 |
| 2011 | | <u>77,077</u> |
| | \$ | <u>909,516</u> |

Total rent expense for the combined leases was \$166,386 for the year ended December 31, 2006.

13. Subsequent Events

On January 1, 2007 the Company terminated and commuted its quota share reinsurance agreement with Glacier Reinsurance AG. Effective January 1, 2007, the Company and its affiliated company HomeWise Preferred Insurance Company (collectively, the Reinsured) entered into a quota share reinsurance agreement with Harlequin Insurance (Bermuda) SAC Limited (the Reinsurer). Under the terms of the agreement, which expire on May 31, 2008, the Reinsurer assumes 75% of the Reinsured's net liabilities for losses (loss and loss adjustment expense) after taking into effect the Reinsured's excess of loss reinsurance coverage provided by the FHCF and, through May 31, 2007, the coverage provided by open market excess of loss reinsurance purchased by the Reinsured. Under the terms of the agreement, the Reinsured cedes 75% of their gross premiums after deducting the cost of the above referenced inuring reinsurance to the Reinsurer. The Reinsured cedes 75% of their cover gross losses to the Reinsurer after deducting recoveries from the referenced inuring reinsurance. The ceding commission from the Reinsurer to the Reinsured is on a reimbursement basis wherein the Reinsurer reimburses the Reinsured for 75% of their acquisition and overhead expenses. The agreement includes an Event Cap for ceded losses of 44% of the ceded premium earned during the term. It also includes an Aggregate Loss and Expense Ratio Cap wherein the maximum amount of losses and ceding commission payable by the Reinsurer under this Agreement in the aggregate shall be limited to 150% of the ceded premium earned during the term. In the event either cap is met, the Reinsured share in recoveries in proportion to their respective subject losses to the total of losses subject to the agreement. Obligations of the Reinsurer to the Reinsured are collateralized by funds held in a reinsurance trust account maintained in a United States bank.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

13. Subsequent Events (continued)

As of December 31, 2006, the Company had filed for arbitration regarding the Office's denial of the Company's proposed 80% rate increase, which it had implemented under Florida's "Use and File" Statutes. The panel awarded the Company an approved rate increase of 75.4%. The effect of the arbitration award is included in the accompanying statutory basis financial statements.

As of December 31, 2006, the Company was in negotiations with Citizens regarding ownership of a \$3.1 million reinsurance surcharge. The Company's position was that the surcharge was properly ceded to the Company when it assumed policies from Citizens in January and March of 2006. Citizens maintained that the surcharge was improperly ceded to the Company and should be returned. The Company has reached an agreement in principle with Citizens wherein the Company will return 25% of the disputed amount to Citizens and has included the agreed-upon amount (\$2.3 million) in assumed premiums in the accompanying statement of operations.

14. Reconciliation of Annual Statement to Audited Financial Statements

Differences exist between amounts reported in the audited statutory financial statements and those reported in the annual statement of the Company for the year ended December 31, 2006, resulting from reclassification of reinsurance balances and other liabilities. Presented below is a reconciliation of amounts previously reported to the Office and those amounts appearing in the audited statutory financial statements for the year ended December 31, 2006.

| | Audited Financial Statement Amount | Annual Statement Amount | Increase (Decrease) |
|---------------------------|---|--|--------------------------------|
| Total admitted assets | \$ 28,385,281 | \$ 28,566,558 | \$ (181,277) |
| Total liabilities | 19,232,926 | 19,414,204 | (181,278) |
| Total capital and surplus | 9,152,355 | 9,152,354 | 1 |
| Net loss | 384,201 | 384,202 | (1) |

Other Financial Information

SUMMARY INVESTMENT SCHEDULE

| Investment Categories | Gross Investment Holdings | | Admitted Assets as Reported in the Annual Statement | |
|---|---------------------------|-----------------|---|-----------------|
| | 1 Amount | 2 Percentage | 3 Amount | 4 Percentage |
| 1. Bonds: | | | | |
| 1.1 U.S. treasury securities | | 0.0 | | 0.0 |
| 1.2 U.S. government agency obligations (excluding mortgage-backed securities): | | | | |
| 1.21 Issued by U.S. government agencies | | 0.0 | | 0.0 |
| 1.22 Issued by U.S. government sponsored agencies | | 0.0 | | 0.0 |
| 1.3 Foreign government (including Canada, excluding mortgage-backed securities) | | 0.0 | | 0.0 |
| 1.4 Securities issued by states, territories and possessions and political subdivisions in the U.S.: | | | | |
| 1.41 States, territories and possessions general obligations | | 0.0 | | 0.0 |
| 1.42 Political subdivisions of states, territories & possessions & political subdivisions general obligations | | 0.0 | | 0.0 |
| 1.43 Revenue and assessment obligations | | 0.0 | | 0.0 |
| 1.44 Industrial development and similar obligations | | 0.0 | | 0.0 |
| 1.5 Mortgage-backed securities (includes residential and commercial MBS): | | | | |
| 1.51 Pass-through securities: | | | | |
| 1.511 Issued or guaranteed by GNMA | | 0.0 | | 0.0 |
| 1.512 Issued or guaranteed by FNMA and FHLMC | | 0.0 | | 0.0 |
| 1.513 All other | | 0.0 | | 0.0 |
| 1.52 CMOs and REMICs: | | | | |
| 1.521 Issued or guaranteed by GNMA, FNMA, FHLMC or VA | | 0.0 | | 0.0 |
| 1.522 Issued by non-U.S. Government issuers and collateralized by mortgage-backed securities issued or guaranteed by agencies shown in Line 1.521 | | 0.0 | | 0.0 |
| 1.523 All other | | 0.0 | | 0.0 |
| 2. Other debt and other fixed income securities (excluding short-term): | | | | |
| 2.1 Unaffiliated domestic securities (includes credit tenant loans rated by the SVO) | | 0.0 | | 0.0 |
| 2.2 Unaffiliated foreign securities | | 0.0 | | 0.0 |
| 2.3 Affiliated securities | | 0.0 | | 0.0 |
| 3. Equity interests: | | | | |
| 3.1 Investments in mutual funds | | 0.0 | | 0.0 |
| 3.2 Preferred stocks: | | | | |
| 3.21 Affiliated | | 0.0 | | 0.0 |
| 3.22 Unaffiliated | | 0.0 | | 0.0 |
| 3.3 Publicly traded equity securities (excluding preferred stocks): | | | | |
| 3.31 Affiliated | | 0.0 | | 0.0 |
| 3.32 Unaffiliated | | 0.0 | | 0.0 |
| 3.4 Other equity securities: | | | | |
| 3.41 Affiliated | | 0.0 | | 0.0 |
| 3.42 Unaffiliated | | 0.0 | | 0.0 |
| 3.5 Other equity interests including tangible personal property under lease: | | | | |
| 3.51 Affiliated | | 0.0 | | 0.0 |
| 3.52 Unaffiliated | | 0.0 | | 0.0 |
| 4. Mortgage loans: | | | | |
| 4.1 Construction and land development | | 0.0 | | 0.0 |
| 4.2 Agricultural | | 0.0 | | 0.0 |
| 4.3 Single family residential properties | | 0.0 | | 0.0 |
| 4.4 Multifamily residential properties | | 0.0 | | 0.0 |
| 4.5 Commercial loans | | 0.0 | | 0.0 |
| 4.6 Mezzanine real estate loans | | 0.0 | | 0.0 |
| 5. Real estate investments: | | | | |
| 5.1 Property occupied by company | | 0.0 | | 0.0 |
| 5.2 Property held for production of income (including \$.....0 of property acquired in satisfaction of debt) | | 0.0 | | 0.0 |
| 5.3 Property held for sale (including \$.....0 property acquired in satisfaction of debt) | | 0.0 | | 0.0 |
| 6. Contract loans | | 0.0 | | 0.0 |
| 7. Receivables for securities | | 0.0 | | 0.0 |
| 8. Cash, cash equivalents and short-term investments | 22,421,119 | 98.6 | 22,421,119 | 98.6 |
| 9. Other invested assets | 310,371 | 1.4 | 310,371 | 1.4 |
| 10. Total invested assets | 22,731,490 | 100.0 | 22,731,490 | 100.0 |

See report of independent auditors.



SUPPLEMENTAL INVESTMENT RISKS INTERROGATORIES

Due April 1

For the year ended December 31, 2006

Of HomeWise Insurance Company

Address (City, State, Zip Code): Tampa FL 33647

NAIC Group Code.....4111

NAIC Company Code.....12438

Employer's ID Number.....20-3395013

The Investment Risks Interrogatories are to be filed by April 1. They are also to be included with the Audited Statutory Financial Statements.

Answer the following interrogatories by reporting the applicable U.S. dollar amounts and percentages of the reporting entity's total admitted assets held in that category of investments.

1. Reporting entity's total admitted assets as reported on Page 2 of this annual statement. \$ 28,566,558

2. Ten largest exposures to a single issuer/borrower/investment.

| 1 | 2 | 3 | 4 |
|--------|---|--------------|-------------------------------------|
| Issuer | Description of Exposure | Amount | Percentage of Total Admitted Assets |
| 2.01 | U.S. Treasury Note, 3.00%, 10/1/06 to 10/1/11 | \$ 1,000,000 | 0.000 % |
| 2.02 | U.S. Treasury Note, 3.00%, 10/1/06 to 10/1/11 | \$ 1,000,000 | 0.000 % |
| 2.03 | U.S. Treasury Note, 3.00%, 10/1/06 to 10/1/11 | \$ 1,000,000 | 0.000 % |
| 2.04 | U.S. Treasury Note, 3.00%, 10/1/06 to 10/1/11 | \$ 1,000,000 | 0.000 % |
| 2.05 | U.S. Treasury Note, 3.00%, 10/1/06 to 10/1/11 | \$ 1,000,000 | 0.000 % |
| 2.06 | U.S. Treasury Note, 3.00%, 10/1/06 to 10/1/11 | \$ 1,000,000 | 0.000 % |
| 2.07 | U.S. Treasury Note, 3.00%, 10/1/06 to 10/1/11 | \$ 1,000,000 | 0.000 % |
| 2.08 | U.S. Treasury Note, 3.00%, 10/1/06 to 10/1/11 | \$ 1,000,000 | 0.000 % |
| 2.09 | U.S. Treasury Note, 3.00%, 10/1/06 to 10/1/11 | \$ 1,000,000 | 0.000 % |
| 2.10 | U.S. Treasury Note, 3.00%, 10/1/06 to 10/1/11 | \$ 1,000,000 | 0.000 % |

3. Amounts and percentages of the reporting entity's total admitted assets held in bonds and preferred stocks by NAIC rating.

| Bonds | 1 | 2 |
|------------------|--------------|---------|
| 3.01 NAIC-1 | \$ 1,000,000 | 0.000 % |
| 3.02 NAIC-2 | \$ 1,000,000 | 0.000 % |
| 3.03 NAIC-3 | \$ 1,000,000 | 0.000 % |
| 3.04 NAIC-4 | \$ 1,000,000 | 0.000 % |
| 3.05 NAIC-5 | \$ 1,000,000 | 0.000 % |
| 3.06 NAIC-6 | \$ 1,000,000 | 0.000 % |
| Preferred Stocks | 3 | 4 |
| 3.07 P/RP-1 | \$ 1,000,000 | 0.000 % |
| 3.08 P/RP-2 | \$ 1,000,000 | 0.000 % |
| 3.09 P/RP-3 | \$ 1,000,000 | 0.000 % |
| 3.10 P/RP-4 | \$ 1,000,000 | 0.000 % |
| 3.11 P/RP-5 | \$ 1,000,000 | 0.000 % |
| 3.12 P/RP-6 | \$ 1,000,000 | 0.000 % |

4. Assets held in foreign investments:

| | |
|---|----------------|
| 4.01 Are assets held in foreign investments less than 2.5% of the reporting entity's total admitted assets? | Yes [] No [X] |
| 4.02 Total admitted assets held in foreign investments | \$ 0.000 % |
| 4.03 Foreign-currency-denominated investments | \$ 0.000 % |
| 4.04 Insurance liabilities denominated in that same foreign currency | \$ 0.000 % |

If response to 4.01 above is yes, responses are not required for interrogatories 5-10.

5. Aggregate foreign investment exposure categorized by NAIC sovereign rating:

| 1 | 2 |
|--------------------------------------|------------|
| 5.01 Countries rated NAIC-1 | \$ 0.000 % |
| 5.02 Countries rated NAIC-2 | \$ 0.000 % |
| 5.03 Countries rated NAIC-3 or below | \$ 0.000 % |

6. Two largest foreign investment exposures to a single country, categorized by the country's NAIC sovereign rating:

| 1 | 2 |
|-------------------------|------------|
| Countries rated NAIC-1: | |
| 6.01 Country: | \$ 0.000 % |
| 6.02 Country: | \$ 0.000 % |
| Countries rated NAIC-2: | |
| 6.03 Country: | \$ 0.000 % |
| 6.04 Country: | \$ 0.000 % |

See report of independent auditors.

Countries rated NAIC-3 or below:

| | | | | |
|------|--|----|----|---------|
| 6.05 | Country: | | \$ | 0.000 % |
| 6.06 | Country: | | \$ | 0.000 % |
| | | 1 | 2 | |
| 7. | Aggregate unhedged foreign currency exposure: | \$ | | 0.000 % |
| 8. | Aggregate unhedged foreign currency exposure categorized by NAIC sovereign rating: | | | |
| 8.01 | Countries rated NAIC-1: | \$ | | 0.000 % |
| 8.02 | Countries rated NAIC-2: | \$ | | 0.000 % |
| 8.03 | Countries rated NAIC-3 or below: | \$ | | 0.000 % |

9. Two largest unhedged foreign currency exposures to a single country, categorized by the country's NAIC sovereign rating:

| | | | | |
|------|----------------------------------|----|---|---------|
| | | 1 | 2 | |
| | Countries rated NAIC-1: | | | |
| 9.01 | Country: | \$ | | 0.000 % |
| 9.02 | Country: | \$ | | 0.000 % |
| | Countries rated NAIC-2: | | | |
| 9.03 | Country: | \$ | | 0.000 % |
| 9.04 | Country: | \$ | | 0.000 % |
| | Countries rated NAIC-3 or below: | | | |
| 9.05 | Country: | \$ | | 0.000 % |
| 9.06 | Country: | \$ | | 0.000 % |

10. Ten largest non-sovereign (i.e. non-governmental) foreign issues:

| | 1 | 2 | 3 | 4 |
|-------|--------|-------------|----|---------|
| | Issuer | NAIC Rating | | |
| 10.01 | | | \$ | 0.000 % |
| 10.02 | | | \$ | 0.000 % |
| 10.03 | | | \$ | 0.000 % |
| 10.04 | | | \$ | 0.000 % |
| 10.05 | | | \$ | 0.000 % |
| 10.06 | | | \$ | 0.000 % |
| 10.07 | | | \$ | 0.000 % |
| 10.08 | | | \$ | 0.000 % |
| 10.09 | | | \$ | 0.000 % |
| 10.10 | | | \$ | 0.000 % |

11. Amounts and percentages of the reporting entity's total admitted assets held in Canadian investments and unhedged Canadian currency exposure:

| | | |
|-------|---|----------------|
| 11.01 | Are assets held in Canadian investments less than 2.5% of the reporting entity's total admitted assets? | Yes [] No [X] |
| | If response to 11.01 is yes, detail is not required for the remainder of Interrogatory 11. | |
| 11.02 | Total admitted assets held in Canadian Investments | \$ 0.000 % |
| 11.03 | Canadian currency-denominated investments | \$ 0.000 % |
| 11.04 | Canadian-denominated insurance liabilities | \$ 0.000 % |
| 11.05 | Unhedged Canadian currency exposure | \$ 0.000 % |

12. Report aggregate amounts and percentages of the reporting entity's total admitted assets held in investments with contractual sales restrictions.

| | | |
|-------|--|----------------|
| 12.01 | Are assets held in investments with contractual sales restrictions less than 2.5% of the reporting entity's total admitted assets? | Yes [] No [X] |
| | If response to 12.01 is yes, responses are not required for the remainder of Interrogatory 12. | |

| | | | | |
|-------|---|----|---|---------|
| | 1 | 2 | 3 | |
| 12.02 | Aggregate statement value of investments with contractual sales restrictions: | \$ | | 0.000 % |
| | Largest 3 investments with contractual sales restrictions: | | | |
| 12.03 | | \$ | | 0.000 % |
| 12.04 | | \$ | | 0.000 % |
| 12.05 | | \$ | | 0.000 % |

13. Amounts and percentages of admitted assets held in the largest 10 equity interests:

| | | |
|-------|--|----------------|
| 13.01 | Are assets held in equity interest less than 2.5% of the reporting entity's total admitted assets? | Yes [] No [X] |
| | If response to 13.01 above is yes, responses are not required for the remainder of Interrogatory 13. | |

| | | | | |
|-------|----------------|----|---|---------|
| | 1 | 2 | 3 | |
| | Name of Issuer | | | |
| 13.02 | | \$ | | 0.000 % |
| 13.03 | | \$ | | 0.000 % |
| 13.04 | | \$ | | 0.000 % |
| 13.05 | | \$ | | 0.000 % |

| | | |
|-------|----|---------|
| 13.06 | \$ | 0.000 % |
| 13.07 | \$ | 0.000 % |
| 13.08 | \$ | 0.000 % |
| 13.09 | \$ | 0.000 % |
| 13.10 | \$ | 0.000 % |
| 13.11 | \$ | 0.000 % |

14. Amounts and percentages of the reporting entity's total admitted assets held in nonaffiliated, privately placed equities:

14.01 Are assets held in nonaffiliated, privately placed equities less than 2.5% of the reporting entity's total admitted assets? Yes ☐ No ☒

If response to 14.01 above is yes, responses are not required for the remainder of Interrogatory 14.

| | 1 | 2 | 3 |
|--|----|---|---------|
| 14.02 Aggregate statement value of investments held in nonaffiliated, privately placed equities: | \$ | | 0.000 % |
| Largest 3 investments held in nonaffiliated, privately placed equities: | | | |
| 14.03 | \$ | | 0.000 % |
| 14.04 | \$ | | 0.000 % |
| 14.05 | \$ | | 0.000 % |

15. Amounts and percentages of the reporting entity's total admitted assets held in general partnership interests:

15.01 Are assets held in general partnership interests less than 2.5% of the reporting entity's total admitted assets? Yes ☐ No ☒

If response to 15.01 above is yes, responses are not required for the remainder of Interrogatory 15.

| | 1 | 2 | 3 |
|---|----|---|---------|
| 15.02 Aggregate statement value of investments held in general partnership interests: | \$ | | 0.000 % |
| Largest 3 investments in general partnership interests: | | | |
| 15.03 | \$ | | 0.000 % |
| 15.04 | \$ | | 0.000 % |
| 15.05 | \$ | | 0.000 % |

16. Amounts and percentages of the reporting entity's total admitted assets held in mortgage loans:

16.01 Are mortgage loans reported in Schedule B less than 2.5% of the reporting entity's total admitted assets? Yes ☐ No ☒

If response to 16.01 above is yes, responses are not required for the remainder of Interrogatory 16 and Interrogatory 17.

| | 1 | 2 | 3 |
|--|----|---|---------|
| Type (Residential, Commercial, Agricultural) | | | |
| 16.02 | \$ | | 0.000 % |
| 16.03 | \$ | | 0.000 % |
| 16.04 | \$ | | 0.000 % |
| 16.05 | \$ | | 0.000 % |
| 16.06 | \$ | | 0.000 % |
| 16.07 | \$ | | 0.000 % |
| 16.08 | \$ | | 0.000 % |
| 16.09 | \$ | | 0.000 % |
| 16.10 | \$ | | 0.000 % |
| 16.11 | \$ | | 0.000 % |

Amount and percentage of the reporting entity's total admitted assets held in the following categories of mortgage loans:

| | Loans |
|--|------------|
| 16.12 Construction loans | \$ 0.000 % |
| 16.13 Mortgage loans over 90 days past due | \$ 0.000 % |
| 16.14 Mortgage loans in the process of foreclosure | \$ 0.000 % |
| 16.15 Mortgage loans foreclosed | \$ 0.000 % |
| 16.16 Restructured mortgage loans | \$ 0.000 % |

17. Aggregate mortgage loans having the following loan-to-value ratios as determined from the most current appraisal as of the annual statement date:

| <u>Loan-to-Value</u> | <u>Residential</u> | | <u>Commercial</u> | | <u>Agricultural</u> | |
|----------------------|--------------------|------------|-------------------|------------|---------------------|------------|
| | 1 | 2 | 3 | 4 | 5 | 6 |
| 17.01 above 95% | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % |
| 17.02 91% to 95% | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % |
| 17.03 81% to 90% | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % |
| 17.04 71% to 80% | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % |
| 17.05 below 70% | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % |

18. Amounts and percentages of the reporting entity's total admitted assets held in each of the five largest investments in real estate:

18.01 Are assets held in real estate reported less than 2.5% of the reporting entity's total admitted assets? Yes ☐ No ☒

If response to 18.01 above is yes, responses are not required for the remainder of Interrogatory 18.

Largest five investments in any one parcel or group of contiguous parcels of real estate.

| Description | 2 | 3 |
|-------------|----|---------|
| 18.02 | \$ | 0.000 % |
| 18.03 | \$ | 0.000 % |
| 18.04 | \$ | 0.000 % |
| 18.05 | \$ | 0.000 % |
| 18.06 | \$ | 0.000 % |

19. Report aggregate amounts and percentages of the reporting entity's total admitted assets held in mezzanine real estate loans.

19.01 Are assets held in investments held in mezzanine real estate loans less than 2.5% of the reporting entity's admitted assets? Yes ☐ No ☒

Is response to 19.01 is yes, responses are not required for the remainder of Interrogatory 19.

| | 1 | 2 | 3 |
|--|----|---------|---|
| 19.02 Aggregate statement value of investments held in mezzanine real estate loans | \$ | 0.000 % | |
| Largest three investments held in mezzanine real estate loans: | | | |
| 19.03 | \$ | 0.000 % | |
| 19.04 | \$ | 0.000 % | |
| 19.05 | \$ | 0.000 % | |

20. Amounts and percentages of the reporting entity's total admitted assets subject to the following types of agreements:

| | At Year-End | | At End of Each Quarter | | |
|---|-------------|---------|------------------------|---------|---------|
| | 1 | 2 | 1st Qtr | 2nd Qtr | 3rd Qtr |
| 20.01 Securities lending (do not include assets held as collateral for such transactions) | \$ | 0.000 % | \$ | | \$ |
| 20.02 Repurchase agreements | \$ | 0.000 % | \$ | | \$ |
| 20.03 Reverse repurchase agreements | \$ | 0.000 % | \$ | | \$ |
| 20.04 Dollar repurchase agreements | \$ | 0.000 % | \$ | | \$ |
| 20.05 Dollar reverse repurchase agreements | \$ | 0.000 % | \$ | | \$ |

21. Amounts and percentages indicated below for warrants not attached to other financial instruments, options, caps and floors:

| | Owned | | Written | |
|-------------------------|-------|---------|---------|---------|
| | 1 | 2 | 3 | 4 |
| 21.01 Hedging | \$ | 0.000 % | \$ | 0.000 % |
| 21.02 Income generation | \$ | 0.000 % | \$ | 0.000 % |
| 21.03 Other | \$ | 0.000 % | \$ | 0.000 % |

22. Amounts and percentages of the reporting entity's total admitted assets of potential exposure for collars, swaps, and forwards:

| | At Year-End | | At End of Each Quarter | | |
|-------------------------|-------------|---------|------------------------|---------|---------|
| | 1 | 2 | 1st Qtr | 2nd Qtr | 3rd Qtr |
| 22.01 Hedging | \$ | 0.000 % | \$ | | \$ |
| 22.02 Income generation | \$ | 0.000 % | \$ | | \$ |
| 22.03 Replications | \$ | 0.000 % | \$ | | \$ |
| 22.04 Other | \$ | 0.000 % | \$ | | \$ |

23. Amounts and percentages of the reporting entity's total admitted assets of potential exposure for futures contracts:

| | At Year-End | | At End of Each Quarter | | |
|-------------------------|-------------|---------|------------------------|---------|---------|
| | 1 | 2 | 1st Qtr | 2nd Qtr | 3rd Qtr |
| 23.01 Hedging | \$ | 0.000 % | \$ | | \$ |
| 23.02 Income generation | \$ | 0.000 % | \$ | | \$ |
| 23.03 Replications | \$ | 0.000 % | \$ | | \$ |
| 23.04 Other | \$ | 0.000 % | \$ | | \$ |

HomeWise Insurance Company

Selected General Interrogatories Relating to Reinsurance

December 31, 2006

- 7.1 Has the reporting entity reinsured any risk with any other entity under a quota share reinsurance contract that includes a provision that would limit the reinsurer's losses below the stated quota share percentage (e.g., a deductible, a loss ratio corridor, a loss cap, an aggregate limit or any similar provisions)?.....Yes ☒ No ☐
- 7.2 If yes, indicate the number of reinsurance contracts containing such provisions.....1
- 7.3 If yes, does the amount of reinsurance credit taken reflect the reduction in quota share coverage caused by any applicable limiting provision(s)?.....Yes ☒ No ☐
- 9.1 Has the reporting entity ceded any risk under any reinsurance contract (or under multiple contracts with the same reinsurer or its affiliates) for which during the period covered by the statement: (i) it recorded a positive or negative underwriting result greater than 3% of prior year-end surplus as regards policyholders or it reported calendar year written premium ceded or year-end loss and loss expense reserves ceded greater than 3% of prior year-end surplus as regards policyholders; (ii) it accounted for that contract as reinsurance and not as a deposit; and (iii) the contract(s) contain one or more of the following features or other features that would have similar results:
- (a) A contract term longer than two years and the contract is noncancellable by the reporting entity during the contract term;
 - (b) A limited or conditional cancellation provision under which cancellation triggers an obligation by the reporting entity, or an affiliate of the reporting entity, to enter into a new reinsurance contract with the reinsurer, or an affiliate of the reinsurer;
 - (c) Aggregate stop loss reinsurance coverage;
 - (d) An unconditional or unilateral right by either party to commute the reinsurance contract except for such provisions which are only triggered by a decline in the credit status of the other party;
 - (e) A provision permitting reporting of losses, or payment of losses, less frequently than on a quarterly basis (unless there is no activity during the period); or
 - (f) Payment schedule, accumulating retentions from multiple years or any feature inherently designed to delay timing of the reimbursement to the ceding entity.....Yes ☐ No ☒
- 9.2 Has the reporting entity during the period covered by the statement ceded any risk under any reinsurance contract (or under multiple contracts with the same reinsurer or its affiliates), excluding cessions to approved pooling agreements or to captive insurance companies that are directly or indirectly controlling, controlled by, or under common control with (i) one or more unaffiliated policyholders of the reporting entity, or (ii) an association of which one or more unaffiliated policyholders of the reporting entity is a member, where:
- (a) The written premium ceded to the reinsurer by the reporting entity or its affiliates represents fifty percent (50%) or more of the entire direct and assumed premium written by the reinsurer based on its most recently available financial statement; or
 - (b) Twenty-five percent (25%) or more of the written premium ceded to the reinsurer has been retroceded back to the reporting entity or its affiliates.....Yes ☐ No ☒

See report of independent auditors.

HomeWise Insurance Company

Selected General Interrogatories Relating to Reinsurance (continued)


- 9.3 If yes to 9.1 or 9.2, please provide the following information in the Reinsurance Summary Supplemental Filing for General Interrogatory 9:
- (a) The aggregate financial statement impact gross of all such ceded reinsurance contracts on the balance sheet and statement of income;
 - (b) A summary of the reinsurance contract terms and indicate whether it applies to the contracts meeting the criteria in 9.1 or 9.2; and
 - (c) A brief discussion of management's principle objectives in entering into the reinsurance contract including the economic purpose to be achieved.
- 9.4 Except for transactions meeting the requirements of paragraph 30 of SSAP No. 62, *Property and Casualty Reinsurance*, has the reporting entity ceded any risk under reinsurance contract (or multiple contracts with the same reinsurer or its affiliates) during the period covered by the financial statement, and either:
- (a) Accounted for that contract as reinsurance (either prospective or retroactive) under statutory accounting principles (SAP) and as a deposit under generally accepted accounting principles (GAAP); or
 - (b) Accounted for that contract as reinsurance under GAAP and as a deposit under SAP?.....Yes ☐ No ☒
- 9.5 If yes to 9.4, explain in the Reinsurance Summary Supplemental Filing for General Interrogatory 9 (Section D) why the contract(s) is treated different for GAAP and SAP.



Statutory Basis Financial Statements
and Other Financial Information

HomeWise Insurance Company

*Years ended December 31, 2007 and 2006
with Report of Independent Auditors*

Thomas Howell
 Ferguson P.A.

HomeWise Insurance Company
Statutory Basis Financial Statements
and Other Financial Information
Years ended December 31, 2007 and 2006

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Report of Independent Auditors

The Board of Directors
HomeWise Insurance Company

We have audited the accompanying statements of admitted assets, liabilities and capital and surplus - statutory basis of the HomeWise Insurance Company (the Company) as of December 31, 2007 and 2006, and the related statutory basis statements of operations, changes in capital and surplus, and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As described in Note 1, the accompanying statutory basis financial statements have been prepared in conformity with accounting practices prescribed or permitted by the Florida Office of Insurance Regulation, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the admitted assets, liabilities and capital and surplus of HomeWise Insurance Company as of December 31, 2007 and 2006, and the results of its operations and its cash flows for the years then ended on the basis of accounting described in Note 1.

Thomas Howell
▲ Ferguson P.A.

Page Two

Our audits were made for the purpose of forming an opinion on the statutory basis financial statements taken as a whole. The supplemental disclosures included in other financial information as of and for the year ended December 31, 2007, are presented to comply with the National Association of Insurance Commissioners' *Accounting Practices and Procedures Manual* and are not a required part of the statutory basis financial statements. This other financial information has been subjected to the auditing procedures applied in the audits of the statutory basis financial statements and, in our opinion, is fairly stated in all material respects in relation to the statutory basis financial statements taken as a whole.

This report is intended solely for the use of the Board of Directors and management of HomeWise Insurance Company and for filing with the state insurance regulatory authorities and should not be used for any other purpose.

Thomas Howell Ferguson P.A.

May 9, 2008

HomeWise Insurance Company

Statements of Admitted Assets, Liabilities and Capital and Surplus - Statutory Basis

| | December 31, | |
|--|---------------|---------------|
| | 2007 | 2006 |
| Admitted assets | | |
| Cash and invested assets: | | |
| Cash and cash equivalents | \$ 4,475,371 | \$ 20,673,342 |
| Short-term investments | 2,166,986 | 2,058,147 |
| Total cash and invested assets | 6,642,357 | 22,731,489 |
| Accrued investment income | 13,866 | 19,518 |
| Premiums receivable | 969,600 | 3,662,727 |
| Reinsurance balances recoverable | 4,288 | 764,564 |
| Electronic data processing equipment, net | 111,750 | 90,815 |
| Receivables from parent and affiliates | 4,401,316 | 48,217 |
| Net deferred tax asset | 24,658 | 183,011 |
| Federal income taxes recoverable | 660,278 | 780,575 |
| Other assets | 833,866 | 104,365 |
| Total admitted assets | \$ 13,661,979 | \$ 28,385,281 |
| Liabilities and capital and surplus | | |
| Liabilities: | | |
| Loss and loss adjustment expense reserves | \$ 70,190 | \$ 80,702 |
| Unearned premiums, net | 1,358,639 | 2,663,052 |
| Reinsurance premiums payable | 1,390,154 | 12,652,500 |
| Accounts payable and accrued expenses | 326,956 | 1,160,934 |
| Payable to affiliates | 295,464 | 1,489,850 |
| Payable to Citizens Property Insurance Corporation | 533,176 | 1,185,888 |
| Total liabilities | 3,974,579 | 19,232,926 |
| Capital and surplus | 9,687,400 | 9,152,355 |
| Total liabilities and capital and surplus | \$ 13,661,979 | \$ 28,385,281 |

See accompanying notes.

HomeWise Insurance Company
Statements of Operations - Statutory Basis

| | Years ended December 31, | |
|--|--------------------------|--------------|
| | 2007 | 2006 |
| Underwriting income: | | |
| Premiums earned, net of reinsurance ceded | \$ 2,651,949 | \$ 4,337,035 |
| Underwriting expenses: | | |
| Losses and loss adjustment expenses incurred | (14,429) | 240,555 |
| Underwriting, acquisition, and other expenses incurred | 2,232,468 | 5,078,323 |
| Total underwriting expenses | 2,218,039 | 5,318,878 |
| Net underwriting gain (loss) | 433,910 | (981,843) |
| Net investment income | 529,899 | 638,975 |
| Other expense | (4,461) | (127) |
| Income (loss) before federal income tax expense | 959,348 | (342,995) |
| Federal income tax expense | 183,424 | 41,206 |
| Net income (loss) | \$ 775,924 | \$ (384,201) |

See accompanying notes.

HomeWise Insurance Company
Statements of Changes in Capital and Surplus - Statutory Basis
Years ended December 31, 2007 and 2006

| | <u>Common Stock</u> | | <u>Gross Paid-in and Contributed Surplus</u> | <u>Unassigned Funds</u> | <u>Total</u> |
|---------------------------------|---------------------|-------------------|--|-----------------------------|---------------------|
| | <u>Shares</u> | <u>Per Value</u> | | | |
| Balance as of December 31, 2005 | 100,000 | \$ 100,000 | \$ 9,400,000 | \$ 31,287 | \$ 9,531,287 |
| Change in deferred income taxes | - | - | - | 183,011 | 183,011 |
| Change in nonadmitted assets | - | - | - | (177,742) | (177,742) |
| Net loss | - | - | - | (384,201) | (384,201) |
| Balance as of December 31, 2006 | 100,000 | 100,000 | 9,400,000 | (347,645) | 9,152,355 |
| Issuance of common stock | 550,000 | 550,000 | (550,000) | - | - |
| Change in deferred income taxes | - | - | - | (158,354) | (158,354) |
| Change in nonadmitted assets | - | - | - | (82,525) | (82,525) |
| Net income | - | - | - | 775,924 | 775,924 |
| Balance as of December 31, 2007 | <u>650,000</u> | <u>\$ 650,000</u> | <u>\$ 8,850,000</u> | <u>\$ 187,400</u> | <u>\$ 9,687,400</u> |

See accompanying notes.

HomeWise Insurance Company
Statements of Cash Flows - Statutory Basis

| | Years ended December 31, | |
|---|----------------------------|-----------------------------|
| | <u>2007</u> | <u>2006</u> |
| Operating activities | | |
| Premiums (paid) collected, net of reinsurance | \$ (7,870,979) | \$ 17,172,332 |
| Net investment income received | 535,551 | 622,074 |
| Losses and loss adjustment expenses recovered (paid) | 249,693 | (409,917) |
| Underwriting, acquisition, and other expenses paid | (2,557,825) | (4,504,711) |
| Income taxes paid | (63,127) | (827,303) |
| Net cash (used in) provided by operating activities | <u>(9,706,687)</u> | <u>12,052,475</u> |
| Financing and miscellaneous activities | | |
| Other miscellaneous (uses) sources | <u>(6,382,445)</u> | 1,142,971 |
| Net cash (used in) provided by financing and miscellaneous activities | <u>(6,382,445)</u> | 1,142,971 |
| Net (decrease) increase in cash | (16,089,132) | 13,195,446 |
| Cash at beginning of year | <u>22,731,489</u> | 9,536,043 |
| Cash at end of year | <u><u>\$ 6,642,357</u></u> | <u><u>\$ 22,731,489</u></u> |
| Cash consists of the following: | | |
| Cash and cash equivalents | \$ 4,475,371 | \$ 20,673,342 |
| Short-term investments | <u>2,166,986</u> | <u>2,058,147</u> |
| | <u><u>\$ 6,642,357</u></u> | <u><u>\$ 22,731,489</u></u> |

See accompanying notes.

HomeWise Insurance Company
Notes to Statutory Basis Financial Statements
Years ended December 31, 2007 and 2006

1. Summary of Significant Accounting Policies

Organization and Description of Company

HomeWise Insurance Company (the Company), a wholly-owned subsidiary of HomeWise Holdings, Inc. (HHI), an insurance holding company, is domiciled in the state of Florida. The Company received its Certificate of Authority from the Florida Office of Insurance Regulation (the Office) on December 5, 2005, and commenced operations on January 12, 2006. The Company is affiliated with HomeWise Management Company (HMC) and HomeWise Preferred Insurance Company (HPIC), which are wholly-owned subsidiaries of HHI.

The Company writes wind-only coverage exclusively in the state of Florida, an area that is exposed to damage from hurricanes and severe storms. The Company attempts to mitigate its exposure to losses from storms by purchasing quota share and catastrophe reinsurance coverage. However, such a storm, depending on its path and severity, could result in losses to the Company exceeding its reinsurance protection and could have a material adverse effect on the financial condition and results of operations of the Company.

Basis of Presentation

The accompanying statutory basis financial statements have been prepared in accordance with statutory accounting practices (SAP) prescribed or permitted by the Office. Such statutory practices require preparation of the financial statements in accordance with the National Association of Insurance Commissioners' (NAIC) *Accounting Practices and Procedures Manual* subject to deviations prescribed by the Office. SAP is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America (GAAP). Such practices vary in certain respects from those under GAAP. The Company's significant accounting practices and the variances from GAAP are summarized below:

- Certain assets designated as "nonadmitted," principally past-due uncollected premiums, prepaid expenses, and other assets not specifically identified as an admitted asset within the *Accounting Practices and Procedures Manual*, are excluded from the accompanying statements of admitted assets, liabilities, and capital and surplus and are charged directly to unassigned surplus. Under GAAP, such assets would be included in the balance sheets at net realizable values.
- Loss and loss adjustment expense reserves and unearned premiums ceded to reinsurers have been reported as reductions of the related liabilities rather than as assets as would be required under GAAP.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

1. Summary of Significant Accounting Policies (continued)

Basis of Presentation (continued)

- Cash in the statements of cash flows represents cash, cash equivalents, and short-term investments with remaining maturities of one year or less. Under GAAP, the corresponding caption of cash and cash equivalents would include cash balances and investments with initial maturities of three months or less.
- The costs of acquiring and renewing business are expensed when incurred. Under GAAP, such costs, to the extent recoverable, would be deferred and amortized over the effective period of the related insurance policies.
- Deferred tax assets are limited to 1) the amount of federal income taxes paid in prior years that can be recovered through loss carrybacks for existing temporary differences that reverse by the end of the subsequent calendar year, plus 2) the lesser of the remaining gross deferred tax assets expected to be realized within one year of the financial statement date or 10% of capital and surplus excluding any net deferred tax assets, "electronic data processing" (EDP) equipment and operating software and any net positive goodwill, plus 3) the amount of remaining gross deferred tax assets that can be offset against existing gross deferred tax liabilities. The remaining deferred tax assets are nonadmitted. Deferred taxes do not include amounts for state income taxes. Under GAAP, state income taxes would be included in the computation of deferred taxes, a deferred tax asset would be recorded for the amount of gross deferred tax assets expected to be realized in future years, and a valuation allowance would be established for deferred tax assets not realizable.
- Commissions allowed by reinsurers on business ceded are reported as a reduction of expenses when incurred to the extent the amount does not exceed actual acquisition costs, rather than being deferred and amortized with deferred policy acquisition costs as would be required by GAAP. Commissions in excess of the acquisition costs, if any, would be deferred and recognized over the policy term consistent with GAAP.
- Certain other reported amounts are classified or presented differently in the financial statements prepared on the basis of SAP than they would be under GAAP. Statutory requirements require that the financial statements of the Company be filed with state regulatory authorities. Accordingly, the financial statements are presented in a format similar to the filed annual statement, which differs from the format of financial statements presented under GAAP. Required statutory disclosures that are not applicable to the Company are not included in the notes to these statutory financial statements.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

1. Summary of Significant Accounting Policies (continued)

Other significant accounting practices are as follows:

Recognition of Premium Revenues

Premiums are recorded as earned on a monthly pro rata basis over the contract period that the related policies are expected to be in force. The portion of premiums not earned at the end of the year is recorded as unearned premiums. Premiums collected prior to the effective date of the policy are recorded as a liability.

Cash and Cash Equivalents

Cash and cash equivalents include demand deposits with financial institutions and other highly liquid investments with original maturities of three months or less.

Investments

Short-term investments are highly liquid investments with remaining maturities of one year or less.

Concentration of Credit Risk

The Company's financial instruments exposed to concentrations of credit risk consist primarily of its cash and cash equivalents, short-term investments, reinsurance recoveries, and premiums receivable. The Company maintains its cash and cash equivalents at several quality financial institutions. Bank deposit accounts, at times, may exceed federally insured limits. The Company has not experienced any losses in such accounts. The Company believes it is not exposed to any significant credit risk on cash and cash equivalents.

All investment transactions have credit exposure to the extent that a counterparty may default on an obligation to the Company. Credit risk is a consequence of carrying investment positions. To manage credit risk, the Company focuses primarily on highly liquid debt instruments, reviews the credit strength of all entities in which it invests, limits its exposure in any one investment, and monitors portfolio quality, taking into account credit ratings assigned by recognized credit rating organizations.

Electronic Data Processing (EDP) Equipment

The admitted value of the Company's EDP equipment and operating software is limited to 3% of capital and surplus. The admitted portion is reported at cost, less accumulated depreciation of \$83,693 and \$27,631 at December 31, 2007 and 2006, respectively. EDP equipment and operating software is depreciated using the straight-line method over the lesser of its useful life or three years. Other furniture and equipment is recorded as a non-admitted asset and depreciated using the straight-line method over the estimated useful life of seven years. Depreciation expense charged to operations was \$79,293 and \$37,661 in 2007 and 2006, respectively.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

1. Summary of Significant Accounting Policies (continued)

Reinsurance

The accompanying statutory basis financial statements reflect reserves for premiums and losses and loss adjustment expenses (LAE), net of reinsurance ceded (See Note 6). Those reinsurance arrangements allow management to control exposure to potential losses arising from large risks. A significant portion of the reinsurance is effected under a quota share reinsurance agreement. Amounts recoverable from reinsurers are estimated in a manner consistent with the loss and LAE reserves associated with the reinsured policies. Reinsurance premiums, losses, and LAE are accounted for on bases consistent with those used in accounting for the original policies issued and the terms of the reinsurance contracts.

Loss and Loss Adjustment Expense (LAE) Reserves

Loss and LAE reserves represent the estimated ultimate net cost of all unpaid reported and unreported losses and LAE. The reserves for unpaid losses and LAE are estimated using individual case-basis estimates for reported losses and actuarial estimates for losses incurred but not yet reported. Those estimates are subject to the effects of trends in loss severity and frequency. Although considerable variability is inherent in such estimates, management believes that the reserves for losses and LAE are adequate. The estimates are continually reviewed and adjusted as necessary as experience develops or new information becomes known; such adjustments are included in current operations. The ultimate settlement of losses and LAE may vary significantly from the estimated amounts included in the financial statements. The Company does not discount its loss and LAE reserves.

The anticipated effect of inflation is implicitly considered when estimating liabilities for losses and LAE. While anticipated price increases due to inflation are considered in estimating the ultimate claim costs, the increase in average severities of claims is caused by a number of factors that vary with the individual type of policy written. Future average severities are projected based on historical trends adjusted for implemented changes in underwriting standards, policy provisions, and general economic trends. Those anticipated trends are monitored based on actual development and the estimated liabilities are modified if necessary.

Loss and LAE reserves are reported net of reinsurance recoverables for unpaid losses and LAE. Losses and LAE ceded through reinsurance are credited against losses and LAE incurred.

Guaranty Fund and Residual Market Pool Assessments

The Company is subject to assessments by a Florida guaranty fund, a residual market pool, and a state catastrophe reinsurance pool. The activities of this fund and these pools include collecting funds from solvent insurance companies to cover losses resulting from the insolvency or rehabilitation of other insurance companies or deficits generated by Florida Insurance Guaranty Association (FIGA), Citizens Property Insurance Corporation (Citizens), and the Florida Hurricane Catastrophe Fund (FHCF).

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

1. Summary of Significant Accounting Policies (continued)

Guaranty Fund and Residual Market Pool Assessments (continued)

The Company's policy is to recognize its obligation for guaranty fund, Citizens, and FHCF assessments when the Company has the information available to reasonably estimate its liabilities. Guaranty fund assessments are generally available for recoupment from policyholders and as such, amounts assessed are recorded as a recoverable asset. Amounts recoverable are generally expected to be collected over the following year. For the year ended December 31, 2007, the Company was assessed \$755,526 (none in 2006).

Income Taxes

The Company calculates its state and federal income tax liabilities based upon the statutory rates in effect during the year.

Use of Estimates

The preparation of statutory basis financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the statutory basis financial statements, and the reported amounts of revenues and expenses during the reporting period. Such estimates and assumptions could change in the future as more information becomes known, which could impact the amounts reported and described in the financial statements.

2. Regulatory Requirements and Restrictions

Florida Statutes Section 624.408 requires the Company to maintain minimum capital and surplus of \$4 million and to meet the risk-based capital requirements (see Note 9). Additionally, Florida Statutes Section 624.4095 requires the Company to maintain a ratio of the product of written premiums times 0.90 to surplus of no greater than 10-to-1 for gross written premiums and 4-to-1 for net written premiums. The Company is in compliance with these requirements.

Additionally, the Company is required to maintain an amount on deposit with the state of Florida to secure the payment of claims. Cash on deposit in the amount of \$326,483 and \$310,371 has been assigned to the Office as of December 31, 2007 and 2006, respectively, to satisfy this requirement. This deposit was included in cash and cash equivalents in the accompanying statements of admitted assets, liabilities, and capital and surplus.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

3. Investments

Short-term investments consist of U.S. Government money market funds that have a maturity of one year or less from the date of purchase and are stated at cost, which approximates fair value.

Major categories of the Company's net investment income are summarized as follows:

| | Years ended December 31, | |
|---|--------------------------|-------------------|
| | <u>2007</u> | <u>2006</u> |
| Investment income: | | |
| Cash and cash equivalents | \$ 439,564 | \$ 1,029,790 |
| Short-term investments | <u>109,604</u> | <u>65,774</u> |
| | 549,168 | 1,095,564 |
| Investment expense: | | |
| Interest expense on funds held under reinsurance agreements | - | (435,082) |
| Interest expense on arbitration | - | (6,981) |
| Bank fees | <u>(19,269)</u> | <u>(14,526)</u> |
| | <u>(19,269)</u> | <u>(456,589)</u> |
| Net investment income | <u>\$ 529,899</u> | <u>\$ 638,975</u> |

4. Premiums Receivable

Premiums receivable includes amounts due from HomeWise Management Company, the Company's managing general agent (MGA), who collects all premiums and remits them to the Company. The Company nonadmits balances due from insureds and deferred installments for which a portion of the receivable is more than 90 days past due and exceeds the related unearned premium. Premiums receivable is charged to bad debt expense in the period determined uncollectible. Recoveries received on amounts previously charged-off are credited to bad debt expense in the period received.

Premiums receivable consists of the following:

| | December 31, | |
|---------------------------------|-------------------|---------------------|
| | <u>2007</u> | <u>2006</u> |
| Premiums receivable, gross | \$ 969,600 | \$ 3,666,143 |
| Nonadmitted premiums receivable | <u>-</u> | <u>(3,416)</u> |
| Premiums receivable, net | <u>\$ 969,600</u> | <u>\$ 3,662,727</u> |

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

5. Loss and Loss Adjustment Expense (LAE) Reserves

The following table provides a reconciliation of the beginning and ending reserve balances for losses and LAE, net of reinsurance recoverables.

| | December 31, | |
|--|----------------|--------------|
| | 2007 | 2006 |
| | (in thousands) | |
| Loss and LAE reserves at beginning of year | \$ 81 | \$ - |
| Losses and LAE incurred related to: | | |
| Current year | 67 | 241 |
| Prior years | (81) | - |
| | (14) | 241 |
| Losses and LAE paid related to: | | |
| Current year | 36 | 160 |
| Prior years | (39) | - |
| | (3) | 160 |
| Loss and LAE reserves at end of year | \$ <u>70</u> | \$ <u>81</u> |

Anticipated reinsurance recoverables on unpaid losses and LAE are approximately \$94,000 and \$242,000 at December 31, 2007 and 2006, respectively. Reinsurance recoverables on paid losses and LAE are approximately \$4,000 and \$250,000 at December 31, 2007 and 2006, respectively.

In 2007, net incurred losses and LAE attributable to insured events of prior years have decreased by \$81,000 as a result of re-estimation of unpaid losses and loss adjustment expenses. Original estimates are decreased or increased as additional information becomes known regarding individual claims.

6. Reinsurance

Certain premiums and losses are ceded to other insurance companies under various reinsurance agreements. The reinsurance agreements provide the Company with increased capacity to write more risk and maintain its exposure to loss within its capital resources. As of December 31, 2007 and 2006, the Company's reinsurance program consisted of quota share and excess of loss reinsurance for catastrophic events. Following is a summary of the reinsurance coverage.

Effective January 1, 2007, the Company and its affiliated company, HomeWise Preferred Insurance Company (collectively, the Reinsured), entered into a quota share reinsurance agreement with Harlequin Insurance (Bermuda) SAC Limited (the Reinsurer). Under the terms of the agreement, which expires on May 31, 2008, the Reinsurer assumes 75% of the Reinsured's net liabilities for losses (loss and loss adjustment expense) after taking into effect the Reinsured's excess of loss reinsurance coverage provided by the FHCF and, through May 31, 2007, the coverage provided by open market excess of loss reinsurance purchased by the Reinsured. Under the terms of the agreement, the Reinsured cedes 75% of their gross premiums after deducting the cost of the above referenced inuring reinsurance to the Reinsurer. The Reinsured cedes 75% of

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

6. Reinsurance (continued)

covered gross losses to the Reinsurer after deducting recoveries from the referenced inuring reinsurance. The ceding commission from the Reinsurer to the Reinsured is on a reimbursement basis wherein the Reinsurer reimburses the Reinsured for 75% of their acquisition and overhead expenses. The agreement includes an Event Cap for ceded losses of 44% of the ceded premium earned during the term. It also includes an Aggregate Loss and Expense Ratio Cap wherein the maximum amount of losses and ceding commission payable by the Reinsurer under this Agreement in the aggregate shall be limited to 150% of the ceded premium earned during the term. In the event either cap is met, the Reinsured share in recoveries in proportion to their respective subject losses to the total of losses subject to the agreement. Obligations of the Reinsurer to the Reinsured are collateralized by funds held in a reinsurance trust account maintained in a United States bank. Premiums ceded under the quota share agreement, net of reinsurer's pro rata cost of catastrophe coverages, and ceding commissions were \$17,535,964 and \$13,258,493, respectively, for the year December 31, 2007. The ceding commissions have been recorded as a reduction of underwriting, acquisition, and other expenses in the accompanying statements of operations.

Effective January 4, 2006, the Company entered into a quota share agreement that generally provides coverage for 75% of all losses net of other reinsurance coverages. The reinsurer's maximum liability per occurrence shall be limited to 75% of \$20,000,000, and as respects to any one risk shall be 75% of \$4,000,000. The reinsurer allows the Company a ceding commission percentage equal to that of the Company's acquisition costs. Premiums ceded under the quota share agreement, net of reinsurer's pro rata cost of catastrophe coverages and ceding commissions were \$19,541,734 and \$13,831,937, respectively, for the year December 31, 2006. The ceding commissions have been recorded as a reduction of underwriting, acquisition, and other expenses in the accompanying statements of operations. In addition, the reinsurer shall pay the Company a 15% profit commission on net profit to be determined at the expiration of the contract period, May 31, 2007.

The catastrophe excess of loss coverage is provided by agreements with commercial reinsurers and by the FHCF. For the year ended December 31, 2007, the excess of loss treaties generally provide coverage on ultimate net losses of approximately \$107,400,000 in excess of \$2,700,000 per occurrence, not to exceed approximately \$111,700,000 for all occurrences. The FHCF provided coverage for 90% of the losses from qualifying catastrophic events in excess of approximately \$19,700,000 up to a maximum of approximately \$93,100,000, plus 100% of \$10,000,000 in excess of \$2,700,000 (drop down layer). For the year ended December 31, 2007, premiums of \$1,283,217 and \$9,034,430 were ceded under the commercial excess catastrophe agreements and FHCF, respectively. For the year ended December 31, 2006, the excess of loss treaties generally provide coverage on ultimate net losses of approximately \$142,600,000 in excess of \$5,200,000 per occurrence, not to exceed approximately \$158,700,000 for all occurrences. The FHCF provided coverage for 90% of the losses from qualifying catastrophic events in excess of approximately \$34,300,000 up to a maximum of approximately \$142,600,000, plus 100% of \$10,000,000 in excess of \$2,900,000 (drop down layer). For the year ended December 31, 2006, premiums of \$13,110,945 and \$6,223,942 were ceded under the commercial excess catastrophe agreements and FHCF, respectively.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

6. Reinsurance (continued)

The FHCF provides coverage for named hurricanes only and provides no coverage after the one time limit is exhausted. Reinsurance premiums for the FHCF are paid on a total insured value basis. In the event of a loss assessment, the Company may recoup the assessments from its policyholders.

Effective June 1, 2007 and 2006, the Company executed reinsurance premium protection agreements to reinsure the reinstatement premium payment obligations which accrue to the Company under the private catastrophe excess of loss agreements. The coverage is limited to 100% of the original contracted reinsurance placement. Premiums ceded under the reinsurance premium protection agreements during 2007 and 2006 were \$551,517 and \$7,723,023, respectively.

The Company's reinsured risks are treated, to the extent of the reinsurance, as though they are risks for which the Company is not liable. However, the Company remains liable in the event the reinsuring companies do not meet their obligations under these reinsurance agreements. Given the quality of the reinsuring companies, management believes this possibility to be remote. See Note 5 for recoveries due from reinsurers relating to paid and unpaid losses and LAE.

On May 31, 2007, the Company terminated and commuted its excess of loss reinsurance agreement with Catlin Insurance Company Ltd. There were no losses assumed or gain or loss recognized on the commutation. Per the agreement, the Company was owed the amount in the experience account that was established under the original reinsurance agreement. That amount, calculated pursuant to the agreements, was \$822,000. The experience account balance was reduced by a commutation settlement charge of \$360,000. The net settlement amount of \$522,000 was received by the Company on July 22, 2007.

The Company terminated and commuted its quota share reinsurance agreement with Glacier Reinsurance AG on January 1, 2007. As a result of the commutation, \$7,989,164 in unearned premium was returned to the Company and \$6,833,689 in ceding commission was returned to Glacier Reinsurance AG. The cession of any future losses at January 1, 2007 and forward was also terminated. The Company also increased its ceded loss and loss adjustment paid and reduced its ceded reserves to recognize the effect of releasing the insurer from its obligation under the treaty. The net effect of the commutation was an increase in losses incurred of \$210,623. The reinsurance agreement with Glacier Reinsurance AG was replaced with a 75% quota share agreement with Harlequin Insurance (Bermuda) SAC Limited effective January 1, 2007.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

6. Reinsurance (continued)

The effects of reinsurance on premiums written and earned at December 31, are as follows:

| | 2007 | | 2006 | |
|------------------|---------------------|---------------------|---------------------|---------------------|
| | Written | Earned | Written | Earned |
| Direct premiums | \$ 21,766,628 | \$ 33,475,449 | \$ 37,776,317 | \$ 13,858,975 |
| Assumed premiums | (2,343) | 375,374 | 21,873,836 | 21,496,120 |
| Ceded premiums | <u>(20,416,752)</u> | <u>(31,198,874)</u> | <u>(52,650,065)</u> | <u>(31,018,060)</u> |
| Net premiums | <u>\$ 1,347,533</u> | <u>\$ 2,651,949</u> | <u>\$ 7,000,088</u> | <u>\$ 4,337,035</u> |

The following table summarizes the effect of ceded unearned premiums on the direct unearned premiums reserve and the related commission equity at December 31:

| | 2007 | 2006 |
|---------------------------|-----------------------|-----------------------|
| Direct unearned premiums | \$ 12,208,521 | \$ 23,917,342 |
| Assumed unearned premiums | - | 377,716 |
| Ceded unearned premiums | <u>(10,849,882)</u> | <u>(21,632,006)</u> |
| Unearned premiums, net | <u>\$ 1,358,639</u> | <u>\$ 2,663,052</u> |
| Assumed commission equity | \$ - | \$ 60,435 |
| Ceded commission equity | <u>(3,227,628)</u> | <u>(6,382,638)</u> |
| Commission equity, net | <u>\$ (3,227,628)</u> | <u>\$ (6,322,203)</u> |

At December 31, 2007 and 2006, no individual reinsurer owed the Company an unsecured amount that was greater than 3% of the Company's surplus.

For the year ended December 31, 2007, recoveries under reinsurance contracts amounted to \$518,929 (none in 2006).

7. Policy Assumption Agreement

The Company assumed written premiums of \$21,873,836 during 2006 under a policy assumption agreement with Citizens. The Company provided a ceding commission to Citizens of 16% of assumed premiums to cover the acquisition costs incurred by Citizens. Total ceding commissions charged to operations in 2006 were \$3,499,814 (none in 2007).

8. Income Taxes

Income before federal income taxes differs from taxable income principally due to differences in loss and LAE reserves and unearned premiums for tax and statutory basis financial reporting purposes.

State income taxes are classified as taxes, licenses, and fees in the NAIC Annual Statement and as underwriting, acquisition, and other expenses on the statements of operations.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

8. Income Taxes (continued)

A. Components of deferred tax assets (DTAs) and deferred tax liabilities (DTLs) are as follows:

| | December 31, | |
|---|--------------------|-------------------|
| | 2007 | 2006 |
| Gross DTAs | \$ 182,436 | \$ 252,962 |
| Gross DTLs | (157,778) | (35,370) |
| Net admitted DTAs | 24,658 | 217,592 |
| Nonadmitted DTAs | - | (34,581) |
| Net admitted DTAs | <u>\$ 24,658</u> | <u>\$ 183,011</u> |
| (Decrease) increase in nonadmitted DTAs | <u>\$ (34,581)</u> | <u>\$ 34,581</u> |

B. Unrecognized DTLs

There are no unrecognized DTLs.

C. Current tax and change in deferred tax:

The provision for income taxes incurred is:

| | Years ended December 31, | |
|---------------------------------|--------------------------|------------------|
| | 2007 | 2006 |
| Current year income tax expense | \$ 120,253 | \$ 41,206 |
| Prior year under accrual | 63,171 | - |
| Current income taxes incurred | <u>\$ 183,424</u> | <u>\$ 41,206</u> |

The tax effect of temporary differences at December 31, 2007, that give rise to significant deferred tax assets and deferred tax liabilities are as follows:

| DTAs | Statutory | Tax | Difference | Tax Effect |
|-------------------------|-----------|--------------|--------------|---------------------|
| Unpaid losses and LAE | \$ 70,190 | \$ 65,608 | \$ 4,582 | \$ 1,558 |
| Unearned premiums | 1,358,639 | 1,086,911 | 271,728 | 92,388 |
| Nonadmitted assets | - | 260,266 | 260,266 | 88,490 |
| Gross DTAs | | | | <u>\$ 182,436</u> |
| Nonadmitted DTAs | | | | <u>\$ -</u> |
| DTLs | Statutory | Tax | Difference | Tax Effect |
| Furniture and equipment | \$ - | \$ (211,223) | \$ (211,223) | \$ (71,816) |
| Prepaid expenses | - | (32,400) | (32,400) | (11,016) |
| Profit sharing expense | - | (220,429) | (220,429) | (74,946) |
| Gross DTLs | | | | <u>\$ (157,778)</u> |

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

8. Income Taxes (continued)

The changes in the main components of DTAs and DTLs are as follows:

| DTAs Resulting from Book/Tax Differences | | December 31, | | |
|---|-------------------|---------------------|--------------------|--|
| | <u>2007</u> | <u>2006</u> | <u>Change</u> | |
| Unpaid losses and LAE | \$ 1,558 | \$ 1,923 | \$ (365) | |
| Unearned premiums | 92,388 | 181,087 | (88,699) | |
| Nonadmitted assets | <u>88,490</u> | <u>69,952</u> | <u>18,538</u> | |
| Gross DTAs | <u>\$ 182,436</u> | <u>\$ 252,962</u> | <u>\$ (70,526)</u> | |
| Nonadmitted DTAs | <u>\$ -</u> | <u>\$ (34,581)</u> | <u>\$ 34,581</u> | |

| DTLs Resulting from Book/Tax Differences | | December 31, | | |
|---|---------------------|---------------------|---------------------|--|
| | <u>2007</u> | <u>2006</u> | <u>Change</u> | |
| Furniture and equipment | \$ (71,816) | \$ (29,591) | \$ (42,225) | |
| Prepaid expenses | (11,016) | (5,779) | (5,237) | |
| Profit sharing expense | <u>(74,946)</u> | <u>-</u> | <u>(74,946)</u> | |
| Gross DTLs | <u>\$ (157,778)</u> | <u>\$ (35,370)</u> | <u>\$ (122,408)</u> | |

The change in gross DTAs of \$(70,256) and gross DTLs of \$(122,408) is the change in net deferred income taxes before the consideration of nonadmitted DTAs.

D. Reconciliation of federal income tax rate to actual effective rate:

The significant book-to-tax adjustments were as follows:

| | <u>2007</u> | <u>Effective Tax Rate</u> | <u>2006</u> | <u>Effective Tax Rate</u> |
|--------------------------------------|-------------------|-------------------------------|---------------------|-------------------------------|
| Provision computed at statutory rate | \$ 326,178 | 34.00 % | \$ (116,618) | (34.00)% |
| Nonadmitted assets | (18,538) | (1.93) | (69,952) | (20.39) |
| Other | <u>68,718</u> | <u>7.16</u> | <u>10,184</u> | <u>2.96</u> |
| Total | <u>\$ 376,358</u> | <u>39.23 %</u> | <u>\$ (176,386)</u> | <u>(51.43)%</u> |
| Federal income tax | \$ 183,424 | 19.12 % | \$ 41,206 | 12.01 % |
| Change in deferred taxes | <u>192,934</u> | <u>20.11</u> | <u>(217,592)</u> | <u>(63.44)</u> |
| Statutory income taxes | <u>\$ 376,358</u> | <u>39.23 %</u> | <u>\$ (176,386)</u> | <u>(51.43)%</u> |

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

8. Income Taxes (continued)

E. Operating loss and tax credit carryforwards:

1. At December 31, 2007 and 2006, the Company had no unused capital loss carryforwards available to offset against future taxable income.
2. The following is income tax expense that is available for recoupment in the event of future net losses:

| <u>Year</u> | <u>Amount</u> |
|-------------|---------------|
| 2007 | \$ 120,253 |
| 2006 | 104,377 |

F. Consolidated federal income tax return:

The Company files a consolidated income tax return with the following:
HomeWise Holdings, Inc.
HomeWise Preferred Insurance Company
HomeWise Management Company

9. Capital and Surplus

The Company has authorized 1,000,000 shares of \$1 par value common stock, of which 650,000 and 100,000 shares are issued and outstanding at December 31, 2007 and 2006, respectively. The parent company, HomeWise Holdings, Inc., is the sole shareholder. No other classes of common or preferred shares were issued during 2007 or 2006.

Property and casualty insurance companies are subject to certain risk-based capital (RBC) requirements as specified by the NAIC. Under those requirements, the amount of capital and surplus maintained by a property and casualty insurance company is to be determined based on the various risk factors related to it. The Company's capital and surplus exceeds the RBC requirements at December 31, 2007 and 2006, respectively.

The maximum amount of dividends that may be paid by property and casualty insurance companies without prior approval of the Office is subject to restrictions relating to statutory surplus and net income. Furthermore, in accordance with the Company's Certificate of Authority Consent Order, during the first three years of operations it may only pay dividends that are approved in advance by the Office. The Company did not declare or pay any dividends during the years ended December 31, 2007 or 2006.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

9. Capital and Surplus (continued)

The Company is currently in the process of applying to the Louisiana Department of Insurance for a certificate of authority in that state. To meet the Louisiana regulation that the Company's minimum common capital stock be \$650,000, the Company issued 550,000 of its \$1 par value authorized shares of common stock to its parent, HHI, in a non-cash transaction. The issuance of these shares was accounted for by reclassifying \$550,000 from the gross paid-in and contributed surplus account to common stock. This transaction does not impact the total policyholder surplus or ownership of the Company.

10. Related Party Transactions

The Company is a wholly-owned subsidiary of HomeWise Holdings, Inc. (HHI) and is affiliated with HomeWise Management Company (HMC) and HomeWise Preferred Insurance Company (HPIC), which are also wholly-owned subsidiaries of HHI.

Effective January 1, 2006, the Company entered into a managing general agency agreement with HMC. Pursuant to the agreement, HMC provides to the Company premium billing, claims management and underwriting functions. During 2007 and 2006, expenses incurred related to this agreement totaled \$6,967,680 and \$12,994,250, respectively. At December 31, 2007 and 2006, the Company has a net payable due to HMC in the amount of \$295,464 and \$1,489,850, respectively.

Effective December 5, 2005, the Company entered into a service agreement with HHI. Pursuant to the agreement, HHI provides to the Company capital management services, investor management and relations, and assists with overall general management of the Company. During 2007 and 2006, expenses incurred related to this agreement totaled \$214,370 and \$591,640, respectively. At December 31, 2007 and 2006, the Company has a receivable due from HHI in the amount of \$271,751 and \$40,592, respectively.

The Company is also party to a Cost Allocation Agreement with HPIC, HMC, and HHI in which expenses benefiting more than one company are allocated based upon direct allocation or revenue allocation rules, whichever is most appropriate for the expenses. At December 31, 2007 and 2006, the Company has a receivable due from HPIC in the amount of \$4,129,565 and \$7,625, respectively.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

11. Premiums Produced by Managing General Agents or Third Party Administrators

The Company uses a managing general agent, HMC, to write and administer insurance products. HMC has contracted with an unaffiliated service company to provide this function. The total premium produced and serviced through the contract during 2007 is summarized below. The Company retains underwriting authority for all policies issued under these agreements.

| <u>Name and Address</u> | <u>FEI Number</u> | <u>Exclusive Contract</u> | <u>Type of Business Written</u> | <u>Type of Authority Granted</u> | <u>Direct Premium Written</u> |
|---|-------------------|---------------------------|---------------------------------|--|-------------------------------|
| HomeWise Management Company, Inc. 18302 Highwoods Preserve Prkwy Suite 110 Tampa, FL 33647 | 20-3395152 | Yes | Wind-only | Premium collection, claims adjustment, binding authority, and underwriting | \$ 21,766,628 |

12. Lease Commitments

On September 2, 2005, the Company entered into an operating lease agreement for office space in Tallahassee, Florida, which is effective October 15, 2005, through October 31, 2008. This lease was terminated effective May 31, 2007.

On May 1, 2006, the Company also entered into an operating lease agreement for office space in Tampa, Florida, which is effective June 1, 2006, through May 31, 2011. The Company has the option to renew the term of the lease for an additional five year period at the prevailing rental rate at that time, provided the Company gives the lessor written notice nine months prior to its intent to renew the lease.

Approximate future lease payments under these operating leases are as follows at December 31, 2007:

| | |
|------|---------------------|
| 2008 | \$ 293,875 |
| 2009 | 305,844 |
| 2010 | 317,813 |
| 2011 | <u>134,500</u> |
| | <u>\$ 1,052,032</u> |

Total rent expense for the combined leases was \$266,409 and \$166,386 for the years ended December 31, 2007 and 2006, respectively.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

13. Reconciliation of Annual Statement to Audited Financial Statements

Differences exist between amounts reported in the audited statutory financial statements and those reported in the annual statement of the Company for the year ended December 31, 2007, resulting from reclassification of other assets and rounding. Presented below is a reconciliation of amounts previously reported to the Office and those amounts appearing in the audited statutory financial statements for the year ended December 31, 2007.

| | Audited Financial Statement Amount | Annual Statement Amount | Increase (Decrease) |
|---------------------------|---|--|--------------------------------|
| Total admitted assets | \$ 13,661,979 | \$ 13,635,171 | \$ 26,808 |
| Total liabilities | 3,974,579 | 3,947,773 | 26,806 |
| Total capital and surplus | 9,687,400 | 9,687,398 | 2 |
| Net income | 775,924 | 775,921 | 3 |

Other Financial Information

SUMMARY INVESTMENT SCHEDULE

| Investment Categories | Gross Investment Holdings | | Admitted Assets as Reported in the Annual Statement | |
|--|---------------------------|-----------------|---|-----------------|
| | 1 Amount | 2 Percentage | 3 Amount | 4 Percentage |
| 1. Bonds: | | | | |
| 1.1 U.S. treasury securities: | | 0.0 | | 0.0 |
| 1.2 U.S. government agency obligations (excluding mortgage-backed securities): | | | | |
| 1.21 Issued by U.S. government agencies: | | 0.0 | | 0.0 |
| 1.22 Issued by U.S. government sponsored agencies: | | 0.0 | | 0.0 |
| 1.3 Foreign government (including Canada, excluding mortgage-backed securities): | | 0.0 | | 0.0 |
| 1.4 Securities issued by states, territories and possessions and political subdivisions in the U.S.: | | | | |
| 1.41 States, territories and possessions general obligations: | | 0.0 | | 0.0 |
| 1.42 Political subdivisions of states, territories & possessions & political subdivisions general obligations: | | 0.0 | | 0.0 |
| 1.43 Revenue and assessment obligations: | | 0.0 | | 0.0 |
| 1.44 Industrial development and similar obligations: | | 0.0 | | 0.0 |
| 1.5 Mortgage-backed securities (includes residential and commercial MBS): | | | | |
| 1.51 Pass-through securities: | | | | |
| 1.511 Issued or guaranteed by GNMA: | | 0.0 | | 0.0 |
| 1.512 Issued or guaranteed by FNMA and FHLMC: | | 0.0 | | 0.0 |
| 1.513 All other: | | 0.0 | | 0.0 |
| 1.52 CMOs and REMICs: | | | | |
| 1.521 Issued or guaranteed by GNMA, FNMA, FHLMC or VA: | | 0.0 | | 0.0 |
| 1.522 Issued by non-U.S. Government issuers and collateralized by mortgage-backed securities issued or guaranteed by agencies shown in Line 1.521: | | 0.0 | | 0.0 |
| 1.523 All other: | | 0.0 | | 0.0 |
| 2. Other debt and other fixed income securities (excluding short-term): | | | | |
| 2.1 Unaffiliated domestic securities (includes credit tenant loans rated by the SVO): | | 0.0 | | 0.0 |
| 2.2 Unaffiliated foreign securities: | | 0.0 | | 0.0 |
| 2.3 Affiliated securities: | | 0.0 | | 0.0 |
| 3. Equity interests: | | | | |
| 3.1 Investments in mutual funds: | | 0.0 | | 0.0 |
| 3.2 Preferred stocks: | | | | |
| 3.21 Affiliated: | | 0.0 | | 0.0 |
| 3.22 Unaffiliated: | | 0.0 | | 0.0 |
| 3.3 Publicly traded equity securities (excluding preferred stocks): | | | | |
| 3.31 Affiliated: | | 0.0 | | 0.0 |
| 3.32 Unaffiliated: | | 0.0 | | 0.0 |
| 3.4 Other equity securities: | | | | |
| 3.41 Affiliated: | | 0.0 | | 0.0 |
| 3.42 Unaffiliated: | | 0.0 | | 0.0 |
| 3.5 Other equity interests including tangible personal property under lease: | | | | |
| 3.51 Affiliated: | | 0.0 | | 0.0 |
| 3.52 Unaffiliated: | | 0.0 | | 0.0 |
| 4. Mortgage loans: | | | | |
| 4.1 Construction and land development: | | 0.0 | | 0.0 |
| 4.2 Agricultural: | | 0.0 | | 0.0 |
| 4.3 Single family residential properties: | | 0.0 | | 0.0 |
| 4.4 Multifamily residential properties: | | 0.0 | | 0.0 |
| 4.5 Commercial loans: | | 0.0 | | 0.0 |
| 4.6 Mezzanine real estate loans: | | 0.0 | | 0.0 |
| 5. Real estate investments: | | | | |
| 5.1 Property occupied by company: | | 0.0 | | 0.0 |
| 5.2 Property held for production of income (including \$.....0 of property acquired in satisfaction of debt): | | 0.0 | | 0.0 |
| 5.3 Property held for sale (including \$.....0 property acquired in satisfaction of debt): | | 0.0 | | 0.0 |
| 6. Contract loans: | | 0.0 | | 0.0 |
| 7. Receivables for securities: | | 0.0 | | 0.0 |
| 8. Cash, cash equivalents and short-term investments: | 6,642,357 | 100.0 | 6,642,357 | 100.0 |
| 9. Other invested assets: | | 0.0 | | 0.0 |
| 10. Total invested assets: | 6,642,357 | 100.0 | 6,642,357 | 100.0 |

See report of independent auditors.



SUPPLEMENTAL INVESTMENT RISKS INTERROGATORIES

Due April 1

For the year ended December 31, 2007

Of HomeWise Insurance Company

Address (City, State, Zip Code): Tampa FL 33647

NAIC Group Code.....4111

NAIC Company Code.....12438

Employer's ID Number.....20-3395013

The Investment Risks Interrogatories are to be filed by April 1. They are also to be included with the Audited Statutory Financial Statements. Answer the following interrogatories by reporting the applicable U.S. dollar amounts and percentages of the reporting entity's total admitted assets held in that category of investments.

1. Reporting entity's total admitted assets as reported on Page 2 of this annual statement. \$.....13,635,171

2. Ten largest exposures to a single issuer/borrower/investment:

| 1 | 2 | 3 | 4 |
|--------|-------------------------|---------|-------------------------------------|
| Issuer | Description of Exposure | Amount | Percentage of Total Admitted Assets |
| 2.01 | | \$..... | 0.000 % |
| 2.02 | | \$..... | 0.000 % |
| 2.03 | | \$..... | 0.000 % |
| 2.04 | | \$..... | 0.000 % |
| 2.05 | | \$..... | 0.000 % |
| 2.06 | | \$..... | 0.000 % |
| 2.07 | | \$..... | 0.000 % |
| 2.08 | | \$..... | 0.000 % |
| 2.09 | | \$..... | 0.000 % |
| 2.10 | | \$..... | 0.000 % |

3. Amounts and percentages of the reporting entity's total admitted assets held in bonds and preferred stocks by NAIC rating.

| | 1 | 2 |
|-------------------------|---------|---------|
| <u>Bonds</u> | | |
| 3.01 NAIC-1..... | \$..... | 0.000 % |
| 3.02 NAIC-2..... | \$..... | 0.000 % |
| 3.03 NAIC-3..... | \$..... | 0.000 % |
| 3.04 NAIC-4..... | \$..... | 0.000 % |
| 3.05 NAIC-5..... | \$..... | 0.000 % |
| 3.06 NAIC-6..... | \$..... | 0.000 % |
| <u>Preferred Stocks</u> | | |
| 3.07 PRP-1..... | \$..... | 0.000 % |
| 3.08 PRP-2..... | \$..... | 0.000 % |
| 3.09 PRP-3..... | \$..... | 0.000 % |
| 3.10 PRP-4..... | \$..... | 0.000 % |
| 3.11 PRP-5..... | \$..... | 0.000 % |
| 3.12 PRP-6..... | \$..... | 0.000 % |

4. Assets held in foreign investments:

| | |
|---|----------------|
| 4.01 Are assets held in foreign investments less than 2.5% of the reporting entity's total admitted assets? | Yes [X] No [] |
| 4.02 Total admitted assets held in foreign investments | \$.....0.000 % |
| 4.03 Foreign-currency-denominated investments | \$.....0.000 % |
| 4.04 Insurance liabilities denominated in that same foreign currency | \$.....0.000 % |

If response to 4.01 above is yes, responses are not required for Interrogatories 5-10.

5. Aggregate foreign investment exposure categorized by NAIC sovereign rating:

| | 1 | 2 |
|---|---------|---------|
| 5.01 Countries rated NAIC-1..... | \$..... | 0.000 % |
| 5.02 Countries rated NAIC-2..... | \$..... | 0.000 % |
| 5.03 Countries rated NAIC-3 or below..... | \$..... | 0.000 % |

6. Two largest foreign investment exposures to a single country, categorized by the country's NAIC sovereign rating:

| | 1 | 2 |
|----------------------------------|---------|---------|
| Countries rated NAIC-1: | | |
| 6.01 Country: | \$..... | 0.000 % |
| 6.02 Country: | \$..... | 0.000 % |
| Countries rated NAIC-2: | | |
| 6.03 Country: | \$..... | 0.000 % |
| 6.04 Country: | \$..... | 0.000 % |
| Countries rated NAIC-3 or below: | | |
| 6.05 Country: | \$..... | 0.000 % |
| 6.06 Country: | \$..... | 0.000 % |

7. Aggregate unbudgeted foreign currency exposure:

See report of independent auditors.

B. Aggregate unhedged foreign currency exposure categorized by NAIC sovereign rating:

| | | |
|---------------------------------------|----|---------|
| B.01 Countries rated NAIC-1: | \$ | 0.000 % |
| B.02 Countries rated NAIC-2: | \$ | 0.000 % |
| B.03 Countries rated NAIC-3 or below: | \$ | 0.000 % |

C. Two largest unhedged foreign currency exposures to a single country, categorized by the country's NAIC sovereign rating:

| | 1 | 2 |
|----------------------------------|----|---------|
| Countries rated NAIC-1: | | |
| C.01 Country: | \$ | 0.000 % |
| C.02 Country: | \$ | 0.000 % |
| Countries rated NAIC-2: | | |
| C.03 Country: | \$ | 0.000 % |
| C.04 Country: | \$ | 0.000 % |
| Countries rated NAIC-3 or below: | | |
| C.05 Country: | \$ | 0.000 % |
| C.06 Country: | \$ | 0.000 % |

10. Ten largest non-sovereign (i.e. non-governmental) foreign issues:

| | 1 Issuer | 2 NAIC Rating | 3 | 4 |
|-------|-------------|------------------|----|---------|
| 10.01 | | | \$ | 0.000 % |
| 10.02 | | | \$ | 0.000 % |
| 10.03 | | | \$ | 0.000 % |
| 10.04 | | | \$ | 0.000 % |
| 10.05 | | | \$ | 0.000 % |
| 10.06 | | | \$ | 0.000 % |
| 10.07 | | | \$ | 0.000 % |
| 10.08 | | | \$ | 0.000 % |
| 10.09 | | | \$ | 0.000 % |
| 10.10 | | | \$ | 0.000 % |

11. Amounts and percentages of the reporting entity's total admitted assets held in Canadian investments and unhedged Canadian currency exposure:

| | |
|---|----------------|
| 11.01 Are assets held in Canadian investments less than 2.5% of the reporting entity's total admitted assets? | Yes [X] No [] |
| If response to 11.01 is yes, detail is not required for the remainder of Interrogatory 11. | |
| 11.02 Total admitted assets held in Canadian Investments | \$ 0.000 % |
| 11.03 Canadian currency-denominated investments | \$ 0.000 % |
| 11.04 Canadian-denominated insurance liabilities | \$ 0.000 % |
| 11.05 Unhedged Canadian currency exposure | \$ 0.000 % |

12. Report aggregate amounts and percentages of the reporting entity's total admitted assets held in investments with contractual sales restrictions.

| | |
|--|----------------|
| 12.01 Are assets held in investments with contractual sales restrictions less than 2.5% of the reporting entity's total admitted assets? | Yes [X] No [] |
| If response to 12.01 is yes, responses are not required for the remainder of Interrogatory 12. | |
| 12.02 Aggregate statement value of investments with contractual sales restrictions: | \$ 0.000 % |
| Largest 3 investments with contractual sales restrictions: | |
| 12.03 | \$ 0.000 % |
| 12.04 | \$ 0.000 % |
| 12.05 | \$ 0.000 % |

13. Amounts and percentages of admitted assets held in the largest 10 equity interests:

| | | | |
|--|--|----|----------------|
| 13.01 | Are assets held in equity interest less than 2.5% of the reporting entity's total admitted assets? | | Yes [X] No [] |
| If response to 13.01 above is yes, responses are not required for the remainder of Interrogatory 13. | | | |
| | 1 | 2 | 3 |
| | Name of Issuer | | |
| 13.02 | | \$ | 0.000 % |
| 13.03 | | \$ | 0.000 % |
| 13.04 | | \$ | 0.000 % |
| 13.05 | | \$ | 0.000 % |
| 13.06 | | \$ | 0.000 % |
| 13.07 | | \$ | 0.000 % |
| 13.08 | | \$ | 0.000 % |
| 13.09 | | \$ | 0.000 % |
| 13.10 | | \$ | 0.000 % |
| 13.11 | | \$ | 0.000 % |

14. Amounts and percentages of the reporting entity's total admitted assets held in nonaffiliated, privately placed equities:

14.01 Are assets held in nonaffiliated, privately placed equities less than 2.5% of the reporting entity's total admitted assets?

Yes [X] No []

If response to 14.01 above is yes, responses are not required for the remainder of Interrogatory 14.

| 1 | 2 | 3 |
|--|----|---------|
| 14.02 Aggregate statement value of investments held in nonaffiliated, privately placed equities: | \$ | 0.000 % |
| Largest 3 investments held in nonaffiliated, privately placed equities: | | |
| 14.03 | \$ | 0.000 % |
| 14.04 | \$ | 0.000 % |
| 14.05 | \$ | 0.000 % |

15. Amounts and percentages of the reporting entity's total admitted assets held in general partnership interests:

15.01 Are assets held in general partnership interests less than 2.5% of the reporting entity's total admitted assets?

Yes [X] No []

If response to 15.01 above is yes, responses are not required for the remainder of Interrogatory 15.

| 1 | 2 | 3 |
|---|----|---------|
| 15.02 Aggregate statement value of investments held in general partnership interests: | \$ | 0.000 % |
| Largest 3 investments in general partnership interests: | | |
| 15.03 | \$ | 0.000 % |
| 15.04 | \$ | 0.000 % |
| 15.05 | \$ | 0.000 % |

16. Amounts and percentages of the reporting entity's total admitted assets held in mortgage loans:

16.01 Are mortgage loans reported in Schedule B less than 2.5% of the reporting entity's total admitted assets?

Yes [X] No []

If response to 16.01 above is yes, responses are not required for the remainder of Interrogatory 16 and Interrogatory 17.

| 1 | 2 | 3 |
|--|----|---------|
| Type (Residential, Commercial, Agricultural) | | |
| 16.02 | \$ | 0.000 % |
| 16.03 | \$ | 0.000 % |
| 16.04 | \$ | 0.000 % |
| 16.05 | \$ | 0.000 % |
| 16.06 | \$ | 0.000 % |
| 16.07 | \$ | 0.000 % |
| 16.08 | \$ | 0.000 % |
| 16.09 | \$ | 0.000 % |
| 16.10 | \$ | 0.000 % |
| 16.11 | \$ | 0.000 % |

Amount and percentage of the reporting entity's total admitted assets held in the following categories of mortgage loans:

| | Loans |
|--|------------|
| 16.12 Construction loans | \$ 0.000 % |
| 16.13 Mortgage loans over 90 days past due | \$ 0.000 % |
| 16.14 Mortgage loans in the process of foreclosure | \$ 0.000 % |
| 16.15 Mortgage loans foreclosed | \$ 0.000 % |
| 16.16 Restructured mortgage loans | \$ 0.000 % |

17. Aggregate mortgage loans having the following loan-to-value ratios as determined from the most current appraisal as of the annual statement date:

| Loan-to-Value | 1 | 2 | 3 | 4 | 5 | 6 |
|------------------|-------------|------------|------------|------------|--------------|------------|
| | Residential | | Commercial | | Agricultural | |
| 17.01 above 95% | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % |
| 17.02 91% to 95% | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % |
| 17.03 81% to 90% | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % |
| 17.04 71% to 80% | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % |
| 17.05 below 70% | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % |

18. Amounts and percentages of the reporting entity's total admitted assets held in each of the five largest investments in real estate:

18.01 Are assets held in real estate reported less than 2.5% of the reporting entity's total admitted assets?

Yes [X] No []

If response to 18.01 above is yes, responses are not required for the remainder of Interrogatory 18.

Largest five investments in any one parcel or group of contiguous parcels of real estate.

| Description | 2 | 3 |
|-------------|----|---------|
| 18.02 | \$ | 0.000 % |
| 18.03 | \$ | 0.000 % |
| 18.04 | \$ | 0.000 % |
| 18.05 | \$ | 0.000 % |
| 18.06 | \$ | 0.000 % |

19. Report aggregate amounts and percentages of the reporting entity's total admitted assets held in investments in mezzanine real estate loans.

19.01 Are assets held in investments held in mezzanine real estate loans less than 2.5% of the reporting entity's admitted assets?

Yes [X] No []

If response to 19.01 is yes, responses are not required for the remainder of Interrogatory 19.

| 1 | 2 | 3 |
|--|----|---------|
| 19.02 Aggregate statement value of investments held in mezzanine real estate loans | \$ | 0.000 % |
| Largest three investments held in mezzanine real estate loans: | | |
| 19.03 | \$ | 0.000 % |
| 19.04 | \$ | 0.000 % |
| 19.05 | \$ | 0.000 % |

20. Amounts and percentages of the reporting entity's total admitted assets subject to the following types of agreements:

| | <u>At Year-End</u> | | <u>1st Qtr</u> | <u>At End of Each Quarter</u> | |
|--|--------------------|---------|----------------|-------------------------------|---------|
| | 1 | 2 | 3 | 2nd Qtr | 3rd Qtr |
| | | | | 4 | 5 |
| 20.01 Securities lending (do not include assets held as collateral for such transactions)..... | \$..... | 0.000 % | \$..... | \$..... | \$..... |
| 20.02 Repurchase agreements..... | \$..... | 0.000 % | \$..... | \$..... | \$..... |
| 20.03 Reverse repurchase agreements..... | \$..... | 0.000 % | \$..... | \$..... | \$..... |
| 20.04 Dollar repurchase agreements..... | \$..... | 0.000 % | \$..... | \$..... | \$..... |
| 20.05 Dollar reverse repurchase agreements..... | \$..... | 0.000 % | \$..... | \$..... | \$..... |

21. Amounts and percentages indicated below for warrants not attached to other financial instruments, options, caps and floors:

| | <u>Owned</u> | | <u>Written</u> | |
|------------------------------|--------------|---------|----------------|---------|
| | 1 | 2 | 3 | 4 |
| 21.01 Hedging..... | \$..... | 0.000 % | \$..... | 0.000 % |
| 21.02 Income generation..... | \$..... | 0.000 % | \$..... | 0.000 % |
| 21.03 Other..... | \$..... | 0.000 % | \$..... | 0.000 % |

22. Amounts and percentages of the reporting entity's total admitted assets of potential exposure for collars, swaps, and forwards:

| | <u>At Year-End</u> | | <u>1st Qtr</u> | <u>At End of Each Quarter</u> | |
|------------------------------|--------------------|---------|----------------|-------------------------------|---------|
| | 1 | 2 | 3 | 2nd Qtr | 3rd Qtr |
| | | | | 4 | 5 |
| 22.01 Hedging..... | \$..... | 0.000 % | \$..... | \$..... | \$..... |
| 22.02 Income generation..... | \$..... | 0.000 % | \$..... | \$..... | \$..... |
| 22.03 Replications..... | \$..... | 0.000 % | \$..... | \$..... | \$..... |
| 22.04 Other..... | \$..... | 0.000 % | \$..... | \$..... | \$..... |

23. Amounts and percentages of the reporting entity's total admitted assets of potential exposure for futures contracts:

| | <u>At Year-End</u> | | <u>1st Qtr</u> | <u>At End of Each Quarter</u> | |
|------------------------------|--------------------|---------|----------------|-------------------------------|---------|
| | 1 | 2 | 3 | 2nd Qtr | 3rd Qtr |
| | | | | 4 | 5 |
| 23.01 Hedging..... | \$..... | 0.000 % | \$..... | \$..... | \$..... |
| 23.02 Income generation..... | \$..... | 0.000 % | \$..... | \$..... | \$..... |
| 23.03 Replications..... | \$..... | 0.000 % | \$..... | \$..... | \$..... |
| 23.04 Other..... | \$..... | 0.000 % | \$..... | \$..... | \$..... |

HomeWise Insurance Company

Selected General Interrogatories Relating to Reinsurance

December 31, 2007

- 7.1 Has the reporting entity reinsured any risk with any other entity under a quota share reinsurance contract that includes a provision that would limit the reinsurer's losses below the stated quota share percentage (e.g., a deductible, a loss ratio corridor, a loss cap, an aggregate limit or any similar provisions)? Yes ☒ No ☐
- 7.2 If yes, indicate the number of reinsurance contracts containing such provisions. 1
- 7.3 If yes, does the amount of reinsurance credit taken reflect the reduction in quota share coverage caused by any applicable limiting provision(s)? Yes ☒ No ☐
- 9.1 Has the reporting entity ceded any risk under any reinsurance contract (or under multiple contracts with the same reinsurer or its affiliates) for which during the period covered by the statement: (i) it recorded a positive or negative underwriting result greater than 3% of prior year-end surplus as regards policyholders or it reported calendar year written premium ceded or year-end loss and loss expense reserves ceded greater than 3% of prior year-end surplus as regards policyholders; (ii) it accounted for that contract as reinsurance and not as a deposit; and (iii) the contract(s) contain one or more of the following features or other features that would have similar results:
- (a) A contract term longer than two years and the contract is noncancellable by the reporting entity during the contract term;
 - (b) A limited or conditional cancellation provision under which cancellation triggers an obligation by the reporting entity, or an affiliate of the reporting entity, to enter into a new reinsurance contract with the reinsurer, or an affiliate of the reinsurer;
 - (c) Aggregate stop loss reinsurance coverage;
 - (d) An unconditional or unilateral right by either party to commute the reinsurance contract except for such provisions which are only triggered by a decline in the credit status of the other party;
 - (e) A provision permitting reporting of losses, or payment of losses, less frequently than on a quarterly basis (unless there is no activity during the period); or
 - (f) Payment schedule, accumulating retentions from multiple years or any feature inherently designed to delay timing of the reimbursement to the ceding entity. Yes ☐ No ☒
- 9.2 Has the reporting entity during the period covered by the statement ceded any risk under any reinsurance contract (or under multiple contracts with the same reinsurer or its affiliates), excluding cessions to approved pooling agreements or to captive insurance companies that are directly or indirectly controlling, controlled by, or under common control with (i) one or more unaffiliated policyholders of the reporting entity, or (ii) an association of which one or more unaffiliated policyholders of the reporting entity is a member, where:
- (a) The written premium ceded to the reinsurer by the reporting entity or its affiliates represents fifty percent (50%) or more of the entire direct and assumed premium written by the reinsurer based on its most recently available financial statement; or
 - (b) Twenty-five percent (25%) or more of the written premium ceded to the reinsurer has been retroceded back to the reporting entity or its affiliates. Yes ☐ No ☒

See report of independent auditors.

HomeWise Insurance Company


Selected General Interrogatories Relating to Reinsurance (continued)

- 9.3 If yes to 9.1 or 9.2, please provide the following information in the Reinsurance Summary Supplemental Filing for General Interrogatory 9:
- (a) The aggregate financial statement impact gross of all such ceded reinsurance contracts on the balance sheet and statement of income;
 - (b) A summary of the reinsurance contract terms and indicate whether it applies to the contracts meeting the criteria in 9.1 or 9.2; and
 - (c) A brief discussion of management's principle objectives in entering into the reinsurance contract including the economic purpose to be achieved.
- 9.4 Except for transactions meeting the requirements of paragraph 30 of SSAP No. 62, *Property and Casualty Reinsurance*, has the reporting entity ceded any risk under reinsurance contract (or multiple contracts with the same reinsurer or its affiliates) during the period covered by the financial statement, and either:
- (a) Accounted for that contract as reinsurance (either prospective or retroactive) under statutory accounting principles (SAP) and as a deposit under generally accepted accounting principles (GAAP); or
 - (b) Accounted for that contract as reinsurance under GAAP and as a deposit under SAP?.....Yes ☐ No ☒
- 9.5 If yes to 9.4, explain in the Reinsurance Summary Supplemental Filing for General Interrogatory 9 (Section D) why the contract(s) is treated different for GAAP and SAP.

Statutory Basis Financial Statements
and Other Financial Information

HomeWise Insurance Company

*Years ended December 31, 2008 and 2007
with Report of Independent Auditors*

Thomas Howell
 Ferguson P.A.

HomeWise Insurance Company
Statutory Basis Financial Statements
and Other Financial Information
Years ended December 31, 2008 and 2007

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Report of Independent Auditors

The Board of Directors
HomeWise Insurance Company

We have audited the accompanying statements of admitted assets, liabilities and capital and surplus - statutory basis of HomeWise Insurance Company (the Company) as of December 31, 2008 and 2007, and the related statutory basis statements of operations, changes in capital and surplus, and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As described in Note 1, the accompanying statutory basis financial statements have been prepared in conformity with accounting practices prescribed or permitted by the Florida Office of Insurance Regulation, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the admitted assets, liabilities and capital and surplus of HomeWise Insurance Company as of December 31, 2008 and 2007, and the results of its operations and its cash flows for the years then ended on the basis of accounting described in Note 1.

Thomas Howell
▲ Ferguson P.A.

Page Two

Our audits were made for the purpose of forming an opinion on the statutory basis financial statements taken as a whole. The supplemental disclosures included in other financial information as of and for the year ended December 31, 2008, are presented to comply with the National Association of Insurance Commissioners' *Accounting Practices and Procedures Manual* and are not a required part of the statutory basis financial statements. This other financial information has been subjected to the auditing procedures applied in the audits of the statutory basis financial statements and, in our opinion, is fairly stated in all material respects in relation to the statutory basis financial statements taken as a whole.

This report is intended solely for the use of the Board of Directors and management of HomeWise Insurance Company and for filing with the state insurance regulatory authorities and should not be used for any other purpose.

Thomas Howell Ferguson P.A.

May 13, 2009

HomeWise Insurance Company

Statements of Admitted Assets, Liabilities and Capital and Surplus - Statutory Basis

| | December 31, | |
|--|---------------|---------------|
| | 2008 | 2007 |
| Admitted assets | | |
| Cash and invested assets: | | |
| Short-term investments | \$ 2,231,467 | \$ 2,166,986 |
| Cash and cash equivalents | 3,814,707 | 4,475,371 |
| Total cash and invested assets | 6,046,174 | 6,642,357 |
| Accrued investment income | 7,762 | 13,866 |
| Premiums receivable | 839,085 | 969,600 |
| Reinsurance balances recoverable | 1,406,688 | 4,288 |
| Federal income taxes recoverable | 1,629,206 | 660,278 |
| Net deferred tax asset | - | 24,658 |
| Electronic data processing equipment, net | 220,633 | 111,750 |
| Receivables from parent and affiliates | 3,972,670 | 4,401,316 |
| Other assets | 520,757 | 833,866 |
| Total admitted assets | \$ 14,642,975 | \$ 13,661,979 |
| Liabilities and capital and surplus | | |
| Liabilities: | | |
| Loss and loss adjustment expense reserves | \$ 210,649 | \$ 70,190 |
| Unearned premiums, net | 1,210,680 | 1,358,639 |
| Reinsurance premiums payable | 1,228,276 | 1,390,154 |
| Accounts payable and accrued expenses | 334,535 | 326,956 |
| Payable to affiliates | 3,263,021 | 295,464 |
| Payable to Citizens Property Insurance Corporation | - | 533,176 |
| Total liabilities | 6,247,161 | 3,974,579 |
| Capital and surplus | 8,395,814 | 9,687,400 |
| Total liabilities and capital and surplus | \$ 14,642,975 | \$ 13,661,979 |

See accompanying notes.

HomeWise Insurance Company
Statements of Operations - Statutory Basis

| | Years ended December 31, | |
|---|------------------------------|--------------------------|
| | 2008 | 2007 |
| Underwriting income: | | |
| Premiums earned, net of reinsurance ceded | \$ 1,362,358 | \$ 2,651,949 |
| Underwriting expenses: | | |
| Losses and loss adjustment expenses incurred | 243,595 | (14,429) |
| Underwriting, acquisition, and other expenses incurred | 3,242,916 | 2,232,468 |
| Total underwriting expenses | <u>3,486,511</u> | <u>2,218,039</u> |
| Net underwriting (loss) gain | (2,124,153) | 433,910 |
| Net investment income | 107,349 | 529,899 |
| Other income (expense) | 4,561 | (4,461) |
| (Loss) income before federal income tax (benefit) expense | <u>(2,012,243)</u> | 959,348 |
| Federal income tax (benefit) expense | <u>(968,927)</u> | 183,424 |
| Net (loss) income | <u><u>\$ (1,043,316)</u></u> | <u><u>\$ 775,924</u></u> |

See accompanying notes.

HomeWise Insurance Company

Statements of Changes in Capital and Surplus - Statutory Basis

Years ended December 31, 2008 and 2007

| | Common Stock | | Gross Paid-in and Contributed Surplus | | |
|---------------------------------|--------------|------------|--|---------------------|--------------|
| | Shares | Par Value | | Unassigned Funds | Total |
| Balance as of December 31, 2006 | 100,000 | \$ 100,000 | \$ 9,400,000 | \$ (347,645) | \$ 9,152,355 |
| Issuance of common stock | 550,000 | 550,000 | (550,000) | - | - |
| Change in deferred income taxes | - | - | - | (158,354) | (158,354) |
| Change in nonadmitted assets | - | - | - | (82,525) | (82,525) |
| Net income | - | - | - | 775,924 | 775,924 |
| Balance as of December 31, 2007 | 650,000 | 650,000 | 8,850,000 | 187,400 | 9,687,400 |
| Change in deferred income taxes | - | - | - | 42,148 | 42,148 |
| Change in nonadmitted assets | - | - | - | (290,418) | (290,418) |
| Net loss | - | - | - | (1,043,316) | (1,043,316) |
| Balance as of December 31, 2008 | 650,000 | \$ 650,000 | \$ 8,850,000 | \$ (1,104,186) | \$ 8,395,814 |

See accompanying notes.

HomeWise Insurance Company
Statements of Cash Flows - Statutory Basis

| | Years ended December 31, | |
|---|----------------------------|----------------------------|
| | 2008 | 2007 |
| Operating activities | | |
| Premiums collected (paid), net of reinsurance | \$ 649,860 | \$ (7,870,979) |
| Net investment income received | 113,453 | 535,551 |
| Losses and loss adjustment expenses (paid) recovered | (1,505,536) | 249,693 |
| Underwriting, acquisition, and other expenses paid | (3,050,573) | (2,557,825) |
| Income taxes paid | - | (63,127) |
| Net cash used in operating activities | <u>(3,792,796)</u> | <u>(9,706,687)</u> |
| Financing and miscellaneous activities | | |
| Other miscellaneous sources (uses) | <u>3,196,613</u> | <u>(6,382,445)</u> |
| Net cash provided by (used in) financing and miscellaneous activities | <u>3,196,613</u> | <u>(6,382,445)</u> |
| Net decrease in cash | (596,183) | (16,089,132) |
| Cash at beginning of year | <u>6,642,357</u> | <u>22,731,489</u> |
| Cash at end of year | <u><u>\$ 6,046,174</u></u> | <u><u>\$ 6,642,357</u></u> |
| Cash consists of the following: | | |
| Cash and cash equivalents | \$ 3,814,707 | \$ 4,475,371 |
| Short-term investments | <u>2,231,467</u> | <u>2,166,986</u> |
| | <u><u>\$ 6,046,174</u></u> | <u><u>\$ 6,642,357</u></u> |

See accompanying notes.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

Years ended December 31, 2008 and 2007

1. Summary of Significant Accounting Policies

Organization and Description of Company

HomeWise Insurance Company (the Company), a wholly-owned subsidiary of HomeWise Holdings, Inc. (HHI), an insurance holding company, is domiciled in the state of Florida. The Company received its Certificate of Authority from the Florida Office of Insurance Regulation (the Office) on December 5, 2005, and commenced operations on January 12, 2006. The Company received a Certificate of Authority from the state of Louisiana on August 6, 2008, and commenced operations on November 25, 2008. The Company is affiliated with HomeWise Management Company (HMC) and HomeWise Preferred Insurance Company (HPIC), which are wholly-owned subsidiaries of HHI.

The Company writes coverage exclusively in the states of Florida and Louisiana, areas that are exposed to damage from hurricanes and severe storms. The Company attempts to mitigate its exposure to losses from storms by purchasing quota share and catastrophe reinsurance coverage. However, such a storm, depending on its path and severity, could result in losses to the Company exceeding its reinsurance protection and could have a material adverse effect on the financial condition and results of operations of the Company.

Basis of Presentation

The accompanying statutory basis financial statements have been prepared in accordance with statutory accounting practices (SAP) prescribed or permitted by the Florida Office of Insurance Regulation (the Office). Such statutory practices require preparation of the financial statements in accordance with the National Association of Insurance Commissioners' (NAIC) *Accounting Practices and Procedures Manual* subject to deviations prescribed by the Office. SAP is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America (GAAP). Such practices vary in certain respects from those under GAAP. The Company's significant accounting practices and the variances from GAAP are summarized below:

- Certain assets designated as "nonadmitted," principally past-due uncollected premiums, prepaid expenses, and other assets not specifically identified as an admitted asset within the *Accounting Practices and Procedures Manual*, are excluded from the accompanying statements of admitted assets, liabilities, and capital and surplus and are charged directly to unassigned surplus. Under GAAP, such assets would be included in the balance sheet at net realizable values.
- Loss and loss adjustment expense reserves and unearned premiums ceded to reinsurers have been reported as reductions of the related liabilities rather than as assets as would be required under GAAP.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

1. Summary of Significant Accounting Policies (continued)

Basis of Presentation (continued)

- Cash in the statements of cash flows represents cash, cash equivalents, and short-term investments with remaining maturities of one year or less. Under GAAP, the corresponding caption of cash and cash equivalents would include cash balances and investments with initial maturities of three months or less.
- The costs of acquiring and renewing business are expensed when incurred. Under GAAP, such costs, to the extent recoverable, would be deferred and amortized over the effective period of the related insurance policies.
- Deferred tax assets are limited to 1) the amount of federal income taxes paid in prior years that can be recovered through loss carrybacks for existing temporary differences that reverse by the end of the subsequent calendar year, plus 2) the lesser of the remaining gross deferred tax assets expected to be realized within one year of the financial statement date or 10% of capital and surplus excluding any net deferred tax assets, "electronic data processing" (EDP) equipment and operating software and any net positive goodwill, plus 3) the amount of remaining gross deferred tax assets that can be offset against existing gross deferred tax liabilities. The remaining deferred tax assets are nonadmitted. Deferred taxes do not include amounts for state income taxes. Under GAAP, state income taxes would be included in the computation of deferred taxes, a deferred tax asset would be recorded for the amount of gross deferred tax assets expected to be realized in future years, and a valuation allowance would be established for deferred tax assets not realizable.
- Commissions allowed by reinsurers on business ceded are reported as a reduction of expenses when incurred to the extent the amount does not exceed actual acquisition costs, rather than being deferred and amortized with deferred policy acquisition costs as would be required by GAAP. Commissions in excess of the acquisition costs, if any, would be deferred and recognized over the policy term consistent with GAAP.
- Certain other reported amounts are classified or presented differently in the financial statements prepared on the basis of SAP than they would be under GAAP. Statutory requirements require that the financial statements of the Company be filed with state regulatory authorities. Accordingly, the financial statements are presented in a format similar to the filed annual statement, which differs from the format of financial statements presented under GAAP. Required statutory disclosures that are not applicable to the Company are not included in the notes to these statutory financial statements.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

1. Summary of Significant Accounting Policies (continued)

Basis of Presentation (continued)

Other significant accounting practices are as follows:

Recognition of Premium Revenues

Premiums are recorded as earned on a daily pro rata basis over the contract period that the related policies are expected to be in force. The portion of premiums not earned at the end of the year is recorded as unearned premiums. Premiums collected prior to the effective date of the policy are recorded as a liability.

Cash and Cash Equivalents

Cash and cash equivalents include demand deposits with financial institutions and other highly liquid investments with original maturities of three months or less and certificates of deposit with original maturities of one year or less and are principally stated at cost, which approximates fair value.

Investments

Investments are recorded at admitted asset values as prescribed by the valuation procedures of the NAIC's Securities Valuation Office (SVO). The valuation technique used to measure fair value (market value) is to obtain the published securities' fair value from the SVO publication, Valuation of Securities. If the specific security is not listed in this publication, then the fair value is obtained from a registered U.S. exchange.

Short-term investments include investments with original maturities of one year or less from the time of acquisition and are principally stated at cost, which approximates fair value.

Concentration of Credit Risk

The Company's financial instruments exposed to concentrations of credit risk consist primarily of its cash and cash equivalents, short-term investments, reinsurance recoveries, and premium revenue. The Company maintains its cash and cash equivalents at several financial institutions. Deposits with financial institutions are insured by the Federal Deposit Insurance Corporation (FDIC). On October 3, 2008, FDIC coverage increased from \$100,000 to \$250,000 per depositor until December 31, 2009. Bank deposit accounts, at times, may exceed federally insured limits. The Company has not experienced any losses in such accounts.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

1. Summary of Significant Accounting Policies (continued)

Concentration of Credit Risk (continued)

All investment transactions have credit exposure to the extent that a counterparty may default on an obligation to the Company. Credit risk is a consequence of carrying investment positions. To manage credit risk, the Company focuses primarily on highly liquid debt instruments, reviews the credit strength of all entities in which it invests, limits its exposure in any one investment, and monitors portfolio quality, taking into account credit ratings assigned by recognized credit rating organizations.

Electronic Data Processing (EDP) Equipment

The admitted value of the Company's EDP equipment is limited to 3% of capital and surplus. The admitted portion is reported at cost, less accumulated depreciation of \$174,870 and \$83,693 at December 31, 2008 and 2007, respectively. EDP equipment is depreciated using the straight-line method over the lesser of its useful life or three years. Other furniture and equipment is recorded as a non-admitted asset and depreciated using the straight-line method over the estimated useful life of seven years. Depreciation expense charged to operations was \$157,016 and \$79,293 in 2008 and 2007, respectively.

Reinsurance

The accompanying statutory basis financial statements reflect reserves for premiums and losses and loss adjustment expenses (LAE), net of reinsurance ceded (see Note 6). Those reinsurance arrangements allow management to control exposure to potential losses arising from large risks. A significant portion of the reinsurance is effected under a quota share reinsurance agreement. Amounts recoverable from reinsurers are estimated in a manner consistent with the loss and LAE reserves associated with the reinsured policies. Reinsurance premiums, losses, and LAE are accounted for on bases consistent with those used in accounting for the original policies issued and the terms of the reinsurance contracts.

Loss and Loss Adjustment Expense (LAE) Reserves

Loss and LAE reserves represent the estimated ultimate net cost of all unpaid reported and unreported losses and LAE. The reserves for unpaid losses and LAE are estimated using individual case-basis estimates for reported losses and actuarial estimates for losses incurred but not yet reported. Those estimates are subject to the effects of trends in loss severity and frequency. Although considerable variability is inherent in such estimates, management believes that the reserves for losses and LAE are adequate. The estimates are continually reviewed and adjusted as necessary as experience develops or new information becomes known; such adjustments are included in current operations. The ultimate settlement of losses and LAE may vary significantly from the estimated amounts included in the financial statements. The Company does not discount its loss and LAE reserves.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

1. Summary of Significant Accounting Policies (continued)

Loss and Loss Adjustment Expense (LAE) Reserves (continued)

The anticipated effect of inflation is implicitly considered when estimating liabilities for losses and LAE. While anticipated price increases due to inflation are considered in estimating the ultimate claim costs, the increase in average severities of claims is caused by a number of factors that vary with the individual type of policy written. Future average severities are projected based on historical trends adjusted for implemented changes in underwriting standards, policy provisions, and general economic trends. Those anticipated trends are monitored based on actual development and the estimated liabilities are modified if necessary.

Loss and LAE reserves are reported net of reinsurance recoverables for unpaid losses and LAE. Losses and LAE ceded through reinsurance are credited against losses and LAE incurred.

Guaranty Fund and Residual Market Pool Assessments

The Company is subject to assessments by a Florida guaranty fund, a residual market pool, and a state catastrophe reinsurance pool. The activities of this fund and these pools include collecting funds from solvent insurance companies to cover losses resulting from the insolvency or rehabilitation of other insurance companies or deficits generated by Florida Insurance Guaranty Association (FIGA), Citizens Property Insurance Corporation (Citizens), and the Florida Hurricane Catastrophe Fund (FHCF).

The Company's policy is to recognize its obligation for FIGA, Citizens, and FHCF assessments when the Company has the information available to reasonably estimate its liabilities. FIGA, Citizens, and FHCF assessments are generally available for recoupment from policyholders and as such, amounts are recorded as a recoverable asset. Amounts recoverable are generally expected to be collected during the year following assessment.

The Company was assessed \$755,526 by FIGA in 2007 (none in 2008). The FIGA assessment recoverable from policyholders was \$227,145 and \$755,526 at December 31, 2008 and 2007, respectively.

Certain Citizens and FHCF assessments are collected from policyholders as policies are written and subsequently remitted to the assessing entity. Amounts due from policyholders for these assessments were \$17,692 and \$81,082 at December 31, 2008 and 2007, respectively. The liability for assessments collected but not remitted to Citizens and FHCF totaled \$62,611 and \$55,773 at December 31, 2008 and 2007, respectively.

Income Taxes

The Company calculates its state and federal income tax liabilities based upon the statutory rates in effect during the year.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

1. Summary of Significant Accounting Policies (continued)

Use of Estimates

The preparation of statutory basis financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the statutory basis financial statements, and the reported amounts of revenues and expenses during the reporting period. Such estimates and assumptions could change in the future as more information becomes known, which could impact the amounts reported and described in the financial statements.

2. Regulatory Requirements and Restrictions

Florida Statutes Section 624.408 requires the Company to maintain minimum capital and surplus of \$4 million and to meet the risk-based capital requirements (see Note 8). Additionally, Florida Statutes Section 624.4095 requires the Company to maintain a ratio of the product of written premiums times 0.90 to surplus of no greater than 10-to-1 for gross written premiums and 4-to-1 for net written premiums. The Company is in compliance with these requirements.

Additionally, the Company is required to maintain deposits pursuant to Florida and Louisiana statutes to help secure the payment of claims. Cash on deposit in the amount of \$342,595 and \$326,483 has been assigned to the Office as of December 31, 2008 and 2007, respectively, and a certificate of deposit in the amount of \$100,000 has been assigned to the Louisiana Department of Insurance as of December 31, 2008 (none at December 31, 2007), to satisfy this requirement. These amounts are included in cash and cash equivalents in the accompanying statements of admitted assets, liabilities, and capital and surplus at December 31, 2008 and 2007.

3. Investments

Short-term investments consist of U.S. Government money market funds that have a maturity of one year or less from the date of purchase and are stated at cost, which approximates fair value.

Major categories of the Company's net investment income are summarized as follows:

| | Years ended December 31, | |
|---------------------------|--------------------------|-------------------|
| | 2008 | 2007 |
| Investment income: | | |
| Cash and cash equivalents | \$ 76,351 | \$ 439,564 |
| Short-term investments | <u>64,787</u> | <u>109,604</u> |
| | 141,138 | 549,168 |
| Investment expense: | | |
| Bank fees | <u>(33,789)</u> | <u>(19,269)</u> |
| Net investment income | <u>\$ 107,349</u> | <u>\$ 529,899</u> |

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

4. Premiums Receivable

Premiums receivable includes amounts due from HomeWise Management Company, the Company's managing general agent (MGA), who collects all premiums and remits them to the Company. The Company nonadmits balances due from insureds and deferred installments for which a portion of the receivable is more than 90 days past due and exceeds the related unearned premium. Premiums receivable is charged to bad debt expense in the period determined uncollectible. Recoveries received on amounts previously charged-off are credited to bad debt expense in the period received. Premiums receivable totaled \$839,085 and \$969,600, with no nonadmitted premiums receivable, as of December 31, 2008 and 2007, respectively.

5. Loss and Loss Adjustment Expense (LAE) Reserves

The following table provides a reconciliation of the beginning and ending reserve balances for losses and LAE, net of reinsurance recoverables.

| | December 31, | |
|--|-----------------------|--------------|
| | 2008 | 2007 |
| | <i>(in thousands)</i> | |
| Loss and LAE reserves at beginning of year | \$ 70 | \$ 81 |
| Losses and LAE incurred related to: | | |
| Current year | 263 | 67 |
| Prior years | <u>(19)</u> | <u>(81)</u> |
| | 244 | (14) |
| Losses and LAE paid related to: | | |
| Current year | 174 | 36 |
| Prior years | <u>(71)</u> | <u>(39)</u> |
| | <u>103</u> | <u>(3)</u> |
| Loss and LAE reserves at end of year | <u>\$ 211</u> | <u>\$ 70</u> |

Anticipated reinsurance recoverables on unpaid losses and LAE are approximately \$162,000 and \$94,000 at December 31, 2008 and 2007, respectively. Reinsurance recoverables on paid losses and LAE are approximately \$135,000 and \$4,000 at December 31, 2008 and 2007, respectively.

In 2008 and 2007, net incurred losses and LAE attributable to insured events of prior years have decreased by \$19,000 and \$81,000, respectively, as a result of reestimation of unpaid losses and loss adjustment expenses. Original estimates are decreased or increased as additional information becomes known regarding individual claims.

6. Reinsurance

Certain premiums and benefits are ceded to other insurance companies under various reinsurance agreements. The reinsurance agreements provide the Company with increased capacity to write more risk and maintain its exposure to loss within its capital resources. As of December 31, 2008 and 2007, the Company's reinsurance program consisted of quota share and excess of loss reinsurance for catastrophic events. Following is a summary of the reinsurance coverage.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

6. Reinsurance (continued)

Effective June 1, 2008, the Company and its affiliated company, HomeWise Preferred Insurance Company (collectively, the Reinsured), entered into a quota share reinsurance agreement with Swiss Reinsurance America Corporation (the Reinsurer). Under the terms of the agreement, which expires on May 31, 2009, the Reinsurer assumes 75% of the Reinsured's net liabilities for losses (loss and loss adjustment expense) after taking into effect the Reinsured's excess of loss reinsurance coverage provided by the FHCF and the first layer of the commercial excess of loss. Under the terms of the agreement, the Reinsured cedes 75% of gross premiums after deducting the cost of the above referenced inuring reinsurance to the Reinsurer. The Reinsured cedes 75% of covered gross losses to the Reinsurer after deducting recoveries from the referenced inuring reinsurance. The maximum losses ceded under this agreement are limited to \$150 million per event and \$210 million for all occurrences. The Company and the Reinsurer entered into an aggregate excess of loss agreement to reinsure the Reinsurer's catastrophe obligation under the quota share agreement. The Reinsurer reimburses the Company for the premiums relating to this coverage. The ceding commission from the Reinsurer to the Reinsured is on a reimbursement basis wherein the Reinsurer reimburses the Reinsured for 75% of acquisition and overhead expenses limited to 31%. The ceding commissions have been recorded as a reduction of underwriting, acquisition, and other expenses in the accompanying statements of operations.

Effective January 1, 2007, the Company and its affiliated company, HomeWise Preferred Insurance Company (collectively, the Reinsured), entered into a quota share reinsurance agreement with Harlequin Insurance (Bermuda) SAC Limited (the Reinsurer or Harlequin). Under the terms of the agreement, which expired on May 31, 2008, the Reinsurer assumed 75% of the Reinsured's net liabilities for losses (loss and loss adjustment expense) after taking into effect the Reinsured's excess of loss reinsurance coverage provided by the FHCF and, through May 31, 2007, the coverage provided by open market excess of loss reinsurance purchased by the Reinsured. Under the terms of the agreement, the Reinsured ceded 75% of gross premiums after deducting the cost of the above referenced inuring reinsurance to the Reinsurer. The Reinsured ceded 75% of covered gross losses to the Reinsurer after deducting recoveries from the referenced inuring reinsurance. The agreement included an Event Cap for ceded losses of 44% of the ceded premium earned during the term. It also included an Aggregate Loss and Expense Ratio Cap where in the maximum amount of losses and ceding commissions payable by the Reinsurer under this agreement in the aggregate shall be limited to 150% of the ceded premium earned during the term. In the event either cap is met, the Reinsured shares in recoveries in proportion to their respective subject losses to the total of losses subject to the agreement. The ceding commission from the Reinsurer to the Reinsured is on a reimbursement basis wherein the Reinsurer reimburses the Reinsured for 75% of acquisition and overhead expenses. The ceding commissions have been recorded as a reduction of underwriting, acquisition, and other expenses in the accompanying statements of operations. Effective May 31, 2008, this agreement terminated and was subsequently commuted. There was no gain or loss recorded from the commutation, however, there was a final adjustment to ceding commissions as prescribed by the agreement.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

6. Reinsurance (continued)

The catastrophe excess of loss coverage is provided by agreements with commercial reinsurers and by the FHCF. Coverage under the FHCF is limited to qualifying storms occurring in the state of Florida. For the year ended December 31, 2008, the commercial excess of loss treaties generally provide 100% coverage on ultimate net losses of approximately \$9,300,000 in excess of \$2,900,000 and 25% coverage on ultimate net losses of approximately \$12,700,000 in excess of approximately \$12,200,000 per occurrence, not to exceed approximately \$12,500,000 for all occurrences. The FHCF provided coverage for 90% of the losses from qualifying catastrophic events in excess of approximately \$12,200,000 up to a maximum of approximately \$72,900,000. For the year ended December 31, 2007, the commercial excess of loss treaties generally provide coverage on ultimate net losses of approximately \$14,100,000 in excess of \$12,800,000 per occurrence, not to exceed approximately \$28,100,000 for all occurrences. The FHCF provided coverage for 90% of the losses from qualifying catastrophic events in excess of approximately \$19,700,000 up to a maximum of approximately \$123,100,000, plus 100% of \$10,000,000 in excess of \$2,700,000 (drop down layer).

The FHCF provides coverage for named hurricanes only and provides no coverage after the one time limit is exhausted. Reinsurance premiums for the FHCF are paid on a total insured value basis. In the event of a loss assessment, the Company may recoup the assessments from its policyholders.

Effective June 1, 2008 and 2007, the Company executed reinsurance premium protection agreements to reinsure the reinstatement premium payment obligations which accrue to the Company under the private catastrophe excess of loss agreements. The coverage is limited to 100% of the original contracted reinsurance placement.

The Company's reinsured risks are treated, to the extent of the reinsurance, as though they are risks for which the Company is not liable. However, the Company remains liable in the event the reinsuring companies do not meet their obligations under these reinsurance agreements. Given the quality of the reinsuring companies, management believes this possibility to be remote. See Note 5 for recoveries due from reinsurers relating to paid and unpaid losses and LAE.

On May 31, 2007, the Company terminated and commuted its excess of loss reinsurance agreement with Catlin Insurance Company Ltd. There were no losses assumed or gain or loss recognized on the commutation. Per the agreement, the Company was owed the amount in the experience account that was established under the original reinsurance agreement. That amount, calculated pursuant to the agreements, was \$822,000. The experience account balance was reduced by a commutation settlement charge of \$360,000. The net settlement amount of \$522,000 was received by the Company on July 22, 2007.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

6. Reinsurance (continued)

The Company terminated and commuted its quota share reinsurance agreement with Glacier Reinsurance AG on January 1, 2007. As a result of the commutation, \$7,989,164 in unearned premium was returned to the Company and \$6,833,689 in ceding commission was returned to Glacier Reinsurance AG. The cession of any future losses at January 1, 2007 and forward was also terminated. The Company also increased its ceded loss and loss adjustment paid and reduced its ceded reserves to recognize the effect of releasing the insurer from its obligation under the treaty. The net effect of the commutation was an increase in losses incurred of \$210,623. The reinsurance agreement with Glacier Reinsurance AG was replaced with a 75% quota share agreement with Harlequin Insurance (Bermuda) SAC Limited effective January 1, 2007.

The effects of reinsurance on premiums written and earned at December 31 are as follows:

| | 2008 | | 2007 | |
|------------------|---------------------|---------------------|---------------------|---------------------|
| | <u>Written</u> | <u>Earned</u> | <u>Written</u> | <u>Earned</u> |
| Direct premiums | \$ 11,943,311 | \$ 16,941,545 | \$ 21,766,628 | \$ 33,475,449 |
| Assumed premiums | - | - | (2,343) | 375,374 |
| Ceded premiums | <u>(10,728,913)</u> | <u>(15,579,187)</u> | <u>(20,416,752)</u> | <u>(31,198,874)</u> |
| Net premiums | <u>\$ 1,214,398</u> | <u>\$ 1,362,358</u> | <u>\$ 1,347,533</u> | <u>\$ 2,651,949</u> |

The following table summarizes the effect of ceded unearned premiums on the direct unearned premiums reserve and the related commission equity at December 31:

| | <u>2008</u> | <u>2007</u> |
|--------------------------|-----------------------|-----------------------|
| Direct unearned premiums | \$ 7,210,289 | \$ 12,208,521 |
| Ceded unearned premiums | <u>(5,999,609)</u> | <u>(10,849,882)</u> |
| Unearned premiums, net | <u>\$ 1,210,680</u> | <u>\$ 1,358,639</u> |
| Commission equity, net | <u>\$ (1,676,392)</u> | <u>\$ (3,227,628)</u> |

At December 31, 2008 and 2007, unsecured reinsurance recoverables on paid and unpaid losses and LAE and unearned premiums by reinsurers that were equal to or greater than 3% of surplus, is as follows:

| | <u>2008</u> | <u>2007</u> |
|---------------------------------------|--------------|-------------|
| Swiss Reinsurance America Corporation | \$ 3,502,000 | \$ - |
| Florida Hurricane Catastrophe Fund | 979,000 | 3,737,000 |

For the years ended December 31, 2008 and 2007, recoveries under reinsurance contracts totaled \$282,554 and \$518,929, respectively.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

7. Income Taxes

Income before federal income taxes differs from taxable income principally due to differences in loss and LAE reserves and unearned premiums for tax and statutory basis financial reporting purposes.

State income taxes are classified as taxes, licenses, and fees in the NAIC Annual Statement and as underwriting, acquisition, and other expenses on the statements of operations.

A. Components of deferred tax assets (DTAs) and deferred tax liabilities (DTLs) are as follows:

| | December 31, | |
|---|---------------------|--------------------|
| | 2008 | 2007 |
| Gross DTAs | \$ 252,727 | \$ 182,436 |
| Gross DTLs | <u>(185,921)</u> | <u>(157,778)</u> |
| Net admitted DTAs | 66,806 | 24,658 |
| Nonadmitted DTAs | <u>(66,806)</u> | <u>-</u> |
| Net admitted DTAs | <u>\$ -</u> | <u>\$ 24,658</u> |
| | | |
| Increase (decrease) in nonadmitted DTAs | <u>\$ 66,806</u> | <u>\$ (34,581)</u> |

B. Unrecognized DTLs

There are no unrecognized DTLs.

C. Current tax and change in deferred tax:

The provision for income taxes incurred is:

| | Years ended December 31, | |
|---|---------------------------------|-------------------|
| | 2008 | 2007 |
| Current year income tax (benefit) expense | \$ (866,185) | \$ 120,253 |
| Prior year (over) under accrual | <u>(102,742)</u> | <u>63,171</u> |
| Current income taxes incurred | <u>\$ (968,927)</u> | <u>\$ 183,424</u> |

The tax effect of temporary differences at December 31, 2008 that give rise to significant deferred tax assets and deferred tax liabilities are as follows:

| DTAs | Statutory | Tax | Difference | Tax Effect |
|-----------------------|------------------|------------|-------------------|-------------------|
| Unpaid losses and LAE | \$ 210,000 | \$ 192,700 | \$ 17,300 | \$ 5,882 |
| Unearned premiums | 1,210,680 | 968,544 | 242,136 | 82,326 |
| Nonadmitted assets | - | 483,878 | 483,878 | 164,519 |
| Gross DTAs | | | | <u>\$ 252,727</u> |
| | | | | |
| Nonadmitted DTAs | | | | <u>\$ 66,806</u> |

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

7. Income Taxes (continued)

| DTLs | <u>Statutory</u> | <u>Tax</u> | <u>Difference</u> | <u>Tax Effect</u> |
|------------------|-------------------------|-------------------|--------------------------|--------------------------|
| Fixed assets | \$ - | \$ (478,881) | \$ (478,881) | \$ (162,820) |
| Prepaid expenses | - | (67,943) | (67,943) | <u>(23,101)</u> |
| Gross DTLs | | | | <u>\$ (185,921)</u> |

The changes in the main components of DTAs and DTLs are as follows:

| DTAs Resulting from Book/Tax Differences | December 31, | | |
|---|---------------------|--------------------|----------------------|
| | <u>2008</u> | <u>2007</u> | <u>Change</u> |
| Unpaid losses and LAE | \$ 5,882 | \$ 1,558 | \$ 4,324 |
| Unearned premiums | 82,326 | 92,388 | (10,062) |
| Nonadmitted assets | <u>164,519</u> | <u>88,490</u> | <u>76,029</u> |
| Gross DTAs | <u>\$ 252,727</u> | <u>\$ 182,436</u> | <u>\$ 70,291</u> |

| | | | |
|------------------|------------------|-------------|------------------|
| Nonadmitted DTAs | <u>\$ 66,806</u> | <u>\$ -</u> | <u>\$ 66,806</u> |
|------------------|------------------|-------------|------------------|

| DTLs Resulting from Book/Tax Differences | December 31, | | |
|---|---------------------|---------------------|----------------------|
| | <u>2008</u> | <u>2007</u> | <u>Change</u> |
| Furniture and equipment | \$ (162,820) | \$ (71,816) | \$ (91,004) |
| Prepaid expenses | (23,101) | (11,016) | (12,085) |
| Profit sharing expense | <u>-</u> | <u>(74,946)</u> | <u>74,946</u> |
| Gross DTLs | <u>\$ (185,921)</u> | <u>\$ (157,778)</u> | <u>\$ (28,143)</u> |

The change in gross DTAs and DTLs of \$42,148 is the change in net deferred income taxes before the consideration of nonadmitted DTAs and DTLs.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

7. Income Taxes (continued)

D. Reconciliation of federal income tax rate to actual effective rate:

The significant book-to-tax adjustments were as follows:

| | <u>2008</u> | <u>Effective Tax Rate</u> | <u>2007</u> | <u>Effective Tax Rate</u> |
|--------------------------------------|-----------------------|-------------------------------|-------------------|-------------------------------|
| Provision computed at statutory rate | \$ (684,161) | 34.00 % | \$ 326,178 | 34.00 % |
| Nondeductible items | 9,918 | (0.49) | - | - |
| Prior period tax adjustment | (260,803) | 12.96 | - | - |
| Nonadmitted assets | (76,029) | 3.78 | (18,538) | (1.93) |
| Other | - | - | 68,718 | 7.16 |
| Total | <u>\$ (1,011,075)</u> | <u>50.25 %</u> | <u>\$ 376,358</u> | <u>39.23 %</u> |
| Federal income tax | \$ (968,927) | 48.16 % | \$ 183,424 | 19.12 % |
| Change in deferred taxes | <u>(42,148)</u> | <u>2.09</u> | <u>192,934</u> | <u>20.11</u> |
| Statutory income taxes | <u>\$ (1,011,075)</u> | <u>50.25 %</u> | <u>\$ 376,358</u> | <u>39.23 %</u> |

E. Operating loss and tax credit carryforwards:

1. At December 31, 2008 and 2007, the Company had no unused capital loss carryforwards available to offset against future taxable income.
2. The following is income tax expense that is available for recoupment in the event of future net losses:

| <u>Year</u> | <u>Amount</u> |
|-------------|---------------|
| 2008 | \$ - |
| 2007 | 120,253 |

F. Consolidated federal income tax return:

The Company files a consolidated income tax return with the following:

HomeWise Holdings, Inc.

HomeWise Preferred Insurance Company

HomeWise Management Company

The method of allocation between the companies is subject to written agreement, approved by the Board of Directors. Allocation is based upon separate return calculations with current credit for net losses. Intercompany balances are settled quarterly.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

8. Capital and Surplus

The Company has authorized 1,000,000 shares of \$1 par value common stock, of which 650,000 shares are issued and outstanding at December 31, 2008 and 2007. The parent company, HomeWise Holdings, Inc., is the sole shareholder. No other classes of common or preferred shares were issued during 2008 or 2007.

Property and casualty insurance companies are subject to certain risk-based capital (RBC) requirements as specified by the NAIC. Under those requirements, the amount of capital and surplus maintained by a property and casualty insurance company is to be determined based on the various risk factors related to it. The Company is in compliance with the RBC requirements at December 31, 2008 and 2007, respectively.

The maximum amount of dividends that may be paid by property and casualty insurance companies without prior approval of the Office is subject to restrictions relating to statutory surplus and net income. Furthermore, in accordance with the Company's Certificate of Authority Consent Order, during the first three years of operations it may only pay dividends that are approved in advance by the Office. The Company did not declare or pay any dividends during the years ended December 31, 2008 or 2007.

During 2007, to meet the Louisiana regulation that the Company's minimum common capital stock be \$650,000, the Company issued 550,000 of its \$1 par value authorized shares of common stock to its parent, HHI, in a noncash transaction. The issuance of these shares was accounted for by reclassifying \$550,000 from the gross paid-in and contributed surplus account to common stock. This transaction does not impact the total policyholder surplus or ownership of the Company.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

9. Related Party Transactions

The Company is a wholly-owned subsidiary of HomeWise Holdings, Inc. (HHI) and is affiliated with HomeWise Management Company (HMC) and HomeWise Preferred Insurance Company (HPIC), which are also wholly-owned subsidiaries of HHI.

Effective January 1, 2006, the Company entered into a managing general agency agreement with HMC. Pursuant to the agreement, HMC provides to the Company premium billing, claims management and underwriting functions. During 2008 and 2007, expenses incurred related to this agreement totaled \$3,275,793 and \$6,967,680, respectively. At December 31, 2008 and 2007, the Company has a net payable due to HMC in the amount of \$3,263,021 and \$295,464, respectively.

Effective December 5, 2005, the Company entered into a service agreement with HHI. Pursuant to the agreement, HHI provides to the Company capital management services, investor management and relations, and assists with overall general management of the Company. During 2008 and 2007, expenses incurred related to this agreement totaled \$116,993 and \$214,370, respectively. At December 31, 2008 and 2007, the Company has a receivable due from HHI in the amount of \$519 and \$271,751, respectively.

The Company is also party to a Cost Allocation Agreement with HPIC, HMC, and HHI in which expenses benefiting more than one company are allocated based upon direct allocation or revenue allocation rules, whichever is most appropriate for the expenses. At December 31, 2008 and 2007, the Company has a receivable due from HPIC in the amount of \$3,972,151 and \$4,129,565, respectively.

10. Premiums Produced by Managing General Agents or Third Party Administrators

The Company uses a managing general agent, HMC, to write and administer insurance products. HMC has contracted with an unaffiliated service company to provide this function. The total premium produced and serviced through the contract during 2008 is summarized below. The Company retains underwriting authority for all policies issued under these agreements.

| <u>Name and Address</u> | <u>FEI Number</u> | <u>Exclusive Contract</u> | <u>Type of Business Written</u> | <u>Type of Authority Granted</u> | <u>Direct Premium Written</u> |
|---|-------------------|---------------------------|---------------------------------|--|-------------------------------|
| HomeWise Management Company, Inc. 18302 Highwoods Preserve Prkwy Suite 110 Tampa, FL 33647 | 20-3395152 | Yes | Wind-only | Premium collection, claims adjustment, binding authority, and underwriting | S 11,943,311 |

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

11. Lease Commitments

On September 2, 2005, the Company entered into an operating lease agreement for office space in Tallahassee, Florida, which is effective October 15, 2005, through October 31, 2008. This lease was terminated effective May 31, 2007.

On May 1, 2006, the Company also entered into an operating lease agreement for office space in Tampa, Florida, which is effective June 1, 2006, through May 31, 2011. The Company has the option to renew the term of the lease for an additional five year period at the prevailing rental rate at that time, provided the Company gives the lessor written notice nine months prior to its intent to renew the lease. Expenses associated with this lease are allocated equally between the Company and HPIC.

Approximate future lease payments under the operating lease are as follows at December 31, 2008:

| | | |
|------|----|-----------------------|
| 2009 | \$ | 248,453 |
| 2010 | | 258,323 |
| 2011 | | <u>109,348</u> |
| | \$ | <u><u>616,124</u></u> |

Total rent expense for the combined leases was \$184,969 and \$266,409 for the years ended December 31, 2008 and 2007, respectively.

Other Financial Information

SUMMARY INVESTMENT SCHEDULE

| Investment Categories | Gross Investment Holdings | | Admitted Assets as Reported in the Annual Statement | |
|--|---------------------------|-----------------|---|-----------------|
| | 1 Amount | 2 Percentage | 3 Amount | 4 Percentage |
| 1. Bonds: | | | | |
| 1.1 U.S. treasury securities: | | 0.0 | | 0.0 |
| 1.2 U.S. government agency obligations (excluding mortgage-backed securities): | | | | |
| 1.21 Issued by U.S. government agencies: | | 0.0 | | 0.0 |
| 1.22 Issued by U.S. government sponsored agencies: | | 0.0 | | 0.0 |
| 1.3 Foreign government (including Canada, excluding mortgage-backed securities): | | 0.0 | | 0.0 |
| 1.4 Securities issued by states, territories and possessions and political subdivisions in the U.S.: | | | | |
| 1.41 States, territories and possessions general obligations: | | 0.0 | | 0.0 |
| 1.42 Political subdivisions of states, territories & possessions & political subdivisions general obligations: | | 0.0 | | 0.0 |
| 1.43 Revenue and assessment obligations: | | 0.0 | | 0.0 |
| 1.44 Industrial development and similar obligations: | | 0.0 | | 0.0 |
| 1.5 Mortgage-backed securities (includes residential and commercial MBS): | | | | |
| 1.51 Pass-through securities: | | | | |
| 1.511 Issued or guaranteed by GNMA: | | 0.0 | | 0.0 |
| 1.512 Issued or guaranteed by FNMA and FHLMC: | | 0.0 | | 0.0 |
| 1.513 All other: | | 0.0 | | 0.0 |
| 1.52 CMOs and REMICs: | | | | |
| 1.521 Issued or guaranteed by GNMA, FNMA, FHLMC or VA: | | 0.0 | | 0.0 |
| 1.522 Issued by non-U.S. Government issuers and collateralized by mortgage-backed securities issued or guaranteed by agencies shown in Line 1.521: | | 0.0 | | 0.0 |
| 1.523 All other: | | 0.0 | | 0.0 |
| 2. Other debt and other fixed income securities (excluding short-term): | | | | |
| 2.1 Unaffiliated domestic securities (includes credit tenant loans rated by the SVO): | | 0.0 | | 0.0 |
| 2.2 Unaffiliated foreign securities: | | 0.0 | | 0.0 |
| 2.3 Affiliated securities: | | 0.0 | | 0.0 |
| 3. Equity interests: | | | | |
| 3.1 Investments in mutual funds: | | 0.0 | | 0.0 |
| 3.2 Preferred stocks: | | | | |
| 3.21 Affiliated: | | 0.0 | | 0.0 |
| 3.22 Unaffiliated: | | 0.0 | | 0.0 |
| 3.3 Publicly traded equity securities (excluding preferred stocks): | | | | |
| 3.31 Affiliated: | | 0.0 | | 0.0 |
| 3.32 Unaffiliated: | | 0.0 | | 0.0 |
| 3.4 Other equity securities: | | | | |
| 3.41 Affiliated: | | 0.0 | | 0.0 |
| 3.42 Unaffiliated: | | 0.0 | | 0.0 |
| 3.5 Other equity interests including tangible personal property under lease: | | | | |
| 3.51 Affiliated: | | 0.0 | | 0.0 |
| 3.52 Unaffiliated: | | 0.0 | | 0.0 |
| 4. Mortgage loans: | | | | |
| 4.1 Construction and land development: | | 0.0 | | 0.0 |
| 4.2 Agricultural: | | 0.0 | | 0.0 |
| 4.3 Single family residential properties: | | 0.0 | | 0.0 |
| 4.4 Multifamily residential properties: | | 0.0 | | 0.0 |
| 4.5 Commercial loans: | | 0.0 | | 0.0 |
| 4.6 Mezzanine real estate loans: | | 0.0 | | 0.0 |
| 5. Real estate investments: | | | | |
| 5.1 Property occupied by company: | | 0.0 | | 0.0 |
| 5.2 Property held for production of income (including \$0 of property acquired in satisfaction of debt): | | 0.0 | | 0.0 |
| 5.3 Property held for sale (including \$0 of property acquired in satisfaction of debt): | | 0.0 | | 0.0 |
| 6. Contract loans: | | 0.0 | | 0.0 |
| 7. Receivables for securities: | | 0.0 | | 0.0 |
| 8. Cash, cash equivalents and short-term investments: | 6,046,174 | 100.0 | 6,046,174 | 100.0 |
| 9. Other invested assets: | | 0.0 | | 0.0 |
| 10. Total invested assets: | 6,046,174 | 100.0 | 6,046,174 | 100.0 |

SUPPLEMENTAL INVESTMENT RISKS INTERROGATORIES

For the year ended December 31, 2008

(To be filed by April 1)

Of HomeWise Insurance Company

Address (City, State, Zip Code): Tampa FL 33647

NAIC Group Code.....4111

NAIC Company Code.....12438

Employer's ID Number.....20-3395013

The Investment Risks Interrogatories are to be filed by April 1. They are also to be included with the Audited Statutory Financial Statements.

Answer the following interrogatories by reporting the applicable U.S. dollar amounts and percentages of the reporting entity's total admitted assets held in that category of investments.

1. Reporting entity's total admitted assets as reported on Page 2 of this annual statement. \$.....14,642,975

2. Ten largest exposures to a single issuer/borrower/investment.

| | 1 | 2 | 3 | 4 |
|------|---------------------------------------|------------------------------------|------------------|-------------------------------------|
| | Issuer | Description of Exposure | Amount | Percentage of Total Admitted Assets |
| 2.01 | First Amer Govt Oblig Fd Instl Inv Ci | Class One Money Market Mutual Fund | \$.....2,231,467 | 15.239 % |
| 2.02 | | | \$.....0.000 | 0.000 % |
| 2.03 | | | \$.....0.000 | 0.000 % |
| 2.04 | | | \$.....0.000 | 0.000 % |
| 2.05 | | | \$.....0.000 | 0.000 % |
| 2.06 | | | \$.....0.000 | 0.000 % |
| 2.07 | | | \$.....0.000 | 0.000 % |
| 2.08 | | | \$.....0.000 | 0.000 % |
| 2.09 | | | \$.....0.000 | 0.000 % |
| 2.10 | | | \$.....0.000 | 0.000 % |

3. Amounts and percentages of the reporting entity's total admitted assets held in bonds and preferred stocks by NAIC rating.

| | Bonds | 1 | 2 |
|------|------------------|------------------|----------|
| 3.01 | NAIC-1 | \$.....2,231,467 | 15.239 % |
| 3.02 | NAIC-2 | \$.....0.000 | 0.000 % |
| 3.03 | NAIC-3 | \$.....0.000 | 0.000 % |
| 3.04 | NAIC-4 | \$.....0.000 | 0.000 % |
| 3.05 | NAIC-5 | \$.....0.000 | 0.000 % |
| 3.06 | NAIC-6 | \$.....0.000 | 0.000 % |
| | Preferred Stocks | 3 | 4 |
| 3.07 | P/RP-1 | \$.....0.000 | 0.000 % |
| 3.08 | P/RP-2 | \$.....0.000 | 0.000 % |
| 3.09 | P/RP-3 | \$.....0.000 | 0.000 % |
| 3.10 | P/RP-4 | \$.....0.000 | 0.000 % |
| 3.11 | P/RP-5 | \$.....0.000 | 0.000 % |
| 3.12 | P/RP-6 | \$.....0.000 | 0.000 % |

4. Assets held in foreign investments:

| | | |
|--|--|----------------|
| 4.01 | Are assets held in foreign investments less than 2.5% of the reporting entity's total admitted assets? | Yes [X] No [] |
| If response to 4.01 above is yes, responses are not required for interrogatories 5-10. | | |
| 4.02 | Total admitted assets held in foreign investments | \$.....0.000 % |
| 4.03 | Foreign-currency-denominated investments | \$.....0.000 % |
| 4.04 | Insurance liabilities denominated in that same foreign currency | \$.....0.000 % |

5. Aggregate foreign investment exposure categorized by NAIC sovereign rating:

| | 1 | 2 |
|------|---------------------------------|----------------|
| 5.01 | Countries rated NAIC-1 | \$.....0.000 % |
| 5.02 | Countries rated NAIC-2 | \$.....0.000 % |
| 5.03 | Countries rated NAIC-3 or below | \$.....0.000 % |

6. Largest foreign investment exposures by country, categorized by the country's NAIC sovereign rating:

| | 1 | 2 |
|----------------------------------|------------|----------------|
| Countries rated NAIC-1: | | |
| 6.01 | Country 1: | \$.....0.000 % |
| 6.02 | Country 2: | \$.....0.000 % |
| Countries rated NAIC-2: | | |
| 6.03 | Country 1: | \$.....0.000 % |
| 6.04 | Country 2: | \$.....0.000 % |
| Countries rated NAIC-3 or below: | | |
| 6.05 | Country 1: | \$.....0.000 % |
| 6.06 | Country 2: | \$.....0.000 % |

| | | | |
|---|--------|-------------|---------|
| | 1 | 2 | |
| 7. Aggregate unhedged foreign currency exposure: | \$ | | 0.000 % |
| 8. Aggregate unhedged foreign currency exposure categorized by NAIC sovereign rating: | 1 | 2 | |
| 8.01 Countries rated NAIC-1: | \$ | | 0.000 % |
| 8.02 Countries rated NAIC-2: | \$ | | 0.000 % |
| 8.03 Countries rated NAIC-3 or below: | \$ | | 0.000 % |
| 9. Largest unhedged foreign currency exposures by country, categorized by the country's NAIC sovereign rating: | 1 | 2 | |
| Countries rated NAIC-1: | | | |
| 9.01 Country 1: | \$ | | 0.000 % |
| 9.02 Country 2: | \$ | | 0.000 % |
| Countries rated NAIC-2: | | | |
| 9.03 Country 1: | \$ | | 0.000 % |
| 9.04 Country 2: | \$ | | 0.000 % |
| Countries rated NAIC-3 or below: | | | |
| 9.05 Country 1: | \$ | | 0.000 % |
| 9.06 Country 2: | \$ | | 0.000 % |
| 10. Ten largest non-sovereign (i.e. non-governmental) foreign issues: | 1 | 2 | |
| | Issuer | NAIC Rating | |
| 10.01 | | | 0.000 % |
| 10.02 | | | 0.000 % |
| 10.03 | | | 0.000 % |
| 10.04 | | | 0.000 % |
| 10.05 | | | 0.000 % |
| 10.06 | | | 0.000 % |
| 10.07 | | | 0.000 % |
| 10.08 | | | 0.000 % |
| 10.09 | | | 0.000 % |
| 10.10 | | | 0.000 % |
| 11. Amounts and percentages of the reporting entity's total admitted assets held in Canadian investments and unhedged Canadian currency exposure: | | | |
| 11.01 Are assets held in Canadian investments less than 2.5% of the reporting entity's total admitted assets? | | Yes [X] | No [] |
| If response to 11.01 is yes, detail is not required for the remainder of Interrogatory 11. | | | |
| 11.02 Total admitted assets held in Canadian Investments | \$ | | 0.000 % |
| 11.03 Canadian currency-denominated investments | \$ | | 0.000 % |
| 11.04 Canadian-denominated insurance liabilities | \$ | | 0.000 % |
| 11.05 Unhedged Canadian currency exposure | \$ | | 0.000 % |
| 12. Report aggregate amounts and percentages of the reporting entity's total admitted assets held in investments with contractual sales restrictions. | | | |
| 12.01 Are assets held in investments with contractual sales restrictions less than 2.5% of the reporting entity's total admitted assets? | | Yes [X] | No [] |
| If response to 12.01 is yes, responses are not required for the remainder of Interrogatory 12. | | | |
| | 1 | 2 | 3 |
| 12.02 Aggregate statement value of investments with contractual sales restrictions: | \$ | | 0.000 % |
| Largest three investments with contractual sales restrictions: | | | |
| 12.03 | \$ | | 0.000 % |
| 12.04 | \$ | | 0.000 % |
| 12.05 | \$ | | 0.000 % |
| 13. Amounts and percentages of admitted assets held in the ten largest equity interests: | | | |
| 13.01 Are assets held in equity interest less than 2.5% of the reporting entity's total admitted assets? | | Yes [X] | No [] |
| If response to 13.01 above is yes, responses are not required for the remainder of Interrogatory 13. | | | |
| | 1 | 2 | 3 |
| Name of Issuer | | | |
| 13.02 | \$ | | 0.000 % |
| 13.03 | \$ | | 0.000 % |
| 13.04 | \$ | | 0.000 % |
| 13.05 | \$ | | 0.000 % |
| 13.06 | \$ | | 0.000 % |
| 13.07 | \$ | | 0.000 % |
| 13.08 | \$ | | 0.000 % |
| 13.09 | \$ | | 0.000 % |
| 13.10 | \$ | | 0.000 % |
| 13.11 | \$ | | 0.000 % |

14. Amounts and percentages of the reporting entity's total admitted assets held in nonaffiliated, privately placed equities:

14.01 Are assets held in nonaffiliated, privately placed equities less than 2.5% of the reporting entity's total admitted assets?

Yes ☒ No ☐

If response to 14.01 above is yes, responses are not required for the remainder of Interrogatory 14.

| 1 | 2 | 3 |
|--|----|---------|
| 14.02 Aggregate statement value of investments held in nonaffiliated, privately placed equities: | \$ | 0.000 % |
| Largest three investments held in nonaffiliated, privately placed equities: | | |
| 14.03 | \$ | 0.000 % |
| 14.04 | \$ | 0.000 % |
| 14.05 | \$ | 0.000 % |

15. Amounts and percentages of the reporting entity's total admitted assets held in general partnership interests:

15.01 Are assets held in general partnership interests less than 2.5% of the reporting entity's total admitted assets?

Yes ☒ No ☐

If response to 15.01 above is yes, responses are not required for the remainder of Interrogatory 15.

| 1 | 2 | 3 |
|---|----|---------|
| 15.02 Aggregate statement value of investments held in general partnership interests: | \$ | 0.000 % |
| Largest three investments in general partnership interests: | | |
| 15.03 | \$ | 0.000 % |
| 15.04 | \$ | 0.000 % |
| 15.05 | \$ | 0.000 % |

16. Amounts and percentages of the reporting entity's total admitted assets held in mortgage loans:

16.01 Are mortgage loans reported in Schedule B less than 2.5% of the reporting entity's total admitted assets?

Yes ☒ No ☐

If response to 16.01 above is yes, responses are not required for the remainder of Interrogatory 16 and Interrogatory 17.

| 1 | 2 | 3 |
|--|----|---------|
| Type (Residential, Commercial, Agricultural) | | |
| 16.02 | \$ | 0.000 % |
| 16.03 | \$ | 0.000 % |
| 16.04 | \$ | 0.000 % |
| 16.05 | \$ | 0.000 % |
| 16.06 | \$ | 0.000 % |
| 16.07 | \$ | 0.000 % |
| 16.08 | \$ | 0.000 % |
| 16.09 | \$ | 0.000 % |
| 16.10 | \$ | 0.000 % |
| 16.11 | \$ | 0.000 % |

Amount and percentage of the reporting entity's total admitted assets held in the following categories of mortgage loans:

| | Loans |
|--|------------|
| 16.12 Construction loans | \$ 0.000 % |
| 16.13 Mortgage loans over 90 days past due | \$ 0.000 % |
| 16.14 Mortgage loans in the process of foreclosure | \$ 0.000 % |
| 16.15 Mortgage loans foreclosed | \$ 0.000 % |
| 16.16 Restructured mortgage loans | \$ 0.000 % |

17. Aggregate mortgage loans having the following loan-to-value ratios as determined from the most current appraisal as of the annual statement date:

| Loan-to-Value | Residential | | Commercial | | Agricultural | |
|------------------|-------------|------------|------------|------------|--------------|------------|
| | 1 | 2 | 3 | 4 | 5 | 6 |
| 17.01 above 95% | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % |
| 17.02 91% to 95% | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % |
| 17.03 81% to 90% | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % |
| 17.04 71% to 80% | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % |
| 17.05 below 70% | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % | \$ 0.000 % |

18. Amounts and percentages of the reporting entity's total admitted assets held in each of the five largest investments in real estate.

18.01 Are assets held in real estate reported less than 2.5% of the reporting entity's total admitted assets?

Yes ☒ No ☐

If response to 18.01 above is yes, responses are not required for the remainder of Interrogatory 18.

Largest five investments in any one parcel or group of contiguous parcels of real estate.

| Description | 2 | 3 |
|-------------|------------|------------|
| 18.02 | \$ 0.000 % | \$ 0.000 % |
| 18.03 | \$ 0.000 % | \$ 0.000 % |
| 18.04 | \$ 0.000 % | \$ 0.000 % |
| 18.05 | \$ 0.000 % | \$ 0.000 % |
| 18.06 | \$ 0.000 % | \$ 0.000 % |

19. Report aggregate amounts and percentages of the reporting entity's total admitted assets held in investments held in mezzanine real estate loans.

19.01 Are assets held in investments held in mezzanine real estate loans less than 2.5% of the reporting entity's admitted assets?

Yes ☒ No ☐

If response to 19.01 is yes, responses are not required for the remainder of Interrogatory 19.

| 1 | 2 | 3 |
|---|----|---------|
| 19.02 Aggregate statement value of investments held in mezzanine real estate loans: | \$ | 0.000 % |
| Largest three investments held in mezzanine real estate loans: | | |
| 19.03 | \$ | 0.000 % |
| 19.04 | \$ | 0.000 % |
| 19.05 | \$ | 0.000 % |

20. Amounts and percentages of the reporting entity's total admitted assets subject to the following types of agreements:

| | <u>At Year-End</u> | | 1st Qtr | <u>At End of Each Quarter</u> | |
|--|--------------------|---------|---------|-------------------------------|---------|
| | 1 | 2 | | 2nd Qtr | 3rd Qtr |
| 20.01 Securities lending agreements (do not include assets held as collateral for such transactions) | \$ | 0.000 % | \$ | \$ | \$ |
| 20.02 Repurchase agreements | \$ | 0.000 % | \$ | \$ | \$ |
| 20.03 Reverse repurchase agreements | \$ | 0.000 % | \$ | \$ | \$ |
| 20.04 Dollar repurchase agreements | \$ | 0.000 % | \$ | \$ | \$ |
| 20.05 Dollar reverse repurchase agreements | \$ | 0.000 % | \$ | \$ | \$ |

21. Amounts and percentages of the reporting entity's total admitted assets for warrants not attached to other financial instruments, options, caps and floors:

| | <u>Owned</u> | | | <u>Written</u> | |
|-------------------------|--------------|---------|----|----------------|---------|
| | 1 | 2 | | 3 | 4 |
| 21.01 Hedging | \$ | 0.000 % | \$ | \$ | 0.000 % |
| 21.02 Income generation | \$ | 0.000 % | \$ | \$ | 0.000 % |
| 21.03 Other | \$ | 0.000 % | \$ | \$ | 0.000 % |

22. Amounts and percentages of the reporting entity's total admitted assets of potential exposure for collars, swaps, and forwards:

| | <u>At Year-End</u> | | 1st Qtr | <u>At End of Each Quarter</u> | |
|-------------------------|--------------------|---------|---------|-------------------------------|---------|
| | 1 | 2 | | 2nd Qtr | 3rd Qtr |
| 22.01 Hedging | \$ | 0.000 % | \$ | \$ | \$ |
| 22.02 Income generation | \$ | 0.000 % | \$ | \$ | \$ |
| 22.03 Replications | \$ | 0.000 % | \$ | \$ | \$ |
| 22.04 Other | \$ | 0.000 % | \$ | \$ | \$ |

23. Amounts and percentages of the reporting entity's total admitted assets of potential exposure for futures contracts:

| | <u>At Year-End</u> | | 1st Qtr | <u>At End of Each Quarter</u> | |
|-------------------------|--------------------|---------|---------|-------------------------------|---------|
| | 1 | 2 | | 2nd Qtr | 3rd Qtr |
| 23.01 Hedging | \$ | 0.000 % | \$ | \$ | \$ |
| 23.02 Income generation | \$ | 0.000 % | \$ | \$ | \$ |
| 23.03 Replications | \$ | 0.000 % | \$ | \$ | \$ |
| 23.04 Other | \$ | 0.000 % | \$ | \$ | \$ |

HomeWise Insurance Company

Selected General Interrogatories Relating to Reinsurance

December 31, 2008

- 7.1 Has the reporting entity reinsured any risk with any other entity under a quota share reinsurance contract that includes a provision that would limit the reinsurer's losses below the stated quota share percentage (e.g., a deductible, a loss ratio corridor, a loss cap, an aggregate limit or any similar provisions)?.....Yes ☒ No ☐
- 7.2 If yes, indicate the number of reinsurance contracts containing such provisions.....1
- 7.3 If yes, does the amount of reinsurance credit taken reflect the reduction in quota share coverage caused by any applicable limiting provision(s)?.....Yes ☒ No ☐
- 9.1 Has the reporting entity ceded any risk under any reinsurance contract (or under multiple contracts with the same reinsurer or its affiliates) for which during the period covered by the statement: (i) it recorded a positive or negative underwriting result greater than 5% of prior year-end surplus as regards policyholders or it reported calendar year written premium ceded or year-end loss and loss expense reserves ceded greater than 5% of prior year-end surplus as regards policyholders; (ii) it accounted for that contract as reinsurance and not as a deposit; and (iii) the contract(s) contain one or more of the following features or other features that would have similar results:
- (a) A contract term longer than two years and the contract is noncancellable by the reporting entity during the contract term;
 - (b) A limited or conditional cancellation provision under which cancellation triggers an obligation by the reporting entity, or an affiliate of the reporting entity, to enter into a new reinsurance contract with the reinsurer, or an affiliate of the reinsurer;
 - (c) Aggregate stop loss reinsurance coverage;
 - (d) A unilateral right by either party to commute the reinsurance contract, whether conditional or not, except for such provisions which are only triggered by a decline in the credit status of the other party;
 - (e) A provision permitting reporting of losses, or payment of losses, less frequently than on a quarterly basis (unless there is no activity during the period); or
 - (f) Payment schedule, accumulating retentions from multiple years or any feature inherently designed to delay timing of the reimbursement to the ceding entity.....Yes ☐ No ☒
- 9.2 Has the reporting entity during the period covered by the statement ceded any risk under any reinsurance contract (or under multiple contracts with the same reinsurer or its affiliates), for which, during the period covered by the statement, it recorded a positive or negative underwriting result greater than 5% of prior year-end surplus as regards policyholders or it reported calendar year premium ceded or year-end loss and loss expense reserves ceded greater than 5% of prior year-end surplus as regards policyholders; excluding cessions to approved pooling agreements or to captive insurance companies that are directly or indirectly controlling, controlled by, or under common control with (i) one or more unaffiliated policyholders of the reporting entity, or (ii) an association of which one or more unaffiliated policyholders of the reporting entity is a member, where:
- (a) The written premium ceded to the reinsurer by the reporting entity or its affiliates represents fifty percent (50%) or more of the entire direct and assumed premium written by the reinsurer based on its most recently available financial statement; or
 - (b) Twenty-five percent (25%) or more of the written premium ceded to the reinsurer has been retroceded back to the reporting entity or its affiliates in a separate reinsurance contract?.....Yes ☐ No ☒

HomeWise Insurance Company

Selected General Interrogatories Relating to Reinsurance

- 9.3 If yes to 9.1 or 9.2, please provide the following information in the Reinsurance Summary Supplemental Filing for General Interrogatory 9:
- (a) The aggregate financial statement impact gross of all such ceded reinsurance contracts on the balance sheet and statement of income;
 - (b) A summary of the reinsurance contract terms and indicate whether it applies to the contracts meeting the criteria in 9.1 or 9.2; and
 - (c) A brief discussion of management's principle objectives in entering into the reinsurance contract including the economic purpose to be achieved.
- 9.4 Except for transactions meeting the requirements of paragraph 31 of SSAP No. 62, *Property and Casualty Reinsurance*, has the reporting entity ceded any risk under any reinsurance contract (or multiple contracts with the same reinsurer or its affiliates) during the period covered by the financial statement, and either:
- (a) Accounted for that contract as reinsurance (either prospective or retroactive) under statutory accounting principles (SAP) and as a deposit under generally accepted accounting principles (GAAP); or
 - (b) Accounted for that contract as reinsurance under GAAP and as a deposit under SAP?.....Yes ☐ No ☒
- 9.5 If yes to 9.4, explain in the Reinsurance Summary Supplemental Filing for General Interrogatory 9 (Section D) why the contract(s) is treated different for GAAP and SAP.

See report of independent auditors.

Statutory Basis Financial Statements
and Other Financial Information

HomeWise Insurance Company

*Years ended December 31, 2009 and 2008
with Report of Independent Auditors*

Thomas Howell
 Ferguson P.A.

HomeWise Insurance Company
Statutory Basis Financial Statements
and Other Financial Information
Years ended December 31, 2009 and 2008

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Report of Independent Auditors

The Board of Directors
HomeWise Insurance Company

We have audited the accompanying statements of admitted assets, liabilities, and capital and surplus - statutory basis of HomeWise Insurance Company (the Company) as of December 31, 2009 and 2008, and the related statutory basis statements of operations, changes in capital and surplus, and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As described more fully in Note 1 to the financial statements, these financial statements have been prepared in conformity with accounting practices prescribed or permitted by the Florida Office of Insurance Regulation, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the admitted assets, liabilities and capital and surplus of HomeWise Insurance Company as of December 31, 2009 and 2008, and the results of its operations and its cash flows for the years then ended on the basis of accounting described in Note 1.

Our audits were made for the purpose of forming an opinion on the statutory basis financial statements taken as a whole. The summary investment schedule (Schedule 1), supplemental investment risks interrogatories (Schedule 2), and the selected general interrogatories relating to reinsurance (Schedule 3) included in other financial information as of and for the year ended December 31, 2009, are presented to comply with the National Association of Insurance Commissioners' *Accounting Practices and Procedures Manual* and are not a required part of the statutory basis financial statements. The additional information has been subjected to the auditing procedures applied in the audits of the statutory basis financial statements and, in our opinion, is fairly stated in all material respects in relation to the statutory basis financial statements taken as a whole.

This report is intended solely for the use of the Board of Directors and management of HomeWise Insurance Company and for filing with the Florida Office of Insurance Regulation and is not intended to be and should not be used by anyone other than these specified parties.

Thomas Howell Ferguson P.A.

March 23, 2010

HomeWise Insurance Company

Statements of Admitted Assets, Liabilities, and Capital and Surplus - Statutory Basis

| | December 31, | |
|--|----------------------|----------------------|
| | 2009 | 2008 |
| Admitted assets | | |
| Cash and invested assets: | | |
| Short-term investments | \$ 5,687,089 | \$ 2,231,467 |
| Cash and cash equivalents | <u>8,298,372</u> | <u>3,814,707</u> |
| Total cash and invested assets | 13,985,461 | 6,046,174 |
| Accrued investment income | 11,924 | 7,762 |
| Premiums receivable | 6,409,016 | 839,085 |
| Reinsurance balances recoverable | 365,365 | 1,406,688 |
| Federal income taxes recoverable | 118 | 1,629,206 |
| Net deferred tax asset | 708,396 | - |
| Electronic data processing equipment, net | - | 220,633 |
| Receivables from parent and affiliates | 1,359,469 | 3,972,670 |
| Capital contribution receivable | 13,000,000 | - |
| Other assets | <u>296,813</u> | <u>520,757</u> |
| Total admitted assets | <u>\$ 36,136,562</u> | <u>\$ 14,642,975</u> |
| Liabilities and capital and surplus | | |
| Liabilities: | | |
| Loss and loss adjustment expense reserves | \$ 574,123 | \$ 210,649 |
| Unearned premiums, net | 6,906,109 | 1,210,680 |
| Reinsurance premiums payable | 6,499,800 | 1,228,276 |
| Provision for reinsurance | 80,000 | - |
| Accounts payable and accrued expenses | 453,552 | 334,535 |
| Taxes, licenses, and fees payable | 523,116 | - |
| Return premiums payable | 504,285 | - |
| Payable to affiliates | <u>333,407</u> | <u>3,263,021</u> |
| Total liabilities | 15,874,392 | 6,247,161 |
| Capital and surplus | <u>20,262,170</u> | <u>8,395,814</u> |
| Total liabilities and capital and surplus | <u>\$ 36,136,562</u> | <u>\$ 14,642,975</u> |

See accompanying notes.

HomeWise Insurance Company

Statements of Operations - Statutory Basis

| | <u>Years ended</u> <u>2009</u> | <u>December 31,</u> <u>2008</u> |
|--|-----------------------------------|------------------------------------|
| Underwriting income: | | |
| Premiums earned, net of reinsurance ceded | \$ 4,555,001 | \$ 1,362,358 |
| Underwriting expenses: | | |
| Losses and loss adjustment expenses incurred | 1,228,091 | 243,595 |
| Underwriting, acquisition, and other expenses | <u>5,273,642</u> | <u>3,238,904</u> |
| Total underwriting expenses | <u>6,501,733</u> | <u>3,482,499</u> |
| Net underwriting loss | (1,946,732) | (2,120,141) |
| Net investment income | 5,110 | 107,349 |
| Other income | <u>93,716</u> | <u>549</u> |
| Loss before federal income tax expense (benefit) | (1,847,906) | (2,012,243) |
| Federal income tax expense (benefit) | <u>255,049</u> | <u>(968,927)</u> |
| Net loss | \$ <u><u>(2,102,955)</u></u> | \$ <u><u>(1,043,316)</u></u> |

See accompanying notes.

HomeWise Insurance Company

Statements of Changes in Capital and Surplus - Statutory Basis

Years ended December 31, 2009 and 2008

| | Common Stock | | Gross Paid-in and Contributed | | Unassigned Funds | | Total |
|--|--------------|------------|-------------------------------------|----------------|---------------------|--|-------|
| | Shares | Par Value | Surplus | | | | |
| Balance as of December 31, 2007 | 650,000 | \$ 650,000 | \$ 8,850,000 | \$ 187,400 | \$ 9,687,400 | | |
| Change in deferred income taxes | - | - | - | 42,148 | 42,148 | | |
| Change in nonadmitted assets | - | - | - | (290,418) | (290,418) | | |
| Net loss | - | - | - | (1,043,316) | (1,043,316) | | |
| Balance as of December 31, 2008 | 650,000 | 650,000 | 8,850,000 | (1,104,186) | 8,395,814 | | |
| Capital contributions | - | - | 13,000,000 | - | 13,000,000 | | |
| Change in deferred income taxes | - | - | - | 641,590 | 641,590 | | |
| Change in nonadmitted assets | - | - | - | 407,721 | 407,721 | | |
| Change in provision for reinsurance | - | - | - | (80,000) | (80,000) | | |
| Net loss | - | - | - | (2,102,955) | (2,102,955) | | |
| Balance as of December 31, 2009 | 650,000 | \$ 650,000 | \$ 21,850,000 | \$ (2,237,830) | \$ 20,262,170 | | |

See accompanying notes.

HomeWise Insurance Company
Statements of Cash Flows - Statutory Basis

| | <u>Years ended</u> <u>2009</u> | <u>December 31,</u> <u>2008</u> |
|---|-----------------------------------|------------------------------------|
| Operating activities | | |
| Premiums collected, net of reinsurance | \$ 10,456,308 | \$ 649,860 |
| Net investment income received | 948 | 113,453 |
| Other income received | 81,442 | - |
| Losses and loss adjustment expenses recovered (paid) | 176,706 | (1,505,536) |
| Underwriting, acquisition, and other expenses paid | (4,602,173) | (3,050,573) |
| Federal income taxes recovered | <u>1,374,039</u> | <u>-</u> |
| Net cash provided by (used in) operating activities | <u>7,487,270</u> | <u>(3,792,796)</u> |
| Financing activities | | |
| Other miscellaneous sources | <u>452,017</u> | <u>3,196,613</u> |
| Net cash provided by financing activities | <u>452,017</u> | <u>3,196,613</u> |
| Net increase (decrease) in cash | 7,939,287 | (596,183) |
| Cash at beginning of year | <u>6,046,174</u> | <u>6,642,357</u> |
| Cash at end of year | <u>\$ 13,985,461</u> | <u>\$ 6,046,174</u> |
| Cash consists of the following: | | |
| Cash and cash equivalents | \$ 8,298,372 | \$ 3,814,707 |
| Short-term investments | <u>5,687,089</u> | <u>2,231,467</u> |
| | <u>\$ 13,985,461</u> | <u>\$ 6,046,174</u> |

See accompanying notes.

HomeWise Insurance Company
Notes to Statutory Basis Financial Statements

Years ended December 31, 2009 and 2008

1. Summary of Significant Accounting Policies

Organization and Description of Company

HomeWise Insurance Company (the Company), a wholly-owned subsidiary of HomeWise Holdings, Inc. (HHI), an insurance holding company, is domiciled in the state of Florida. The Company received its Certificate of Authority from the Florida Office of Insurance Regulation (the Office) on December 5, 2005, and commenced operations on January 12, 2006. The Company received a Certificate of Authority from the state of Louisiana on August 6, 2008, and commenced operations on November 25, 2008. The Company is affiliated with HomeWise Management Company (HMC) and HomeWise Preferred Insurance Company (HPIC), which are wholly-owned subsidiaries of HHI.

The Company writes coverage exclusively in the states of Florida and Louisiana, areas that are exposed to damage from hurricanes and severe storms. The Company attempts to mitigate its exposure to losses from storms by purchasing quota share and catastrophe reinsurance coverage. However, such a storm, depending on its path and severity, could result in losses to the Company exceeding its reinsurance protection and could have a material adverse effect on the financial condition and results of operations of the Company.

Basis of Presentation

The accompanying statutory basis financial statements have been prepared in accordance with statutory accounting practices (SAP) prescribed or permitted by the Florida Office of Insurance Regulation (the Office). Such statutory practices require preparation of the financial statements in accordance with the National Association of Insurance Commissioners' (NAIC) *Accounting Practices and Procedures Manual* subject to deviations prescribed by the Office. SAP is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America (GAAP). Such practices vary in certain respects from those under GAAP. The Company's significant accounting practices and the variances from GAAP are summarized below:

- Certain assets designated as "nonadmitted," principally past-due uncollected premiums, prepaid expenses, and other assets not specifically identified as an admitted asset within the *Accounting Practices and Procedures Manual*, are excluded from the accompanying statements of admitted assets, liabilities, and capital and surplus and are charged directly to unassigned surplus. Under GAAP, such assets would be included in the balance sheet at net realizable values.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

1. Summary of Significant Accounting Policies (continued)

Basis of Presentation (continued)

- Loss and loss adjustment expense reserves and unearned premiums ceded to reinsurers have been reported as reductions of the related liabilities rather than as assets as would be required under GAAP.
- Cash in the statements of cash flows represents cash, cash equivalents, and short-term investments with remaining maturities of one year or less. Under GAAP, the corresponding caption of cash and cash equivalents would include cash balances and investments with initial maturities of three months or less.
- The costs of acquiring and renewing business are expensed when incurred. Under GAAP, such costs, to the extent recoverable, would be deferred and amortized over the effective period of the related insurance policies.
- Deferred tax assets are limited to 1) the amount of federal income taxes paid in prior years that can be recovered through loss carrybacks for existing temporary differences that reverse by the end of the subsequent calendar year, plus 2) the lesser of the remaining gross deferred tax assets expected to be realized within one year of the financial statement date or 10% of capital and surplus excluding any net deferred tax assets, "electronic data processing" (EDP) equipment and operating software and any net positive goodwill, plus 3) the amount of remaining gross deferred tax assets that can be offset against existing gross deferred tax liabilities. The remaining deferred tax assets are nonadmitted. Deferred taxes do not include amounts for state income taxes. Under GAAP, state income taxes would be included in the computation of deferred taxes, a deferred tax asset would be recorded for the amount of gross deferred tax assets expected to be realized in future years, and a valuation allowance would be established for deferred tax assets not realizable.
- Commissions allowed by reinsurers on business ceded are reported as a reduction of expense when incurred to the extent the amount does not exceed actual acquisition costs, rather than being deferred and amortized with deferred policy acquisition costs as would be required by GAAP. Commissions in excess of the acquisition costs, if any, would be deferred and recognized over the policy term consistent with GAAP.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

1. Summary of Significant Accounting Policies (continued)

Basis of Presentation (continued)

- Certain other reported amounts are classified or presented differently in the financial statements prepared on the basis of SAP than they would be under GAAP. Statutory requirements require that the financial statements of the Company be filed with state regulatory authorities. Accordingly, the financial statements are presented in a format similar to the filed annual statement, which differs from the format of financial statements presented under GAAP. Required statutory disclosures that are not applicable to the Company are not included in the notes to these statutory financial statements.

Other significant accounting practices are as follows:

Recognition of Premium Revenues

Premiums are recorded as earned on a daily pro rata basis over the contract period that the related policies are expected to be in force. The portion of premiums not earned at the end of the year is recorded as unearned premiums. Premiums collected prior to the effective date of the policy are recorded as a liability.

Cash and Cash Equivalents

Cash and cash equivalents include demand deposits with several financial institutions and other highly liquid investments with original maturities of three months or less and certificates of deposit with original maturities of one year or less and are principally stated at cost, which approximates fair value.

Investments

Investments are recorded at admitted asset values as prescribed by the valuation procedures of the NAIC's Securities Valuation Office (SVO). The valuation technique used to measure fair value (market value) is to obtain the published securities' fair value from the SVO publication, *Valuation of Securities*. If the specific security is not listed in this publication, then the fair value is obtained from a registered U.S. exchange.

Short-term investments include investments with original maturities of one year or less from the time of acquisition and are principally stated at cost, which approximates fair value.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

1. Summary of Significant Accounting Policies (continued)

Concentration of Credit Risk

The Company's financial instruments exposed to concentrations of credit risk consist primarily of its cash and cash equivalents, short-term investments, reinsurance recoveries, and premium revenue. The Company maintains its cash and cash equivalents at several financial institutions. Deposits with financial institutions are insured by the Federal Deposit Insurance Corporation (FDIC). On October 3, 2008, FDIC coverage increased from \$100,000 to \$250,000 per depositor until December 31, 2009. On May 20, 2009, the FDIC extended this increase in per depositor coverage to December 31, 2013. Bank deposit accounts, at times, may exceed federally insured limits. The Company has not experienced any losses in such accounts.

All investment transactions have credit exposure to the extent that a counterparty may default on an obligation to the Company. Credit risk is a consequence of carrying investment positions. To manage credit risk, the Company focuses primarily on highly liquid debt instruments, reviews the credit strength of all entities in which it invests, limits its exposure in any one investment, and monitors portfolio quality, taking into account credit ratings assigned by recognized credit rating organizations.

Electronic Data Processing (EDP) Equipment

The admitted value of the Company's EDP equipment is limited to 3% of capital and surplus. The admitted portion is reported at cost, less accumulated depreciation of \$174,870 at December 31, 2008 (none at December 31, 2009). EDP equipment is depreciated using the straight-line method over the lesser of its useful life or three years. Other furniture and equipment is recorded as a nonadmitted asset and depreciated using the straight-line method over the estimated useful life of seven years. Depreciation expense charged to operations was \$135,689 and \$157,016 in 2009 and 2008, respectively.

Reinsurance

The accompanying statutory basis financial statements reflect reserves for premiums and losses and loss adjustment expenses (LAE), net of reinsurance ceded (see Note 6). Those reinsurance arrangements allow management to control exposure to potential losses arising from large risks. A significant portion of the reinsurance is effected under a quota share reinsurance agreement. Amounts recoverable from reinsurers are estimated in a manner consistent with the loss and LAE reserves associated with the reinsured policies. Reinsurance premiums, losses, and LAE are accounted for on bases consistent with those used in accounting for the original policies issued and the terms of the reinsurance contracts.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

1. Summary of Significant Accounting Policies (continued)

Loss and Loss Adjustment Expense (LAE) Reserves

Loss and LAE reserves represent the estimated ultimate net cost of all unpaid reported and unreported losses and LAE. The reserves for unpaid losses and LAE are estimated using individual case-basis estimates for reported losses and actuarial estimates for losses incurred but not yet reported. Those estimates are subject to the effects of trends in loss severity and frequency. Although considerable variability is inherent in such estimates, management believes that the reserves for losses and LAE are adequate. The estimates are continually reviewed and adjusted as necessary as experience develops or new information becomes known; such adjustments are included in current operations. The ultimate settlement of losses and LAE may vary significantly from the estimated amounts included in the financial statements. The Company does not discount its loss and LAE reserves.

The anticipated effect of inflation is implicitly considered when estimating liabilities for losses and LAE. While anticipated price increases due to inflation are considered in estimating the ultimate claim costs, the increase in average severities of claims is caused by a number of factors that vary with the individual type of policy written. Future average severities are projected based on historical trends adjusted for implemented changes in underwriting standards, policy provisions, and general economic trends. Those anticipated trends are monitored based on actual development and the estimated liabilities are modified if necessary.

Loss and LAE reserves are reported net of reinsurance recoverables for unpaid losses and LAE. Losses and LAE ceded through reinsurance are credited against losses and LAE incurred.

Guaranty Fund and Residual Market Pool Assessments

The Company is subject to assessments by a Florida guaranty fund, a residual market pool, and a state catastrophe reinsurance pool. The activities of this fund and these pools include collecting funds from solvent insurance companies to cover losses resulting from the insolvency or rehabilitation of other insurance companies or deficits generated by Florida Insurance Guaranty Association (FIGA), Citizens Property Insurance Corporation (Citizens), and the Florida Hurricane Catastrophe Fund (FHCF).

The Company's policy is to recognize its obligation for guaranty fund, Citizens, and FHCF assessments when the Company has the information available to reasonably estimate its liabilities. Guaranty fund, Citizens, and FHCF assessments are generally available for recoupment from policyholders and as such, amounts assessed are recorded as a recoverable asset. Amounts recoverable are generally expected to be collected during the year following assessment.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

1. Summary of Significant Accounting Policies (continued)

Guaranty Fund and Residual Market Pool Assessments (continued)

The Company was assessed \$95,153 by FIGA in 2009 (none in 2008). The FIGA assessment recoverable from policyholders was \$95,153 and \$227,145 at December 31, 2009 and 2008, respectively.

Certain Citizens and FHCF assessments are collected from policyholders as policies are written and subsequently remitted to the assessing entity. Amounts due from policyholders for these assessments were \$105,999 and \$17,692 at December 31, 2009 and 2008, respectively. The liability for assessments collected but not remitted to Citizens and FHCF totaled \$294,763 and \$62,611 at December 31, 2009 and 2008, respectively.

Income Taxes

The Company calculates its state and federal income tax liabilities based upon the statutory rates in effect during the year.

Subsequent Events

The Company has evaluated subsequent events through March 23, 2010, the date the financial statements were available to be issued.

Use of Estimates

The preparation of statutory basis financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the statutory basis financial statements, and the reported amounts of revenues and expenses during the reporting period. Such estimates and assumptions could change in the future as more information becomes known, which could impact the amounts reported and described in the financial statements.

Reclassification

Certain 2008 amounts in the financial statements have been reclassified to conform to the 2009 financial statement presentation.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

2. Regulatory Requirements and Restrictions

Florida Statute 624.408 requires the Company to maintain minimum capital and surplus of \$4 million and to meet the risk-based capital requirements (see Note 8). Additionally, Florida Statute 624.4095 requires the Company to maintain a ratio of the product of written premiums times 0.90 to surplus of no greater than 10-to-1 for gross written premiums and 4-to-1 for net written premiums. The Company is in compliance with these requirements.

Additionally, the Company is required to maintain deposits pursuant to Florida and Louisiana statutes to help secure the payment of claims. Cash on deposit in the amount of \$348,756 and \$342,595 has been assigned to the Office as of December 31, 2009 and 2008, respectively, and a certificate of deposit in the amount of \$100,000 has been assigned to the Louisiana Department of Insurance as of December 31, 2009 and 2008, to satisfy this requirement. These amounts are included in cash and cash equivalents in the accompanying statements of admitted assets, liabilities, and capital and surplus at December 31, 2009 and 2008.

3. Investments

Short-term investments consist of money market funds that have a maturity of one year or less from the date of purchase and are stated at cost, which approximates fair value.

Major categories of the Company's net investment income are summarized as follows:

| | Years ended December 31, | |
|---------------------------|---------------------------------|-------------------|
| | 2009 | 2008 |
| Investment income: | | |
| Cash and cash equivalents | \$ 15,810 | \$ 76,351 |
| Short-term investments | <u>16,760</u> | <u>64,787</u> |
| Total investment income | 32,570 | 141,138 |
| Investment expense: | | |
| Bank fees | <u>(27,460)</u> | <u>(33,789)</u> |
| Net investment income | <u>\$ 5,110</u> | <u>\$ 107,349</u> |

4. Premiums Receivable

Premiums receivable includes amounts due from HomeWise Management Company, the Company's managing general agent (MGA), who collects all premiums and remits them to the Company. The Company nonadmits balances due from insureds and deferred installments for which a portion of the receivable is more than 90 days past due and exceeds the related unearned premium. Premiums receivable is charged to bad debt expense in the period determined uncollectible. Recoveries received on amounts previously charged-off are credited to bad debt expense in the period received. Premiums receivable totaled \$6,409,016 and \$839,085, with no nonadmitted premiums receivable, as of December 31, 2009 and 2008, respectively.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

5. Loss and Loss Adjustment Expense (LAE) Reserves

The following table provides a reconciliation of the beginning and ending reserve balances for losses and LAE, net of reinsurance recoverables.

| | December 31, | |
|--|-----------------------|---------------|
| | 2009 | 2008 |
| | <i>(in thousands)</i> | |
| Loss and LAE reserves at beginning of year | \$ 211 | \$ 70 |
| Losses and LAE incurred related to: | | |
| Current year | 1,413 | 263 |
| Prior years | <u>(185)</u> | <u>(19)</u> |
| | 1,228 | 244 |
| Losses and LAE paid related to: | | |
| Current year | 841 | 174 |
| Prior years | <u>24</u> | <u>(71)</u> |
| | 865 | 103 |
| Loss and LAE reserves at end of year | <u>\$ 574</u> | <u>\$ 211</u> |

Anticipated reinsurance recoverables on unpaid losses and LAE are approximately \$1,399,000 and \$162,000 at December 31, 2009 and 2008, respectively. Reinsurance recoverables on paid losses and LAE are approximately \$365,000 and \$135,000 at December 31, 2009 and 2008, respectively.

In 2009 and 2008, net incurred losses and LAE attributable to insured events of prior years have developed favorably by \$(185,000) and \$(19,000), respectively, as a result of reestimation of unpaid losses and loss adjustment expenses. Original estimates are decreased or increased as additional information becomes known regarding individual claims.

6. Reinsurance

Certain premiums and benefits are ceded to other insurance companies under various reinsurance agreements. The reinsurance agreements provide the Company with increased capacity to write more risks and maintain its exposure to loss within its capital resources. As of December 31, 2009 and 2008, the Company's reinsurance program consisted of catastrophe excess of loss reinsurance and quota share treaties. Following is a summary of the reinsurance coverage.

Effective June 1, 2009, the Company and its affiliated company, HomeWise Preferred Insurance Company (collectively, the Reinsured), entered into quota share reinsurance agreements with Signet Star Re (Signet), Hannover Reinsurance (Ireland) Ltd. (Hannover), and Greenlight Reinsurance Ltd. (Greenlight) (collectively, the Reinsurers). Signet has a 30% participation. Hannover and Greenlight each have a 35% participation.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

6. Reinsurance (continued)

Under the terms of the agreements, as amended June 30, 2009, the Reinsurers assume a percentage (85% on policies written through December 31, 2009, and 75% on policies written thereafter) of the Reinsured's incurred losses and loss adjustment expenses, subject to several exclusions. The Company cedes a percentage (85% on policies written through December 31, 2009, and 75% on policies written thereafter) of its gross premiums, subject to several exclusions, after deducting a portion of the cost of the excess of loss reinsurance treaties, described below. The quota share agreements with Signet and Hannover expire on May 31, 2010, while the agreement with Greenlight expires on May 31, 2011.

The reinsurance agreements are subject to loss retention corridors, whereby the Reinsured retain losses above a minimum gross loss ratio ranging from 25% to 33% up to a maximum gross loss ratio ranging from 37% to 42%. The limitations on maximum losses ceded under this agreement vary by participating reinsurer. The ceding commission from the Reinsurers is equal to a blended rate of 31.07% of the Reinsurers' share of gross written premium, prior to the deduction of any premiums paid to catastrophe excess of loss protection. The current year and prior year (described below) ceding commissions have been recorded as a reduction of underwriting, acquisition, and other expenses in the accompanying statements of operations.

Effective June 1, 2008, the Company and its affiliated company, HomeWise Preferred Insurance Company (collectively, the Reinsured), entered into a quota share reinsurance agreement with Swiss Reinsurance America Corporation (the Reinsurer). Under the terms of the agreement, which expired on May 31, 2009, and was subsequently commuted, the Reinsurer assumed 75% of the Reinsured's net liabilities for losses (loss and loss adjustment expense) after taking into effect the Reinsured's excess of loss reinsurance coverage provided by the FHCF and the commercial excess of loss. Under the terms of the agreement, the Reinsured ceded 75% of gross premiums after deducting the cost of the above referenced inuring reinsurance to the Reinsurer. The Reinsured ceded 75% of covered gross losses to the Reinsurer after deducting recoveries from the referenced inuring reinsurance. The maximum losses ceded under this agreement were limited to \$150 million per event and \$210 million for all occurrences. The Company and the Reinsurer entered into an aggregate excess of loss agreement to reinsure the Reinsurer's catastrophe obligation under the quota share agreement. The Reinsurer reimbursed the Company for the premiums relating to this coverage. The ceding commission from the Reinsurer to the Reinsured was on a reimbursement basis wherein the Reinsurer reimbursed the Reinsured for 75% of acquisition and overhead expenses limited to 31%.

In 2009, the Company commuted its reinsurance agreement with Swiss Re (see above), and in 2008, the Company commuted its quota share agreement with its previous quota share provider. In 2009 and 2008, the Company did not enter into or engage in any loss portfolio transfer for any lines of business.

The catastrophe excess of loss coverage is provided by agreements with commercial reinsurers and by the FHCF. Coverage under the FHCF is limited to qualifying storms occurring in the state of Florida. For the year ended December 31, 2009, the commercial excess of loss treaties

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

6. Reinsurance (continued)

generally provide coverage on ultimate net losses of approximately \$26,500,000 in excess of \$2,520,000 per occurrence, not to exceed approximately \$51,200,000 for all occurrences. The FHCF provided coverage for 90% of the losses from qualifying catastrophic events in excess of approximately \$18,600,000 up to a maximum of approximately \$97,200,000. For the year ended December 31, 2008, the commercial excess of loss treaties generally provide 100% coverage on ultimate net losses of approximately \$9,300,000 in excess of \$2,900,000 and 25% coverage on ultimate net losses of approximately \$12,700,000 in excess of approximately \$12,200,000 per occurrence, not to exceed approximately \$25,000,000 for all occurrences. The FHCF provided coverage for 90% of the losses from qualifying catastrophic events in excess of approximately \$12,200,000 up to a maximum of approximately \$72,900,000.

For 2009, the Company and its affiliated company, HomeWise Preferred Insurance Company, entered into the commercial catastrophe excess of loss coverage agreements described above. The 2009 amounts shown above represent the Company's share of the total agreements.

The FHCF provides coverage for named hurricanes only and provides no coverage after the one time limit is exhausted. Reinsurance premiums for the FHCF are paid on a total insured value basis. In the event of a loss assessment, the Company may recoup the assessments from its policyholders.

Effective June 1, 2009 and 2008, the Company executed reinsurance premium protection agreements to reinsure the reinstatement premium payment obligations which accrue to the Company under the private catastrophe excess of loss agreements. The coverage is limited to 100% of the original contracted reinsurance placement.

The Company's reinsured risks are treated, to the extent of the reinsurance, as though they are risks for which the Company is not liable. However, the Company remains liable in the event the reinsuring companies do not meet their obligations under these reinsurance agreements. Given the quality of the reinsuring companies, management believes this possibility to be remote. See Note 5 for recoveries due from reinsurers relating to paid and unpaid losses and LAE.

The effects of reinsurance on premiums written and earned are as follows:

| | 2009 | | 2008 | |
|-----------------|----------------------|---------------------|---------------------|---------------------|
| | Written | Earned | Written | Earned |
| Direct premiums | \$ 38,926,642 | \$ 23,728,632 | \$ 11,943,311 | \$ 16,941,545 |
| Ceded premiums | <u>(28,676,212)</u> | <u>(19,173,631)</u> | <u>(10,728,913)</u> | <u>(15,579,187)</u> |
| Net premiums | <u>\$ 10,250,430</u> | <u>\$ 4,555,001</u> | <u>\$ 1,214,398</u> | <u>\$ 1,362,358</u> |

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

6. Reinsurance (continued)

The following table summarizes the effect of ceded unearned premiums on the direct unearned premiums reserve and provides the related commission equity at December 31:

| | <u>2009</u> | <u>2008</u> |
|--------------------------|-----------------------|-----------------------|
| Direct unearned premiums | \$ 22,408,299 | \$ 7,210,289 |
| Ceded unearned premiums | <u>(15,502,190)</u> | <u>(5,999,609)</u> |
| Unearned premiums, net | <u>\$ 6,906,109</u> | <u>\$ 1,210,680</u> |
| Commission equity, net | <u>\$ (4,495,765)</u> | <u>\$ (1,676,392)</u> |

At December 31, 2009 and 2008, unsecured reinsurance recoverables on paid and unpaid losses and LAE and unearned premiums by reinsurer that were equal to or greater than 3% of surplus are as follows:

| | <u>2009</u> | <u>2008</u> |
|---------------------------------------|--------------|-------------|
| Signet Star (Berkley Insurance Co.) | \$ 2,935,000 | \$ - |
| Florida Hurricane Catastrophe Fund | 1,683,000 | 979,000 |
| Swiss Reinsurance America Corporation | - | 3,502,000 |

For the years ended December 31, 2009 and 2008, recoveries under reinsurance contracts totaled \$1,684,176 and \$282,554, respectively.

7. Income Taxes

Income before federal income taxes differs from taxable income principally due to differences in loss and LAE reserves and unearned premiums for tax and statutory basis financial reporting purposes.

State income taxes are classified as taxes, licenses, and fees in the NAIC Annual Statement and as underwriting, acquisition, and other expenses in the accompanying statements of operations.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

7. Income Taxes (continued)

A. The components of net deferred tax assets (DTAs) and deferred tax liabilities (DTLs) at December 31, are as follows:

| | 2009 | | |
|------------------------------|-----------------|----------------|--------------------|
| | <u>Ordinary</u> | <u>Capital</u> | <u>Total</u> |
| Total gross DTAs | \$ 796,804 | \$ - | \$ 796,804 |
| Total gross DTLs | 88,408 | - | <u>88,408</u> |
| Net DTA | | | 708,396 |
| Nonadmitted DTAs | | | - |
| Net admitted DTAs | | | <u>\$ 708,396</u> |
| Decrease in nonadmitted DTAs | | | <u>\$ (66,806)</u> |

| | 2008 | | |
|------------------------------|-----------------|----------------|------------------|
| | <u>Ordinary</u> | <u>Capital</u> | <u>Total</u> |
| Total gross DTAs | \$ 252,727 | \$ - | \$ 252,727 |
| Total gross DTLs | 185,921 | - | <u>185,921</u> |
| Net DTA | | | 66,806 |
| Nonadmitted DTAs | | | <u>(66,806)</u> |
| Net admitted DTA | | | <u>\$ -</u> |
| Increase in nonadmitted DTAs | | | <u>\$ 66,806</u> |

The Company has not elected to admit additional DTAs pursuant to SSAP 10R, paragraph 10(e). The current period election does not differ from the prior reporting period.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

7. Income Taxes (continued)

The amount of each result or component of the calculation, by tax character, of paragraphs 10.a., 10.b.i., 10.b.ii., and 10.c. are as follows:

| | 2009 | | |
|--|----------|---------|------------|
| | Ordinary | Capital | Total |
| Can be recovered through loss carrybacks (10.a.) | \$ - | \$ - | \$ - |
| Lesser of: | | | |
| Expected to be recognized within one year (10.b.i.) | 791,602 | - | 791,602 |
| Ten percent of adjusted capital and surplus (10.b.ii.) | 740,262 | - | 740,262 |
| Adjusted gross DTAs offset against existing DTLs (10.c.) | 56,542 | - | 56,542 |
| Risk-based capital level used in paragraph 10.d.: | | | |
| Total adjusted capital | | | 20,262,170 |
| Authorized control level | | | 2,555,084 |

| | 2008 | | |
|--|----------|---------|-----------|
| | Ordinary | Capital | Total |
| Can be recovered through loss carrybacks (10.a.) | \$ - | \$ - | \$ - |
| Lesser of: | | | |
| Expected to be recognized within one year (10.b.i.) | - | - | - |
| Ten percent of adjusted capital and surplus (10.b.ii.) | - | - | - |
| Adjusted gross DTAs offset against existing DTLs (10.c.) | 185,920 | - | 185,920 |
| Risk-based capital level used in paragraph 10.d.: | | | |
| Total adjusted capital | | | 8,395,814 |
| Authorized control level | | | 1,658,335 |

The following amounts resulting from the calculation in paragraphs 10.a., 10.b., and 10.c.:

| | 2009 | 2008 |
|------------------------|------------|------------|
| Admitted DTAs | \$ 708,396 | \$ - |
| Admitted assets | 36,136,562 | 14,642,975 |
| Statutory surplus | 20,262,170 | 8,395,814 |
| Total adjusted capital | 20,262,170 | 8,395,814 |

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

7. Income Taxes (continued)

B. Unrecognized DTLs:

Not applicable.

C. Current tax and change in deferred tax:

The provisions for income taxes incurred on earnings for the years ended December 31 are:

| | Years ended December 31, | |
|---------------------------------|--------------------------|---------------------|
| | 2009 | 2008 |
| Current year income tax expense | \$ - | \$ (866,185) |
| Prior year under (over) accrual | <u>255,049</u> | <u>(102,742)</u> |
| Current income taxes incurred | <u>\$ 255,049</u> | <u>\$ (968,927)</u> |

The tax effect of temporary differences that give rise to significant deferred tax assets and deferred tax liabilities is as follows:

| | December 31, | |
|-----------------------------------|-------------------|------------------|
| | 2009 | 2008 |
| Deferred Tax Assets: | | |
| Discount on unpaid losses and LAE | \$ 13,003 | \$ 5,882 |
| 20% of unearned premiums | 469,615 | 82,326 |
| Nonadmitted assets | 48,607 | 164,519 |
| Profit sharing | 46,330 | - |
| Charitable contribution | 23,375 | - |
| Other | <u>195,874</u> | <u>-</u> |
| Total DTAs | 796,804 | 252,727 |
| Nonadmitted DTAs | <u>-</u> | <u>(66,806)</u> |
| Admitted DTAs | <u>796,804</u> | <u>185,921</u> |
| Deferred Tax Liabilities: | | |
| Depreciation of fixed assets | (71,279) | (162,820) |
| Other | <u>(17,129)</u> | <u>(23,101)</u> |
| Total DTLs | <u>(88,408)</u> | <u>(185,921)</u> |
| Net admitted DTAs | <u>\$ 708,396</u> | <u>\$ -</u> |

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

7. Income Taxes (continued)

The change in net deferred income taxes is comprised of the following:

| | December 31, | | |
|---|-------------------|------------------|-------------------|
| | <u>2009</u> | <u>2008</u> | <u>Change</u> |
| Total gross DTAs | \$ 796,804 | \$ 252,727 | \$ 544,077 |
| Total gross DTLs | <u>(88,408)</u> | <u>(185,921)</u> | <u>97,513</u> |
| Net DTA | <u>\$ 708,396</u> | <u>\$ 66,806</u> | 641,590 |
| Deferred tax on change in net unrealized capital gains | | | <u>-</u> |
| Change in net deferred income tax | | | <u>\$ 641,590</u> |

D. Reconciliation of federal income tax rate to actual effective rate:

The significant book-to-tax adjustments were as follows:

| | <u>2009</u> | <u>Percentage of Pre-Tax Income</u> |
|--------------------------------------|---------------------|---|
| | | <u>\$(1,847,906)</u> |
| Provision computed at statutory rate | \$ (628,289) | (34.00)% |
| Nondeductible items | 340 | 0.02 |
| Change in nonadmitted assets | 115,911 | 6.27 |
| Prior period adjustment | <u>125,497</u> | <u>6.79</u> |
| Total | <u>\$ (386,541)</u> | <u>(20.92)%</u> |
| Federal income tax | \$ 255,049 | 13.80 % |
| Change in deferred taxes | <u>(641,590)</u> | <u>(34.72)</u> |
| Statutory income taxes | <u>\$ (386,541)</u> | <u>(20.92)%</u> |

E. Operating loss and tax credit carryforwards and protective tax deposits:

- At December 31, 2009 and 2008, the Company had no unused capital losses and \$576,093 of net operating loss carryforwards available to offset against future taxable income.
- The following is income tax expense that is available for recoupment in the event of future net losses:

| <u>Year</u> | <u>Amount</u> |
|-------------|---------------|
| 2009 | \$ - |
| 2008 | - |

- The Company did not have any protective tax deposits under Section 6603 of the Internal Revenue Code.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

7. Income Taxes (continued)

F. Consolidated federal income tax return:

The Company's federal income tax return is consolidated with the following entities:

HomeWise Holdings, Inc.
HomeWise Preferred Insurance Company
HomeWise Management Company

The method of allocation between the companies is subject to written agreement, approved by the Board of Directors. Allocation is based upon separate return calculations with current credit for net losses. Intercompany balances are settled quarterly.

8. Capital and Surplus

The Company has authorized 1,000,000 shares of \$1 par value common stock, of which 650,000 shares are issued and outstanding at December 31, 2009 and 2008. No other classes of common or preferred shares were issued during 2009 or 2008. The parent company, HHI, is the sole shareholder. In February 2010, HHI made a cash contribution of additional paid-in capital totaling \$13,000,000. The Company received authorization from the Office to report the related capital contribution receivable at December 31, 2009, as an admitted asset in accordance with Statement on Statutory Accounting Principles No. 72, *Surplus and Quasi-reorganizations*.

Property and casualty insurance companies are subject to certain Risk-based Capital (RBC) requirements as specified by the NAIC. Under those requirements, the amount of capital and surplus maintained by a property and casualty insurance company is to be determined based on the various risk factors related to it. The Company is in compliance with the RBC requirements at December 31, 2009 and 2008, respectively.

The maximum amount of dividends that may be paid by property and casualty insurance companies without prior approval of the Office is subject to restrictions relating to statutory surplus and net income. Furthermore, in accordance with the Company's Certificate of Authority Consent Order, during the first three years of operations it may only pay dividends that are approved in advance by the Office. The Company did not declare or pay any dividends during the years ended December 31, 2009 or 2008.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

9. Related Party Transactions

The Company is a wholly-owned subsidiary of HomeWise Holdings, Inc. (HHI) and is affiliated with HomeWise Management Company (HMC) and HomeWise Preferred Insurance Company (HPIC), which are also wholly-owned subsidiaries of HHI.

Effective January 1, 2006, the Company entered into a managing general agency agreement with HMC. Pursuant to the agreement, HMC provides to the Company premium billing, claims management and underwriting functions. During 2009 and 2008, expenses incurred related to this agreement totaled \$10,117,751 and \$3,275,793, respectively. At December 31, 2009 and 2008, the Company has a net receivable due from (payable due to) HMC in the amount of \$641,776 and \$(3,263,021), respectively.

Effective December 5, 2005, the Company entered into a service agreement with HHI. Pursuant to the agreement, HHI provides to the Company capital management services, investor management and relations, and assists with overall general management of the Company. During 2009 and 2008, expenses incurred related to this agreement totaled \$381,802 and \$116,993, respectively. At December 31, 2009 and 2008, the Company has a receivable due from HHI in the amount of \$717,693 and \$519, respectively.

The Company is also party to a Cost Allocation Agreement with HPIC, HMC, and HHI in which expenses benefiting more than one company are allocated based upon direct allocation or revenue allocation rules, whichever is most appropriate for the expenses. At December 31, 2009 and 2008, the Company has a (payable due to) receivable due from HPIC in the amount of \$(333,407) and \$3,972,151, respectively.

The Company reported a capital contribution of \$13,000,000 from HHI in 2009 that was received in February 2010 (see Note 8).

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

10. Premiums Produced by Managing General Agents or Third Party Administrators

The Company uses a managing general agent, HMC, to write and administer insurance products. HMC has contracted with an unaffiliated service company to provide this function. The total premium produced and serviced through the contract during 2009 is summarized below. The Company retains underwriting authority for all policies issued under these agreements.

| <u>Name and Address</u> | <u>FEI Number</u> | <u>Exclusive Contract</u> | <u>Type of Business Written</u> | <u>Type of Authority Granted</u> | <u>Direct Premium Written</u> |
|--|-------------------|---------------------------|---------------------------------|---|-------------------------------|
| HomeWise Management Company, Inc. 18302 Highwoods Preserve Parkway, Suite 110 Tampa, FL 33647 | 20-3395152 | Yes | Homeowners | Premium collection, claims adjustments, binding authority, and underwriting | \$ 38,926,642 |

11. Leases

On May 1, 2006, the Company entered into an operating lease agreement for office space in Tampa, Florida, which is effective June 1, 2006, through May 31, 2011. The Company has the option to renew the term of the lease for an additional five year period at the prevailing rental rate at that time, provided the Company gives the lessor written notice nine months prior to its intent to renew the lease. Expenses associated with this lease are allocated equally between the Company and HPIC.

Approximate future lease payments under this lease are as follows at December 31, 2009:

| | |
|------|-------------------|
| 2010 | \$ 505,131 |
| 2011 | <u>218,697</u> |
| | <u>\$ 723,828</u> |

Total rent expense for the lease was \$274,845 and \$184,969 for the years ended December 31, 2009 and 2008, respectively. The current year rent expense includes \$274,845 of reimbursements received by HPIC for HPIC's share of the lease expense.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

12. Reconciliation of Annual Statement to Audited Financial Statements

Differences exist between amounts reported in the audited statutory financial statements and those reported in the annual statement of the Company for the year ended December 31, 2009, resulting from reclassification of premiums receivable and return premiums payable and rounding. Presented below is a reconciliation of amounts previously reported to the Office and those amounts appearing in the audited statutory financial statements for the year ended December 31, 2009.

| | Audited Financial Statement Amount | Annual Statement Amount | Increase (Decrease) |
|---------------------------|---|--|--------------------------------|
| Total admitted assets | \$ 36,136,562 | \$ 35,632,277 | \$ 504,285 |
| Total liabilities | 15,874,392 | 15,370,107 | 504,285 |
| Total capital and surplus | 20,262,170 | 20,262,170 | - |
| Net loss | 2,102,955 | 2,102,954 | 1 |

13. Subsequent Events

On March 23, 2010, HHI announced that it signed an agreement in principle with 21st Century Holding Company (Nasdaq: TCHC) to sell all of the outstanding shares of the Company and HMC. The agreement in principle also includes a renewal rights agreement to acquire certain insurance policies from HPIC. The proposed transaction is subject to customary definitive documentation, regulatory approval, and completion of satisfactory due diligence by 21st Century Holding Company. The projected closing date for the transaction is on or before June 1, 2010.

Other Financial Information

SUMMARY INVESTMENT SCHEDULE

| Investment Categories | Gross Investment Holdings | | Admitted Assets as Reported in the Annual Statement | |
|--|---------------------------|-----------------|---|-----------------|
| | 1 Amount | 2 Percentage | 3 Amount | 4 Percentage |
| 1. Bonds: | | | | |
| 1.1 U.S. treasury securities: | | 0.0 | | 0.0 |
| 1.2 U.S. government agency obligations (excluding mortgage-backed securities): | | | | |
| 1.21 Issued by U.S. government agencies: | | 0.0 | | 0.0 |
| 1.22 Issued by U.S. government sponsored agencies: | | 0.0 | | 0.0 |
| 1.3 Non-U.S. government (including Canada, excluding mortgage-backed securities): | | 0.0 | | 0.0 |
| 1.4 Securities issued by states, territories and possessions and political subdivisions in the U.S.: | | | | |
| 1.41 States, territories and possessions general obligations: | | 0.0 | | 0.0 |
| 1.42 Political subdivisions of states, territories & possessions & political subdivisions general obligations: | | 0.0 | | 0.0 |
| 1.43 Revenue and assessment obligations: | | 0.0 | | 0.0 |
| 1.44 Industrial development and similar obligations: | | 0.0 | | 0.0 |
| 1.5 Mortgage-backed securities (includes residential and commercial MBS): | | | | |
| 1.51 Pass-through securities: | | | | |
| 1.511 Issued or guaranteed by GNMA: | | 0.0 | | 0.0 |
| 1.512 Issued or guaranteed by FNMA and FHLMC: | | 0.0 | | 0.0 |
| 1.513 All other: | | 0.0 | | 0.0 |
| 1.52 CMOs and REMICs: | | | | |
| 1.521 Issued or guaranteed by GNMA, FNMA, FHLMC or VA: | | 0.0 | | 0.0 |
| 1.522 Issued by non-U.S. Government issuers and collateralized by mortgage-backed securities issued or guaranteed by agencies shown in Line 1.521: | | 0.0 | | 0.0 |
| 1.523 All other: | | 0.0 | | 0.0 |
| 2. Other debt and other fixed income securities (excluding short-term): | | | | |
| 2.1 Unaffiliated domestic securities (includes credit tenant loans and hybrid securities): | | 0.0 | | 0.0 |
| 2.2 Unaffiliated non-U.S. securities (including Canada): | | 0.0 | | 0.0 |
| 2.3 Affiliated securities: | | 0.0 | | 0.0 |
| 3. Equity interests: | | | | |
| 3.1 Investments in mutual funds: | | 0.0 | | 0.0 |
| 3.2 Preferred stocks: | | | | |
| 3.21 Affiliated: | | 0.0 | | 0.0 |
| 3.22 Unaffiliated: | | 0.0 | | 0.0 |
| 3.3 Publicly traded equity securities (excluding preferred stocks): | | | | |
| 3.31 Affiliated: | | 0.0 | | 0.0 |
| 3.32 Unaffiliated: | | 0.0 | | 0.0 |
| 3.4 Other equity securities: | | | | |
| 3.41 Affiliated: | | 0.0 | | 0.0 |
| 3.42 Unaffiliated: | | 0.0 | | 0.0 |
| 3.5 Other equity interests including tangible personal property under lease: | | | | |
| 3.51 Affiliated: | | 0.0 | | 0.0 |
| 3.52 Unaffiliated: | | 0.0 | | 0.0 |
| 4. Mortgage loans: | | | | |
| 4.1 Construction and land development: | | 0.0 | | 0.0 |
| 4.2 Agricultural: | | 0.0 | | 0.0 |
| 4.3 Single family residential properties: | | 0.0 | | 0.0 |
| 4.4 Multifamily residential properties: | | 0.0 | | 0.0 |
| 4.5 Commercial loans: | | 0.0 | | 0.0 |
| 4.6 Mezzanine real estate loans: | | 0.0 | | 0.0 |
| 5. Real estate investments: | | | | |
| 5.1 Property occupied by company: | | 0.0 | | 0.0 |
| 5.2 Property held for production of income (including \$.....0 of property acquired in satisfaction of debt): | | 0.0 | | 0.0 |
| 5.3 Property held for sale (including \$.....0 property acquired in satisfaction of debt): | | 0.0 | | 0.0 |
| 6. Contract loans: | | 0.0 | | 0.0 |
| 7. Receivables for securities: | | 0.0 | | 0.0 |
| 8. Cash, cash equivalents and short-term investments: | | | 13,965,461 | 100.0 |
| 9. Other invested assets: | | 0.0 | | 0.0 |
| 10. Total invested assets: | 0 | 0.0 | 13,965,461 | 100.0 |

SUPPLEMENTAL INVESTMENT RISKS INTERROGATORIES

For the year ended December 31, 2009

(To be filed by April 1)

Of HomeWise Insurance Company

Address (City, State, Zip Code): Tampa FL 33647

NAIC Group Code.....4111

NAIC Company Code.....12438

Employer's ID Number.....20-3395013

The Investment Risks Interrogatories are to be filed by April 1. They are also to be included with the Audited Statutory Financial Statements.

Answer the following interrogatories by reporting the applicable U.S. dollar amounts and percentages of the reporting entity's total admitted assets held in that category of investments.

1. Reporting entity's total admitted assets as reported on Page 2 of this annual statement. \$.....35,632,277

2. Ten largest exposures to a single issuer/borrower/investment.

| | 1 | 2 | 3 | 4 |
|------|-------------------------------------|--|------------------|-------------------------------------|
| | Issuer | Description of Exposure | Amount | Percentage of Total Admitted Assets |
| 2.01 | Federated Investors | Money Market Prime Cash Obligations Fund | \$.....3,449,454 | 9.681 % |
| 2.02 | First American Funds | Govt. Oblig Fd Instl Inv Cl | \$.....2,237,635 | 6.280 % |
| 2.03 | Florida Dept. of Financial Services | Treasury Cash Fund Deposit | \$.....348,755 | 0.979 % |
| 2.04 | Capital One Bank | Certificate of Deposit | \$.....100,000 | 0.281 % |
| 2.05 | | | \$..... | 0.000 % |
| 2.06 | | | \$..... | 0.000 % |
| 2.07 | | | \$..... | 0.000 % |
| 2.08 | | | \$..... | 0.000 % |
| 2.09 | | | \$..... | 0.000 % |
| 2.10 | | | \$..... | 0.000 % |

3. Amounts and percentages of the reporting entity's total admitted assets held in bonds and preferred stocks by NAIC rating.

| | 1 | 2 |
|------|------------------|----------------------------|
| | Bonds | |
| 3.01 | NAIC-1 | \$.....13,714,923 38.490 % |
| 3.02 | NAIC-2 | \$..... 0.000 % |
| 3.03 | NAIC-3 | \$..... 0.000 % |
| 3.04 | NAIC-4 | \$..... 0.000 % |
| 3.05 | NAIC-5 | \$..... 0.000 % |
| 3.06 | NAIC-6 | \$..... 0.000 % |
| | 3 | 4 |
| | Preferred Stocks | |
| 3.07 | PIRP-1 | \$..... 0.000 % |
| 3.08 | PIRP-2 | \$..... 0.000 % |
| 3.09 | PIRP-3 | \$..... 0.000 % |
| 3.10 | PIRP-4 | \$..... 0.000 % |
| 3.11 | PIRP-5 | \$..... 0.000 % |
| 3.12 | PIRP-6 | \$..... 0.000 % |

4. Assets held in foreign investments:

| | | |
|------|--|-----------------|
| 4.01 | Are assets held in foreign investments less than 2.5% of the reporting entity's total admitted assets? | Yes [X] No [] |
| | If response to 4.01 above is yes, responses are not required for interrogatories 5-10. | |
| 4.02 | Total admitted assets held in foreign investments | \$..... 0.000 % |
| 4.03 | Foreign-currency-denominated investments | \$..... 0.000 % |
| 4.04 | Insurance liabilities denominated in that same foreign currency | \$..... 0.000 % |

5. Aggregate foreign investment exposure categorized by NAIC sovereign rating:

| | 1 | 2 |
|------|---------------------------------|-----------------|
| 5.01 | Countries rated NAIC-1 | \$..... 0.000 % |
| 5.02 | Countries rated NAIC-2 | \$..... 0.000 % |
| 5.03 | Countries rated NAIC-3 or below | \$..... 0.000 % |

6. Largest foreign investment exposures by country, categorized by the country's NAIC sovereign rating:

| | 1 | 2 |
|----------------------------------|------------|-----------------|
| Countries rated NAIC-1: | | |
| 6.01 | Country 1: | \$..... 0.000 % |
| 6.02 | Country 2: | \$..... 0.000 % |
| Countries rated NAIC-2: | | |
| 6.03 | Country 1: | \$..... 0.000 % |
| 6.04 | Country 2: | \$..... 0.000 % |
| Countries rated NAIC-3 or below: | | |
| 6.05 | Country 1: | \$..... 0.000 % |
| 6.06 | Country 2: | \$..... 0.000 % |

| | | | | |
|--|---|------------------|-------------|---------|
| | | 1 | 2 | |
| 7. | Aggregate unhedged foreign currency exposure: | \$ | | 0.000 % |
| 8. | Aggregate unhedged foreign currency exposure categorized by NAIC sovereign rating: | 1 | 2 | |
| 8.01 | Countries rated NAIC-1: | \$ | | 0.000 % |
| 8.02 | Countries rated NAIC-2: | \$ | | 0.000 % |
| 8.03 | Countries rated NAIC-3 or below: | \$ | | 0.000 % |
| 9. | Largest unhedged foreign currency exposures by country, categorized by the country's NAIC sovereign rating: | 1 | 2 | |
| Countries rated NAIC-1: | | | | |
| 9.01 | Country 1: | \$ | | 0.000 % |
| 9.02 | Country 2: | \$ | | 0.000 % |
| Countries rated NAIC-2: | | | | |
| 9.03 | Country 1: | \$ | | 0.000 % |
| 9.04 | Country 2: | \$ | | 0.000 % |
| Countries rated NAIC-3 or below: | | | | |
| 9.05 | Country 1: | \$ | | 0.000 % |
| 9.06 | Country 2: | \$ | | 0.000 % |
| 10. | Ten largest non-sovereign (i.e. non-governmental) foreign issues: | 1 | 2 | |
| | | Issuer | NAIC Rating | |
| 10.01 | | | | 0.000 % |
| 10.02 | | | | 0.000 % |
| 10.03 | | | | 0.000 % |
| 10.04 | | | | 0.000 % |
| 10.05 | | | | 0.000 % |
| 10.06 | | | | 0.000 % |
| 10.07 | | | | 0.000 % |
| 10.08 | | | | 0.000 % |
| 10.09 | | | | 0.000 % |
| 10.10 | | | | 0.000 % |
| 11. | Amounts and percentages of the reporting entity's total admitted assets held in Canadian investments and unhedged Canadian currency exposure: | | | |
| 11.01 | Are assets held in Canadian investments less than 2.5% of the reporting entity's total admitted assets? | Yes [X] No [] | | |
| If response to 11.01 is yes, detail is not required for the remainder of Interrogatory 11. | | | | |
| 11.02 | Total admitted assets held in Canadian Investments | \$ | | 0.000 % |
| 11.03 | Canadian currency-denominated investments | \$ | | 0.000 % |
| 11.04 | Canadian-denominated insurance liabilities | \$ | | 0.000 % |
| 11.05 | Unhedged Canadian currency exposure | \$ | | 0.000 % |
| 12. | Report aggregate amounts and percentages of the reporting entity's total admitted assets held in investments with contractual sales restrictions. | | | |
| 12.01 | Are assets held in investments with contractual sales restrictions less than 2.5% of the reporting entity's total admitted assets? | Yes [X] No [] | | |
| If response to 12.01 is yes, responses are not required for the remainder of Interrogatory 12. | | | | |
| | | 1 | 2 | 3 |
| 12.02 | Aggregate statement value of investments with contractual sales restrictions: | \$ | | 0.000 % |
| Largest three investments with contractual sales restrictions: | | | | |
| 12.03 | | \$ | | 0.000 % |
| 12.04 | | \$ | | 0.000 % |
| 12.05 | | \$ | | 0.000 % |
| 13. | Amounts and percentages of admitted assets held in the ten largest equity interests: | | | |
| 13.01 | Are assets held in equity interest less than 2.5% of the reporting entity's total admitted assets? | Yes [X] No [] | | |
| If response to 13.01 above is yes, responses are not required for the remainder of Interrogatory 13. | | | | |
| | | 1 | 2 | 3 |
| Name of Issuer | | | | |
| 13.02 | | \$ | | 0.000 % |
| 13.03 | | \$ | | 0.000 % |
| 13.04 | | \$ | | 0.000 % |
| 13.05 | | \$ | | 0.000 % |
| 13.06 | | \$ | | 0.000 % |
| 13.07 | | \$ | | 0.000 % |
| 13.08 | | \$ | | 0.000 % |
| 13.09 | | \$ | | 0.000 % |
| 13.10 | | \$ | | 0.000 % |
| 13.11 | | \$ | | 0.000 % |

14. Amounts and percentages of the reporting entity's total admitted assets held in nonaffiliated, privately placed equities:

14.01 Are assets held in nonaffiliated, privately placed equities less than 2.5% of the reporting entity's total admitted assets?

Yes ☒ No ☐

If response to 14.01 above is yes, responses are not required for the remainder of Interrogatory 14.

| 1 | 2 | 3 |
|--|----|---------|
| 14.02 Aggregate statement value of investments held in nonaffiliated, privately placed equities: | \$ | 0.000 % |
| Largest three investments held in nonaffiliated, privately placed equities: | | |
| 14.03 | \$ | 0.000 % |
| 14.04 | \$ | 0.000 % |
| 14.05 | \$ | 0.000 % |

15. Amounts and percentages of the reporting entity's total admitted assets held in general partnership interests:

15.01 Are assets held in general partnership interests less than 2.5% of the reporting entity's total admitted assets?

Yes ☒ No ☐

If response to 15.01 above is yes, responses are not required for the remainder of Interrogatory 15.

| 1 | 2 | 3 |
|---|----|---------|
| 15.02 Aggregate statement value of investments held in general partnership interests: | \$ | 0.000 % |
| Largest three investments in general partnership interests: | | |
| 15.03 | \$ | 0.000 % |
| 15.04 | \$ | 0.000 % |
| 15.05 | \$ | 0.000 % |

16. Amounts and percentages of the reporting entity's total admitted assets held in mortgage loans:

16.01 Are mortgage loans reported in Schedule B less than 2.5% of the reporting entity's total admitted assets?

Yes ☒ No ☐

If response to 16.01 above is yes, responses are not required for the remainder of Interrogatory 16 and Interrogatory 17.

| 1 | 2 | 3 |
|--|----|---------|
| Type (Residential, Commercial, Agricultural) | | |
| 16.02 | \$ | 0.000 % |
| 16.03 | \$ | 0.000 % |
| 16.04 | \$ | 0.000 % |
| 16.05 | \$ | 0.000 % |
| 16.06 | \$ | 0.000 % |
| 16.07 | \$ | 0.000 % |
| 16.08 | \$ | 0.000 % |
| 16.09 | \$ | 0.000 % |
| 16.10 | \$ | 0.000 % |
| 16.11 | \$ | 0.000 % |

Amount and percentage of the reporting entity's total admitted assets held in the following categories of mortgage loans:

| | Loans | |
|--|-------|---------|
| 16.12 Construction loans | \$ | 0.000 % |
| 16.13 Mortgage loans over 90 days past due | \$ | 0.000 % |
| 16.14 Mortgage loans in the process of foreclosure | \$ | 0.000 % |
| 16.15 Mortgage loans foreclosed | \$ | 0.000 % |
| 16.16 Restructured mortgage loans | \$ | 0.000 % |

17. Aggregate mortgage loans having the following loan-to-value ratios as determined from the most current appraisal as of the annual statement date:

| Statement Case: | | | | | | |
|------------------|-------------|---------|------------|---------|--------------|---------|
| Loan-to-Value | Residential | | Commercial | | Agricultural | |
| | 1 | 2 | 3 | 4 | 5 | 6 |
| 17.01 above 95% | \$ | 0.000 % | \$ | 0.000 % | \$ | 0.000 % |
| 17.02 91% to 95% | \$ | 0.000 % | \$ | 0.000 % | \$ | 0.000 % |
| 17.03 81% to 90% | \$ | 0.000 % | \$ | 0.000 % | \$ | 0.000 % |
| 17.04 71% to 80% | \$ | 0.000 % | \$ | 0.000 % | \$ | 0.000 % |
| 17.05 below 70% | \$ | 0.000 % | \$ | 0.000 % | \$ | 0.000 % |

18. Amounts and percentages of the reporting entity's total admitted assets held in each of the five largest investments in real estate:

18.01 Are assets held in real estate reported less than 2.5% of the reporting entity's total admitted assets?

Yes ☒ No ☐

If response to 18.01 above is yes, responses are not required for the remainder of Interrogatory 18.

Largest five investments in any one parcel or group of contiguous parcels of real estate.

| Description | 2 | 3 |
|-------------|----|---------|
| 18.02 | \$ | 0.000 % |
| 18.03 | \$ | 0.000 % |
| 18.04 | \$ | 0.000 % |
| 18.05 | \$ | 0.000 % |
| 18.06 | \$ | 0.000 % |

19. Report aggregate amounts and percentages of the reporting entity's total admitted assets held in investments held in mezzanine real estate loans.

19.01 Are assets held in investments held in mezzanine real estate loans less than 2.5% of the reporting entity's admitted assets?

Yes ☒ No ☐

If response to 19.01 is yes, responses are not required for the remainder of Interrogatory 19.

| 1 | 2 | 3 |
|---|----|---------|
| 19.02 Aggregate statement value of investments held in mezzanine real estate loans: | \$ | 0.000 % |
| Largest three investments held in mezzanine real estate loans: | | |
| 19.03 | \$ | 0.000 % |
| 19.04 | \$ | 0.000 % |
| 19.05 | \$ | 0.000 % |

20. Amounts and percentages of the reporting entity's total admitted assets subject to the following types of agreements:

| | <u>At Year-End</u> | | <u>1st Qtr</u> | <u>At End of Each Quarter</u> | |
|--|--------------------|---------|----------------|-------------------------------|---------|
| | 1 | 2 | | 2nd Qtr | 3rd Qtr |
| | | | 3 | 4 | 5 |
| 20.01 Securities lending agreements (do not include assets held as collateral for such transactions) | \$ | 0.000 % | \$ | \$ | \$ |
| 20.02 Repurchase agreements | \$ | 0.000 % | \$ | \$ | \$ |
| 20.03 Reverse repurchase agreements | \$ | 0.000 % | \$ | \$ | \$ |
| 20.04 Dollar repurchase agreements | \$ | 0.000 % | \$ | \$ | \$ |
| 20.05 Dollar reverse repurchase agreements | \$ | 0.000 % | \$ | \$ | \$ |

21. Amounts and percentages of the reporting entity's total admitted assets for warrants not attached to other financial instruments, options, caps and floors:

| | <u>Owned</u> | | | <u>Written</u> | |
|-------------------------|--------------|---------|----|----------------|---------|
| | 1 | 2 | | 3 | 4 |
| 21.01 Hedging | \$ | 0.000 % | \$ | \$ | 0.000 % |
| 21.02 Income generation | \$ | 0.000 % | \$ | \$ | 0.000 % |
| 21.03 Other | \$ | 0.000 % | \$ | \$ | 0.000 % |

22. Amounts and percentages of the reporting entity's total admitted assets of potential exposure for collars, swaps, and forwards:

| | <u>At Year-End</u> | | <u>1st Qtr</u> | <u>At End of Each Quarter</u> | |
|-------------------------|--------------------|---------|----------------|-------------------------------|---------|
| | 1 | 2 | | 2nd Qtr | 3rd Qtr |
| | | | 3 | 4 | 5 |
| 22.01 Hedging | \$ | 0.000 % | \$ | \$ | \$ |
| 22.02 Income generation | \$ | 0.000 % | \$ | \$ | \$ |
| 22.03 Replications | \$ | 0.000 % | \$ | \$ | \$ |
| 22.04 Other | \$ | 0.000 % | \$ | \$ | \$ |

23. Amounts and percentages of the reporting entity's total admitted assets of potential exposure for futures contracts:

| | <u>At Year-End</u> | | <u>1st Qtr</u> | <u>At End of Each Quarter</u> | |
|-------------------------|--------------------|---------|----------------|-------------------------------|---------|
| | 1 | 2 | | 2nd Qtr | 3rd Qtr |
| | | | 3 | 4 | 5 |
| 23.01 Hedging | \$ | 0.000 % | \$ | \$ | \$ |
| 23.02 Income generation | \$ | 0.000 % | \$ | \$ | \$ |
| 23.03 Replications | \$ | 0.000 % | \$ | \$ | \$ |
| 23.04 Other | \$ | 0.000 % | \$ | \$ | \$ |

See report of independent auditors.

HomeWise Insurance Company

Selected General Interrogatories Relating to Reinsurance

December 31, 2009

- 7.1 Has the reporting entity reinsured any risk with any other entity under a quota share reinsurance contract that includes a provision that would limit the reinsurer's losses below the stated quota share percentage (e.g., a deductible, a loss ratio corridor, a loss cap, an aggregate limit or any similar provisions)? Yes ☒ No ☐
- 7.2 If yes, indicate the number of reinsurance contracts containing such provisions.....3
- 7.3 If yes, does the amount of reinsurance credit taken reflect the reduction in quota share coverage caused by any applicable limiting provision(s)? Yes ☒ No ☐
- 9.1 Has the reporting entity ceded any risk under any reinsurance contract (or under multiple contracts with the same reinsurer or its affiliates) for which during the period covered by the statement: (i) it recorded a positive or negative underwriting result greater than 5% of prior year-end surplus as regards policyholders or it reported calendar year written premium ceded or year-end loss and loss expense reserves ceded greater than 5% of prior year-end surplus as regards policyholders; (ii) it accounted for that contract as reinsurance and not as a deposit; and (iii) the contract(s) contain one or more of the following features or other features that would have similar results:
- (a) A contract term longer than two years and the contract is noncancellable by the reporting entity during the contract term;
 - (b) A limited or conditional cancellation provision under which cancellation triggers an obligation by the reporting entity, or an affiliate of the reporting entity, to enter into a new reinsurance contract with the reinsurer, or an affiliate of the reinsurer;
 - (c) Aggregate stop loss reinsurance coverage;
 - (d) A unilateral right by either party to commute the reinsurance contract, whether conditional or not, except for such provisions which are only triggered by a decline in the credit status of the other party;
 - (e) A provision permitting reporting of losses, or payment of losses, less frequently than on a quarterly basis (unless there is no activity during the period); or
 - (f) Payment schedule, accumulating retentions from multiple years or any feature inherently designed to delay timing of the reimbursement to the ceding entity..... Yes ☐ No ☒
- 9.2 Has the reporting entity during the period covered by the statement ceded any risk under any reinsurance contract (or under multiple contracts with the same reinsurer or its affiliates), for which, during the period covered by the statement, it recorded a positive or negative underwriting result greater than 5% of prior year-end surplus as regards policyholders or it reported calendar year premium ceded or year-end loss and loss expense reserves ceded greater than 5% of prior year-end surplus as regards policyholders; excluding cessions to approved pooling agreements or to captive insurance companies that are directly or indirectly controlling, controlled by, or under common control with (i) one or more unaffiliated policyholders of the reporting entity, or (ii) an association of which one or more unaffiliated policyholders of the reporting entity is a member, where:
- (a) The written premium ceded to the reinsurer by the reporting entity or its affiliates represents fifty percent (50%) or more of the entire direct and assumed premium written by the reinsurer based on its most recently available financial statement; or
 - (b) Twenty-five percent (25%) or more of the written premium ceded to the reinsurer has been retroceded back to the reporting entity or its affiliates in a separate reinsurance contract? Yes ☐ No ☒

HomeWise Insurance Company

Selected General Interrogatories Relating to Reinsurance

- 9.3 If yes to 9.1 or 9.2, please provide the following information in the Reinsurance Summary Supplemental Filing for General Interrogatory 9:
- (a) The aggregate financial statement impact gross of all such ceded reinsurance contracts on the balance sheet and statement of income;
 - (b) A summary of the reinsurance contract terms and indicate whether it applies to the contracts meeting the criteria in 9.1 or 9.2; and
 - (c) A brief discussion of management's principle objectives in entering into the reinsurance contract including the economic purpose to be achieved.
- 9.4 Except for transactions meeting the requirements of paragraph 31 of SSAP No. 62, *Property and Casualty Reinsurance*, has the reporting entity ceded any risk under any reinsurance contract (or multiple contracts with the same reinsurer or its affiliates) during the period covered by the financial statement, and either:
- (a) Accounted for that contract as reinsurance (either prospective or retroactive) under statutory accounting principles (SAP) and as a deposit under generally accepted accounting principles (GAAP); or
 - (b) Accounted for that contract as reinsurance under GAAP and as a deposit under SAP?..... Yes ☐ No ☒
- 9.5 If yes to 9.4, explain in the Reinsurance Summary Supplemental Filing for General Interrogatory 9 (Section D) why the contract(s) is treated different for GAAP and SAP.

See report of independent auditors.

Statutory Basis Financial Statements
and Other Financial Information

HomeWise Insurance Company

*Years ended December 31, 2010 and 2009
with Report of Independent Auditors*

Thomas Howell
 Ferguson P.A.

HomeWise Insurance Company
Statutory Basis Financial Statements
and Other Financial Information
Years ended December 31, 2010 and 2009

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Report of Independent Auditors

The Board of Directors
HomeWise Insurance Company

We have audited the accompanying statements of admitted assets, liabilities, and capital and surplus - statutory basis of HomeWise Insurance Company (the Company) as of December 31, 2010 and 2009, and the related statutory basis statements of operations, changes in capital and surplus, and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As described more fully in Note 1 to the financial statements, these financial statements have been prepared in conformity with accounting practices prescribed or permitted by the Florida Office of Insurance Regulation, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the admitted assets, liabilities and capital and surplus of HomeWise Insurance Company as of December 31, 2010 and 2009, and the results of its operations and its cash flows for the years then ended on the basis of accounting described in Note 1.

Thomas Howell
Ferguson, C.P.A.

Page Two

Our audits were conducted for the purpose of forming an opinion on the statutory basis financial statements taken as a whole. The summary investment schedule (Schedule 1), supplemental investment risks interrogatories (Schedule 2), and the selected general interrogatories relating to reinsurance (Schedule 3) included in other financial information as of and for the year ended December 31, 2010, are presented to comply with the National Association of Insurance Commissioners' *Accounting Practices and Procedures Manual* and are not a required part of the statutory basis financial statements. The additional information has been subjected to the auditing procedures applied in the audits of the statutory basis financial statements and, in our opinion, is fairly stated in all material respects in relation to the statutory basis financial statements taken as a whole.

This report is intended solely for the use of the Board of Directors and management of HomeWise Insurance Company and for filing with the Florida Office of Insurance Regulation and is not intended to be and should not be used by anyone other than these specified parties.

Thomas Howell Ferguson C.P.A.

April 5, 2011

HomeWise Insurance Company

Statements of Admitted Assets, Liabilities, and Capital and Surplus - Statutory Basis

| | December 31, | |
|--|----------------------|----------------------|
| | <u>2010</u> | <u>2009</u> |
| Admitted assets | | |
| Cash and invested assets: | | |
| Short-term investments | \$ 12,485,943 | \$ 5,687,089 |
| Cash and cash equivalents | <u>2,651,494</u> | <u>8,298,372</u> |
| Total cash and invested assets | 15,137,437 | 13,985,461 |
| Accrued investment income | 3,232 | 11,924 |
| Premiums receivable | 15,236,676 | 6,409,016 |
| Reinsurance balances recoverable | 5,246,644 | 365,365 |
| Federal income taxes recoverable | 118 | 118 |
| Net deferred tax asset | 1,111,649 | 708,396 |
| Receivables from parent and affiliates | 9,117,855 | 1,359,469 |
| Capital contribution receivable | - | 13,000,000 |
| Other assets | <u>2,839,305</u> | <u>296,813</u> |
| Total admitted assets | <u>\$ 48,692,916</u> | <u>\$ 36,136,562</u> |
| Liabilities and capital and surplus | | |
| Liabilities: | | |
| Loss and loss adjustment expense reserves | \$ 7,396,674 | \$ 574,123 |
| Unearned premiums, net | 4,664,895 | 6,906,109 |
| Reinsurance premiums payable | 9,688,931 | 6,499,800 |
| Provision for reinsurance | - | 80,000 |
| Accounts payable and accrued expenses | 849,318 | 453,552 |
| Taxes, licenses, and fees payable | 2,038,715 | 523,116 |
| Return premiums payable | - | 504,285 |
| Payable to affiliates | <u>5,254,595</u> | <u>333,407</u> |
| Total liabilities | 29,893,128 | 15,874,392 |
| Capital and surplus | <u>18,799,788</u> | <u>20,262,170</u> |
| Total liabilities and capital and surplus | <u>\$ 48,692,916</u> | <u>\$ 36,136,562</u> |

See accompanying notes.

HomeWise Insurance Company
Statements of Operations - Statutory Basis

| | <u>Years ended</u> <u>2010</u> | <u>December 31,</u> <u>2009</u> |
|---|-----------------------------------|------------------------------------|
| Underwriting income: | | |
| Premiums earned, net of reinsurance ceded | \$ 15,363,099 | \$ 4,555,001 |
| Underwriting expenses: | | |
| Losses and loss adjustment expenses incurred | 14,873,129 | 1,228,091 |
| Underwriting, acquisition, and other expenses | <u>2,940,725</u> | <u>5,273,642</u> |
| Total underwriting expenses | <u>17,813,854</u> | <u>6,501,733</u> |
| Net underwriting loss | (2,450,755) | (1,946,732) |
| Net investment income | 15,502 | 5,110 |
| Other income | <u>402,846</u> | <u>93,716</u> |
| Loss before federal income tax expense | (2,032,407) | (1,847,906) |
| Federal income tax expense | <u>-</u> | <u>255,049</u> |
| Net loss | <u>\$ (2,032,407)</u> | <u>\$ (2,102,955)</u> |

See accompanying notes.

HomeWise Insurance Company

Statements of Changes in Capital and Surplus - Statutory Basis

Years ended December 31, 2010 and 2009

| | Common Stock | | Gross Paid-in and Contributed | | Unassigned Funds | | Total |
|-------------------------------------|--------------|------------|-------------------------------|----|------------------|----|-------------|
| | Shares | Par Value | Surplus | | Funds | | |
| Balance as of December 31, 2008 | 650,000 | \$ 650,000 | \$ 8,850,000 | \$ | (1,104,186) | \$ | 8,395,814 |
| Capital contributions | - | - | 13,000,000 | | - | | 13,000,000 |
| Change in deferred income taxes | - | - | - | | 641,590 | | 641,590 |
| Change in nonadmitted assets | - | - | - | | 407,721 | | 407,721 |
| Change in provision for reinsurance | - | - | - | | (80,000) | | (80,000) |
| Net loss | - | - | - | | (2,102,955) | | (2,102,955) |
| Balance as of December 31, 2009 | 650,000 | 650,000 | 21,850,000 | | (2,237,830) | | 20,262,170 |
| Change in deferred income taxes | - | - | - | | 672,965 | | 672,965 |
| Change in nonadmitted assets | - | - | - | | (182,940) | | (182,940) |
| Change in provision for reinsurance | - | - | - | | 80,000 | | 80,000 |
| Net loss | - | - | - | | (2,032,407) | | (2,032,407) |
| Balance as of December 31, 2010 | 650,000 | \$ 650,000 | \$ 21,850,000 | \$ | (3,700,212) | \$ | 18,799,788 |

See accompanying notes.

HomeWise Insurance Company

Statements of Cash Flows - Statutory Basis

| | Years ended 2010 | December 31, 2009 |
|---|----------------------|----------------------|
| Operating activities | | |
| Premiums collected, net of reinsurance | \$ 6,977,566 | \$ 10,456,308 |
| Net investment income received | 24,194 | 948 |
| Other income received | 377,246 | 81,442 |
| Losses and loss adjustment expenses (paid) recovered | (12,931,857) | 176,706 |
| Underwriting, acquisition, and other expenses paid | (1,451,828) | (4,602,173) |
| Federal income taxes recovered | - | 1,374,039 |
| Net cash (used in) provided by operating activities | <u>(7,004,679)</u> | <u>7,487,270</u> |
| Financing activities | | |
| Capital contributions received | 13,000,000 | - |
| Other miscellaneous (uses) sources | <u>(4,843,345)</u> | <u>452,017</u> |
| Net cash provided by financing activities | <u>8,156,655</u> | <u>452,017</u> |
| Net increase in cash | 1,151,976 | 7,939,287 |
| Cash at beginning of year | <u>13,985,461</u> | <u>6,046,174</u> |
| Cash at end of year | <u>\$ 15,137,437</u> | <u>\$ 13,985,461</u> |
| Cash consists of the following: | | |
| Cash and cash equivalents | \$ 2,651,494 | \$ 8,298,372 |
| Short-term investments | <u>12,485,943</u> | <u>5,687,089</u> |
| | <u>\$ 15,137,437</u> | <u>\$ 13,985,461</u> |

See accompanying notes.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

Years ended December 31, 2010 and 2009

1. Summary of Significant Accounting Policies

Organization and Description of Company

HomeWise Insurance Company (the Company), a wholly-owned subsidiary of HomeWise Holdings, Inc. (HHI), an insurance holding company, is domiciled in the state of Florida. The Company received its Certificate of Authority from the Florida Office of Insurance Regulation (the Office) on December 5, 2005, and commenced operations on January 12, 2006. The Company received a Certificate of Authority from the state of Louisiana on August 6, 2008, and commenced operations on November 25, 2008. The Company is affiliated with HomeWise Management Company (HMC) and HomeWise Preferred Insurance Company (HPIC), which are wholly-owned subsidiaries of HHI.

The Company writes coverage exclusively in the states of Florida and Louisiana, areas that are exposed to damage from hurricanes and severe storms. The Company attempts to mitigate its exposure to losses from storms by purchasing quota share and catastrophe reinsurance coverage. However, such a storm, depending on its path and severity, could result in losses to the Company exceeding its reinsurance protection and could have a material adverse effect on the financial condition and results of operations of the Company.

Basis of Presentation

The accompanying statutory basis financial statements have been prepared in accordance with statutory accounting practices (SAP) prescribed or permitted by the Florida Office of Insurance Regulation (the Office). Such statutory practices require preparation of the financial statements in accordance with the National Association of Insurance Commissioners' (NAIC) *Accounting Practices and Procedures Manual* subject to deviations prescribed by the Office. SAP is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America (GAAP). Such practices vary in certain respects from those under GAAP. The Company's significant accounting practices and the variances from GAAP are summarized below:

- Certain assets designated as "nonadmitted," principally past-due uncollected premiums, prepaid expenses, and other assets not specifically identified as an admitted asset within the *Accounting Practices and Procedures Manual*, are excluded from the accompanying statements of admitted assets, liabilities, and capital and surplus and are charged directly to unassigned surplus. Under GAAP, such assets would be included in the balance sheet at net realizable values.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

1. Summary of Significant Accounting Policies (continued)

Basis of Presentation (continued)

- Loss and loss adjustment expense reserves and unearned premiums ceded to reinsurers have been reported as reductions of the related liabilities rather than as assets as would be required under GAAP.
- Cash in the statements of cash flows represents cash, cash equivalents, and short-term investments with remaining maturities of one year or less. Under GAAP, the corresponding caption of cash and cash equivalents would include cash balances and investments with initial maturities of three months or less.
- The costs of acquiring and renewing business are expensed when incurred. Under GAAP, such costs, to the extent recoverable, would be deferred and amortized over the effective period of the related insurance policies.
- Deferred tax assets are limited to 1) the amount of federal income taxes paid in prior years that can be recovered through loss carrybacks for existing temporary differences that reverse by the end of the subsequent calendar year, plus 2) the lesser of the remaining gross deferred tax assets expected to be realized within one year of the financial statement date or 10% of capital and surplus excluding any net deferred tax assets, electronic data processing (EDP) equipment and operating software and any net positive goodwill, plus 3) the amount of remaining gross deferred tax assets that can be offset against existing gross deferred tax liabilities. The remaining deferred tax assets are nonadmitted. Beginning in 2009, gross deferred income tax assets are reduced by a valuation allowance if the Company determines it is more likely than not that some portion or all of the gross deferred tax assets will not be realized. Deferred taxes do not include amounts for state income taxes. Under GAAP, state income taxes would be included in the computation of deferred taxes, a deferred tax asset would be recorded for the amount of gross deferred tax assets expected to be realized in future years, and a valuation allowance would be established for deferred tax assets not realizable.
- Commissions allowed by reinsurers on business ceded are reported as a reduction of expense when incurred to the extent the amount does not exceed actual acquisition costs, rather than being deferred and amortized with deferred policy acquisition costs as would be required by GAAP. Commissions in excess of the acquisition costs, if any, would be deferred and recognized over the policy term consistent with GAAP.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

1. Summary of Significant Accounting Policies (continued)

Basis of Presentation (continued)

- A provision for reinsurance is recorded as a liability and the change between years is recorded as a gain or loss directly to unassigned surplus. This provision is determined in accordance with NAIC Annual Statement instructions and generally provides for a reserve for uncollectible reinsurance.
- Certain other reported amounts are classified or presented differently in the financial statements prepared on the basis of SAP than they would be under GAAP. Statutory requirements require that the financial statements of the Company be filed with state regulatory authorities. Accordingly, the financial statements are presented in a format similar to the filed annual statement, which differs from the format of financial statements presented under GAAP. Required statutory disclosures that are not applicable to the Company are not included in the notes to these statutory financial statements.

Other significant accounting practices are as follows:

Recognition of Premium Revenues

Premiums are recorded as earned on a daily pro rata basis over the contract period that the related policies are expected to be in force. The portion of premiums not earned at the end of the year is recorded as unearned premiums. Premiums collected prior to the effective date of the policy are recorded as a liability.

Cash and Cash Equivalents

Cash and cash equivalents include demand deposits with several financial institutions and other highly liquid investments with original maturities of three months or less and certificates of deposit with original maturities of one year or less and are principally stated at cost, which approximates fair value.

Investments

Investments are recorded at admitted asset values as prescribed by the valuation procedures of the NAIC's Securities Valuation Office (SVO). The valuation technique used to measure fair value (market value) is to obtain the published securities' fair value from the SVO publication, *Valuation of Securities*. If the specific security is not listed in this publication, then the fair value is obtained from a registered U.S. exchange.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

1. Summary of Significant Accounting Policies (continued)

Investments (continued)

Short-term investments include investments with original maturities of one year or less from the time of acquisition and are principally stated at cost, which approximates fair value.

Concentration of Credit Risk

The Company's financial instruments exposed to concentrations of credit risk consist primarily of its cash and cash equivalents, short-term investments, reinsurance recoveries, and premium revenue. The Company maintains its cash and cash equivalents at several financial institutions. Deposits with financial institutions are insured by the Federal Deposit Insurance Corporation (FDIC) up to \$250,000 per depositor. Bank deposit accounts, at times, may exceed federally insured limits. The Company has not experienced any losses in such accounts.

All investment transactions have credit exposure to the extent that a counterparty may default on an obligation to the Company. Credit risk is a consequence of carrying investment positions. To manage credit risk, the Company focuses primarily on highly liquid debt instruments, reviews the credit strength of all entities in which it invests, limits its exposure in any one investment, and monitors portfolio quality, taking into account credit ratings assigned by recognized credit rating organizations.

Reinsurance

The accompanying statutory basis financial statements reflect reserves for premiums and losses and loss adjustment expenses (LAE), net of reinsurance ceded (see Note 6). Those reinsurance arrangements allow management to control exposure to potential losses arising from large risks and catastrophic events. A significant portion of the reinsurance is effected under a quota share reinsurance agreement. Amounts recoverable from reinsurers are estimated in a manner consistent with the loss and LAE reserves associated with the reinsured policies. Reinsurance premiums, losses, and LAE are accounted for on bases consistent with those used in accounting for the original policies issued and the terms of the reinsurance contracts.

Loss and Loss Adjustment Expense (LAE) Reserves

Loss and LAE reserves represent the estimated ultimate net cost of all unpaid reported and unreported losses and LAE. The reserves for unpaid losses and LAE are estimated using individual case-basis estimates for reported losses and actuarial estimates for losses incurred but not yet reported. Those estimates are subject to the effects of trends in loss severity and frequency. Although considerable variability is inherent in such estimates, management believes that the reserves for losses and LAE are adequate. The estimates are continually reviewed and adjusted as necessary as experience develops or new information becomes known; such adjustments are included in current operations. The ultimate settlement of losses and LAE may vary significantly from the estimated amounts included in the financial statements. The Company does not discount its loss and LAE reserves.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

1. Summary of Significant Accounting Policies (continued)

Loss and Loss Adjustment Expense (LAE) Reserves (continued)

The anticipated effect of inflation is implicitly considered when estimating liabilities for losses and LAE. While anticipated price increases due to inflation are considered in estimating the ultimate claim costs, the increase in average severities of claims is caused by a number of factors that vary with the individual type of policy written. Future average severities are projected based on historical trends adjusted for implemented changes in underwriting standards, policy provisions, and general economic trends. Those anticipated trends are monitored based on actual development and the estimated liabilities are modified if necessary.

Loss and LAE reserves are reported net of reinsurance recoverables for unpaid losses and LAE. Losses and LAE ceded through reinsurance are credited against losses and LAE incurred.

Guaranty Fund and Residual Market Pool Assessments

The Company is subject to assessments by a Florida guaranty fund, a residual market pool, and a state catastrophe reinsurance pool. The activities of this fund and these pools include collecting funds from solvent insurance companies to cover losses resulting from the insolvency or rehabilitation of other insurance companies or deficits generated by Florida Insurance Guaranty Association (FIGA), Citizens Property Insurance Corporation (Citizens), and the Florida Hurricane Catastrophe Fund (FHCF).

The Company's policy is to recognize its obligation for guaranty fund, Citizens, and FHCF assessments when the Company has the information available to reasonably estimate its liabilities. Guaranty fund, Citizens, and FHCF assessments are generally available for recoupment from policyholders and as such, amounts assessed are recorded as a recoverable asset. Amounts recoverable are generally expected to be collected during the year following assessment.

The Company was assessed \$95,153 by FIGA in 2009 (none in 2010). The FIGA assessment recoverable from policyholders, including amounts acquired from HPIC (see Note 9), was \$945,234 and \$95,153 at December 31, 2010 and 2009, respectively.

Certain Citizens and FHCF assessments are collected from policyholders as policies are written and subsequently remitted to the assessing entity. Amounts due from policyholders for these assessments were \$248,396 and \$105,999 at December 31, 2010 and 2009, respectively. The liability for assessments collected but not remitted to Citizens and FHCF totaled \$706,972 and \$294,763 at December 31, 2010 and 2009, respectively.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

1. Summary of Significant Accounting Policies (continued)

Income Taxes

The Company calculates its state and federal income tax liabilities based upon the statutory rates in effect during the year.

Subsequent Events

The Company has evaluated subsequent events through April 5, 2011, the date the financial statements were available to be issued. During the period from December 31, 2010 to April 5, 2011, the Company did not have any material recognizable subsequent events other than the proposed merger described in Note 13.

Use of Estimates

The preparation of statutory basis financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the statutory basis financial statements, and the reported amounts of revenues and expenses during the reporting period. Such estimates and assumptions could change in the future as more information becomes known, which could impact the amounts reported and described in the financial statements.

2. Regulatory Requirements and Restrictions

Florida Statute 624.408 requires the Company to maintain capital and surplus of \$4 million or 10% of the Company's total liabilities for losses, loss adjustment expenses, and unearned premiums, whichever is greater, and to meet the risk-based capital requirements as discussed in Note 8. Additionally, Florida Statute 624.4095 requires the Company to maintain a ratio of the product of written premiums times 0.90 to surplus of no greater than 10-to-1 for gross written premiums and 4-to-1 for net written premiums. The Company is in compliance with these requirements.

Additionally, the Company is required to maintain deposits pursuant to Florida and Louisiana statutes to help secure the payment of claims. Cash on deposit in the amount of \$359,861 and \$348,756 has been assigned to the Office as of December 31, 2010 and 2009, respectively, and a certificate of deposit in the amount of \$100,000 has been assigned to the Louisiana Department of Insurance as of December 31, 2010 and 2009, to satisfy this requirement. These amounts are included in cash and cash equivalents in the accompanying statements of admitted assets, liabilities, and capital and surplus at December 31, 2010 and 2009.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

3. Investments

Short-term investments consist of money market funds that have a maturity of one year or less from the date of purchase and are stated at cost, which approximates fair value.

Major categories of the Company's net investment income are summarized as follows:

| | Years ended December 31, | |
|---------------------------|--------------------------|-----------------|
| | 2010 | 2009 |
| Investment income: | | |
| Cash and cash equivalents | \$ 14,902 | \$ 15,810 |
| Short-term investments | <u>28,434</u> | <u>16,760</u> |
| Total investment income | 43,336 | 32,570 |
| Investment expense: | | |
| Bank fees | <u>(27,834)</u> | <u>(27,460)</u> |
| Net investment income | <u>\$ 15,502</u> | <u>\$ 5,110</u> |

4. Premiums Receivable

Premiums receivable includes amounts due from HomeWise Management Company, the Company's managing general agent (MGA), who collects all premiums and remits them to the Company. The Company nonadmits balances due from insureds and deferred installments for which a portion of the receivable is more than 90 days past due and exceeds the related unearned premium. Premiums receivable is charged to bad debt expense in the period determined uncollectible. Recoveries received on amounts previously charged-off are credited to bad debt expense in the period received. Premiums receivable at December 31, 2010 and 2009, totaled \$15,236,676 and \$6,409,016, respectively, net of \$1,505 of nonadmitted premiums receivable, as of December 31, 2010 (none in 2009).

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

5. Loss and Loss Adjustment Expense (LAE) Reserves

The following table provides a reconciliation of the beginning and ending reserve balances for losses and LAE, net of reinsurance recoverables.

| | December 31, | |
|--|-----------------------|---------------|
| | 2010 | 2009 |
| | <i>(in thousands)</i> | |
| Loss and LAE reserves at beginning of year | \$ 574 | \$ 211 |
| Losses and LAE incurred related to: | | |
| Current year | 13,644 | 1,413 |
| Prior years | <u>1,229</u> | <u>(185)</u> |
| | 14,873 | 1,228 |
| Losses and LAE paid related to: | | |
| Current year | 6,808 | 841 |
| Prior years | <u>1,242</u> | <u>24</u> |
| | 8,050 | 865 |
| Loss and LAE reserves at end of year | <u>\$ 7,397</u> | <u>\$ 574</u> |

Anticipated reinsurance recoverables on unpaid losses and LAE are approximately \$2,872,000 and \$1,399,000 at December 31, 2010 and 2009, respectively. Reinsurance recoverables on paid losses and LAE are approximately \$5,247,000 and \$365,000 at December 31, 2010 and 2009, respectively.

Net incurred losses and LAE attributable to insured events of prior years have increased (decreased) \$1,229,000 and \$(185,000) in 2010 and 2009, respectively, as a result of reestimation of unpaid losses and loss adjustment expenses. Original estimates are decreased or increased as additional information becomes known regarding individual claims.

6. Reinsurance

Certain premiums and benefits are ceded to other insurance companies under various reinsurance agreements. The reinsurance agreements provide the Company with increased capacity to write more risks and maintain its exposure to loss within its capital resources. As of December 31, 2010 and 2009, the Company's reinsurance program consisted of catastrophe excess of loss reinsurance and quota share treaties. Following is a summary of the reinsurance coverage.

Effective June 1, 2010, the Company and its affiliated company, HomeWise Preferred Insurance Company (collectively, the Reinsured), entered into a quota share reinsurance agreement with Greenlight Reinsurance Ltd. (Greenlight). Under the terms of the agreement, Greenlight assumes a percentage (80% on policies written through December 31, 2010, with loss dates between June 1 and December 31, 2010; 90% on policies written through December 31, 2010, with loss dates after December 31, 2010; 85% on policies written after December 31, 2010, through May 31,

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

6. Reinsurance (continued)

2011; and 80% on policies written thereafter) of the Reinsured's incurred losses and loss adjustment expenses, subject to several exclusions. The Reinsured cedes a percentage of gross premiums (equal to the percentage of losses assumed by Greenlight as described above), subject to several exclusions, after deducting a portion of the cost of the excess of loss reinsurance treaties, described below. The agreement is effective through May 31, 2012.

The reinsurance agreement is subject to a loss retention corridor, whereby the Reinsured retains losses above a minimum gross loss ratio ranging from 40.33% to 42.26% up to a maximum gross loss ratio ranging from 62.91% to 65%. Maximum losses ceded under this agreement are limited to 93% of the premiums earned for policies written through December 31, 2010, and 90% of the premiums earned for policies written thereafter. The ceding commission from Greenlight is equal to 31% of Greenlight's share of gross written premium, prior to the deduction of any premiums paid for catastrophe excess of loss protection. Additionally, the Reinsured is allowed a profit commission on a sliding scale basis for loss ratios under 42.26%. The current and prior year (described below) ceding commissions have been recorded as a reduction of underwriting, acquisition, and other expenses in the accompanying statements of operations.

Effective June 1, 2009, the Reinsured entered into quota share reinsurance agreements with Signet Star Re (Signet), Hannover Reinsurance (Ireland) Ltd. (Hannover), and Greenlight Reinsurance Ltd. (Greenlight) (collectively, the Reinsurers). Signet has a 30% participation. Hannover and Greenlight each have a 35% participation.

Under the terms of the agreements, as amended June 30, 2009, the Reinsurers assume a percentage (85% on policies written through December 31, 2009, and 75% on policies written thereafter) of the Reinsured's incurred losses and loss adjustment expenses, subject to several exclusions. The Reinsured cede a percentage (85% on policies written through December 31, 2009, and 75% on policies written thereafter) of their gross premiums, subject to several exclusions, after deducting a portion of the cost of the excess of loss reinsurance treaties, described below. The quota share agreements with Signet and Hannover expired on May 31, 2010, while the agreement with Greenlight expires on May 31, 2011.

The reinsurance agreements are subject to loss retention corridors, whereby the Reinsured retain losses above a minimum gross loss ratio ranging from 25% to 33% up to a maximum gross loss ratio ranging from 37% to 42%. The limitations on maximum losses ceded under the agreements vary by participating reinsurer. The ceding commission from the Reinsurers is equal to a blended rate of 31.07% of the Reinsurers' share of gross written premium, prior to the deduction of any premiums paid to catastrophe excess of loss protection.

The Company did not enter into or engage in any loss portfolio transfer for any lines of business during 2010 or 2009.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

6. Reinsurance (continued)

The catastrophe excess of loss coverage is provided by agreements with commercial reinsurers and by the FHCF. Coverage under the FHCF is limited to qualifying storms occurring in the state of Florida. For the year ended December 31, 2010, the commercial excess of loss treaties generally provide coverage on ultimate net losses of approximately \$79,600,000 in excess of \$6,000,000 per occurrence, not to exceed approximately \$159,200,000 for all occurrences. The FHCF provided coverage for 90% of the losses from qualifying catastrophic events in excess of approximately \$88,700,000 up to a maximum of approximately \$375,600,000, plus 100% of qualifying losses in excess of approximately \$6,100,000 (drop down layer) up to a maximum of approximately \$16,100,000. The drop down layer provides for one automatic reinstatement at 100% of its original limit. For the year ended December 31, 2009, the commercial excess of loss treaties generally provide coverage on ultimate net losses of approximately \$26,500,000 in excess of \$2,520,000 per occurrence, not to exceed approximately \$51,200,000 for all occurrences. The FHCF provided coverage for 90% of the losses from qualifying catastrophic events in excess of approximately \$18,600,000 up to a maximum of approximately \$97,200,000.

For 2009, the Company and its affiliated company, HomeWise Preferred Insurance Company, entered into the commercial catastrophe excess of loss coverage agreements described above. The 2009 amounts shown above represent the Company's share of the total agreements.

The FHCF provides coverage for named hurricanes only and provides no coverage after the one time limit is exhausted. Reinsurance premiums for the FHCF are paid on a total insured value basis. In the event of a loss assessment, the Company may recoup the assessments from its policyholders.

Effective June 1, 2010 and 2009, the Company executed reinsurance premium protection agreements to reinsure the reinstatement premium payment obligations which accrue to the Company under the private catastrophe excess of loss agreements. The coverage is limited to 100% of the original contracted reinsurance placement.

The Company's reinsured risks are treated, to the extent of the reinsurance, as though they are risks for which the Company is not liable. However, the Company remains liable in the event the reinsuring companies do not meet their obligations under these reinsurance agreements. Given the quality of the reinsuring companies, management believes this possibility to be remote. See Note 5 for recoveries due from reinsurers relating to paid and unpaid losses and LAE.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

6. Reinsurance (continued)

The effects of reinsurance on premiums written and earned are as follows:

| | Years ended December 31, | | | |
|-----------------|--------------------------|----------------------|----------------------|---------------------|
| | 2010 | | 2009 | |
| | Written | Earned | Written | Earned |
| Direct premiums | \$ 146,671,003 | \$ 102,314,483 | \$ 38,926,642 | \$ 23,728,632 |
| Ceded premiums | <u>(133,549,118)</u> | <u>(86,951,384)</u> | <u>(28,676,212)</u> | <u>(19,173,631)</u> |
| Net premiums | <u>\$ 13,121,885</u> | <u>\$ 15,363,099</u> | <u>\$ 10,250,430</u> | <u>\$ 4,555,001</u> |

The following table summarizes the effect of ceded unearned premiums on the direct unearned premiums reserve and provides the related commission equity at December 31:

| | 2010 | 2009 |
|--------------------------|------------------------|-----------------------|
| Direct unearned premiums | \$ 66,764,819 | \$ 22,408,299 |
| Ceded unearned premiums | <u>(62,099,924)</u> | <u>(15,502,190)</u> |
| Unearned premiums, net | <u>\$ 4,664,895</u> | <u>\$ 6,906,109</u> |
| Commission equity, net | <u>\$ (17,523,000)</u> | <u>\$ (4,496,000)</u> |

The following table shows the effect of reinsurance on loss and loss adjustment expenses incurred:

| | Years ended December 31, | |
|--|--------------------------|---------------------|
| | 2010 | 2009 |
| Direct losses and loss adjustment expenses incurred | \$ 29,734,856 | \$ 4,412,265 |
| Assumed losses and loss adjustment expenses incurred | - | (32,063) |
| Ceded losses and loss adjustment expenses incurred | <u>(14,861,727)</u> | <u>(3,152,111)</u> |
| Losses and loss adjustment expenses incurred, net | <u>\$ 14,873,129</u> | <u>\$ 1,228,091</u> |

At December 31, 2010 and 2009, unsecured reinsurance recoverables on paid and unpaid losses and LAE and unearned premiums by reinsurer that were equal to or greater than 3% of surplus are as follows:

| | 2010 | 2009 |
|-------------------------------------|---------------|--------------|
| Florida Hurricane Catastrophe Fund | \$ 12,291,000 | \$ 1,683,000 |
| Signet Star (Berkley Insurance Co.) | 2,922,000 | 2,935,000 |

For the years ended December 31, 2010 and 2009, recoveries under reinsurance contracts totaled \$8,507,882 and \$1,684,176, respectively.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

7. Income Taxes

Income before federal income taxes differs from taxable income principally due to differences in loss and LAE reserves and unearned premiums for tax and statutory basis financial reporting purposes.

State income taxes are classified as taxes, licenses, and fees in the NAIC Annual Statement and as underwriting, acquisition, and other expenses in the accompanying statements of operations.

A. The components of net deferred tax assets (DTAs) and deferred tax liabilities (DTLs) at December 31 are as follows:

| | 2010 | | |
|--------------------------------|--------------|---------|---------------------|
| | Ordinary | Capital | Total |
| Total gross DTAs | \$ 1,501,104 | \$ - | \$ 1,501,104 |
| Total gross DTLs | - | - | <u>119,743</u> |
| Net DTA | | | 1,381,361 |
| Nonadmitted DTAs | | | <u>269,712</u> |
| Net admitted DTA (see Note 13) | | | <u>\$ 1,111,649</u> |
| | | | |
| Increase in nonadmitted DTAs | | | <u>\$ 269,712</u> |

| | 2009 | | |
|------------------------------|------------|---------|--------------------|
| | Ordinary | Capital | Total |
| Total gross DTAs | \$ 796,804 | \$ - | \$ 796,804 |
| Total gross DTLs | - | - | <u>88,408</u> |
| Net DTA | | | 708,396 |
| Nonadmitted DTAs | | | - |
| Net admitted DTAs | | | <u>\$ 708,396</u> |
| | | | |
| Decrease in nonadmitted DTAs | | | <u>\$ (66,806)</u> |

The Company has not elected to admit additional DTAs pursuant to SSAP 10R, paragraph 10(e). The current period election does not differ from the prior reporting period.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

7. Income Taxes (continued)

The amount of each result or component of the calculation, by tax character, of paragraphs 10.a., 10.b.i., 10.b.ii., and 10.c. are as follows:

| | 2010 | | |
|--|-----------|---------|------------|
| | Ordinary | Capital | Total |
| Can be recovered through loss carrybacks (10.a.) | \$ - | \$ - | \$ - |
| Lesser of: | | | |
| Expected to be recognized within one year (10.b.i.) | 1,454,109 | - | 1,454,109 |
| Ten percent of adjusted capital and surplus (10.b.ii.) | 1,933,698 | - | 1,933,698 |
| Adjusted gross DTAs offset against existing DTLs (10.c.) | 119,743 | - | 119,743 |
| Risk-based capital level used in paragraph 10.d.: | | | |
| Total adjusted capital | | | 18,799,788 |
| Authorized control level | | | 3,215,330 |

| | 2009 | | |
|--|----------|---------|------------|
| | Ordinary | Capital | Total |
| Can be recovered through loss carrybacks (10.a.) | \$ - | \$ - | \$ - |
| Lesser of: | | | |
| Expected to be recognized within one year (10.b.i.) | 791,602 | - | 791,602 |
| Ten percent of adjusted capital and surplus (10.b.ii.) | 740,262 | - | 740,262 |
| Adjusted gross DTAs offset against existing DTLs (10.c.) | 56,542 | - | 56,542 |
| Risk-based capital level used in paragraph 10.d.: | | | |
| Total adjusted capital | | | 20,262,170 |
| Authorized control level | | | 2,555,084 |

The following amounts resulting from the calculation in paragraphs 10.a., 10.b., and 10.c. are as follows:

| | 2010 | 2009 |
|------------------------|--------------|------------|
| Admitted DTAs | \$ 1,111,649 | \$ 708,396 |
| Admitted assets | 48,692,916 | 36,136,562 |
| Statutory surplus | 18,799,788 | 20,262,170 |
| Total adjusted capital | 18,799,788 | 20,262,170 |

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

7. Income Taxes (continued)

B. Unrecognized DTLs:

Not applicable.

C. Current tax and change in deferred tax:

The provisions for income taxes incurred on earnings for the years ended December 31 is:

| | <u>2010</u> | <u>2009</u> |
|---------------------------------|-------------|-------------------|
| Current year income tax expense | \$ - | \$ - |
| Prior year under accrual | - | 255,049 |
| Current income taxes incurred | <u>\$ -</u> | <u>\$ 255,049</u> |

The tax effect of temporary differences that give rise to significant deferred tax assets and deferred tax liabilities is as follows:

| | <u>December 31,</u> <u>2010</u> | <u>2009</u> | <u>Change</u> |
|-----------------------------------|------------------------------------|-------------------|-------------------|
| Deferred Tax Assets: | | | |
| Discount on unpaid losses and LAE | \$ 117,488 | \$ 13,003 | \$ 104,485 |
| 20% of unearned premiums | 317,213 | 469,615 | (152,402) |
| Nonadmitted assets | 19,105 | 48,607 | (29,502) |
| Profit sharing | 46,330 | 46,330 | - |
| Charitable contribution | 23,375 | 23,375 | - |
| Net operating loss | <u>977,593</u> | <u>195,874</u> | <u>781,719</u> |
| Total DTAs | 1,501,104 | 796,804 | 704,300 |
| Nonadmitted DTAs | <u>269,712</u> | - | <u>269,712</u> |
| Admitted DTAs | <u>1,231,392</u> | <u>796,804</u> | <u>434,588</u> |
| Deferred Tax Liabilities: | | | |
| Depreciation of fixed assets | (96,619) | (71,279) | (25,340) |
| Other | <u>(23,124)</u> | <u>(17,129)</u> | <u>(5,995)</u> |
| Total DTLs | <u>(119,743)</u> | <u>(88,408)</u> | <u>(31,335)</u> |
| Net admitted DTAs | <u>\$ 1,111,649</u> | <u>\$ 708,396</u> | <u>\$ 403,253</u> |

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

7. Income Taxes (continued)

The change in net deferred income taxes is comprised of the following:

| | December 31, | | |
|--|---------------------|-------------------|-------------------|
| | <u>2010</u> | <u>2009</u> | <u>Change</u> |
| Total gross DTAs | \$ 1,501,104 | \$ 796,804 | \$ 704,300 |
| Total gross DTLs | <u>(119,743)</u> | <u>(88,408)</u> | <u>(31,335)</u> |
| Net DTA | <u>\$ 1,381,361</u> | <u>\$ 708,396</u> | 672,965 |
| Deferred tax on change in net unrealized capital gains | | | - |
| Change in net deferred income tax | | | <u>\$ 672,965</u> |

D. Reconciliation of federal income tax rate to actual effective rate:

The significant book-to-tax adjustments were as follows:

| | <u>2010</u> | <u>Percentage of Pre-Tax Income</u> |
|--------------------------------------|---------------------|---|
| Provision computed at statutory rate | \$ (691,018) | (34.00)% |
| Nondeductible items | 15,810 | 0.78 |
| Change in nonadmitted assets | 29,502 | 1.45 |
| Other | <u>(27,259)</u> | <u>(1.34)</u> |
| Total | <u>\$ (672,965)</u> | <u>(33.11)%</u> |
| Federal income tax | \$ - | - % |
| Change in deferred taxes | <u>(672,965)</u> | <u>(33.11)</u> |
| Statutory income taxes | <u>\$ (672,965)</u> | <u>(33.11)%</u> |

E. Operating loss and tax credit carryforwards, and protective tax deposits:

- At December 31, 2010 and 2009, the Company had no unused capital losses and approximately \$2,875,000 of net operating loss carryforwards available to offset against future taxable income. This carryforward originated in 2009 and expires in 2029.
- The following is income tax expense that is available for recoupment in the event of future net losses:

| <u>Year</u> | <u>Amount</u> |
|-------------|---------------|
| 2010 | \$ - |
| 2009 | - |

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

7. Income Taxes (continued)

3. The Company did not have any protective tax deposits under Section 6603 of the Internal Revenue Code.

F. Consolidated federal income tax return:

The Company's federal income tax return is consolidated with the following:

HomeWise Holdings, Inc.
HomeWise Preferred Insurance Company
HomeWise Management Company

The method of allocation between the companies is subject to written agreement, approved by the Board of Directors. Allocation is based upon separate return calculations with current credit for net losses. Intercompany balances are settled quarterly.

8. Capital and Surplus

The Company has authorized 1,000,000 shares of \$1 par value common stock, of which 650,000 shares are issued and outstanding at December 31, 2010 and 2009. No other classes of common or preferred shares were issued during 2010 or 2009. The parent company, HHI, is the sole shareholder. In February 2010, HHI made a cash contribution of additional paid-in capital totaling \$13,000,000. The Company received authorization from the Office to report the related capital contribution receivable at December 31, 2009, as an admitted asset in accordance with Statement on Statutory Accounting Principles No. 72, *Surplus and Quasi-reorganizations*.

Property and casualty insurance companies are subject to certain Risk-based Capital (RBC) requirements as specified by the NAIC. Under those requirements, the amount of capital and surplus maintained by a property and casualty insurance company is to be determined based on the various risk factors related to it. The Company is in compliance with the RBC requirements at December 31, 2010 and 2009, respectively.

The maximum amount of dividends that may be paid by property and casualty insurance companies without prior approval of the Office is subject to restrictions relating to statutory surplus and net income. The Company did not declare or pay any dividends during the years ended December 31, 2010 or 2009.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

9. Related Party Transactions

The Company is a wholly-owned subsidiary of HomeWise Holdings, Inc. (HHI) and is affiliated with HomeWise Management Company (HMC) and HomeWise Preferred Insurance Company (HPIC), which are also wholly-owned subsidiaries of HHI.

Effective July 1, 2010, the Company executed a Policy Rights Agreement with HPIC whereby HPIC sells all of its rights, title, and interests in policy information developed by HPIC to the Company. The agreement is in furtherance of HPIC's discontinuance plan filed with the OIR and is intended to provide the Company with the information necessary to determine which of HPIC's policies will be offered replacement coverage with the Company. As compensation, the Company will pay a fee equal to 5% of its direct written premium related to the replacement coverage. Additionally, policies were transferred to the Company that were to be offered replacement coverage by the Company and that acknowledged the Company as primary obligor for loss responsibility as of June 1, 2010. In consideration of the acceptance of the loss responsibility on these policies, the associated unearned premiums were remitted to the Company. The total amount of premium transferred from HPIC under this agreement during 2010 is \$40,228,661 and is recorded as direct written premium. Also, in recognition of the disproportionate allocation of FHCF costs associated with the policy transfer and its related activity, HPIC transferred \$3 million of FHCF premiums to the Company.

Effective June 1, 2010, the Company executed an Assumption Reinsurance Agreement with HPIC whereby HPIC cedes, and the Company assumes, 100% of the liability of HPIC under the policies assumed by the Company arising on or after the effective date. As compensation, HPIC transfers 100% of the unearned premium of the assumed policies as of the effective date to the Company, less a ceding commission. The total amount of premium assumed by the Company during 2010 is \$403,198.

During 2010, commissions relating to the Policy Rights and Assumption Reinsurance Agreements totaled approximately \$4,090,000 and are reported as an increase in underwriting, acquisition, and other expenses.

Effective January 1, 2006, the Company entered into a managing general agency agreement with HMC. Pursuant to the agreement, HMC provides to the Company premium billing, claims management and underwriting functions. During 2010 and 2009, expenses incurred related to this agreement totaled \$28,077,282 and \$10,117,751, respectively. During 2010, HMC forgave \$6,941,000 of these expenses.

Effective December 5, 2005, the Company entered into a service agreement with HHI. Pursuant to the agreement, HHI provides to the Company capital management services, investor management and relations, and assists with overall general management of the Company. This agreement was terminated by mutual consent, effective July 1, 2010. During 2010 and 2009, expenses incurred related to this agreement totaled \$502,379 and \$381,802, respectively.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

9. Related Party Transactions (continued)

The Company is also party to a Cost Allocation Agreement with HPIC, HMC, and HHI in which expenses benefiting more than one company are allocated based upon direct allocation or revenue allocation rules, whichever is most appropriate for the expense. As a result of the Cost Allocation Agreement and the other transactions described above, the Company has a payable due to HPIC of \$5,254,595 and \$333,407, at December 31, 2010 and 2009, respectively; a receivable due from HMC of \$9,116,996 and \$641,776 at December 31, 2010 and 2009, respectively; and a receivable due from HHI of \$859 and \$717,693 at December 31, 2010 and 2009, respectively.

The Company reported a capital contribution of \$13,000,000 from HHI in 2009 that was received in February 2010 (see Note 8).

10. Premiums Produced by Managing General Agents or Third Party Administrators

The Company uses a managing general agent, HMC, to write and administer insurance products. HMC has contracted with an unaffiliated service company to provide this function. The total premium produced and serviced through the contract during 2010 is summarized below. The Company retains underwriting authority for all policies issued under these agreements.

| <u>Name and Address</u> | <u>FEI Number</u> | <u>Exclusive Contract</u> | <u>Type of Business Written</u> | <u>Type of Authority Granted</u> | <u>Direct Premium Written</u> |
|---|-------------------|---------------------------|---------------------------------|--|-------------------------------|
| HomeWise Management Company, Inc. 18302 Highwoods Preserve Parkway, Suite 110 Tampa, FL 33647 | 20-3395152 | Yes | Homeowners | Premium collection, claims adjustments, binding authority, and underwriting | \$ 105,850,595 |

11. Leases

On May 1, 2006, the Company entered into an operating lease agreement for office space in Tampa, Florida, which is effective June 1, 2006, through May 31, 2011. The Company has the option to renew the term of the lease for an additional five year period at the prevailing rental rate at that time, provided the Company gives the lessor written notice nine months prior to its intent to renew the lease. On February 1, 2010, the Company entered into a second operating lease for office space in Tampa, Florida under a non-cancelable lease that expires in 2015. Expenses associated with this lease are allocated equally between the Company and HPIC. Through July 1, 2010, expenses associated with the lease in Tampa, Florida were allocated equally between the Company and HPIC. Subsequent to July 1, 2010, expenses were no longer allocated to HPIC in accordance with HPIC's discontinuance plan.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

11. Leases (continued)

Approximate future lease payments under this lease are as follows at December 31, 2010:

| | | |
|------|----|----------------|
| 2011 | \$ | 254,520 |
| 2012 | | 36,511 |
| 2013 | | 38,105 |
| 2014 | | 39,700 |
| 2015 | | <u>3,320</u> |
| | \$ | <u>372,156</u> |

Total rent expense for leases was \$420,246 and \$274,845 for the years ended December 31, 2010 and 2009, respectively. The current year rent expense includes \$166,100 of reimbursements received from HPIC for HPIC's share of the lease expense.

12. Reconciliation of Annual Statement to Audited Financial Statements

Differences exist between amounts reported in the audited statutory financial statements and those reported in the annual statement of the Company for the year ended December 31, 2010, due to reclassification of related party receivables. Presented below is a reconciliation of amounts previously reported to the Office and those amounts appearing in the audited statutory financial statements for the year ended December 31, 2010.

| | Audited Financial Statement Amount | Annual Statement Amount | Increase (Decrease) |
|---------------------------|---|--|--------------------------------|
| Total admitted assets | \$ 48,692,916 | \$ 43,438,321 | \$ 5,254,595 |
| Total liabilities | 29,893,128 | 24,638,533 | 5,254,595 |
| Total capital and surplus | 18,799,788 | 18,799,788 | - |
| Net loss | 2,032,407 | 2,032,407 | - |

13. Subsequent Events

On March 22, 2010, HomeWise Insurance Company and First Home Insurance Company announced their intent to merge as a result of a transaction between the two insurance companies' parent companies. The proposed transaction is subject to customary definitive documentation, regulatory approval, and completion of satisfactory due diligence. The projected closing date for the transaction is on or before May 31, 2011. Should the transaction occur, the ability of the Company to realize the deferred tax benefit attributable to net operating loss carryforwards may be significantly limited. Therefore, the recorded net deferred tax asset of approximately \$1.1 million at December 31, 2010, may be eliminated.

Other Financial Information

SUMMARY INVESTMENT SCHEDULE

Schedule 1

| Investment Categories | Gross Investment Holdings | | Admitted Assets as Reported in the Annual Statement | |
|--|---------------------------|-----------------|---|-----------------|
| | 1 Amount | 2 Percentage | 3 Amount | 4 Percentage |
| 1. Bonds: | | | | |
| 1.1 U.S. treasury securities: | | 0.0 | | 0.0 |
| 1.2 U.S. government agency obligations (excluding mortgage-backed securities): | | | | |
| 1.21 Issued by U.S. government agencies: | | 0.0 | | 0.0 |
| 1.22 Issued by U.S. government sponsored agencies: | | 0.0 | | 0.0 |
| 1.3 Non-U.S. government (including Canada, excluding mortgage-backed securities): | | 0.0 | | 0.0 |
| 1.4 Securities issued by states, territories and possessions and political subdivisions in the U.S.: | | | | |
| 1.41 States, territories and possessions general obligations: | | 0.0 | | 0.0 |
| 1.42 Political subdivisions of states, territories & possessions & political subdivisions general obligations: | | 0.0 | | 0.0 |
| 1.43 Revenue and assessment obligations: | | 0.0 | | 0.0 |
| 1.44 Industrial development and similar obligations: | | 0.0 | | 0.0 |
| 1.5 Mortgage-backed securities (includes residential and commercial MBS): | | | | |
| 1.51 Pass-through securities: | | | | |
| 1.511 Issued or guaranteed by GNMA: | | 0.0 | | 0.0 |
| 1.512 Issued or guaranteed by FNMA and FHLMC: | | 0.0 | | 0.0 |
| 1.513 All other: | | 0.0 | | 0.0 |
| 1.52 CMOs and REMICs: | | | | |
| 1.521 Issued or guaranteed by GNMA, FNMA, FHLMC or VA: | | 0.0 | | 0.0 |
| 1.522 Issued by non-U.S. Government issuers and collateralized by mortgage-backed securities issued or guaranteed by agencies shown in Line 1.521: | | 0.0 | | 0.0 |
| 1.523 All other: | | 0.0 | | 0.0 |
| 2. Other debt and other fixed income securities (excluding short-term): | | | | |
| 2.1 Unaffiliated domestic securities (includes credit tenant loans and hybrid securities): | | 0.0 | | 0.0 |
| 2.2 Unaffiliated non-U.S. securities (including Canada): | | 0.0 | | 0.0 |
| 2.3 Affiliated securities: | | 0.0 | | 0.0 |
| 3. Equity interests: | | | | |
| 3.1 Investments in mutual funds: | | 0.0 | | 0.0 |
| 3.2 Preferred stocks: | | | | |
| 3.21 Affiliated: | | 0.0 | | 0.0 |
| 3.22 Unaffiliated: | | 0.0 | | 0.0 |
| 3.3 Publicly traded equity securities (excluding preferred stocks): | | | | |
| 3.31 Affiliated: | | 0.0 | | 0.0 |
| 3.32 Unaffiliated: | | 0.0 | | 0.0 |
| 3.4 Other equity securities: | | | | |
| 3.41 Affiliated: | | 0.0 | | 0.0 |
| 3.42 Unaffiliated: | | 0.0 | | 0.0 |
| 3.5 Other equity interests including tangible personal property under lease: | | | | |
| 3.51 Affiliated: | | 0.0 | | 0.0 |
| 3.52 Unaffiliated: | | 0.0 | | 0.0 |
| 4. Mortgage loans: | | | | |
| 4.1 Construction and land development: | | 0.0 | | 0.0 |
| 4.2 Agricultural: | | 0.0 | | 0.0 |
| 4.3 Single family residential properties: | | 0.0 | | 0.0 |
| 4.4 Multifamily residential properties: | | 0.0 | | 0.0 |
| 4.5 Commercial loans: | | 0.0 | | 0.0 |
| 4.6 Mezzanine real estate loans: | | 0.0 | | 0.0 |
| 5. Real estate investments: | | | | |
| 5.1 Property occupied by company: | | 0.0 | | 0.0 |
| 5.2 Property held for production of income (including \$.....0 of property acquired in satisfaction of debt): | | 0.0 | | 0.0 |
| 5.3 Property held for sale (including \$.....0 property acquired in satisfaction of debt): | | 0.0 | | 0.0 |
| 6. Contract loans: | | 0.0 | | 0.0 |
| 7. Receivables for securities: | | 0.0 | | 0.0 |
| 8. Cash, cash equivalents and short-term investments: | | 0.0 | 15,137,437 | 100.0 |
| 9. Other invested assets: | | 0.0 | | 0.0 |
| 10. Total invested assets: | 0 | 0.0 | 15,137,437 | 100.0 |

See report of independent auditors.



SUPPLEMENTAL INVESTMENT RISKS INTERROGATORIES

For the year ended December 31, 2010

(To be filed by April 1)

Of HomeWise Insurance Company

Address (City, State, Zip Code): Tampa FL 33647

NAIC Group Code.....4111

NAIC Company Code.....12438

Employer's ID Number.....20-3395013

The Investment Risks Interrogatories are to be filed by April 1. They are also to be included with the Audited Statutory Financial Statements.
Answer the following interrogatories by reporting the applicable U.S. dollar amounts and percentages of the reporting entity's total admitted assets held in that category of investments.

1. Reporting entity's total admitted assets as reported on Page 2 of this annual statement. \$.....43,438,321

2. Ten largest exposures to a single issuer/borrower/investment.

| | 1 | 2 | 3 | 4 |
|------|-------------------------------------|--|-------------------|-------------------------------------|
| | Issuer | Description of Exposure | Amount | Percentage of Total Admitted Assets |
| 2.01 | Federated Investors | Money Market Prime Cash Obligations Fund | \$.....12,485,943 | 28.744 % |
| 2.02 | Florida Dept. of Financial Services | Treasury Cash Fund Deposit | \$.....348,756 | 0.803 % |
| 2.03 | Capital One Bank | Certificate of Deposit | \$.....100,000 | 0.230 % |
| 2.04 | | | \$..... | 0.000 % |
| 2.05 | | | \$..... | 0.000 % |
| 2.06 | | | \$..... | 0.000 % |
| 2.07 | | | \$..... | 0.000 % |
| 2.08 | | | \$..... | 0.000 % |
| 2.09 | | | \$..... | 0.000 % |
| 2.10 | | | \$..... | 0.000 % |

3. Amounts and percentages of the reporting entity's total admitted assets held in bonds and preferred stocks by NAIC rating.

| | 1 | 2 |
|------|------------------|----------------------------|
| | Bonds | |
| 3.01 | NAIC-1 | \$.....16,452,958 37.877 % |
| 3.02 | NAIC-2 | \$..... 0.000 % |
| 3.03 | NAIC-3 | \$..... 0.000 % |
| 3.04 | NAIC-4 | \$..... 0.000 % |
| 3.05 | NAIC-5 | \$..... 0.000 % |
| 3.06 | NAIC-6 | \$..... 0.000 % |
| | 3 | 4 |
| | Preferred Stocks | |
| 3.07 | PRP-1 | \$..... 0.000 % |
| 3.08 | PRP-2 | \$..... 0.000 % |
| 3.09 | PRP-3 | \$..... 0.000 % |
| 3.10 | PRP-4 | \$..... 0.000 % |
| 3.11 | PRP-5 | \$..... 0.000 % |
| 3.12 | PRP-6 | \$..... 0.000 % |

4. Assets held in foreign investments:

| | | |
|--|--|------------------|
| 4.01 | Are assets held in foreign investments less than 2.5% of the reporting entity's total admitted assets? | Yes [X] No [] |
| If response to 4.01 above is yes, responses are not required for interrogatories 5-10. | | |
| 4.02 | Total admitted assets held in foreign investments | \$..... 0.000 % |
| 4.03 | Foreign-currency-denominated investments | \$..... 0.000 % |
| 4.04 | Insurance liabilities denominated in that same foreign currency | \$..... 0.000 % |

5. Aggregate foreign investment exposure categorized by NAIC sovereign rating:

| | 1 | 2 |
|------|---------------------------------|-----------------|
| 5.01 | Countries rated NAIC-1 | \$..... 0.000 % |
| 5.02 | Countries rated NAIC-2 | \$..... 0.000 % |
| 5.03 | Countries rated NAIC-3 or below | \$..... 0.000 % |

6. Largest foreign investment exposures by country, categorized by the country's NAIC sovereign rating:

| | 1 | 2 |
|----------------------------------|-----------|-----------------|
| Countries rated NAIC-1: | | |
| 6.01 | Country 1 | \$..... 0.000 % |
| 6.02 | Country 2 | \$..... 0.000 % |
| Countries rated NAIC-2: | | |
| 6.03 | Country 1 | \$..... 0.000 % |
| 6.04 | Country 2 | \$..... 0.000 % |
| Countries rated NAIC-3 or below: | | |
| 6.05 | Country 1 | \$..... 0.000 % |
| 6.06 | Country 2 | \$..... 0.000 % |

7. Aggregate unhedged foreign currency exposure: \$..... 0.000 %

| | | | |
|---|----------------------------------|----|---------|
| 6. Aggregate unhedged foreign currency exposure categorized by NAIC sovereign rating: | | 1 | 2 |
| 8.01 | Countries rated NAIC-1: | \$ | 0.000 % |
| 8.02 | Countries rated NAIC-2: | \$ | 0.000 % |
| 8.03 | Countries rated NAIC-3 or below: | \$ | 0.000 % |

| | | | |
|--|------------|----|---------|
| 9. Largest unhedged foreign currency exposures by country, categorized by the country's NAIC sovereign rating: | | 1 | 2 |
| Countries rated NAIC-1: | | | |
| 9.01 | Country 1: | \$ | 0.000 % |
| 9.02 | Country 2: | \$ | 0.000 % |
| Countries rated NAIC-2: | | | |
| 9.03 | Country 1: | \$ | 0.000 % |
| 9.04 | Country 2: | \$ | 0.000 % |
| Countries rated NAIC-3 or below: | | | |
| 9.05 | Country 1: | \$ | 0.000 % |
| 9.06 | Country 2: | \$ | 0.000 % |

| | | | | | |
|---|---------------|--------------------|----|---------|---|
| 10. Ten largest non-sovereign (i.e. non-governmental) foreign issues: | | 1 | 2 | 3 | 4 |
| | <u>Issuer</u> | <u>NAIC Rating</u> | | | |
| 10.01 | | | \$ | 0.000 % | |
| 10.02 | | | \$ | 0.000 % | |
| 10.03 | | | \$ | 0.000 % | |
| 10.04 | | | \$ | 0.000 % | |
| 10.05 | | | \$ | 0.000 % | |
| 10.06 | | | \$ | 0.000 % | |
| 10.07 | | | \$ | 0.000 % | |
| 10.08 | | | \$ | 0.000 % | |
| 10.09 | | | \$ | 0.000 % | |
| 10.10 | | | \$ | 0.000 % | |

| | | |
|---|--|------------------|
| 11. Amounts and percentages of the reporting entity's total admitted assets held in Canadian investments and unhedged Canadian currency exposure: | | |
| 11.01 Are assets held in Canadian investments less than 2.5% of the reporting entity's total admitted assets? | | Yes [X] No [] |
| If response to 11.01 is yes, detail is not required for the remainder of Interrogatory 11. | | |
| 11.02 | Total admitted assets held in Canadian Investments | \$ 0.000 % |
| 11.03 | Canadian currency-denominated investments | \$ 0.000 % |
| 11.04 | Canadian-denominated insurance liabilities | \$ 0.000 % |
| 11.05 | Unhedged Canadian currency exposure | \$ 0.000 % |

| | | |
|---|---|------------------|
| 12. Report aggregate amounts and percentages of the reporting entity's total admitted assets held in investments with contractual sales restrictions. | | |
| 12.01 Are assets held in investments with contractual sales restrictions less than 2.5% of the reporting entity's total admitted assets? | | Yes [X] No [] |
| If response to 12.01 is yes, responses are not required for the remainder of Interrogatory 12. | | |
| | 1 | 2 |
| 12.02 | Aggregate statement value of investments with contractual sales restrictions: | \$ 0.000 % |
| Largest three investments with contractual sales restrictions: | | |
| 12.03 | | \$ 0.000 % |
| 12.04 | | \$ 0.000 % |
| 12.05 | | \$ 0.000 % |

| | | |
|--|-----------------------|------------------|
| 13. Amounts and percentages of admitted assets held in the ten largest equity interests: | | |
| 13.01 Are assets held in equity interest less than 2.5% of the reporting entity's total admitted assets? | | Yes [X] No [] |
| If response to 13.01 above is yes, responses are not required for the remainder of Interrogatory 13. | | |
| | 1 | 2 |
| | <u>Name of Issuer</u> | |
| 13.02 | | \$ 0.000 % |
| 13.03 | | \$ 0.000 % |
| 13.04 | | \$ 0.000 % |
| 13.05 | | \$ 0.000 % |
| 13.06 | | \$ 0.000 % |
| 13.07 | | \$ 0.000 % |
| 13.08 | | \$ 0.000 % |
| 13.09 | | \$ 0.000 % |
| 13.10 | | \$ 0.000 % |
| 13.11 | | \$ 0.000 % |

| | | |
|---|--|------------------|
| 14. Amounts and percentages of the reporting entity's total admitted assets held in nonaffiliated, privately placed equities: | | |
| 14.01 Are assets held in nonaffiliated, privately placed equities less than 2.5% of the reporting entity's total admitted assets? | | Yes [X] No [] |
| If response to 14.01 above is yes, responses are not required for the remainder of Interrogatory 14. | | |
| | 1 | 2 |
| 14.02 | Aggregate statement value of investments held in nonaffiliated, privately placed equities: | \$ 0.000 % |
| Largest three investments held in nonaffiliated, privately placed equities: | | |
| 14.03 | | \$ 0.000 % |
| 14.04 | | \$ 0.000 % |
| 14.05 | | \$ 0.000 % |

15. Amounts and percentages of the reporting entity's total admitted assets held in general partnership interests:

15.01 Are assets held in general partnership interests less than 2.5% of the reporting entity's total admitted assets?

Yes ☒ No ☐

If response to 15.01 above is yes, responses are not required for the remainder of Interrogatory 15.

| 1 | 2 | 3 |
|---|----|---------|
| 15.02 Aggregate statement value of investments held in general partnership interests: | \$ | 0.000 % |
| Largest three investments in general partnership interests: | | |
| 15.03 | \$ | 0.000 % |
| 15.04 | \$ | 0.000 % |
| 15.05 | \$ | 0.000 % |

16. Amounts and percentages of the reporting entity's total admitted assets held in mortgage loans:

16.01 Are mortgage loans reported in Schedule B less than 2.5% of the reporting entity's total admitted assets?

Yes ☒ No ☐

If response to 16.01 above is yes, responses are not required for the remainder of Interrogatory 16 and Interrogatory 17.

| 1 | 2 | 3 |
|--|----|---------|
| Type (Residential, Commercial, Agricultural) | | |
| 16.02 | \$ | 0.000 % |
| 16.03 | \$ | 0.000 % |
| 16.04 | \$ | 0.000 % |
| 16.05 | \$ | 0.000 % |
| 16.06 | \$ | 0.000 % |
| 16.07 | \$ | 0.000 % |
| 16.08 | \$ | 0.000 % |
| 16.09 | \$ | 0.000 % |
| 16.10 | \$ | 0.000 % |
| 16.11 | \$ | 0.000 % |

Amount and percentage of the reporting entity's total admitted assets held in the following categories of mortgage loans:

| | Loans |
|--|------------|
| 16.12 Construction loans | \$ 0.000 % |
| 16.13 Mortgage loans over 90 days past due | \$ 0.000 % |
| 16.14 Mortgage loans in the process of foreclosure | \$ 0.000 % |
| 16.15 Mortgage loans foreclosed | \$ 0.000 % |
| 16.16 Restructured mortgage loans | \$ 0.000 % |

17. Aggregate mortgage loans having the following loan-to-value ratios as determined from the most current appraisal as of the annual statement date:

| <u>Loan-to-Value</u> | <u>Residential</u> | | <u>Commercial</u> | | <u>Agricultural</u> | |
|----------------------|--------------------|---------|-------------------|---------|---------------------|---------|
| | 1 | 2 | 3 | 4 | 5 | 6 |
| 17.01 above 95% | \$ | 0.000 % | \$ | 0.000 % | \$ | 0.000 % |
| 17.02 91% to 95% | \$ | 0.000 % | \$ | 0.000 % | \$ | 0.000 % |
| 17.03 81% to 90% | \$ | 0.000 % | \$ | 0.000 % | \$ | 0.000 % |
| 17.04 71% to 80% | \$ | 0.000 % | \$ | 0.000 % | \$ | 0.000 % |
| 17.05 below 70% | \$ | 0.000 % | \$ | 0.000 % | \$ | 0.000 % |

18. Amounts and percentages of the reporting entity's total admitted assets held in each of the five largest investments in real estate:

18.01 Are assets held in real estate reported less than 2.5% of the reporting entity's total admitted assets?

Yes ☒ No ☐

If response to 18.01 above is yes, responses are not required for the remainder of Interrogatory 18.

Largest five investments in any one parcel or group of contiguous parcels of real estate.

| Description | 2 | 3 |
|-------------|----|---------|
| 18.02 | \$ | 0.000 % |
| 18.03 | \$ | 0.000 % |
| 18.04 | \$ | 0.000 % |
| 18.05 | \$ | 0.000 % |
| 18.06 | \$ | 0.000 % |

19. Report aggregate amounts and percentages of the reporting entity's total admitted assets held in investments held in mezzanine real estate loans.

19.01 Are assets held in investments held in mezzanine real estate loans less than 2.5% of the reporting entity's admitted assets?

Yes ☒ No ☐

If response to 19.01 is yes, responses are not required for the remainder of Interrogatory 19.

| 1 | 2 | 3 |
|---|----|---------|
| 19.02 Aggregate statement value of investments held in mezzanine real estate loans: | \$ | 0.000 % |
| Largest three investments held in mezzanine real estate loans: | | |
| 19.03 | \$ | 0.000 % |
| 19.04 | \$ | 0.000 % |
| 19.05 | \$ | 0.000 % |

20. Amounts and percentages of the reporting entity's total admitted assets subject to the following types of agreements:

| | At Year-End | | At End of Each Quarter | | |
|---|-------------|---------|------------------------|---------|---------|
| | 1 | 2 | 1st Qtr | 2nd Qtr | 3rd Qtr |
| 20.01 Securities lending agreements (do not include assets held as collateral for such transactions). | \$ | 0.000 % | \$ | | \$ |
| 20.02 Repurchase agreements. | \$ | 0.000 % | \$ | | \$ |
| 20.03 Reverse repurchase agreements. | \$ | 0.000 % | \$ | | \$ |
| 20.04 Dollar repurchase agreements. | \$ | 0.000 % | \$ | | \$ |
| 20.05 Dollar reverse repurchase agreements. | \$ | 0.000 % | \$ | | \$ |

21. Amounts and percentages of the reporting entity's total admitted assets for warrants not attached to other financial instruments, options, caps and floors:

| | <u>Owned</u> | | <u>Written</u> | |
|------------------------------|--------------|---------|----------------|---------|
| | 1 | 2 | 3 | 4 |
| 21.01 Hedging..... | \$..... | 0.000 % | \$..... | 0.000 % |
| 21.02 Income generation..... | \$..... | 0.000 % | \$..... | 0.000 % |
| 21.03 Other..... | \$..... | 0.000 % | \$..... | 0.000 % |

22. Amounts and percentages of the reporting entity's total admitted assets of potential exposure for collars, swaps, and forwards:

| | <u>At Year-End</u> | | <u>At End of Each Quarter</u> | | |
|------------------------------|--------------------|---------|-------------------------------|---------|---------|
| | 1 | 2 | 1st Qtr | 2nd Qtr | 3rd Qtr |
| 22.01 Hedging..... | \$..... | 0.000 % | \$..... | \$..... | \$..... |
| 22.02 Income generation..... | \$..... | 0.000 % | \$..... | \$..... | \$..... |
| 22.03 Replications..... | \$..... | 0.000 % | \$..... | \$..... | \$..... |
| 22.04 Other..... | \$..... | 0.000 % | \$..... | \$..... | \$..... |

23. Amounts and percentages of the reporting entity's total admitted assets of potential exposure for futures contracts:

| | <u>At Year-End</u> | | <u>At End of Each Quarter</u> | | |
|------------------------------|--------------------|---------|-------------------------------|---------|---------|
| | 1 | 2 | 1st Qtr | 2nd Qtr | 3rd Qtr |
| 23.01 Hedging..... | \$..... | 0.000 % | \$..... | \$..... | \$..... |
| 23.02 Income generation..... | \$..... | 0.000 % | \$..... | \$..... | \$..... |
| 23.03 Replications..... | \$..... | 0.000 % | \$..... | \$..... | \$..... |
| 23.04 Other..... | \$..... | 0.000 % | \$..... | \$..... | \$..... |

See report of independent auditors.

HomeWise Insurance Company

Selected General Interrogatories Relating to Reinsurance

December 31, 2010

- 7.1 Has the reporting entity reinsured any risk with any other entity under a quota share reinsurance contract that includes a provision that would limit the reinsurer's losses below the stated quota share percentage (e.g., a deductible, a loss ratio corridor, a loss cap, an aggregate limit, or any similar provisions)?.....Yes ☒ No ☐
- 7.2 If yes, indicate the number of reinsurance contracts containing such provisions.....1
- 7.3 If yes, does the amount of reinsurance credit taken reflect the reduction in quota share coverage caused by any applicable limiting provision(s)?.....Yes ☒ No ☐
- 9.1 Has the reporting entity ceded any risk under any reinsurance contract (or under multiple contracts with the same reinsurer or its affiliates) for which during the period covered by the statement: (i) it recorded a positive or negative underwriting result greater than 5% of prior year-end surplus as regards policyholders or it reported calendar year written premium ceded or year-end loss and loss expense reserves ceded greater than 5% of prior year-end surplus as regards policyholders; (ii) it accounted for that contract as reinsurance and not as a deposit; and (iii) the contract(s) contain one or more of the following features or other features that would have similar results:
- (a) A contract term longer than two years and the contract is noncancellable by the reporting entity during the contract term;
 - (b) A limited or conditional cancellation provision under which cancellation triggers an obligation by the reporting entity, or an affiliate of the reporting entity, to enter into a new reinsurance contract with the reinsurer, or an affiliate of the reinsurer;
 - (c) Aggregate stop loss reinsurance coverage;
 - (d) A unilateral right by either party to commute the reinsurance contract, whether conditional or not, except for such provisions which are only triggered by a decline in the credit status of the other party;
 - (e) A provision permitting reporting of losses, or payment of losses, less frequently than on a quarterly basis (unless there is no activity during the period); or
 - (f) Payment schedule, accumulating retentions from multiple years or any feature inherently designed to delay timing of the reimbursement to the ceding entity.....Yes ☐ No ☒
- 9.2 Has the reporting entity during the period covered by the statement ceded any risk under any reinsurance contract (or under multiple contracts with the same reinsurer or its affiliates), for which, during the period covered by the statement, it recorded a positive or negative underwriting result greater than 5% of prior year-end surplus as regards policyholders or it reported calendar year premium ceded or year-end loss and loss expense reserves ceded greater than 5% of prior year-end surplus as regards policyholders; excluding cessions to approved pooling agreements or to captive insurance companies that are directly or indirectly controlling, controlled by, or under common control with (i) one or more unaffiliated policyholders of the reporting entity, or (ii) an association of which one or more unaffiliated policyholders of the reporting entity is a member, where:
- (a) The written premium ceded to the reinsurer by the reporting entity or its affiliates represents fifty percent (50%) or more of the entire direct and assumed premium written by the reinsurer based on its most recently available financial statement; or
 - (b) Twenty-five percent (25%) or more of the written premium ceded to the reinsurer has been retroceded back to the reporting entity or its affiliates in a separate reinsurance contract?.....Yes ☐ No ☒

HomeWise Insurance Company

Selected General Interrogatories Relating to Reinsurance

- 9.3 If yes to 9.1 or 9.2, please provide the following information in the Reinsurance Summary Supplemental Filing for General Interrogatory 9:
- (a) The aggregate financial statement impact gross of all such ceded reinsurance contracts on the balance sheet and statement of income;
 - (b) A summary of the reinsurance contract terms and indicate whether it applies to the contracts meeting the criteria in 9.1 or 9.2; and
 - (c) A brief discussion of management's principle objectives in entering into the reinsurance contract including the economic purpose to be achieved.
- 9.4 Except for transactions meeting the requirements of paragraph 31 of SSAP No. 62, *Property and Casualty Reinsurance*, has the reporting entity ceded any risk under any reinsurance contract (or multiple contracts with the same reinsurer or its affiliates) during the period covered by the financial statement, and either:
- (a) Accounted for that contract as reinsurance (either prospective or retroactive) under statutory accounting principles (SAP) and as a deposit under generally accepted accounting principles (GAAP); or
 - (b) Accounted for that contract as reinsurance under GAAP and as a deposit under SAP?.....Yes ☐ No ☒
- 9.5 If yes to 9.4, explain in the Reinsurance Summary Supplemental Filing for General Interrogatory 9 (Section D) why the contract(s) is treated different for GAAP and SAP.

See report of independent auditors.

Report of Independent Auditors

The Board of Directors
HomeWise Insurance Company

We were engaged to audit the accompanying statement of admitted assets, liabilities, and capital and surplus (deficit) - statutory basis of HomeWise Insurance Company (the Company) as of June 30, 2011, and the related statutory basis statements of operations, changes in capital and surplus (deficit), and cash flows for the six months then ended. These financial statements are the responsibility of the Company's management.

Due to significant executive management turnover, new management at October 21, 2011, was unable to provide written representations as to its responsibility for the fair presentation of the financial statements and other matters which could materially affect the amounts and classification of items included in the financial statements. Such representations are required under generally accepted auditing standards. Additionally, the Company's internal controls over financial reporting were not adequate to reasonably assure the proper recording of transactions. Accordingly, we were unable to extend our auditing procedures sufficiently to determine the extent to which the financial statements may have been affected by these conditions.

As a result of the scope limitations described in the preceding paragraph, the scope of our work was not sufficient to enable us to express, and we do not express, an opinion on the financial statements.

As described more fully in Note 1 to the financial statements, these financial statements have been prepared in conformity with accounting practices prescribed or permitted by the Florida Office of Insurance Regulation, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

As discussed in Note 2 to the financial statements, the Company changed its method of allocating ceded losses recovered under multi-cedent quota share reinsurance agreements between the Company and HomeWise Preferred Insurance Company. Additionally, as a result of the subsequent discovery of facts after the issuance of the independent auditors' report dated April 3, 2011, on the Company's December 31, 2010 statutory financial statements, beginning surplus has been restated.

Thomas Howell
Ferguson P.A.

Page Two

The accompanying statutory basis financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 4 to the financial statements, the Company has incurred a net loss of approximately \$13,422,000 for the six months ended June 30, 2011, its total liabilities exceeded its total admitted assets at June 30, 2011, and it has lost its independent rating subsequent to June 30, 2011, that is generally required for writing new business. This raises substantial doubt about the Company's ability to continue as a going concern. The statutory basis financial statements do not include any adjustments that might result from the outcome of these uncertainties.

This report is intended solely for the use of the Board of Directors and management of HomeWise Insurance Company and for filing with the Florida Office of Insurance Regulation and is not intended to be and should not be used by anyone other than these specified parties.

Thomas Howell Ferguson P.A.

October 21, 2011

HomeWise Insurance Company

Statement of Admitted Assets, Liabilities, and Capital
and Surplus (Deficit) - Statutory Basis

June 30, 2011

Admitted assets

Cash and invested assets:

| | |
|--------------------------------|-------------------|
| Bonds | \$ 1,809,936 |
| Short-term investments | 11,894,300 |
| Cash and cash equivalents | <u>30,225,716</u> |
| Total cash and invested assets | 43,929,952 |

| | |
|--|----------------------|
| Accrued investment income | 26,535 |
| Premiums receivable | 14,871,351 |
| Reinsurance balances recoverable | 8,464,631 |
| Receivables from parent and affiliates | 174,792 |
| Other assets | <u>1,800,651</u> |
| Total admitted assets | <u>\$ 69,267,912</u> |

Liabilities and capital and surplus (deficit)

Liabilities:

| | |
|---|----------------|
| Loss and loss adjustment expense reserves | \$ 19,899,633 |
| Unearned premiums, net | (13,109,243) |
| Reinsurance premiums payable | 58,486,762 |
| Advance premiums | 4,311,912 |
| Accounts payable and accrued expenses | 557,822 |
| Taxes, licenses, and fees payable | 463,775 |
| Payable to affiliates | 141,331 |
| Premium deficiency reserve | <u>600,000</u> |
| Total liabilities | 71,351,992 |

| | |
|-------------------------------|--------------------|
| Capital and surplus (deficit) | <u>(2,084,080)</u> |
|-------------------------------|--------------------|

| | |
|---|----------------------|
| Total liabilities and capital and surplus (deficit) | <u>\$ 69,267,912</u> |
|---|----------------------|

See accompanying notes.

HomeWise Insurance Company
Statement of Operations - Statutory Basis

For the six months ended June 30, 2011

| | |
|---|------------------------|
| Underwriting income: | |
| Premiums earned, net of reinsurance ceded | \$ 3,300,326 |
| Underwriting expenses: | |
| Losses and loss adjustment expenses incurred | 15,195,007 |
| Underwriting, acquisition, and other expenses | <u>1,167,951</u> |
| Total underwriting expenses | <u>16,362,958</u> |
| Net underwriting loss | (13,062,632) |
| Net investment income | 32,265 |
| Other income | 208,345 |
| Change in premium deficiency reserve | <u>(600,000)</u> |
| Loss before federal income tax expense | (13,422,022) |
| Federal income tax expense | <u>118</u> |
| Net loss | <u>\$ (13,422,140)</u> |

See accompanying notes.

HomeWise Insurance Company

Statement of Changes in Capital and Surplus (Deficit) - Statutory Basis

For the six months ended June 30, 2011

| | Common Stock | | Gross Paid-in and Contributed | | Unassigned | Total |
|--|--------------|------------|-------------------------------------|-----------------|----------------|-------|
| | Shares | Par Value | Surplus | Funds | | |
| Balance as of January 1, 2011, as reported | 650,100 | \$ 650,100 | \$ 62,849,900 | \$ (34,988,870) | \$ 28,511,130 | |
| Restatement of surplus (see Note 2) | - | - | - | (10,417,843) | (10,417,843) | |
| Balance as of January 1, 2011, restated | 650,100 | 650,100 | 62,849,900 | (45,406,713) | 18,093,287 | |
| Issuance of common stock | 649,900 | 649,900 | (649,900) | - | - | |
| Cancellation of common stock | (650,000) | (650,000) | 650,000 | - | - | |
| Change in deferred income taxes | - | - | - | (1,381,361) | (1,381,361) | |
| Change in nonadmitted assets | - | - | - | (5,373,866) | (5,373,866) | |
| Net loss | - | - | - | (13,422,140) | (13,422,140) | |
| Balance as of June 30, 2011 | 650,000 | \$ 650,000 | \$ 62,850,000 | \$ (65,584,080) | \$ (2,084,080) | |

See accompanying notes.

HomeWise Insurance Company

Statement of Cash Flows - Statutory Basis

For the six months ended June 30, 2011

Operating activities

| | |
|--|------------------|
| Premiums collected, net of reinsurance | \$ 24,395,838 |
| Net investment income received | 47,459 |
| Other income received | 223,019 |
| Losses and loss adjustment expenses paid | (14,835,652) |
| Underwriting, acquisition, and other expenses paid | (3,705,991) |
| Federal income taxes recovered | <u>348,061</u> |
| Net cash provided by operating activities | <u>6,472,734</u> |

Financing activities

| | |
|---------------------------------------|--------------------|
| Other miscellaneous uses | <u>(2,186,147)</u> |
| Net cash used in financing activities | <u>(2,186,147)</u> |

| | |
|----------------------|-----------|
| Net increase in cash | 4,286,587 |
|----------------------|-----------|

| | |
|-----------------------------|-------------------|
| Cash at beginning of period | <u>37,833,429</u> |
|-----------------------------|-------------------|

| | |
|-----------------------|----------------------|
| Cash at end of period | <u>\$ 42,120,016</u> |
|-----------------------|----------------------|

Cash consists of the following:

| | |
|---------------------------|----------------------|
| Cash and cash equivalents | \$ 30,225,716 |
| Short-term investments | <u>11,894,300</u> |
| | <u>\$ 42,120,016</u> |

See accompanying notes.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

For the six months ended June 30, 2011

1. Summary of Significant Accounting Policies

Organization and Description of Company

First Home Insurance Company (FHIC) was formed on April 5, 2005, as a Florida-domiciled property and casualty insurance company. On May 31, 2011, FHIC merged with HomeWise Insurance Company (HWIC) (see Note 3), a Florida-domiciled property and casualty insurance company and changed its name to HomeWise Insurance Company (merged entities referred throughout as “the Company”).

The Company is a wholly-owned subsidiary of First Home Financial Corporation (FHFC), an insurance holding company incorporated in the state of Delaware. FHFC and First Home Insurance Agency, LLC (FHIA), a licensed managing general agent in the state of Florida, are wholly-owned subsidiaries of First Home Acquisition Corporation (FHAC), a Delaware corporation. FHAC is a wholly-owned subsidiary of Glencoe Acquisition, Inc. (Glencoe), a Delaware corporation.

The Company is affiliated through common ownership with HomeWise Management Company (HMC), a licensed managing general agent in the state of Florida, and HomeWise Preferred Insurance Company (HPIC), a Florida-domiciled property and casualty insurance company. HMC and HPIC are wholly-owned subsidiaries of HomeWise Holdings, Inc. (HWH), an insurance holding company incorporated in the state of Florida. HWH is a wholly-owned subsidiary of Glencoe.

The Company writes coverage exclusively in the states of Florida and Louisiana, areas that are exposed to damage from hurricanes and severe storms. The Company attempts to mitigate its exposure to losses from storms by purchasing quota share and catastrophe reinsurance coverage. However, such a storm, depending on its path and severity, could result in losses to the Company exceeding its reinsurance protection and could have a material adverse effect on the financial condition and results of operations of the Company.

Basis of Presentation

The accompanying statutory basis financial statements have been prepared in accordance with statutory accounting practices (SAP) prescribed or permitted by the Florida Office of Insurance Regulation (the Office). Such statutory practices require preparation of the financial statements in accordance with the National Association of Insurance Commissioners’ (NAIC) *Accounting Practices and Procedures Manual* subject to deviations prescribed by the Office. SAP is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America (GAAP). Such practices vary in certain respects from those under GAAP. The Company's significant accounting practices and the variances from GAAP are summarized below:

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

1. Summary of Significant Accounting Policies (continued)

Basis of Presentation (continued)

- Investments in bonds or debt securities are reported at amortized cost or market value based on their NAIC rating; for GAAP, such fixed maturity investments would be designated at purchase as held-to-maturity, trading, or available-for-sale. Held-to-maturity fixed maturity investments would be reported at amortized cost, and the remaining fixed maturity investments would be reported at fair value with unrealized holding gains and losses reported in operations for those designated as trading and as a component of other comprehensive income for those designated as available-for-sale.
- Fair values of certain investments in bonds are based on actual or estimated market values as quoted in a registered U.S. exchange. Changes between amortized cost and admitted asset investment amounts are credited or charged directly to unassigned surplus rather than to other comprehensive income as would be required under GAAP.
- Certain assets designated as "nonadmitted," principally past-due uncollected premiums, prepaid expenses, and other assets not specifically identified as an admitted asset within the *Accounting Practices and Procedures Manual*, are excluded from the accompanying statements of admitted assets, liabilities, and capital and surplus and are charged directly to unassigned surplus. Under GAAP, such assets would be included in the balance sheet at net realizable values.
- Loss and loss adjustment expense reserves and unearned premiums ceded to reinsurers have been reported as reductions of the related liabilities rather than as assets as would be required under GAAP.
- Cash in the statement of cash flows represents cash, cash equivalents, and short-term investments with remaining maturities of one year or less. Under GAAP, the corresponding caption of cash and cash equivalents would include cash balances and investments with initial maturities of three months or less.
- The costs of acquiring and renewing business are expensed when incurred. Under GAAP, such costs, to the extent recoverable, would be deferred and amortized over the effective period of the related insurance policies.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

1. Summary of Significant Accounting Policies (continued)

Basis of Presentation (continued)

- Deferred tax assets are limited to 1) the amount of federal income taxes paid in prior years that can be recovered through loss carrybacks for existing temporary differences that reverse by the end of the subsequent calendar year, plus 2) the lesser of the remaining gross deferred tax assets expected to be realized within one year of the financial statement date or 10% of capital and surplus excluding any net deferred tax assets, electronic data processing (EDP) equipment and operating software and any net positive goodwill, plus 3) the amount of remaining gross deferred tax assets that can be offset against existing gross deferred tax liabilities. The remaining deferred tax assets are nonadmitted. Gross deferred income tax assets are reduced by a valuation allowance if the Company determines it is more likely than not that some portion or all of the gross deferred tax assets will not be realized. Deferred taxes do not include amounts for state income taxes. Under GAAP, state income taxes would be included in the computation of deferred taxes, a deferred tax asset would be recorded for the amount of gross deferred tax assets expected to be realized in future years, and a valuation allowance would be established for deferred tax assets not realizable.
- Commissions allowed by reinsurers on business ceded are reported as a reduction of expense when incurred to the extent the amount does not exceed actual acquisition costs, rather than being deferred and amortized with deferred policy acquisition costs as would be required by GAAP. Commissions in excess of the acquisition costs, if any, would be deferred and recognized over the policy term consistent with GAAP.
- Certain other reported amounts are classified or presented differently in the financial statements prepared on the basis of SAP than they would be under GAAP. Statutory requirements require that the financial statements of the Company be filed with state regulatory authorities. Accordingly, the financial statements are presented in a format similar to the filed annual statement, which differs from the format of financial statements presented under GAAP. Required statutory disclosures that are not applicable to the Company are not included in the notes to these statutory financial statements.

Other significant accounting practices are as follows:

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

1. Summary of Significant Accounting Policies (continued)

Recognition of Premium Revenues

Premiums are recorded as earned on a daily pro rata basis over the contract period that the related policies are expected to be in force. The portion of premiums not earned at the end of the period is recorded as unearned premiums. Premiums collected prior to the effective date of the policy are recorded as a liability.

Cash and Cash Equivalents

Cash and cash equivalents include demand deposits with several financial institutions and other highly liquid investments with original maturities of three months or less and certificates of deposit with original maturities of one year or less and are principally stated at cost, which approximates fair value.

Investments

Investments are recorded at admitted asset values as prescribed by the valuation procedures of the NAIC's Securities Valuation Office (SVO). The valuation technique used to measure fair value (market value) is to obtain the published securities' fair value from the SVO publication, *Valuation of Securities*. If the specific security is not listed in this publication, then the fair value is obtained from a registered U.S. exchange.

Short-term investments include investments with original maturities of one year or less from the time of acquisition and are principally stated at cost, which approximates fair value.

Concentration of Credit Risk

The Company's financial instruments exposed to concentrations of credit risk consist primarily of its investments, cash and cash equivalents, short-term investments, reinsurance recoveries, and premium revenue. The Company maintains its cash and cash equivalents at several financial institutions. Deposits with financial institutions are insured by the Federal Deposit Insurance Corporation (FDIC) up to \$250,000 per depositor. Bank deposit accounts, at times, may exceed federally insured limits. The Company has not experienced any losses in such accounts.

All investment transactions have credit exposure to the extent that a counterparty may default on an obligation to the Company. Credit risk is a consequence of carrying investment positions. To manage credit risk, the Company focuses primarily on highly liquid debt instruments, reviews the credit strength of all entities in which it invests, limits its exposure in any one investment, and monitors portfolio quality, taking into account credit ratings assigned by recognized credit rating organizations.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

1. Summary of Significant Accounting Policies (continued)

Reinsurance

The accompanying statutory basis financial statements reflect reserves for premiums and losses and loss adjustment expenses (LAE), net of reinsurance ceded (see Note 9). Those reinsurance arrangements allow management to control exposure to potential losses arising from large risks and catastrophic events. A significant portion of the reinsurance is effected under a quota share reinsurance agreement. Amounts recoverable from reinsurers are estimated in a manner consistent with the loss and LAE reserves associated with the reinsured policies. Reinsurance premiums, losses, and LAE are accounted for on bases consistent with those used in accounting for the original policies issued and the terms of the reinsurance contracts.

Loss and Loss Adjustment Expense (LAE) Reserves

Loss and LAE reserves represent the estimated ultimate net cost of all unpaid reported and unreported losses and LAE. The reserves for unpaid losses and LAE are estimated using individual case-basis estimates for reported losses and actuarial estimates for losses incurred but not yet reported. Those estimates are subject to the effects of trends in loss severity and frequency. Although considerable variability is inherent in such estimates, management believes that the reserves for losses and LAE are adequate. The estimates are continually reviewed and adjusted as necessary as experience develops or new information becomes known; such adjustments are included in current operations. The ultimate settlement of losses and LAE may vary significantly from the estimated amounts included in the financial statements. The Company does not discount its loss and LAE reserves.

The anticipated effect of inflation is implicitly considered when estimating liabilities for losses and LAE. While anticipated price increases due to inflation are considered in estimating the ultimate claim costs, the increase in average severities of claims is caused by a number of factors that vary with the individual type of policy written. Future average severities are projected based on historical trends adjusted for implemented changes in underwriting standards, policy provisions, and general economic trends. Those anticipated trends are monitored based on actual development and the estimated liabilities are modified if necessary.

Loss and LAE reserves are reported net of reinsurance recoverables for unpaid losses and LAE. Losses and LAE ceded through reinsurance are credited against losses and LAE incurred.

Premium Deficiency Reserves

Premium deficiency reserves are established for the estimated amount of the anticipated losses, loss adjustment expenses, commissions and other acquisition costs, and maintenance costs that have not previously been expensed in excess of the recorded unearned premium reserve and future installment premiums on existing policies. The Company does not use anticipated investment income as a factor in the premium deficiency calculation.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

1. Summary of Significant Accounting Policies (continued)

Guaranty Fund and Residual Market Pool Assessments

The Company is subject to assessments by a Florida guaranty fund, a residual market pool, and a state catastrophe reinsurance pool. The activities of this fund and these pools include collecting funds from solvent insurance companies to cover losses resulting from the insolvency or rehabilitation of other insurance companies or deficits generated by Florida Insurance Guaranty Association (FIGA), Citizens Property Insurance Corporation (Citizens), and the Florida Hurricane Catastrophe Fund (FHCF).

The Company's policy is to recognize its obligation for guaranty fund, Citizens, and FHCF assessments when the Company has the information available to reasonably estimate its liabilities. Guaranty fund, Citizens, and FHCF assessments are generally available for recoupment from policyholders and as such, amounts assessed are recorded as a recoverable asset. Amounts recoverable are generally expected to be collected during the year following assessment.

The Company was not assessed in 2011. The FIGA assessment recoverable from policyholders for past assessments was \$1,365,890 at June 30, 2011.

Certain Citizens and FHCF assessments are collected from policyholders as policies are written and subsequently remitted to the assessing entity. Amounts due from policyholders for these assessments were \$396,805 at June 30, 2011. The liability for assessments collected and due to Citizens and FHCF totaled \$1,161,917 at June 30, 2011.

Income Taxes

The Company calculates its state and federal income tax liabilities based upon the statutory rates in effect during the year.

Subsequent Events

The Company has evaluated subsequent events through October 21, 2011, the date the financial statements were available to be issued.

Use of Estimates

The preparation of statutory basis financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the statutory basis financial statements, and the reported amounts of revenues and expenses during the reporting period. Such estimates and assumptions could change in the future as more information becomes known, which could impact the amounts reported and described in the financial statements.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

2. Restatement of Surplus

Change in Accounting Method

The Company has changed its method of accounting for ceded losses under its multi-cedent quota share reinsurance contracts. Both HWIC and HPIC are named insureds (cedents) in the 2009-2010 quota share agreement with Hannover Re, Greenlight Re, and Signet Star Re. HWIC and HPIC are also cedents under the 2010-2011 quota share agreement with Greenlight Re.

In June 2011, the accounting for allowable ceded incurred losses under the quota share agreements was changed. Previously, for contracts in which losses exceeded the loss corridor, allowable ceded incurred losses were allocated to HPIC and HWIC in proportion to each cedent's ceded incurred losses. The new method of allocating allowable ceded incurred losses to each cedent is in proportion to each entity's ceded earned premium.

Under the new allocation method, HWIC receives the benefit of ceded incurred losses that had previously been allocated to HPIC on an inception to date basis. Approximately \$3.9 million in ceded incurred losses were transferred from HPIC to HWIC at June 30, 2011, when the adjustment was recorded. Of the \$3.9 million in additional ceded incurred losses, \$3.4 million was a transfer of ceded paid losses that had previously been recorded in HPIC's accounts. These amounts represent an amount that is recoverable from HPIC. Because these amounts are deemed to be not collectible from HPIC, the \$3.4 million due from HPIC has been recorded as a non-admitted asset in the statement of admitted assets, liabilities, and capital and surplus – statutory basis at June 30, 2011.

Of the \$3.9 million in additional ceded incurred losses allocated to HWIC, approximately \$500,000 is due to a transfer of ceded loss reserves from HPIC to HWIC. Because ceded losses are recovered from the quota share reinsurers when the related losses are paid and not when incurred, this amount represents a recoverable from the reinsurer. This amount is included in loss and loss adjustment expense reserves in the statement of admitted assets, liabilities, and capital and surplus – statutory basis at June 30, 2011.

The cumulative effect of the change in accounting increased surplus \$3,891,514 as of January 1, 2011. Additionally, as a result of this accounting change, loss and loss adjustment expenses incurred decreased by \$105,000 for the six months ended June 30, 2011.

Adjustments Relating to Subsequently Discovered Facts

As a result of subsequently discovered facts after the issuance of the independent auditors' report dated April 3, 2011, in the Company's December 31, 2010 statutory financial statements, certain admitted assets and liabilities have been restated and are reported as an adjustment to beginning surplus.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

2. Restatement of Surplus (continued)

Adjustments Relating to Subsequently Discovered Facts (continued)

As discussed in Note 12, HMC began withdrawing advances from the premium trust accounts established for the benefit of the Company in September 2010. These withdrawals were relating to advance premiums that had been deposited in the trust accounts. Florida Statute 626.883 states that premiums received by an administrator on behalf of an insured are deemed to be received by the insurer; therefore, the amount of advance premiums collected by the managing general agent, HMC, of \$3,951,300 as of January 1, 2011, represents a liability of the Company to its policyholders and should have been recorded as such. Advance premium withdrawals by HMC totaled \$3,500,000 at January 1, 2011, and are reported as a nonadmitted asset in accordance with Florida Statute 625.012.

Also discussed in Note 12, certain bank fees have been charged to the premium trust accounts and recorded as an expense by HMC and have not been repaid to the premium trust accounts. At January 1, 2011, the accumulated balance of bank fees, net of interest income, is \$580,712. This balance is also reported as a nonadmitted asset in accordance with Florida Statute 625.012.

Beginning surplus as of January 1, 2011, has been decreased by \$4,080,712 relating to the advances made to HMC from the premium trust accounts.

The subsequent discovery of the inappropriate use of the premium trust accounts by HMC creates substantial uncertainties as to the net realizable value of other admitted assets reported by the Company on its December 31, 2010, statutory financial statements. Accordingly, the amounts reported for receivables from parent and affiliates (\$9,116,996) and net deferred tax asset (\$1,111,649) have been reported as nonadmitted and with a 100% valuation allowance, respectively, as of January 1, 2011.

The restatement of beginning surplus as of January 1, 2011, consists of the following:

| | |
|---|------------------------|
| Cumulative effect of change in accounting method | \$ 3,891,514 |
| Nonadmitted premium trust account advances | (4,080,712) |
| Nonadmitted receivable from parent and affiliates | (9,116,996) |
| Deferred tax asset valuation allowance | (1,111,649) |
| | <u>\$ (10,417,843)</u> |

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

3. Business Combinations

On May 31, 2011, Glencoe Acquisition, Inc. (Glencoe), the ultimate parent company of First Home Insurance Company (NAIC# 10149) (FHIC), acquired all of the outstanding stock of HomeWise Holdings, Inc. (HWH), the parent company of HomeWise Insurance Company (NAIC# 12438) (HWIC). Both FHIC and HWIC were licensed property and casualty insurers in the state of Florida prior to the merger.

Concurrent with the purchase of HWH, FHIC and HWIC merged into one company, with FHIC as the surviving entity. This transaction was accounted for as a statutory merger. No goodwill was recorded as a result of this merger, and no shares of stock were issued as part of this transaction as Glencoe was the ultimate parent of both insurance companies; however, subsequent to the merger, all of the outstanding shares of stock of HWIC were cancelled and FHIC changed its name to HomeWise Insurance Company (NAIC# 10149) (the Company).

The results of operations of the previously separate entities for the period January 1, 2011 through May 31, 2011, prior to the combination that are included in the current combined net loss are as follows:

| <u>January 1, 2011 through May 31, 2011</u> | <u>HWIC</u> | <u>FHIC</u> |
|---|-------------|-------------|
| Net earned premiums | \$ 298,404 | \$ 858,554 |
| Losses and loss adjustment expenses incurred | 6,508,108 | 2,719,826 |
| Underwriting, acquisition, and other expenses | (648,468) | 1,315,745 |

4. Going Concern

The Company incurred a net loss of approximately \$13,422,000 for the six months ended June 30, 2011. At June 30, 2011, its total liabilities exceed its total admitted assets by approximately \$2,084,000. Additionally, as discussed in Note 14, the Company has lost its independent rating subsequent to June 30, 2011, which severely limits its ability to write new or renewal business. The Company's surplus (deficit) position at June 30, 2011, is not in compliance with the minimum requirements under Florida Statute 624.408. As a result of these factors, there is considerable doubt about the ability of the Company to continue as a going concern. The statutory basis financial statements do not include any adjustments that might result from the outcome of this uncertainty.

5. Regulatory Requirements and Restrictions

Florida Statute 624.408 requires the Company to maintain capital and surplus of \$5 million or 10% of the Company's total liabilities for losses, loss adjustment expenses, and unearned premiums, whichever is greater, and to meet the risk-based capital requirements as discussed in Note 11. Additionally, Florida Statute 624.4095 requires the Company to maintain a ratio of the product of written premiums times 0.90 to surplus of no greater than 10-to-1 for gross written premiums and 4-to-1 for net written premiums. The Company is not in compliance with these requirements (see Note 4).

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

5. Regulatory Requirements and Restrictions (continued)

Additionally, the Company is required to maintain deposits pursuant to Florida and Louisiana statutes to help secure the payment of claims. Cash on deposit in the amount of \$363,689 and a long-term note of \$305,700 have been assigned to the Office as of June 30, 2011, and certificates of deposit in the amount of \$200,000 have been assigned to the Louisiana Department of Insurance as of June 30, 2011, to satisfy this requirement. These amounts are included in total cash and invested assets in the accompanying statements of admitted assets, liabilities, and capital and surplus at June 30, 2011.

6. Investments

The aggregate carrying value (amortized cost) and SVO market value of bonds at June 30, 2011, are as follows:

| | <u>Amortized Cost</u> | <u>Gross Unrealized Gains</u> | <u>Gross Unrealized Losses</u> | <u>SVO Market Value</u> |
|--|---------------------------|---------------------------------------|--|---------------------------------|
| Bonds: | | | | |
| U.S. Government and government agencies | \$ <u>1,809,936</u> | \$ <u>21,444</u> | \$ <u>-</u> | \$ <u>1,831,380</u> |

A summary of the aggregate carrying value (amortized cost) and SVO market value of bonds at June 30, 2011, by contractual maturity, is as follows:

| | <u>Amortized Cost</u> | <u>SVO Market Value</u> |
|---------------------------------------|---------------------------|-----------------------------|
| Due in one year or less | \$ 1,504,236 | \$ 1,516,755 |
| Due after one year through five years | <u>305,700</u> | <u>314,625</u> |
| Total | \$ <u>1,809,936</u> | \$ <u>1,831,380</u> |

The expected maturities in the foregoing table may differ from the contractual maturities because certain borrowers have the right to call or prepay obligations with or without call or prepayment penalties. The Company is exposed to certain risks and uncertainties as a result of the current credit crisis and resulting impact on the larger U.S. economy. The nature of those risks and uncertainties may effect changes in cash flows as a result of changes in the liquidity of financial markets.

The Company had no sales or maturities of investments in bonds during the six months ended June 30, 2011.

Short-term investments consist of money market funds that have a maturity of one year or less from the date of purchase and are stated at cost, which approximates fair value.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

6. Investments (continued)

Major categories of the Company's net investment income for the six months ended June 30, 2011, are summarized as follows:

| | |
|---------------------------------|------------------|
| Investment income: | |
| Bonds | \$ 29,781 |
| Short-term investments and cash | <u>15,345</u> |
| Total investment income | 45,126 |
| Investment expenses | <u>(12,861)</u> |
| Net investment income | <u>\$ 32,265</u> |

7. Premiums Receivable

Premiums receivable includes amounts due from HMC and FHIA, the Company's managing general agents (MGA), who collect all premiums and remit them to the Company. The Company nonadmits balances due from insureds and deferred installments for which a portion of the receivable is more than 90 days past due and exceeds the related unearned premium. Premiums receivable is charged to bad debt expense in the period determined uncollectible. Recoveries received on amounts previously charged-off are credited to bad debt expense in the period received. Premiums receivable totaled \$14,871,351, net of \$729,542 of nonadmitted premiums receivable, as of June 30, 2011.

8. Loss and Loss Adjustment Expense (LAE) Reserves

The following table provides a reconciliation of the beginning and ending reserve balances for losses and LAE, net of reinsurance recoverables, at June 30, 2011.

| | |
|--|-----------------------|
| | <i>(in thousands)</i> |
| Loss and LAE reserves at beginning of period | \$ 17,906 |
| Cumulative effect of change in accounting method | (584) |
| Losses and LAE incurred related to: | |
| Current year | 10,902 |
| Prior years | <u>4,293</u> |
| | 15,195 |
| Losses and LAE paid related to: | |
| Current year | 3,972 |
| Prior years | <u>8,645</u> |
| | <u>12,617</u> |
| Loss and LAE reserves at end of period | <u>\$ 19,900</u> |

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

8. Loss and Loss Adjustment Expense (LAE) Reserves (continued)

Anticipated reinsurance recoverables on unpaid losses and LAE are approximately \$11,661,000 at June 30, 2011. Reinsurance recoverables on paid losses and LAE are approximately \$8,465,000 at June 30, 2011.

Net incurred losses and LAE attributable to insured events of prior years have increased \$4,293,000 in the six months ended June 30, 2011, as a result of reestimation of unpaid losses and loss adjustment expenses. Original estimates are decreased or increased as additional information becomes known regarding individual claims.

9. Reinsurance

Certain premiums and benefits are ceded to other insurance companies under various reinsurance agreements. The reinsurance agreements provide the Company with increased capacity to write more risks and maintain its exposure to loss within its capital resources. As of June 30, 2011, the Company's reinsurance program consisted of catastrophe excess of loss reinsurance and quota share treaties. Following is a summary of the reinsurance coverage.

The catastrophe excess of loss coverage is provided by agreements with commercial reinsurers and by the FHCF. Coverage under the FHCF is limited to qualifying storms occurring in the state of Florida. For the six months ended June 30, 2011, the commercial excess of loss treaties generally provide coverage on ultimate net losses of approximately \$91,900,000 in excess of \$8,300,000 per occurrence, not to exceed approximately \$183,800,000 for all occurrences. The FHCF provided coverage for 90% of the losses from qualifying catastrophic events in excess of approximately \$60,800,000 up to a maximum of approximately \$271,700,000, plus 100% of qualifying losses in excess of approximately \$2,900,000 (drop down layer) up to a maximum of approximately \$12,900,000. The drop down layer provides for one automatic reinstatement at 100% of its original limit.

Effective June 1, 2010, HWIC and its affiliated company, HomeWise Preferred Insurance Company (collectively, the Reinsured), entered into a quota share reinsurance agreement with Greenlight Reinsurance Ltd. (Greenlight). Under the terms of the agreement, Greenlight assumes a percentage (80% on policies written through December 31, 2010, with loss dates between June 1 and December 31, 2010; 90% on policies written through December 31, 2010, with loss dates after December 31, 2010; 85% on policies written after December 31, 2010, through May 31, 2011; and 80% on policies written thereafter) of the Reinsured's incurred losses and loss adjustment expenses, subject to several exclusions. The Reinsured cedes a percentage of gross premiums (equal to the percentage of losses assumed by Greenlight as described above), subject to several exclusions, after deducting a portion of the cost of the excess of loss reinsurance treaties, described above. The agreement is effective through May 31, 2012.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

9. Reinsurance (continued)

The reinsurance agreement is subject to a loss retention corridor, whereby the Reinsured retains losses above a minimum gross loss ratio ranging from 40.33% to 42.26% up to a maximum gross loss ratio ranging from 62.91% to 65%. Maximum losses ceded under this agreement are limited to 93% of the premiums earned for policies written through December 31, 2010, and 90% of the premiums earned for policies written thereafter. The ceding commission from Greenlight is equal to 31% of Greenlight's share of gross written premium, prior to the deduction of any premiums paid for catastrophe excess of loss protection. Additionally, the Reinsured is allowed a profit commission on a sliding scale basis for loss ratios under 42.26%. The current year ceding commissions have been recorded as a reduction of underwriting, acquisition, and other expenses in the accompanying statements of operations.

The FHCF provides coverage for named hurricanes only and provides no coverage after the one time limit is exhausted. Reinsurance premiums for the FHCF are paid on a total insured value basis. In the event of a loss assessment, the Company may recoup the assessments from its policyholders.

Effective June 1, 2011, the Company executed reinsurance premium protection agreements to reinsure the reinstatement premium payment obligations which accrue to the Company under the private catastrophe excess of loss agreements. The coverage is limited to 100% of the original contracted reinsurance placement.

The Company's reinsured risks are treated, to the extent of the reinsurance, as though they are risks for which the Company is not liable. However, the Company remains liable in the event the reinsuring companies do not meet their obligations under these reinsurance agreements. Given the quality of the reinsuring companies, management believes this possibility to be remote. See Note 8 for recoveries due from reinsurers relating to paid and unpaid losses and LAE.

The effects of reinsurance on premiums written and earned for the six months ended June 30, 2011, are as follows:

| | <u>Written</u> | <u>Earned</u> |
|-----------------|------------------------|---------------------|
| Direct premiums | \$ 77,081,616 | \$ 77,188,438 |
| Ceded premiums | <u>(96,810,930)</u> | <u>(73,888,112)</u> |
| Net premiums | <u>\$ (19,729,314)</u> | <u>\$ 3,300,326</u> |

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

9. Reinsurance (continued)

The following table summarizes the effect of ceded unearned premiums on the direct unearned premiums reserve and provides the related commission equity at June 30, 2011:

| | |
|--------------------------|------------------------|
| Direct unearned premiums | \$ 78,815,931 |
| Ceded unearned premiums | <u>(91,925,174)</u> |
| Unearned premiums, net | <u>\$ (13,109,243)</u> |
| Commission equity, net | <u>\$ 20,562,680</u> |

The following table shows the effect of reinsurance on loss and loss adjustment expenses incurred during the six months ended June 30, 2011:

| | |
|--|----------------------|
| Direct losses and loss adjustment expenses incurred | \$ 35,266,954 |
| Assumed losses and loss adjustment expenses incurred | 656,262 |
| Ceded losses and loss adjustment expenses incurred | <u>(20,728,209)</u> |
| Losses and loss adjustment expenses incurred, net | <u>\$ 15,195,007</u> |

At June 30, 2011, unsecured reinsurance recoverables on paid and unpaid losses and LAE and unearned premiums by reinsurer that were equal to or greater than 3% of surplus are as follows:

| | |
|------------------------------------|---------------|
| Greenlight Reinsurance | \$ 22,081,000 |
| Florida Hurricane Catastrophe Fund | 2,859,000 |

For the six months ended June 30, 2011, recoveries under reinsurance contracts totaled \$16,777,419.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

10. Income Taxes

Income before federal income taxes differs from taxable income principally due to differences in loss and LAE reserves and unearned premiums for tax and statutory basis financial reporting purposes.

State income taxes are classified as taxes, licenses, and fees in the NAIC Annual Statement and as underwriting, acquisition, and other expenses in the accompanying statement of operations.

A. The components of net deferred tax assets (DTAs) and deferred tax liabilities (DTLs) at June 30, 2011, are as follows:

| | <u>Ordinary</u> | <u>Capital</u> | <u>Total</u> |
|--|-------------------|----------------|-------------------|
| Total gross DTAs | \$15,841,031 | \$ - | \$15,841,031 |
| Statutory valuation allowance adjustment | <u>15,744,412</u> | <u>-</u> | <u>15,744,412</u> |
| Adjusted gross DTAs | 96,619 | - | 96,619 |
| Total gross DTLs | - | - | <u>96,619</u> |
| Net DTA | | | - |
| Nonadmitted DTAs | | | - |
| Net admitted DTA | | | <u>\$ -</u> |
| Increase in nonadmitted DTAs | | | <u>\$ -</u> |

The Company has not elected to admit additional DTAs pursuant to SSAP 10R, paragraph 10(e). The current period election does not differ from the prior reporting period.

The amount of each result or component of the calculation, by tax character, of paragraphs 10.a., 10.b.i., 10.b.ii., and 10.c. are as follows:

| | <u>Ordinary</u> | <u>Capital</u> | <u>Total</u> |
|--|-----------------|----------------|--------------|
| Can be recovered through loss carrybacks (10.a.) | \$ - | \$ - | \$ - |
| Lesser of: | | | |
| Expected to be recognized within one year (10.b.i.) | - | - | - |
| Ten percent of adjusted capital and surplus (10.b.ii.) | - | - | - |
| Adjusted gross DTAs offset against existing DTLs (10.c.) | - | - | - |
| Risk-based capital level used in paragraph 10.d.: | | | |
| Total adjusted capital | | | - |
| Authorized control level | | | - |

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

10. Income Taxes (continued)

The following amounts resulting from the calculation in paragraphs 10.a., 10.b., and 10.c. are as follows:

| | |
|------------------------|------------|
| Admitted DTAs | \$ - |
| Admitted assets | - |
| Statutory surplus | 18,799,788 |
| Total adjusted capital | 18,799,788 |

B. Unrecognized DTLs:

Not applicable.

C. Current tax and change in deferred tax:

The provision for income taxes incurred on earnings for the six months ended June 30 is:

| | |
|---------------------------------|---------------|
| Current year income tax expense | \$ - |
| Prior year underaccrual | 118 |
| Current income taxes incurred | <u>\$ 118</u> |

The tax effect of temporary differences that give rise to significant deferred tax assets and deferred tax liabilities is as follows:

Deferred Tax Assets:

| | |
|-----------------------------------|-------------------|
| Discount on unpaid losses and LAE | \$ 458,701 |
| Nonadmitted assets | 237,027 |
| Profit sharing | 46,330 |
| Charitable contribution | 34,000 |
| Net operating loss | <u>15,064,973</u> |
| Total DTAs | 15,841,031 |
| Statutory valuation allowance | <u>15,744,412</u> |
| Admitted DTAs | <u>96,619</u> |

Deferred Tax Liabilities:

| | |
|------------------------------|---------------|
| Depreciation of fixed assets | <u>96,619</u> |
| Total DTLs | <u>96,619</u> |

| | |
|-------------------|-------------|
| Net admitted DTAs | <u>\$ -</u> |
|-------------------|-------------|

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

10. Income Taxes (continued)

D. Reconciliation of federal income tax rate to actual effective rate:

The significant book-to-tax adjustments were as follows:

| | | Percentage of Pre-Tax Income |
|--------------------------------------|------------------------|---|
| Provision computed at statutory rate | \$ (4,483,175) | 34.00 % |
| Pre-merger excluded statutory income | 1,863,532 | (14.13) |
| Change in nonadmitted assets | (8,902,301) | 67.51 |
| Prior period adjustment | 198,920 | (1.51) |
| Total | <u>\$ (11,323,024)</u> | <u>85.87 %</u> |
| Federal income tax | \$ 118 | 0.00 % |
| Change in deferred taxes | <u>(11,323,142)</u> | <u>85.87</u> |
| Statutory income taxes | <u>\$ (11,323,024)</u> | <u>85.87 %</u> |

E. Operating loss and tax credit carryforwards, and protective tax deposits:

1. At June 30, 2011, the Company had no unused capital losses and approximately \$39,817,000 of net operating loss carryforwards available to offset against future taxable income expiring between 2025 and 2030. Of this amount, approximately \$5,261,000 is subject to limitations under Sec. 382 of the Internal Revenue Code. The limitation caps the net operating loss carryforwards to approximately \$310,000 annually.
2. There is no income tax expense that is available for recoupment in the event of future net losses.
3. The Company did not have any protective tax deposits under Section 6603 of the Internal Revenue Code.

F. Consolidated federal income tax return:

The Company's federal income tax return is consolidated with the following:

Glencoe Acquisition, Inc.
 First Home Acquisition Company, LLC
 HomeWise Holdings, Inc.
 First Home Insurance Agency, LLC
 HomeWise Preferred Insurance Company
 HomeWise Management Company

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

10. Income Taxes (continued)

The method of allocation between the companies is subject to written agreement, approved by the Board of Directors. Allocation is based upon separate return calculations with current credit for net losses. Intercompany balances are settled quarterly.

11. Capital and Surplus

The Company has authorized 1,000,000 shares of \$1 par value common stock, of which 650,000 shares are issued and outstanding at June 30, 2011. By Board of Directors' resolution on May 31, 2011, 649,900 shares of stock were issued to FHFC in a non-cash transaction. In conjunction with the merger of FHIC and HWIC (see Note 3), HWIC cancelled all 650,000 of its issued and outstanding shares on May 31, 2011, and reclassified the common capital stock to paid-in capital. No other classes of common or preferred shares were issued during 2011. The parent company, FHFC, is the sole shareholder.

Property and casualty insurance companies are subject to certain Risk-based Capital (RBC) requirements as specified by the NAIC. Under those requirements, the amount of capital and surplus maintained by a property and casualty insurance company is to be determined based on the various risk factors related to it. RBC requirements are not calculated for interim reporting periods.

The maximum amount of dividends that may be paid by property and casualty insurance companies without prior approval of the Office is subject to restrictions relating to statutory surplus and net income. Furthermore, during the three years following the entry of Consent Order No. 117706-11 on May 23, 2011, the Company may only pay dividends that are approved in advance and in writing by the Office. The Company did not declare or pay any dividends during the six months ended June 30, 2011.

12. Related Party Transactions

The Company's related parties and affiliations are described in Note 1, Organization and Description of the Company.

Effective January 1, 2010, the Company entered into a Technology Services Agreement with an insurance services company that holds an ownership interest in Glencoe. Fees incurred under this agreement totaled \$6,300 for the six months ended June 30, 2011.

Effective May 4, 2005, the Company entered into a service agreement with FHFC. Pursuant to the agreement, FHFC provides to the Company capital management services and investor management and relations and assists with overall general management of the Company. Expenses incurred related to this agreement totaled \$64,666 for the six months ended June 30, 2011. At June 30, 2011, the Company has a net receivable due from FHFC in the amount of \$63,766.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

12. Related Party Transactions (continued)

Effective May 3, 2005, the Company entered into a managing general agency contract with FHIA. Pursuant to the agreement, FHIA provides to the Company premium billing, claims management and underwriting functions. Expenses incurred related to this agreement totaled \$1,106,683 for the six months ended June 30, 2011. At June 30, 2011, the Company has a net receivable due from FHIA in the amount of \$520,641.

The following describes related party agreements executed by HWIC prior to the merger with FHIC that were still in effect subsequent to the merger.

Effective January 1, 2006, HWIC entered into a managing general agency agreement with HMC. Pursuant to the agreement, HMC provides to HWIC premium billing, claims management and underwriting functions. Expenses incurred related to this agreement totaled \$15,686,790 during the six months ended June 30, 2011. During the first quarter of 2011, HWIC and HMC agreed to a reduced compensation rate, which resulted in a \$4,752,850 reduction in fees. Under the terms of this agreement, HMC collects all premiums and deposits them into premium trust accounts for holding until the companies settle at the end of the month. Beginning in September 2010, HMC withdrew amounts relating to advance premium that had been deposited in the provider trust accounts. At June 30, 2011, the total amount of advances withdrawn from the premium trust accounts was \$5,700,000. Additionally, bank fees charged to the premium trust accounts and expensed by the MGA totaling \$600,987 have not been repaid to the premium trust accounts. The Company has recorded a receivable from HMC in the amount of 6,300,987 at June 30, 2011, all of which has been nonadmitted in accordance with Florida Statute 625.012.

HWIC is also party to a Cost Allocation Agreement with HPIC, HMC, and HHI in which expenses benefiting more than one company are allocated based upon direct allocation or revenue allocation rules, whichever is most appropriate for the expense. As a result of the Cost Allocation Agreement and the other transactions described above, the Company has a net receivable due from HPIC of \$812,328 at June 30, 2011, and a receivable due from HMC of \$8,807,436 at June 30, 2011. Amounts receivable from HPIC and HMC of \$707,156 and \$8,807,436, respectively, have been nonadmitted at June 30, 2011.

HomeWise Insurance Company

Notes to Statutory Basis Financial Statements

13. Premiums Produced by Managing General Agents or Third Party Administrators

The Company uses managing general agents, HMC and FHIA, to write and administer insurance products. HMC has contracted with an unaffiliated service company and FHIA has contracted with an affiliated service company to provide this function. The total premium produced and serviced through the contracts during 2011 is summarized below. The Company retains underwriting authority for all policies issued under these agreements.

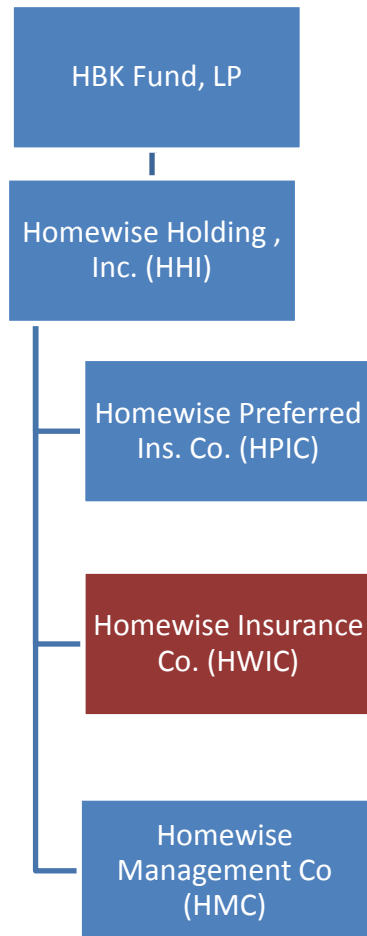
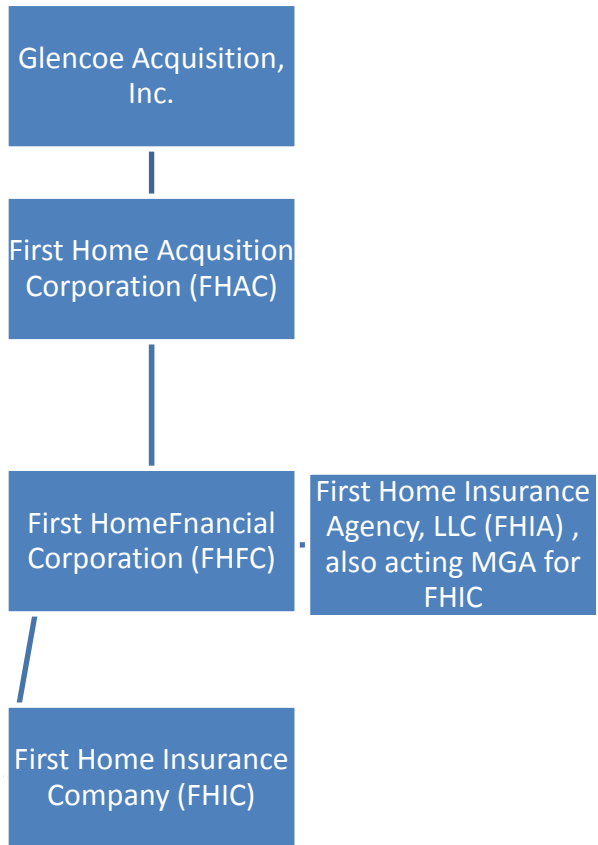
| <u>Name and Address</u> | <u>FEI Number</u> | <u>Exclusive Contract</u> | <u>Type of Business Written</u> | <u>Type of Authority Granted</u> | <u>Direct Premium Written</u> |
|--|-------------------|---------------------------|---------------------------------|---|-------------------------------|
| HomeWise Management Company 4042 Park Oaks Boulevard, Suite 400 Tampa, FL 33610 | 20-3395152 | No | Homeowners | Premium collection, claims adjustments, binding authority, and underwriting | \$ 72,325,713 |
| First Home Insurance Agency, LLC 4042 Park Oaks Boulevard, Suite 400 Tampa, FL 33610 | 20-2634733 | No | Homeowners | Premium collection, claims adjustments, binding authority, and underwriting | \$ 4,755,903 |

14. Subsequent Events

During August 2011, the Company's chief executive officer and chief financial officer departed. The operations of the Company are being overseen by one of the directors of FHFC, the Company's parent, while the Company searches for suitable replacements.

On August 25, 2011, Demotech, Inc. withdrew its Financial Stability Rating® of A, *Exceptional*, assigned to the Company. As a result, the Company's quota share reinsurer has the right to cancel the Company's quota share reinsurance agreement with 60 days written notice.

EXHIBIT II



ORGANIZATION CHART

Homeowners Choice (HCPCI) – Homewoners Choice Inc. (NASDAQ HCII)