Examination Warrant Number 12-00000-10750-R1

Report of Examination of

1st Choice Auto Insurance Company
Everett, Pennsylvania

As of December 31, 2012

TABLE OF CONTENTS

Harrisburg, Pennsylvania
April 2, 2014

Honorable Stephen J. Johnson, CPA
Deputy Insurance Commissioner
Commonwealth of Pennsylvania
Insurance Department
Harrisburg, Pennsylvania

Dear Sir:

In accordance with instructions contained in Examination Warrant Number 12-00000-10750-R1, dated February 29, 2012, an examination was made of

1st Choice Auto Insurance Company, NAIC Code: 10750

a Pennsylvania domiciled property and casualty insurance company, hereinafter referred to as "Company" or "FCA". The examination was conducted at the Company's home office, located at 10591 Lincoln Highway, Everett, Pennsylvania 15537.

A report of this examination is hereby respectfully submitted.

SCOPE OF EXAMINATION

The Company was last examined as of December 31, 2007.

This examination covered the five-year period from January 1, 2008 through December 31, 2012, and consisted of a general survey of the Company's business practices, management, and operations, and an evaluation of the Company's financial condition as of the latter date. Material subsequent events were also reviewed.

Work programs employed in the performance of this examination were designed to comply with the standards promulgated by the Pennsylvania Insurance Department ("Department") and the National Association of Insurance Commissioners ("NAIC").

The format of this report is consistent with the current practices of the Department and the examination format prescribed by the NAIC. It is limited to a description of the Company, a discussion of financial items that are of specific regulatory concern, and a disclosure of other significant regulatory information.

For each year during the period under examination, the Certified Public Accounting ("CPA") firm of Buffamante Whipple Buttafaro, P.C. ("BWB") provided an unqualified audit opinion on the Company's year-end financial statements based on statutory accounting principles. Relevant work performed by the CPA firm, during its annual audit of the Company, was reviewed during the examination and incorporated into the examination workpapers.

The following companies were examined at the same time during the above examination:

Company	NAIC Code
Everett Cash Mutual Insurance Company	17043
Ever-Greene Mutual Insurance Company	17213

HISTORY

The Company was incorporated on March 29, 2000, licensed by the Department on August 30, 2000 and commenced business on August 30, 2000.

There were no changes to the Company's Articles of Incorporation or By-laws during the current examination period.

The Company is currently authorized to transact those classes of insurance described in 40 P.S. § 382 (b)(2) Inland Marine and Auto Physical Damage and (c)(11) Auto Liability.

The Company and affiliates, Everett Cash Mutual Insurance Company and Ever-Greene Mutual Insurance Company, were assigned a group code of 4761 by the NAIC on June 14, 2012.

MANAGEMENT AND CONTROL

CAPITALIZATION

As of the examination date, December 31, 2012 the Company's total capital was $7,621,887, consisting of 2,118 capital shares of issued and outstanding common stock with a par value of $850 per share amounting to $1,800,300, $3,302,183 in paid in and contributed surplus and $2,519,404 in unassigned funds (surplus).

The Company's minimum capital and minimum surplus requirements for the types of business for which it is licensed, pursuant to 40 P. S. § 386, is $850,000 in capital and $425,000 in surplus. The Company has met all governing requirements throughout the examination period.

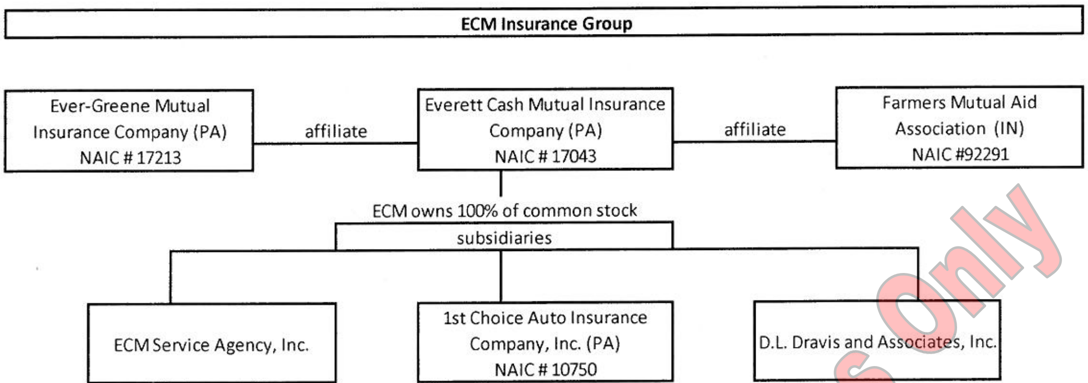
STOCKHOLDER

Everett Cash Mutual Insurance Company ("ECM") holds all issued and outstanding common stock in the Company. There have been no dividends declared or paid to the sole stockholder during the examination period.

INSURANCE HOLDING COMPANY SYSTEM

The Company meets the requirements for filing an Insurance Holding Company System Registration Statement, in compliance with the 40 P.S. §§ 991.1401 - 991.1413. The required filings have been made for all years under examination. ECM is named as the ultimate controlling person in the system.

An organizational chart of the holding company system at December 31, 2012 is as follows:



Everett Cash Mutual Insurance Company is named as the ultimate controlling person in the system. Members of the Holding Company System include the following entities briefly described below:

The **ECM Insurance Group** is comprised of Everett Cash Mutual Insurance Company, Ever-Greene Mutual Insurance Company, 1st Choice Auto Insurance Company, Inc., ECM Service Agency, Inc., Farmers Mutual Aid Association and D.L. Dravis and Associates, Inc. ECM holds one hundred percent (100%) of the outstanding stock of ECM Service Agency, Inc., 1st Choice Auto Insurance Co., Inc. and D.L. Dravis and Associates, Inc. as of December 31, 2012.

ECM is a property and casualty mutual insurance company licensed in Georgia, Indiana, Kentucky, Maryland, North Carolina, Ohio, Pennsylvania, Tennessee and Virginia as of December 31, 2012. The Company has not written any business in Georgia or Tennessee as of December 31, 2012. ECM became licensed in Georgia, Kentucky, Ohio and Tennessee since the prior examination.

ECM has developed computer software known as ChoiceConnect. ChoiceConnect is registered with the United States Copyright Office effective September 6, 2002 and ECM is the listed author. The software has been sold to various insurance companies and is supported by ECM staff. ECM made commission payments to various Company officers and IT employees for the sales and support of the software during the examination period. The Company is currently developing an upgrade to the computer software.

FCA is a property and casualty stock insurance company licensed in Georgia, Indiana, Kentucky, North Carolina, Ohio, Pennsylvania, Tennessee and Virginia as of December 31, 2012. As of December 31, 2012, the Company has not written any business in Georgia, Ohio or Tennessee. FCA became licensed in Georgia, Kentucky, Ohio, Tennessee and Virginia since the prior examination.

Ever-Greene Mutual Insurance Company ("EGM") is a property and casualty mutual insurance company licensed to write business only in Pennsylvania as of December 31, 2012. EGM assumes the Commercial Fire and Extended Coverage business written in Pennsylvania by ECM.

Farmers Mutual Aid Association ("FMAA") is an Indiana domiciled farm mutual insurance company under direct management of ECM.

ECM Service Agency, Inc. ("ECMSA") provides service to the customers of prior agents who are no longer writing business on ECM paper. The Group insurance agents are licensed through ECMSA and the agent appointment fees for the Group are paid through this agency. ECMSA is not an active income producing company.

D.L. Dravis and Associates, Inc. ("DRAVIS") is a claims adjusting company acquired by ECM on March 31, 2011. This company provides claims adjusting services for ECM, FCA, EGM and other insurers in Pennsylvania. ECM transferred their claims adjusters to this Company as of January 1, 2013.

BOARD OF DIRECTORS

Management of the Company is vested in its Board of Directors ("Board"), which was comprised of the following members as of the examination date, December 31, 2012:

Name and Address	Principal Occupation
Randy F. Shaw Everett, Pennsylvania	President and Chief Executive Officer 1st Choice Auto Insurance Company, Inc.
Kenneth C. Stover Roaring Springs, Pennsylvania	President Kenneth C. Stover, Inc.
Donn C. Whetstone Everett, Pennsylvania	Retired
Richard E. Rowan Chambersburg, Pennsylvania	Retired
George H. Bridenbaugh Martinsburg, Pennsylvania	Retired
Jeffrey S. Whetstone Everett, Pennsylvania	President Whetstone Insurance Associates, Inc.
Mark N. Barnhart Roaring Spring, Pennsylvania	Chief Executive Officer NPC, Inc.
Larry R. Webber Hollidaysburg, Pennsylvania	Business Consultant Self-employed Institute for Strategic Management Affiliate

Jerry L. Stanner Howe, Indiana	President Stanner Appraisal Service, Inc.
Bette B. Slayton Bedford, Pennsylvania	President Bedford County Development Association

The members of the Board of Directors were each elected to a three year term. The Company's By-laws state the Directors are to be elected annually. Further discussion and recommendation are below in the By-laws section.

The Company has a conflict of interest policy and the directors and officers sign conflict of interest statements annually.

The member composition of the Board of Directors of the Company is identical with its parent company, ECM, and its affiliates EGM and FMAA.

COMMITTEES

All committees are established at the parent company, ECM, level. As of the examination date, December 31, 2012, the Directors and/or Officers were assigned to serve on the following ECM Committees as listed below:

Audit Committee: Mark N. Barnhart, George H. Bridenbaugh, Richard E. Rowan, Bette B. Slayton

Building and Grounds Committee: Mark N. Barnhart, Bette B. Slayton, Jeffrey S. Whetstone

Compensation Committee: Mark N. Barnhart, George H. Bridenbaugh, Richard E. Rowan, Larry R. Webber

Executive Committee: George H. Bridenbaugh, Richard E. Rowan, Kenneth C. Stover, Donn C. Whetstone

Investment Committee: George H. Bridenbaugh, Randy F. Shaw, Jerry L. Stanner, Donn C. Whetstone, Jeffrey S. Whetstone, Larry R. Webber

The Building and Grounds Committee is an inactive committee with no meetings held during the examination period.

40 P.S.§ 991.1405(c)(3) Standards of management of an insurer within a holding company system, states: "not less than one-third of the directors of a domestic insurer and not less than one-third of the members of each committee of the board of directors of any domestic insurer shall be persons who are not officers or employees of such insurer or of any entity controlling, controlled by or under common control with such insurer and who are not beneficial owners of a controlling interest in the voting stock of such insurer of any such entity. At least one such person must be included in any quorum for the transaction of business of business at any meeting of the board of directors or any committee thereof."

40 P.S. § 991.1405 (c)(4) Standards and management of an insurer within a holding company system, further states that "the board of directors of a domestic insurer shall establish one or more committees comprised solely of directors who are not officers or employees of the

insurer or of any entity controlling, controlled by or under common control with the insurer and who are not beneficial owners of a controlling interest in the voting stock of the insurer or any such entity. The committee or committees shall have the responsibility for recommending the selection of independent certified public accountants, reviewing the insurer's financial condition, the scope and results of the independent audit and any internal audit, nominating candidates for director for election by shareholders or policyholders, evaluating the performance of officers deemed to be principal officers of the insurer and recommending to the board of directors the selection and compensation of the principal officers."

40 P.S. § 991.1405 (c)(4.1) Standards and management of an insurer within a holding company system, states that "the board of directors of a domestic insurer shall establish one or more committees comprised solely of directors who are not officers or employees of the insurer or of any entity controlling, controlled by or under common control with the insurer. The committee or committees shall have responsibility for recommending candidates to be nominated by the board of directors, in addition to any other nominations by voting shareholders or policyholders, for election as directors by voting shareholders or policyholders, evaluating the performance of officers deemed to be principal officers of the insurer and recommending to the board of directors the selection and compensation of the principal officers."

40 P.S. § 991.1405 (c)(5) Standards of management of an insurer within holding company system states that "the provisions of paragraphs (3), (4) and (4.1) shall not apply to a domestic insurer if the person controlling such insurer is an insurer or another business entity having a board of directors and committees thereof which already meet the requirements of paragraphs (3), (4) and (4.1)."

The Company has board membership that meets the necessary independence to comply with paragraph (3) as cited above.

The Company's parent, ECM, has established board committees and independent committees to comply with paragraphs (3), (4) and (4.1) as cited above.

OFFICERS

As of the examination date, December 31, 2012, the following officers were appointed and serving in accordance with the Company's By-laws:

Name	Title
Randy F. Shaw	President and Chief Executive Officer
Kerry S. Foor	Treasurer and Chief Financial Officer
Shirley I. Mock	Secretary

CORPORATE RECORDS

MINUTES

A compliance review of corporate minutes revealed the following:

- The Annual Meetings of the Company's Stockholder were held in compliance with its By-laws.
- The Stockholder elected Directors at such meetings; however the elections were not in compliance with the By-laws as discussed in the By-laws section below.
- The Stockholder ratified the prior year's actions of the officers and directors.
- The Company's Officers were appointed at the Annual Reorganizational Meeting of the Company.
- Quorums were present at all Directors' meetings.
- The Company's investment transactions were approved quarterly by the Board.
- All directors attended Board meetings regularly.
- The Company's reinsurance contract coverage was reviewed with the Board of Directors. Directors approved management's decisions for the reinsurance program.

ARTICLES OF INCORPORATION

There were no changes to the Company's Articles of Incorporation during the examination period.

BY-LAWS

There were no changes to the Company's By-laws during the examination period.

A review of the By-laws showed that the Company was not in compliance with its By-laws, Article III, Section 1 that states "Each Director shall be selected to serve for a term of one year and until his or her successor has been selected and qualified or until his or her death, resignation or removal." The directors were elected to three-year terms on a staggered basis during the examination period.

It is recommended the Company comply with Article III, Section 1 of its By-laws.

SERVICE AND OPERATING AGREEMENTS

Cost Sharing Agreement

The Company is party to a cost sharing agreement with its parent, ECM, and certain other affiliates of the ECM Group. ECM provides certain management services including, but not limited to, operating management, underwriting, claims processing expertise, accounting, financial reporting and record keeping systems, data management capabilities, clerical support and physical plants and equipment to the Company.

The percentage of expenses allocated by ECM to the Company is determined on the ratio of policies written by the Company compared to the total number of policies written by the Group. The Company is required to settle its allocated share of expenses within thirty (30) days subsequent to the receipt of the annual report of expenses prepared by ECM following year-end. The Company pays quarterly deposits to ECM for its expenses.

The cost sharing agreement was revised on May 5, 2009 to be effective January 1, 2009. The agreements are of unlimited duration and define the expenses to be allocated.

Tax Allocation Agreement

The Company is party to a tax allocation agreement with its parent and certain affiliated entities. The previous agreement executed January 23, 2008 was amended and executed June 10, 2011. The amended agreement was made effective for all tax years beginning January 1, 2011, removed 1st Choice Holdings, Inc. from the agreement and added DRAVIS to the agreement. The tax allocation agreement was approved by the Company's Board of Directors.

The agreements with the affiliates meet the standards in 40 P.S. § 991.1405(a)(1).

REINSURANCE

CEDED

Per Risk Excess of Loss

The Company entered into a one-year Per Risk Excess of Loss agreement with its parent, ECM, effective January 1, 2012. The agreement covers automobile liability and collision lines of business written by the Company. The Company retains the first $50,000 and ECM is liable for losses up to $700,000. This agreement was renewed for the 2013 and 2014 reinsurance years with no significant changes.

The Company and its parent, ECM, along with EGM and FMAA ("Group") are named insureds on the following reinsurance agreements with unaffiliated reinsurers:

U.S. RE Corporation as Intermediary

ECM, the Company's sole stockholder and ultimate controlling person, executed reinsurance agreements through U.S. RE Corporation ("US RE"), acting as the intermediary, with the subscribing reinsurers, for the 2012 reinsurance program covering the Group. ECM pays the reinsurance premiums to the unaffiliated reinsurers and then allocates to the affiliated companies their respective amounts based on the risks written by each affiliate. The agreements include insolvency clauses, with cut-through provisions, and cash call provisions. The agreements also include Extra Contractual Obligations ("ECO") and Losses in Excess of Policy Limits ("XPL") coverage. ECM retains the right to cancel subscribing reinsurers in the event of specified triggers and the right to terminate the agreements at expiration in cut-off or run-off status. The agreements do not contain specified settlement due dates unless the cash call provision is invoked. The individual treaties and subscribing reinsurers as of December 31, 2012 are discussed below.

Property Excess of Loss

The Group's reinsurance program includes a one-year dual layer Property Excess of Loss treaty covering the property lines of business. The Group retains $750,000 and the reinsurer is liable for the excess up to $750,000 each loss and $2,250,000 each loss occurrence on the first layer. The Group retains $1,500,000 and the reinsurers are liable for the excess up to $2,250,000 each loss and $4,500,000 each loss occurrence on the second layer. The treaty includes a reinstatement provision whereby the reinsurers' limit of liability is increased to $12,000,000 on the first layer and the second layer remains at a limit of $4,500,000. This agreement has six (6) authorized subscribing reinsurers.

Property Catastrophe Excess of Loss

The Property Catastrophe Excess of Loss coverage is a one-year dual layer treaty covering the property lines of business. The reinsurers' limit of liability is $7,000,000 on the first layer and $5,000,000 on the second layer. If reinstatement is activated, the reinsurers' liability increases to $14,000,000 on the first layer and $10,000,000 on the second. The attachment point for this treaty is $3,000,000 on the first layer and $10,000,000 on the second layer. This agreement has nine (9) authorized subscribing reinsurers and one (1) unauthorized subscribing reinsurer, which has a five percent (5%) share, on the first layer. The second layer has seven (7) authorized reinsurers and one (1) unauthorized reinsurer with a five percent (5%) share. The unauthorized reinsurer is Anadolu Sigorta.

Casualty Excess of Loss

The Casualty Excess of Loss coverage is a one-year dual layer treaty covering the workers' compensation and automobile physical damage and liability policies. The reinsurer's limit of liability for the workers' compensation policies is $500,000 in excess of the Group's retention of $500,000 for the first layer and $4,000,000 in excess of the Group's retention of $1,000,000 for the second layer. The reinsurer's limit of liability for the automobile policies is $250,000 in excess of the $750,000 Group retention. This treaty does not include a reinstatement clause. Scor Reinsurance Company, an authorized reinsurer, is the sole subscribing reinsurer for the agreement.

Casualty Clash

The Casualty Clash coverage is a one-year treaty covering the Group's excess liability after the Casualty Excess of Loss coverage above is exhausted. This covers the workers' compensation and automobile policies. The reinsurers' limit of liability is $1,000,000 in excess of $1,025,000. The agreement includes a reinstatement provision; however the reinsurers' maximum limit of liability is $1,000,000 for any one loss and $2,000,000 for all losses. There are two (2) authorized subscribing reinsurers on this agreement, with QBE Reinsurance Corporation having seventy percent (70%) share.

The reinsurance intermediary, US RE is not licensed by the Department as required by 40 P.S. §321.2 (a) Reinsurance intermediaries; licensing. Furthermore, 40 P.S. § 321.3 stipulates that "transactions between a reinsurance broker and the insurer it represents shall be only entered into pursuant to a written authorization, specifying the responsibilities of each party." Neither the Company nor ECM has entered into a written intermediary agreement with US RE.

It is recommended that Reinsurance Intermediaries utilized for the Company's reinsurance program be licensed in compliance with 40 P.S. § 321.2(a). It is further recommended that the Company have a written Intermediary Agreement with any intermediaries utilized for the Company's reinsurance program in compliance with 40 P.S. § 321.3.

Anadolu Sigorta is not an authorized reinsurer. The Company reported the reinsurer as an authorized reinsurer on the 2012 Annual Statement Schedule F.

It is recommended that the Company follow the NAIC Annual Statement filing instructions by properly reporting unauthorized reinsurers.

General Reinsurance Corporation Umbrella Quota Share

The Umbrella Quota Share treaty covers the Company and its parent, ECM, for commercial umbrella policies effective after January 1, 2008. The reinsurer is liable for seventy-five percent (75%) of the first $1,000,000 and ninety-five percent (95%) of any difference between the policy limit and $1,000,000. The reinsurer's liability limit for ECO and XPL combined in any one occurrence under any one policy is the lesser of $4,500,000 or ninety percent (90%) of each occurrence policy limit. Currently, the Company does not write umbrella coverage policies.

Historically, new risks for the Company have been reinsured with an unaffiliated reinsurer until such time as the risk becomes sufficiently stable and the Company decides to retain the entire risk or to reinsure the risk through a series of affiliated and non-affiliated agreements. Company management reviews these agreements, however there is no record to indicate the Board has guidelines in place for the approval of the agreements.

It is recommended the Company establish a written Reinsurance Policy to provide the Board of Directors a guideline for evaluating the Company's plans or goals in accordance with good business practices. The Board of Directors should adopt agreements, subsequent changes and terminations in accordance with good business practices.

The Company's intercompany ceded reinsurance agreements do not contain specific due dates for premium and loss settlement payments in accordance with NAIC Statements of Statutory Accounting Principles ("SSAP") No. 25, paragraph 7 which states "Transactions between related parties must be in the form of a written agreement. The written agreement must provide for timely settlement of amounts owed, with a specified due date. Amounts owed to the reporting entity over ninety days from the written agreement due date shall be nonadmitted. If the due date is not addressed by the written agreement any uncollected receivable is nonadmitted."

The agreements do not contain required items in accordance with SSAP No. 62R section 8c which states "The agreement shall constitute the entire contract between the parties and must provide no guarantee of profit, directly or indirectly, from the reinsurer to the ceding entity or from the ceding entity to the reinsurer" and 8d which states "The agreement must provide for reports of premiums and losses, and payment of losses, no less frequently than on a quarterly basis, unless there is no activity during the period. The report shall set forth the ceding entity's total loss and loss expense reserves on the policy obligations subject to the agreement, so that the respective obligations of the ceding entity and reinsurer will be recorded and reported on a basis consistent with this statement".

It is recommended that the Company execute intercompany reinsurance agreements that contain specific due dates in accordance with SSAP No. 25, paragraph 7. It is further recommended that the Company execute intercompany reinsurance agreements that contain entire agreement clauses and report clauses that provide for reports to be submitted no less frequently than quarterly in accordance with SSAP No. 62R, sections 8c and 8d.

Cut Through Provisions

The various reinsurance agreements the Company is party to include a provision within the Insolvency clause which allows for the possibility that certain beneficiaries be paid directly by the reinsurer (hereafter referred to as cut-through provisions). 40 P.S. § 442.1(d) states that, "No such credit shall be allowed for reinsurance unless the reinsurance agreement provides that payment by the company shall be made directly to the ceding company or to its liquidator, receiver, or statutory successor." If the Company allows such cut-through provisions to remain in its reinsurance contracts, the Department may consider an adjustment to disallow reinsurance credits related to such contracts. This would mean that no credit shall be allowed as an admitted asset or as a reduction of liability relative to risks ceded by the Company under the contracts that contain a cut-through provision.

It is recommended the Company amend its reinsurance agreements to remove any provision which allows certain beneficiaries to be paid directly by the reinsurer, so as to ensure that the Company will receive reinsurance credit for its reinsurance contracts.

ASSUMED

The Company did not assume reinsurance during the period under examination.

TERRITORY AND PLAN OF OPERATION

The Company is licensed in the following jurisdictions:

Georgia	Indiana	Kentucky
North Carolina	Ohio	Pennsylvania
Tennessee	Virginia	

As of December 31, 2012 the Company was writing business in all states except Georgia, Ohio and Tennessee.

The Company writes private passenger automobile liability, commercial automobile liability and automobile physical damage policies.

Line of Business	Direct and Assumed Premium	Ceded Premium	Net Written Premium	Percentage of Total
December 31, 2012				
Private passenger auto liability	$ 2,465,653	$ 261,435	$ 2,204,218	33.2%
Commercial auto liability	1,959,473	200,687	1,758,786	26.5%
Auto physical damage	3,017,456	342,062	2,675,394	40.3%
Totals	$ 7,442,582	$ 804,184	$ 6,638,398	100.0%

There have been no changes in the Company's marketing philosophy since the prior examination. The Company writes one-year policies through an agency network. The Keystone Insurers Group, a group of independent agents and agencies, is utilized for entry into new states. This group has the experience, contacts, and name recognition in various states, thereby giving the Company an advantage when entering new territories.

SIGNIFICANT OPERATING RATIOS AND TRENDS

The underwriting ratios summarized below are on an earned/incurred basis, and encompass the five-year period covered by this examination.

	Amount	Percentage
Premiums earned	$ 20,423,291	100.0 %
Losses incurred	$ 12,447,013	60.9 %
Loss expenses incurred	1,646,552	8.1 %
Other underwriting expenses incurred	5,969,780	29.2 %
Net underwriting gain or (loss)	359,946	1.8 %
Totals	$ 20,423,291	100.0 %

The Company reported the following net underwriting, investment and other gains or losses during the period under examination:

	2012	2011	2010	2009	2008
Admitted assets	$ 13,517,391	$ 12,352,781	$ 11,637,721	$ 10,844,998	$ 9,774,043
Liabilities	$ 5,895,504	$ 4,793,864	$ 4,094,248	$ 3,717,395	$ 3,447,415
Surplus as regards policyholders	$ 7,621,887	$ 7,558,917	$ 7,543,473	$ 7,127,603	$ 6,326,628
Gross premium written	$ 7,442,582	$ 5,596,657	$ 4,493,186	$ 4,014,154	$ 3,743,643
Net premium written	$ 6,638,398	$ 4,979,969	$ 3,972,013	$ 3,611,981	$ 3,376,932
Underwriting gain/(loss)	$ (545,420)	$ (243,681)	$ 53,624	$ 595,699	$ 499,724
Investment gain/(loss)	$ 434,919	$ 265,521	$ 432,002	$ 360,715	$ 396,988
Other gain/(loss)	$ 52,711	$ 44,671	$ 40,201	$ 37,710	$ 34,223
Net income	$ (23,814)	$ (23,436)	$ 373,380	$ 647,572	$ 596,431

The losses experienced by the Company in 2011 and 2012 are attributed to its expansion into new states beginning in 2009 and the weather related events of 2011 and 2012. The Company is monitoring the risk exposure on the coastal areas and has made changes to the underwriting guidelines for the high risk exposures.

ACCOUNTS AND RECORDS

The Company operates as a shell company with no employees or facilities. ECM provides all key management and operating services to the Company under a Cost Sharing agreement as discussed in the Service and Operating Agreements section of the report. Services include, but are not limited to, operating management, underwriting, claims processing expertise, accounting, financial reporting and record keeping systems, data management capabilities, clerical support and physical plants and equipment.

PENDING LITIGATION

As of December 31, 2012, the Company is subject to litigation and arbitration arising in the normal course of business. As of the date of this examination report, April 2, 2014, the Company is not a party to any material litigation or arbitration, other than as routinely encountered in claims activity, which will, in the opinion of management, have a material adverse effect on the Company's capital and surplus.

FINANCIAL STATEMENTS

The financial condition of the Company, as of December 31, 2012, and the results of its operations for the five-year period under examination, are reflected in the following statements:

Comparative Statement of Assets, Liabilities, Surplus and Other Funds;
Comparative Statement of Income;
Comparative Statement of Capital and Surplus; and
Comparative Statement of Cash Flow

Comparative Statement of Assets, Liabilities, Surplus and Other Funds
As of December 31,

	2012	2011	2010	2009	2008
Bonds	$ 8,665,278	$ 7,122,350	$ 7,305,337	$ 5,963,837	$ 6,265,552
Common stocks	2,143,800	1,311,761	1,901,130	994,674	54,886
Cash, cash equivalents, and short term investments	631,689	2,407,096	1,215,398	2,822,138	2,357,780
Aggregate write-ins for invested assets	0	0	0	1	1
Subtotals, cash and invested assets	11,440,767	10,841,207	10,421,865	9,780,650	8,678,219
Investment income due and accrued	68,034	51,431	66,155	57,143	81,152
Premiums and agents' balances due	1,766,905	1,280,388	1,011,104	870,843	853,948
Amounts recoverable from reinsurers	294	0	1,088	887	0
Net deferred tax asset	241,392	179,756	137,509	135,475	160,724
Aggregate write-ins for other than invested assets	(1)	(1)	0	0	0
Total	$ 13,517,391	$ 12,352,781	$ 11,637,721	$ 10,844,998	$ 9,774,043
Losses	$ 1,183,125	$ 958,356	$ 836,205	$ 709,986	$ 686,000
Loss adjustment expenses	127,000	117,169	117,989	107,000	103,000
Commissions payable, contingent commissions and other similar charges	107,095	52,441	43,873	48,786	28,547
Other expenses	37,700	33,300	29,000	38,220	33,600
Taxes, licenses and fees	49,919	26,617	10,583	10,675	18,673
Current federal and foreign income taxes	82,111	43,838	214,380	346,600	330,266
Unearned premiums	3,747,253	2,768,446	2,190,709	1,938,103	1,800,321
Advance premium	207,718	171,763	144,312	120,790	91,720
Ceded reinsurance premiums payable (net of ceding commissions)	222,092	252,171	209,113	129,602	143,433
Amounts withheld or retained by company for account of others	2,991	0	0	0	0
Payable to parent, subsidiaries and affiliates	128,500	369,763	298,084	267,633	211,855
Total liabilities	5,895,504	4,793,864	4,094,248	3,717,395	3,447,415
Common capital stock	1,800,300	1,800,300	1,800,300	1,800,300	1,800,300
Gross paid in and contributed surplus	3,302,183	3,302,183	3,302,183	3,302,183	2,774,700
Unassigned funds (surplus)	2,519,404	2,456,434	2,440,990	2,025,120	1,751,628
Surplus as regards policyholders	7,621,887	7,558,917	7,543,473	7,127,603	6,326,628
Totals	$ 13,517,391	$ 12,352,781	$ 11,637,721	$ 10,844,998	$ 9,774,043

Comparative Statement of Income
For the Year Ended December 31,

Underwriting Income	2012	2011	2010	2009	2008
Premiums earned	$ 5,659,591	$ 4,402,232	$ 3,719,408	$ 3,474,199	$ 3,167,861
Deductions:					
Losses incurred	3,925,828	2,931,284	2,290,224	1,660,832	1,638,845
Loss expenses incurred	477,990	382,608	322,666	268,659	194,629
Other underwriting expenses incurred	1,801,193	1,332,021	1,052,894	949,009	834,663
Total underwriting deductions	6,205,011	4,645,913	3,665,784	2,878,500	2,668,137
Net underwriting gain or (loss)	(545,420)	(243,681)	53,624	595,699	499,724
Investment Income					
Net investment income earned	280,550	351,141	311,792	352,496	405,095
Net realized capital gains or (losses)	154,369	(85,620)	120,210	8,219	(8,107)
Net investment gain or (loss)	434,919	265,521	432,002	360,715	396,988
Other Income					
Net gain or (loss) from agents' or premium balances charged off	1,224	1,473	737	1,441	0
Finance and service charges not included in premiums	50,010	43,198	39,464	36,269	34,223
Aggregate write-ins for miscellaneous income	1,477	0	0	0	0
Total other income	52,711	44,671	40,201	37,710	34,223
Net income before dividends to policyholders and before federal and foreign income taxes	(57,790)	66,511	525,828	994,124	930,935
Federal and foreign income taxes incurred	(33,976)	89,947	152,448	346,552	334,504
Net income	$ (23,814)	$ (23,436)	$ 373,380	$ 647,572	$ 596,431

Comparative Statement of Capital and Surplus
For the Year Ended December 31,

	2012	2011	2010	2009	2008
Surplus as regards policyholders,					
December 31, previous year	$ 7,558,917	$ 7,543,473	$ 7,127,603	$ 6,326,628	$ 5,820,897
Net income	(23,814)	(23,436)	373,380	647,572	596,431
Net unrealized capital gains or (losses)	16,598	(2,222)	26,701	117,910	(82,644)
Change in net deferred income tax	70,186	41,103	15,789	11,689	15,293
Change in nonadmitted assets	0	0	0	23,804	(23,349)
Surplus adjustments:					
Paid in	0	0	0	527,483	0
Aggregate write-ins for gains and losses in surplus	0	(1)	0	(527,483)	0
Change in surplus as regards policyholder for the year	62,970	15,444	415,870	800,975	505,731
Surplus as regards policyholders,					
December 31, current year	$ 7,621,887	$ 7,558,917	$ 7,543,473	$ 7,127,603	$ 6,326,628

Comparative Statement of Cash Flow
For the Year Ended December 31,

	2012	2011	2010	2009	2008
Cash from Operations					
Premiums collected net of reinsurance	$ 6,157,756	$ 4,781,194	$ 3,934,787	$ 3,610,325	$ 3,294,239
Net investment income	298,967	364,108	298,294	357,394	380,876
Miscellaneous income	52,711	44,671	40,201	37,710	34,223
Total income	6,509,434	5,189,973	4,273,282	4,005,429	3,709,338
Benefit and loss related payments	3,701,353	2,808,045	2,164,206	1,637,733	1,764,845
Commissions, expenses paid and aggregate write-ins for deductions	2,186,996	1,686,547	1,378,796	1,196,807	1,103,403
Federal and foreign income taxes paid (recovered)	26,750	213,958	346,594	334,452	278,700
Total deductions	5,915,099	4,708,550	3,889,596	3,168,992	3,146,948
Net cash from operations	594,335	481,423	383,686	836,437	562,390
Cash from Investments					
Proceeds from investments sold, matured or repaid:					
Bonds	4,635,125	3,900,000	4,800,000	4,990,000	3,425,000
Stocks	1,421,089	658,306	2,836,960	193,592	376,800
Total investment proceeds	6,056,214	4,558,306	7,636,960	5,183,592	3,801,800
Cost of investments acquired (long-term only):					
Bonds	6,171,042	3,715,660	6,115,550	4,593,689	2,944,676
Stocks	2,016,645	204,049	3,542,286	1,017,759	672
Total investments acquired	8,187,687	3,919,709	9,657,836	5,611,448	2,945,348
Net cash from investments	(2,131,473)	638,597	(2,020,876)	(427,856)	856,452
Cash from Financing and Miscellaneous Services					
Other cash provided (applied):					
Other cash provided or (applied)	(238,269)	71,678	30,450	55,777	205,237
Net cash from financing and miscellaneous sources	(238,269)	71,678	30,450	55,777	205,237
Reconciliation of cash and short-term investments:					
Net change in cash and short-term investments	(1,775,407)	1,191,698	(1,606,740)	464,358	1,624,079
Cash and short-term investments:					
Beginning of the year	2,407,096	1,215,398	2,822,138	2,357,780	733,701
End of the year	$ 631,689	$ 2,407,096	$ 1,215,398	$ 2,822,138	$ 2,357,780

SUMMARY OF EXAMINATION CHANGES

There were no changes made to the Company's financial statements as a result of this examination.

NOTES TO FINANCIAL STATEMENTS

ASSETS

INVESTMENTS

As of December 31, 2012, the Company's invested assets were distributed as follows:

	Amount	Percentage
Bonds	$ 8,665,278	75.7 %
Common stocks	2,143,800	18.7 %
Cash	82,653	0.7 %
Short-term investments	549,036	4.9 %
Totals	$ 11,440,767	100.0 %

The Company's bond and short-term investment portfolio had the following quality and maturity profiles:

NAIC Designation	Amount	Percentage
1 - highest quality	$ 8,489,150	92.1 %
2 - high quality	725,164	7.9 %
Totals	$ 9,214,314	100.0 %

Years to Maturity	Amount	Percentage
2 to 5 years	3,408,871	36.9 %
6 to 10 years	2,512,749	27.3 %
11 to 20 years	3,063,976	33.3 %
over 20 years	228,718	2.5 %
Totals	$ 9,214,314	100.0 %

As of December 31, 2012 the Company has approximately eighty-one percent (81%) of its invested assets in cash, short-term investments, and bonds. The Company invests in high quality securities and has the bond portfolio laddered to support reasonable asset-liability matching. Approximately sixty-four percent (64%) of the invested assets have maturity dates of ten years or less.

The Company has approximately twenty one percent (21%) of its invested assets held in a brokerage account as of December 31, 2012. These assets are not covered by a custodial agreement as required by 31 Pa. Code § 148a.3 and are not held by a qualified custodian as required by 31 Pa. Code§ 148a.2. Pennsylvania ("PA") Insurance Regulations require invested assets to be deposited with a qualified custodian and to be covered by a custodial agreement that is in compliance with 31 Pa. Code § 148a.2 and 148a.3, respectively.

It is recommended the Company have all invested assets held by a qualified custodian and covered by a custodial agreement as required by 31 Pa. Code § 148a.

The Company's remaining invested assets are covered by a custodial agreement with National City Bank, which was merged into the PNC Financial Group effective December 31, 2008, that is in compliance with 31 Pa. Code § 148a.3.

The Company has a written investment policy as required by 40 P.S. § 653b (b). The investment policy is reviewed and approved on an annual basis by the Board of Directors. The Company, at December 31, 2012, was following its investment policy.

LIABILITIES

LOSS AND LOSS ADJUSTMENT EXPENSE RESERVES

The Company reported reserves for losses and loss adjustment expenses of $1,183,125 and $127,000, respectively, on the December 31, 2012 Annual Statement.

Steven J. Regnier, ACAS, MAAA, of Regnier Consultant Group, Inc. ("Regnier") has been the Company's appointed actuary for the examination period. For each year of the examination period, Regnier issued a Statement of Actuarial Opinion ("Opinion") concluding that the Company's reserves make a reasonable provision for all unpaid loss and loss adjustment expense obligations of the Company.

In conjunction with the on-site examination, the Department's property and casualty actuarial staff conducted a risk-focused review of the Company's reserves. This review included a review of Regnier's Actuarial Report issued in support of the December 31, 2012 Opinion.

Based upon procedures performed and results obtained, the Department's property and casualty actuarial staff accepts the appointed actuary's opinion that the gross and net reserve amounts carried by the Company "make a reasonable provision for all unpaid loss and loss expense obligations of the company under the terms of its contracts and agreements" as of December 31, 2012.

SUBSEQUENT EVENTS

The Company provided notice to the Department February 28, 2014 of its intent to apply for licensure in the state of Texas.

The application for Intermediary licensure submitted by US RE was received by the Department Licensing Division on April 10, 2014.

The Company's parent, Everett Cash Mutual Insurance Company, has initiated amendments to remove the Insolvency Clause Cut-through provisions in the current reinsurance agreements.

RECOMMENDATIONS

PRIOR EXAMINATION

The prior examination report contained the following recommendations:

1. It is recommended the Company provide the correct information to all questions in the General Interrogatory section of the Annual Statement.

   The Company has complied with this recommendation.

2. It is recommended that the Company's books and records provide clear and accurate disclosure of the expenses that result from services provided under contractual agreement between affiliated parties of the Everett Cash Mutual Group, as required by SSAP Nr. 25, paragraph 17.

   The Company has complied with this recommendation.

3. It is recommended the Company comply with Pennsylvania Statute P.S. 40 § 991.1405 (a) (1) (iv) by correctly maintaining their respective books and records of ECM and FCA related to transactions involving services between the related parties by recording \$527,483 as a capital investment by ECM in FCA as a result of fees forgiven by the ECM Board of Directors.

   The Company has complied with this recommendation.

CURRENT EXAMINATION

As a result of the current examination, the following recommendations are being made:

1. It is recommended the Company comply with Article III, Section 1 of its By-laws. (See "By-laws", page 7)

2. It is recommended that Reinsurance Intermediaries utilized for the Company's reinsurance program be licensed in compliance with 40 P.S. § 321.2(a). It is further recommended that the Company have a written Intermediary Agreement with any intermediaries utilized for the Company's reinsurance program in compliance with 40 P.S. § 321.3. (See "Reinsurance Ceded", page 10)

3. It is recommended that the Company follow the NAIC Annual Statement filing instructions by properly reporting unauthorized reinsurers. (See "Reinsurance Ceded", page 10)

4. It is recommended the Company establish a written Reinsurance Policy to provide the Board of Directors a guideline for evaluating the Company's plans or goals in accordance with good business practices. The Board of Directors should adopt

agreements, subsequent changes and terminations in accordance with good business practices. (See "Reinsurance", page 10)

5. It is recommended that the Company execute intercompany reinsurance agreements that contain specific due dates in accordance with SSAP No. 25, paragraph 7. It is further recommended that the Company execute intercompany reinsurance agreements that contain entire agreement clauses and report clauses that provide for reports to be submitted no less frequently than quarterly in accordance with SSAP No. 62R, sections 8c and 8d. (See "Reinsurance", page 11)

6. It is recommended the Company amend its reinsurance agreements to remove any provision which allows certain beneficiaries to be paid directly by the reinsurer, so as to ensure that the Company will receive reinsurance credit for its reinsurance contracts. (See "Reinsurance, Cut Through Provisions", page 11)

7. It is recommended the Company have all invested assets held by a qualified custodian and covered by a custodial agreement as required by 31 Pa. Code § 148a. (See "Investments", page 19)

CONCLUSION

As a result of this examination, the financial condition of 1st Choice Auto Insurance Company, as of December 31, 2012, was determined to be as follows:

	Amount	Percentage
Admitted assets	$ 13,517,391	100.0 %
Liabilities	$ 5,895,504	43.6 %
Surplus as regards policyholders	7,621,887	56.4 %
Total liabilities and surplus	$ 13,517,391	100.0 %

Since the previous examination, made as of December 31, 2007, the Company's assets increased by $4,555,215, its liabilities increased by $2,754,225, and its surplus increased by $1,800,990.

This examination was conducted by Elaine Nissley, MBA, CISA, PMP, CCSA, CRISC and Diane Rudy, CPA, CIA, CISA of McKonly & Asbury, LLP, and Stephanie Ohnmacht, CFE, and Robin Roberts, CFE of the Department, with the latter in charge.

Respectfully,

Annette B. Szady /cw

Annette B. Szady, CPA
Director, Bureau of Financial Examinations

David R. Evans /cw

David R. Evans, CFE
Examination Manager

Robin Roberts /cw

Robin Roberts, CFE
Examiner-in-Charge

The CFE designation has been conferred by an organization not affiliated with the federal or any state government. However the CFE designation is the only designation recognized by the NAIC for the purposes of directing statutory Association examinations of insurance companies.