



MISSISSIPPI INSURANCE DEPARTMENT

501 N. WEST STREET, SUITE 1001
WOOLFOLK BUILDING
JACKSON, MISSISSIPPI 39201
www.doi.state.ms.us

MIKE CHANEY
Commissioner of Insurance
State Fire Marshal

MAILING ADDRESS
Post Office Box 79
Jackson, Mississippi 39205-0079
TELEPHONE: (601) 359-3569
FAX: (601) 359-2474
WATS: 1-800-562-2957 (Incoming - USA)

March 7, 2008

Daniel Tarantin, Chief Executive Officer
Direct General Insurance Company of Mississippi
1281 Murfreesboro Road
Nashville, TN 37217-2432

Re: Direct General Insurance Company of Mississippi
Report of Examination as of December 31, 2006

Dear Mr. Tarantin:

Enclosed is a Corrected Order in the above-referenced matter.

Please note that the only purpose of the Corrected Order is to change the date of the original Order from January 25, 2007, to January 25, 2008.

If you have any questions pertaining to this matter, please do not hesitate to contact this office.

Sincerely,

MIKE CHANEY
COMMISSIONER OF INSURANCE

BY J. Mark Haire
J. Mark Haire
Special Assistant Attorney General

MC/JMH/bs
Enclosure

**BEFORE THE COMMISSIONER OF INSURANCE
OF THE STATE OF MISSISSIPPI**

**IN RE: REPORT OF EXAMINATION OF DIRECT GENERAL
INSURANCE COMPANY OF MISSISSIPPI**

CAUSE NO. 07-5680

CORRECTED ORDER

THIS CAUSE came before the Commissioner of Insurance of the State of Mississippi for the sole purpose of correcting the date of the Order entered in the matter on January 25, 2007. The actual date this Order was signed by the Commissioner was January 25, 2008. Therefore, by virtue of this Corrected Order, the date of the Order in this matter is changed from January 25, 2007, to the correct date of January 25, 2008. Except for this change to correct the date of the Order, the previous Order entered in this matter is adopted herein in its entirety.

SO ORDERED, this the 7th day of March 2008.

MIKE CHANEY
COMMISSIONER OF INSURANCE
STATE OF MISSISSIPPI

BY


Lee Harrell

Deputy Commissioner



MISSISSIPPI INSURANCE DEPARTMENT

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January 25, 2007

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MIKE CHANEY
Commissioner of Insurance
State Fire Marshal

**CERTIFIED MAIL
RETURN RECEIPT REQUESTED**

Daniel Tarantin, Chief Executive Officer
Direct General Insurance Company of Mississippi
1281 Murfreesboro Road
Nashville TN 37217-2432

RE: Report of Examination as of December 31, 2006

Dear Mr. Tarantin:

In accordance with Miss. Code Ann. § 83-5-201 et seq. (Rev. 1999), an examination of your Company has been completed. Enclosed herewith is the Order adopting the report and a copy of the final report as adopted.

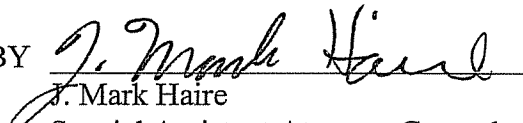
Pursuant to Miss. Code Ann. § 83-5-209(6)(a) (Rev. 1999), the Mississippi Department of Insurance shall continue to hold the content of said report as private and confidential for a period of ten (10) days from the date of the Order. After the expiration of the aforementioned 10-day period, the Department will open the report for public inspection.

If you have any questions or comments, please feel free to contact me.

Sincerely,

MIKE CHANEY
COMMISSIONER OF INSURANCE

BY


J. Mark Haire
Special Assistant Attorney General

MC/JMH/bs
Encls. Order w/exhibit

**BEFORE THE COMMISSIONER OF INSURANCE
OF THE STATE OF MISSISSIPPI**

**IN RE: REPORT OF EXAMINATION OF DIRECT GENERAL
INSURANCE COMPANY OF MISSISSIPPI**

CAUSE NO. 07-5680

ORDER

THIS CAUSE came on for consideration before the Commissioner of Insurance of the State of Mississippi ("Commissioner"), or his designated appointee, in the Offices of the Commissioner, 1001 Woolfolk Building, 501 North West Street, 10th Floor, Jackson, Hinds County, Mississippi, pursuant to Miss. Code Ann. § 83-5-201 et seq. (Rev. 1999). The Commissioner, having fully considered and reviewed the Report of Examination together with any submissions or rebuttals and any relevant portions of the examiner's work papers, makes the following findings of fact and conclusions of law, to-wit:

JURISDICTION

I.

That the Commissioner has jurisdiction over this matter pursuant to the provisions of Miss. Code Ann. § 83-5-201 et seq. (Rev. 1999).

II.

That Direct General Insurance Company of Mississippi is a Mississippi-domiciled Company licensed to write Accident & Health; Automobile Physical Damage/Liability; Casualty/Liability; Fire/Allied Lines; Home/Farm Owners; Inland Marine; Plate Glass; and Trip Accident and Baggage coverages.

FINDINGS OF FACT

III.

That the Commissioner, or his appointee, pursuant to Miss. Code Ann. § 83-5-201 et seq. (Rev. 1999), called for an examination of Direct General Insurance Company of Mississippi and appointed Mitch Rayborn, Examiner-In-Charge, to conduct said examination.

IV.

That on or about October 25, 2007, the draft Report of Examination concerning Direct General Insurance Company of Mississippi for the period of January 1, 2004 through December 31, 2006, was submitted to the Department by the Examiner-In-Charge, Mitch Rayborn.

V.

That on or about November 5, 2007, pursuant to Miss. Code Ann. § 83-5-209(2) (Rev. 1999), the Department forwarded to the Company a copy of the draft report and allowed the Company a 30-day period to submit any rebuttal to the draft report. The Department received the Company's response to the Draft Examination Report in a letter on or about December 4, 2007, and in response thereto, minor revisions were made to the Draft Report.

CONCLUSIONS OF LAW

VI.

The Commissioner, pursuant to Miss. Code Ann. § 83-5-209(3) (Rev. 1999), must consider and review the report along with any submissions or rebuttals and all relevant portions of examiner work papers and enter an Order: (1) adopting the Report of Examination as final or with modifications or corrections; (2) rejecting the Report of Examination with directions to reopen; or (3) calling for an investigatory hearing.

IT IS, THEREFORE, ORDERED, after reviewing the Report of Examination, the Company's rebuttal, and all relevant examiner work papers, that the Report of Examination of Direct General Insurance Company of Mississippi, attached hereto as Exhibit "A", should be and same is hereby adopted as final.

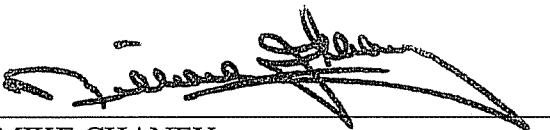
IT IS FURTHER ORDERED that a copy of the adopted Report of Examination, accompanied with this Order, shall be served upon the Company by certified mail, postage pre-paid, return receipt requested.

IT IS FURTHER ORDERED that the Mississippi Department of Insurance shall continue to hold the content of this report as private and confidential for a period of ten (10) days from the date of this Order, pursuant to Miss. Code Ann. § 83-5-209(6)(a) (Rev. 1999).

IT IS FURTHER ORDERED, pursuant to Miss. Code Ann. § 83-5-209(4) (Rev. 1999), that within thirty (30) days of the issuance of the adopted report, Direct General Insurance Company of Mississippi shall file affidavits executed by each of its directors stating under oath that they have received a copy of the adopted report and related orders.

IT IS FURTHER ORDERED that Direct General Insurance Company of Mississippi take the necessary actions and implement the necessary procedures to ensure that all recommendations contained in the Report of Examination are properly and promptly complied with.

SO ORDERED, this the 25th day of January, 2007.

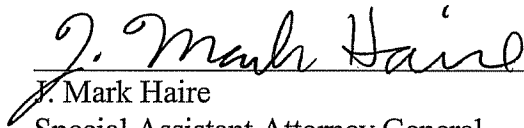


MIKE CHANEY
COMMISSIONER OF INSURANCE
STATE OF MISSISSIPPI

CERTIFICATE OF MAILING

I hereby certify that a true and correct copy of the above and foregoing Order and a copy of the final Report of Examination, as adopted by the Mississippi Department of Insurance, was sent by certified mail, postage pre-paid, return receipt requested, on this the 25th day of January, 2007, to:

**Daniel Tarantin, Chief Executive Officer
Direct General Insurance Company of Mississippi
1281 Murfreesboro Road
Nashville, TN 37217-2432**



J. Mark Haire
Special Assistant Attorney General

J. Mark Haire
Special Assistant Attorney General
Counsel for the Mississippi Department of Insurance
Post Office Box 79
Jackson, MS 39205-0079
(601) 359-3577
Miss. Bar No. 2065

STATE OF MISSISSIPPI
COUNTY OF HINDS

Mitch Rayborn, CFE, FLMI, being duly sworn, states as follows:

1. I have authority to represent the Commissioner of Insurance of the State of Mississippi in the examination of Direct General Insurance Company of Mississippi.
2. The Mississippi Insurance Department is accredited under the National Association of Insurance Commissioners Financial Regulation Accreditation Standards.
3. I have prepared the examination work papers and examination report, and the examination of Direct General Insurance Company of Mississippi as of December 31, 2006, was performed in a manner consistent with the standards and procedures required by the Commissioner of Insurance of the State of Mississippi.

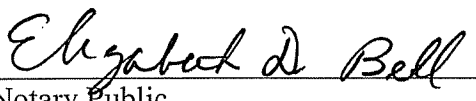
The affidavit says nothing further.



Mitch Rayborn, CFE, FLMI
Examiner

Subscribed and sworn before me this 11th day of January, 2008.

(SEAL)



Notary Public

My commission expires _____
**MISSISSIPPI STATEWIDE NOTARY PUBLIC
MY COMMISSION EXPIRES NOV 23, 2010
BONDED THRU STEGALL NOTARY SERVICE**



Mississippi Insurance Department

Report of Examination

of

**DIRECT GENERAL INSURANCE COMPANY
OF MISSISSIPPI**

**4734 North State Street
Jackson, Mississippi 39206**

As of December 31, 2006

**NAIC Company Code 10889
NAIC ETS No. MS029-C29**

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MIKE CHANEY
Commissioner of Insurance
State Fire Marshal

September 28, 2007

Honorable George Dale
Commissioner of Insurance
State Fire Marshal
Mississippi Insurance Department
501 N. West Street
1001 Woolfolk Building (39201)
Post Office Box 79
Jackson, Mississippi 39205-0079

Honorable Alfred W. Gross
Chair, Financial Condition (E) Subcommittee
Bureau of Insurance
Commonwealth of Virginia
Post Office Box 1157
Richmond, Virginia 23218

Dear Sirs:

Pursuant to Commissioner Dale's instructions and authorization and in compliance with statutory provisions, an examination has been conducted, as of December 31, 2006, of the affairs and financial condition of:

DIRECT GENERAL INSURANCE COMPANY OF MISSISSIPPI
(NAIC COMPANY CODE 10889)
4734 North State Street
Jackson, Mississippi 39206

This examination was commenced in accordance with Miss. Code Ann. § 83-5-201 et seq. and was performed in Nashville, Tennessee at the main administrative office of the Company. The report of examination is herewith submitted.

INTRODUCTION

This examination was performed by examiners representing the Mississippi Insurance Department (“MID”) and covered Direct General Insurance Company of Mississippi (“DGICMS” or “the Company”) operations and financial condition from January 1, 2004, through December 31, 2006, including material transactions and/or events occurring subsequent to the examination date and noted during the course of this examination.

For purposes of this examination report, the examination period is defined as January 1, 2004, through December 31, 2006, and the examination date is defined as December 31, 2006.

SCOPE OF EXAMINATION

This examination was a full scope financial examination that included assessing the Company’s financial condition, its ability to fulfill and manner of fulfillment of its obligations, the nature of its operations, and compliance with the law. A full scope market conduct examination was not performed; however, limited procedures were performed on specific areas of the Company’s market conduct.

This examination was conducted in accordance with procedures recommended by the National Association of Insurance Commissioners (“NAIC”) *Financial Condition Examiners Handbook*.

Reporting in the comments and recommendations section of this report was by exception; therefore, items that were tested and deemed acceptable by the examiners without material change receive little or no comment.

HISTORY OF THE COMPANY

On October 10, 1997, the Company was incorporated under the laws of the State of Mississippi as Direct General Insurance Company of Mississippi, and commenced business on May 7, 1998, with its principal office located in Nashville, Tennessee.

The original Articles of Association authorized 100,000 shares of \$50 par value capital stock. The Company’s initial capitalization consisted of Direct General Corporation purchasing 12,000 shares of the authorized capital stock for an aggregate purchase price of \$2,002,698. On December 28, 2001, the Articles of Association were amended to increase the Company’s capital stock par value to \$100 per share.

Effective December 31, 2001, all outstanding shares of the Company were contributed in the form of a capital contribution from DGC to one of its property and casualty insurance subsidiaries, Direct General Insurance Company (“DGIC”).

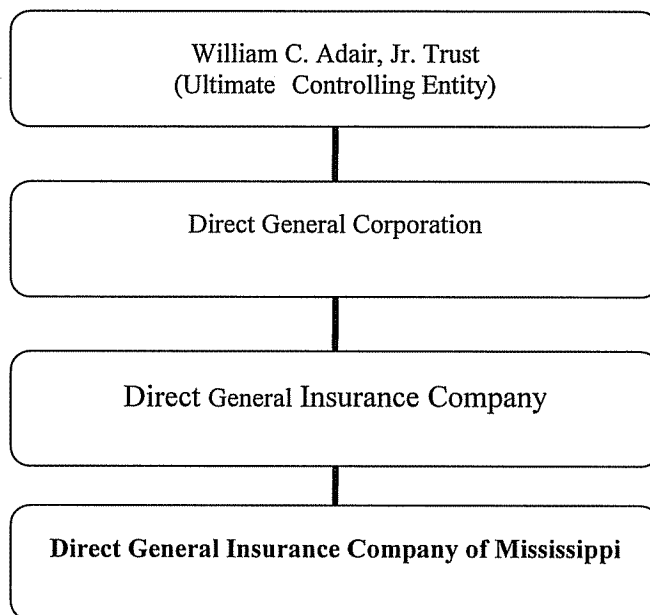
HOLDING COMPANY STRUCTURE

The Company was a member of an insurance holding company system as defined within Miss. Code Ann. § 83-6-1. Holding Company Registration Statements were filed during the examination period with the Mississippi Insurance Department in accordance with Miss. Code Ann. § 83-6-5 and § 83-6-9. The statements and applicable amendments that were filed with the Mississippi Insurance Department during the examination period were reviewed and it appeared that any changes and material transactions by and between the Company and its affiliates were disclosed appropriately.

During the examination period, Company's ultimate parent company was Direct General Corporation ("DGC"), a publicly traded (under the symbol "DRCT") Tennessee business corporation. (See Subsequent Events section in this report for ownership changes subsequent to the examination period.)

Organizational Chart

The following organizational chart displays the direct line of ownership, along with a brief description of each member:



William C. Adair Jr. Trust; The William C. Adair Jr. Trust controlled approximately 32% of Direct General Corporation's outstanding common stock and was the ultimate controlling entity. Tammy R. Adair was the sole trustee and had sole voting and investment control.

Direct General Corporation (“DGC”); This Company was incorporated on September 28, 1993 for the purpose of serving as the ultimate parent company for Direct General’s Holding Company System. Through its subsidiaries, DGC’s core business involved the issuance of nonstandard personal automobile insurance policies throughout most of the southeastern United States. Through its premium finance operations, the premium charges for the majority of the insurance policies sold by the Company were financed, with collateral being the related unearned premium associated with the policy sold.

Direct General Insurance Company (“DGIC”); This company was incorporated under the laws of the State of Florida on December 15, 1990 as Independent Property and Casualty Insurance Company (“IPC”), and began operations on January 1, 1991. Effective March 6, 1997, in contemplation of the company being sold to Direct General Corporation, IPC redomesticated to the State of Tennessee. On March 14, 1997, Direct General Corporation acquired all of the outstanding capital stock of IPC and its name was changed to its present title. Effective December 27, 2000, DGIC was redomesticated to South Carolina. At December 31, 2006, DGIC was authorized to write one or more lines of business in the States of Alabama, Florida, Georgia, Illinois, Indiana, Kansas, Mississippi, Missouri, Oklahoma, Pennsylvania, South Carolina, Tennessee, Texas and Virginia.

Direct General Insurance Company of Mississippi; The Company, wholly owned by Direct General Insurance Company, was incorporated under the laws of the State of Mississippi on October 10, 1997. See the History of the Company caption that begins on page two (2) of this examination report for additional information.

Related Party Agreements and Transactions

Inter-company Cost Sharing Agreement: The Company was a party to an inter-company cost sharing agreement, whereby affiliates of the Company provided underwriting and policy issuance, claims settlement, premium financing, and administrative services for the Company. Per this agreement, during the examination period, the Company paid \$5,116,000, \$5,249,000, and \$4,674,000 for 2006, 2005, and 2004, respectively.

Producer Agreement: The Company was a party to a producer agreement with its affiliated insurance agencies Direct General Insurance Agency, Inc. and Right Choice Insurance Agency, whereby management could pay commissions up to 15% on written premiums to its agencies. Per this agreement, during the examination period, the Company paid \$3,727,000, \$3,361,000, and \$3,174,000 for 2006, 2005 and 2004, respectively.

Consolidated Tax Allocation Agreement: With the exception of Direct Life Insurance Company and Direct General Life Insurance Company, Direct General Corporation’s subsidiaries that are greater than 80% owned are consolidated for federal income tax purposes. A consolidated federal income tax allocation agreement for year 1995 and subsequent years was entered into by the companies. The transactions under this agreement, as associated with the Company, were reviewed and no exceptions were noted.

MANAGEMENT AND CONTROL

Ownership

As of December 31, 2006, the Company had issued and outstanding twelve thousand (12,000) shares of common capital stock with a par value of \$100.00 per share. Direct General Insurance Company owned 100% of the outstanding shares. During the examination period, \$1.4 million in dividends were paid to Direct General Insurance Company.

Board of Directors

The Articles of Association and Bylaws vest the management and control of the Company's business affairs with the Board of Directors (the "Board"). The members of the duly elected Board, along with their place of residence and principal occupation, as of December 31, 2006, were:

<u>Name and Place of Residence</u>	<u>Principal Occupation or Affiliation</u>
Tammy Renee Adair Memphis, Tennessee	President Direct General Corporation
John Todd Hagely Nashville, Tennessee	Senior Vice President and CFO Direct General Corporation
Scott Anton Johnson Memphis, Tennessee	Senior Vice President of Claims Direct General Corporation

Officers

The officers holding the following positions as of December 31, 2006, were:

<u>Name</u>	<u>Position</u>
Tammy Renee Adair	President
John Todd Hagely	Senior Vice President and CFO
Scott Anton Johnson	Senior Vice President of Claims
Steven Russell Harms	VP of Finance and Treasurer
Ronald Franklin Wilson	Secretary
Rebecca Marie Baggett	Assistant Secretary
Constance Ann Collins	Assistant Secretary
Marie St. John Daugherty	Assistant Secretary
Jill Ann Fritts	Assistant Secretary

Conflict of Interest

The Company's officers and directors completed conflict of interest statements on an annual basis during the examination period. During 2006, the parent company issued a Standard Practice Memorandum related the company's Code of Ethics and Policy on Business Conduct, which included an Annual Questionnaire that is to be completed by fiduciaries of the company.

CORPORATE RECORDS

The minutes of the meetings of the Stockholder and Board of Directors, taken during the period covered by the examination, were reviewed and appeared to be complete and in order with regard to recording action on matters brought up at these meetings for deliberation, which included the approval and support of the Company's transactions and events.

FIDELITY BONDS AND OTHER INSURANCE

The Company's parent maintained a comprehensive corporate insurance program. This program included commercial general liability, and commercial property, as well as other policies, as deemed appropriate by DGC's management. DGICMS was a named insured on a financial institution bond with a \$10,000,000 aggregate limit of liability, which exceeded the minimum fidelity coverage suggested by the NAIC for a company of this size.

DIRECTORS', OFFICERS', EMPLOYEES', AND AGENTS' WELFARE

Benefits provided to directors or officers were provided through Direct General Corporation's administrative services subsidiary, Direct Administration, Inc. The Company did not have any direct employees or agents.

REINSURANCE

Prior to 2006, the Company ceded premiums and losses to other insurance companies under various quota share and excess of loss reinsurance agreements in order to provide the Company with the increased capacity to write larger volumes of business while limiting its exposure to losses. The Company's income from operations, coupled with capital contributions from its parent, DGIC, has enabled it to increase its retention of direct business written over the past three years. In 2006, the quota share reinsurance agreement was eliminated.

Reinsurance Intermediary

The Company used the services of Guy Carpenter and Company, Inc., a reinsurance intermediary, to place reinsurance with various reinsurers. Guy Carpenter and Company, Inc. was licensed and authorized by the Mississippi Insurance Department and had the authority to procure placement certificates from various reinsurers in the Company's reinsurance ceded program.

Ceded Reinsurance Agreements:

The Company maintained reinsurance in two layers. For policies issued prior to January 1, 2005, the Company ceded 100% of losses in excess of each state's minimum financial responsibility limit. Loss projections are on a total limits basis. All losses above the financial responsibility limit are ceded for policies issued prior to January 1, 2005. For policies issued after January 1, 2005, the Company retained 100% of losses in excess of each state's minimum financial responsibility limit. The Company also carried catastrophe reinsurance in addition to the quota share and excess of loss treaties.

ACCOUNTS AND RECORDS

The 2006 trial balance of the Company's accounts was tied to the balance sheet of the Company's statutory annual statement filed with the Mississippi Insurance Department, with no exceptions noted. The Company was audited annually by an independent CPA firm.

The MID's consulting actuary recommended that the Company's appointed actuary include additional documentation and improve the documentation in the actuarial report supporting the opinion. Specific recommendations are as follows:

- The actuarial report supporting the actuarial opinion did not include documentation of the calculations of the ULAE/AOE reserve. Rather, it referred to the appointed actuary's review of Company work papers containing the ULAE reserve calculations. The Company work papers were not made part of the actuarial report and were not readily available for examination. The ULAE reserve work papers were subject to the report maintenance requirements per the annual statement instructions. We recommend that future actuarial reports supporting future opinions include documentation of the

calculation of the ULAE reserve so documentation of these reserve calculations are readily available for examination. This recommendation was made in the previous examination report as of December 31, 2003;

- Documentation of material ceded reserve credits should be fully supported in the actuarial report supporting the Statement of Actuarial Opinion. This documentation should be sufficient for another actuary practicing in the same field to evaluate the work.

STATUTORY DEPOSITS

The Company's statutory deposits with the State of Mississippi complied with Miss. Code Ann. § 83-19-31 (2). The following chart displays the Company's deposits as of December 31, 2006:

<u>Type of Security</u>	<u>State Deposited</u>	<u>Par Value</u>	<u>Book Value</u>	<u>Fair Value</u>
FHLB	Mississippi	\$ 100,000	\$ 100,000	\$ 99,790
FHLB	Mississippi	\$ 310,000	\$ 310,000	\$ 307,303
FHLB	Mississippi	\$ 185,000	\$ 185,000	\$ 184,185
MS State Muni	Mississippi	\$ 400,000	\$ 402,999	\$ 403,618
Totals		<u>\$ 995,000</u>	<u>\$ 997,999</u>	<u>\$ 994,896</u>

INTRODUCTION TO THE FINANCIAL STATEMENTS

The following financial statements consist of a Statement of Admitted Assets, Liabilities, Surplus and Other Funds at December 31, 2006, a Statement of Income for year ended December 31, 2006, a Reconciliation of Capital and Surplus for the examination period ended December 31, 2006, and a Reconciliation of Examination Adjustments to Surplus.

DIRECT GENERAL INSURANCE COMPANY OF MISSISSIPPI
STATEMENT OF ADMITTED ASSETS, LIABILITIES, SURPLUS AND OTHER FUNDS
DECEMBER 31, 2006

ADMITTED ASSETS

Bonds	\$34,288,950
Cash and short-term investments	5,562,072
Investment income due and accrued	351,050
Uncollected premiums	3,437,741
Reinsurance recoverable	156,519
Current federal income taxes	182,069
Net deferred taxes	1,179,640
Receivable from parent company	9,801
State income taxes recoverable	<u>1,269</u>
 Total admitted assets	 <u>\$45,169,111</u>

LIABILITIES, SURPLUS AND OTHER FUNDS

Losses	\$10,772,005
Loss adjustment expenses	675,304
Commissions payable, contingent commissions and other similar charges	415,877
Other expenses	75,547
Taxes, licenses and fees	473,885
Unearned premiums	19,361,050
Ceded reinsurance premiums payable	33,618
Funds held by company under reinsurance treaties	70,795
Amounts withheld or retained by company for account of others	3,603
Remittances and items not allocated	6,027
Payable to parent, subsidiaries and affiliates	<u>305,361</u>
Total Liabilities	<u>32,193,072</u>
 Common capital stock	 1,200,000
Gross paid in and contributed surplus	5,852,698
Unassigned funds	<u>5,923,341</u>
Surplus as regards policyholders	<u>12,976,039</u>
 Total liabilities, surplus and other funds	 <u>\$45,169,111</u>

**DIRECT GENREAL INSURANCE COMPANY OF MISSISSIPPI
STATEMENT OF INCOME
FOR YEAR ENDED DECEMBER 31, 2006**

Underwriting Income	
Premiums earned	\$34,017,164
Deductions:	
Losses incurred	23,243,960
Loss expenses incurred	3,583,852
Other underwriting expenses incurred	<u>7,417,866</u>
Net underwriting gain (loss)	(228,514)
 Investment Income	
Net investment income earned	1,334,985
Net realized capital gains (losses)	<u>(31,452)</u>
Net investment income	1,303,533
 Other Income	
Miscellaneous income	<u>123,697</u>
Net income before federal income taxes	1,198,716
Federal income taxes incurred	<u>728,423</u>
Net income	<u>\$ 470,293</u>

**DIRECT GENERAL INSURANCE COMPANY OF MISSISSIPPI
RECONCILIATION OF CAPITAL AND SURPLUS
FOR EXAMINATION PERIOD ENDED DECEMBER 31, 2006**

	2004	2005	2006
Capital and surplus, beginning of year	\$ 7,703,312	\$ 10,880,826	\$ 11,373,094
Net Income (loss)	1,797,513	1,838,652	470,293
Change in net deferred income tax	213,185	(23,712)	396,874
Change in non-admitted assets	66,816	77,328	(264,222)
Paid in surplus	1,100,000	-0-	1,000,000
Dividends to stockholder	-0-	(1,400,000)	-0-
Examination adjustments	-0-	-0-	-0-
Capital and surplus, end of the year	<u>\$ 10,880,826</u>	<u>\$ 11,373,094</u>	<u>\$ 12,976,039</u>

**DIRECT GENERAL INSURANCE COMPANY OF MISSISSIPPI
RECONCILIATION OF EXAMINATION ADJUSTMENTS TO SURPLUS
DECEMBER 31, 2006**

As a result of this examination, there have been no adjustments affecting Surplus as regards policyholders reported by the Company in the December 31, 2006 annual statement. The Surplus as regards policyholders reported by the Company of \$12,976,039 is accepted as reasonably stated for purposes of the balance sheet per the examination.

MARKET CONDUCT ACTIVITIES

A full scope market conduct examination was not conducted; however, particular areas of the Company's market conduct were examined in connection with the financial examination. The particular areas reviewed included the following:

Claims

Claim files were reviewed in conjunction with the review of losses and loss adjustment expenses. Payments reviewed appeared to be timely and to the appropriate parties.

Complaint Handling

The Company maintained a complaint log during the period under examination, and all complaints appeared to have been resolved and no policyholder abuse or undesirable patterns were noted.

Marketing and Sales

Materials used for marketing and sales in the States of Mississippi and Kentucky were reviewed. The majority of the material was designed to promote name recognition and did not appear to mislead or deceive the public.

Privacy

The Company had a privacy policy in place for the protection of its policyholders and this policy appeared to be in compliance with applicable laws and standards.

Producer Licensing

The agents writing business for the Company in the State of Mississippi, at the examination date, were compared to the agents licensed by the MID and no exceptions were noted.

Territory and Plan of Operation

The Company was licensed to write Fire/Allied, Auto Damage/Liability, Casualty/Liability and Home/Farm-owners coverage in the State of Mississippi, and Property and Casualty Insurance, limited to vehicle, liability and glass, in the State of Kentucky. These insurance products were distributed through neighborhood sales offices staffed by agents who are employed by Direct General Insurance Agency, Inc. of Mississippi and Direct General Agency of Kentucky, Inc.

Underwriting and Rating

The Company had appropriate licensure to issue its products, and the applicable policy forms and rates were approved by the MID.

COMMITMENTS AND CONTINGENT LIABILITIES

As of the examination date, the Company was named as a defendant in certain litigation that was still pending at the report date. The Company intends to contest these claims and believes that meritorious defenses exist. The ultimate outcome of this litigation could not be reasonably determined for examination purposes; however, management of the Company does not anticipate any significant losses or costs to result.

COMPLAINCE WITH PREVIOUS RECOMMENDATIONS

In the previous examination report, a recommendation was made that the Company's future actuarial reports supporting the actuarial opinions include documentation of the calculations of the ULAE reserve. The Company has not complied with this recommendation as indicated by recommendation number 1 a. under the caption "Comments and Recommendations".

COMMENTS AND RECOMMENDATIONS

1. The MID's consulting actuary recommended that the Company's appointed actuary include additional documentation and improve the documentation in the actuarial report supporting the opinion. Specific recommendations are as follows: (Page 7)
 - a. The actuarial report supporting the actuarial opinion did not include documentation of the calculations of the ULAE/AOE reserve. Rather, it referred to the appointed actuary's review of Company work papers containing the ULAE reserve calculations. The Company work papers were not made part of the actuarial report and were not readily available for examination. The ULAE reserve work papers were subject to the report maintenance requirements per the annual statement instructions. We recommend that future actuarial reports supporting future opinions include documentation of the calculation of the ULAE reserve so documentation of these reserve calculations are readily available for examination. This recommendation was made in the previous examination report as of December 31, 2003;
 - b. Documentation of material ceded reserve credits should be fully supported in the actuarial report supporting the Statement of Actuarial Opinion. This documentation should be sufficient for another actuary practicing in the same field to evaluate the work.

SUBSEQUENT EVENTS

On March 30, 2007, Elara Holdings, Inc., an affiliate of Calera Capital and TPG Capital and Elara Merger Corporation acquired all of Direct General Corporation's outstanding stock. Elara Holdings, Inc. is domiciled in Delaware. The new management has not made any significant changes in business, culture or business plan.

With this merger, the following new officers were appointed to the Company:

Daniel Tarantin – Chief Executive Officer
Scott Bojczuk – Secretary
Tammy Adair – President
Brian Hanrahan – Vice President – Actuarial Group

With this merger, the former officers had title changes as follows:

John Hagely – Executive Vice President and CFO
Ronald Wilson – Assistant Secretary

As of July 2, 2007, Tammy Adair, President, resigned from the Company. On July 23, 2007, James R. Dickson was appointed President and Amy Sanford as Assistant Secretary.

ACKNOWLEDGMENT

The examiners representing the Mississippi Insurance Department and participating in this examination were:

Automation:	J. Scott Joyner, AES, CISA
Supervising Examiner:	Joseph R. May, CPA, CMA, CFE, CIE, FAHM
Examiner-in-charge:	Mitch Rayborn, CFE, FLMI
Actuary:	Thomas W. Vasey, Merlinos & Associates, Inc.

The courteous cooperation of the officers and employees responsible for assisting in the examination is hereby acknowledged and appreciated.

Respectfully submitted,



Mitch Rayborn, CFE, FLMI
Examiner-in-charge