XXXX XXXXXX ASSOCIATES, L.P.  
  
 INVESTMENT ADVISORY AGREEMENT  
  
 THIS AGREEMENT, effective as of September 1,1997, by and between Penn  
America Insurance Company, and its subsidiary Penn-Star Insurance Company  
(hereinafter collectively referred to as the "Client") and Xxxx Xxxxxx  
Associates, L.P., a Delaware Limited Partnership and registered investment  
advisor under the Investment Advisors Act of 1940, as amended (the "Advisor").  
  
 WHEREAS, the Client desires to appoint and designate the Advisor to provide  
investment advisory and management services for equity assets and such other  
funds and/or securities as Client shall designate, any additions thereof or  
changes therein (the "Account") and the Advisor agrees to so act;  
  
 NOW, THEREFORE, in consideration of the mutual covenants herein contained,  
it is hereby agreed between the parties hereto as follows:  
  
1. APPOINTMENT OF ADVISOR. The Client hereby designates and retains the  
 Advisor to furnish investment advisory and management services for the  
 Account, and the Advisor hereby accepts such appointment and agrees to  
 supervise the investment and reinvestment of assets of the Account in  
 accordance with the terms of this Agreement.  
  
2. CUSTODY SECURITIES AND FUNDS. The Advisor shall at no time receive, retain  
 or physically control any cash, securities or other assets forming any part  
 of the Account.  
  
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3. DISCRETION. The Advisor is hereby granted complete discretion in the  
 management of the investments in the Account, provided that all investment  
 transactions first receive approval, either written or verbal, from the  
 Chairman of the Investment Committee of the Client, and provided further,  
 however, that if the Chairman of the Investment Committee is not available  
 to give such approval and Advisor, in the exercise of its fiduciary  
 responsibility, believes the investment transaction should be executed  
 promptly, and the investment is within Client's Investment Objectives and  
 Policy Guidelines and Advisor's investment selection criteria, then Advisor  
 may execute the investment transaction and so advise the Chairman of the  
 Investment Committee as soon thereafter as possible. Subject to the  
 aforesaid, Advisor is authorized to invest and reinvest the assets in the  
 Account, the proceeds thereof and any additions thereto, to make investment  
 changes and to take any other lawful action with respect to the Account in  
 furtherance of Client's investment objectives, including, without  
 limitation, execution of documents, the making of investment decisions, the  
 placing of brokerage orders, and the rendering of decisions as to the  
 nature, amount and timing of transactions for the Account. Subject to the  
 aforesaid, Advisor shall have complete discretion to designate brokers and  
 to negotiate brokerage commissions and rates for transactions for the  
 Account, subject to the  
  
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 requirements of applicable law. In acting as an investment advisor, the  
 Advisor shall use its best judgment, and shall not be liable for any losses  
 sustained by Client or for any error in judgment, except if Advisor fails  
 to exercise the degree of care, skill, prudence and diligence that a  
 prudent person acting in a like capacity would use, or if Advisor's conduct  
 constitutes bad faith or gross negligence, provided, however, that the  
 foregoing shall not constitute a waiver by the Client of any rights or  
 claims the Client may have under federal or state securities laws,  
 including the anti fraud provisions of those laws.  
  
1. INVESTMENT OBJECTIVE. The Client hereby directs the Advisor to manage the  
 Account in furtherance of Client's investment objectives. The Client's  
 investment objectives are set forth in its Investment Plans, copies of  
 which are attached at Addendums "A" and "B" and incorporated herein as  
 though fully set forth at length. The Client may establish additional or  
 different investment objectives, or impose investment restrictions on the  
 Advisor with respect to the Account, by furnishing written notice to the  
 Advisor of such change. In furtherance of the Client's investment  
 objectives, the Advisor is authorized to enter into those investments set  
 forth in the "Investment Policy Guidelines" section of Client's Investment  
 Plans. See Addendums "A" and"B," pp.2-3.  
  
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2. COMPENSATION AND EXPENSES. Advisor shall be compensated in accordance with  
 Addendum C in this Agreement.  
  
3. ALLOCATION OF BROKERAGE. Where the Advisor places orders for the execution  
 of portfolio transactions for the Account, the Advisor may allocate such  
 transactions to such brokers and dealers for execution on such markets at  
 such prices and at such commission rates as in the good faith judgment of  
 the Advisor will be in the best interest of the Account, taking into  
 consideration in the selection of such brokers and dealers not only the  
 available prices and rates of brokerage commissions but also other relevant  
 factors such as research, execution capabilities, and other services  
 provided by such brokers or dealers which are expected to enhance the  
 general portfolio management capabilities of the Advisor and the value of  
 any ongoing relationship of the Advisor with such brokers and dealers.  
  
4. SERVICE TO OTHER CLIENTS. It is understood that the Advisor performs  
 investment advisory and management services for various clients. Client  
 agrees that the Advisor may give advice and take action with respect to any  
 of its other clients which may differ from advice given or the timing or  
 nature of action taken with respect to the Account so long as it is the  
 Advisor's policy, to the extent practical, to allocate investment  
 opportunities to the Account over a period of time on a fair and equitable  
 basis relative to other clients. It is understood  
  
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 that the Advisor shall not have any obligation to purchase or sell, or to  
 recommend for purchase or sale, for the Account any security which the  
 Advisor, its principals, affiliates, or employees may purchase or sell for  
 its or their own accounts or for the account of any other client, if in the  
 opinion of the Advisor such transaction or investment appears unsuitable,  
 impractical, or undesirable for the Account, subject to Client's approval.  
  
5. CONFIDENTIAL RELATIONSHIP. All investment information and advice furnished  
 by the Advisor to the Client shall be treated as confidential and shall not  
 be disclosed to third parties except as required by law.  
  
6. TERMINATION, ASSIGNMENT, ASSIGNS. This Agreement shall continue until  
 terminated by either party hereto. This Agreement may be terminated upon  
 thirty (30) days written notice by either party to the other of such  
 termination. Fees will be prorated to the date of termination specified in  
 the notice of termination. The Advisor, a limited partnership, will notify  
 the Client within a reasonable time after any change in the members of the  
 partnership. No assignment, as that term is defined in the Investment  
 Advisors Act of 1940, of this Agreement shall be made by Advisor. Subject  
 to the foregoing, this Agreement shall inure to the benefit of the heirs,  
 administrators, personal representatives, successors, or assigns of the  
 parties hereto.  
  
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7. REPRESENTATIONS BY CLIENT. Client represents and confirms that the  
 employment of Advisor and the investment objectives set forth herein are  
 authorized by the governing documents relating to the Account and that the  
 terms hereof do not violate any obligation by which the Client is bound,  
 whether arising by contract, operation of law, or otherwise, and that (a)  
 this Agreement has been duly authorized by appropriate action and when  
 executed and delivered will be binding upon Client in accordance with its  
 terms, and (b) the Client will deliver to Advisor such evidence of such  
 authority as Advisor may reasonably require, whether by way of a certified  
 resolution or otherwise.  
  
8. REPRESENTATIONS OF ADVISOR. Advisor represents that it is a registered  
 investment advisor under the Investment Advisors Act of 1940 as amended  
 and, for employee benefit accounts, acknowledges that it is a fiduciary to  
 the plan under Section 3 (38) of the Employee Retirement Income Security  
 Act of 1974 (ERISA).  
  
9. REPORTS. The Advisor shall furnish the Client a quarterly statement of the  
 value of the Account and the manner by which the fee is calculated. The  
 Advisor shall also furnish such other reports or information as the Client  
 may reasonably request.  
  
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10. CONFIMATIONS. The Client's execution of this Agreement shall constitute  
 authorization for the custodian of the Account to direct confirmation of  
 all transactions in the Account to the Advisor.  
  
11. GENERAL.  
  
 (A) This Agreement shall be construed and enforced in accordance with the  
 laws of Florida.  
  
 (B) All Notices shall be in writing and shall be deemed given if delivered  
 or mailed, certified or registered mail postage prepaid, to the  
 principal office of the party hereto. The Advisor may rely upon any  
 Notice believed by it to be genuine and authorized.  
  
 (C) This Agreement constitutes the entire understanding of the parties and  
 may be amended only by written instrument executed by the parties  
 hereto.  
  
 (D) This Agreement supersedes any and all other agreements that may have  
 been entered into by and between the parties.  
  
 IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be  
executed by their duly authorized officers on the dates appearing below.  
  
 XXXX XXXXXX ASSOCIATES, L.P.  
DATE: 1/12/98 By: /s/ Xxxx X Xxxxxx  
 General Partner  
 Xxxx Xxxxxx, Inc.  
 Xxxx Xxxxxx, President  
  
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DATE: 1/21/98 By: /s/ Xxxxxxxx Xxxxxxx  
 Xxxxxxxx Xxxxxxx  
 Secretary and Treasurer  
 Penn-America Insurance Company  
 and Penn-Star Insurance Company  
  
  
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 Addendum A  
 INVESTMENT PLAN  
 OF  
 PENN-AMERICA INSURANCE COMPANY  
  
 Investment Portfolio - Objectives and Guidelines  
  
 The Board of Directors of PENN AMERICA INSURANCE COMPANY (the "Company")  
authorizes the Company's officers to engage the services of an Investment  
Manager who possesses the necessary personnel and research facilities to manage  
the Company's investment portfolio. The portfolio consists of common stocks,  
preferred stocks and cash equivalents.  
  
 The policy guidelines for the Investment Portfolio shall be as stated  
herein, and are subject to modification with Board approval from time to time by  
the Company after consideration of the advice and recommendations of the  
Investment Manager.  
  
 Execution of All Trades: It is hereby understood that all investment  
transactions must have prior approval either written or verbal, of the Chairman  
of the Investment Committee, Xxxxx Xxxxxxxx, prior to their initiation by the  
investment manager, provided, however, that if the Chairman of the Investment  
Committee is not available to give such approval and Advisor, in the exercise of  
its fiduciary responsibility, believes the investment transaction should be  
executed promptly, and the investment is within Client's Investment Objectives  
and Policy Guidelines and Advisor's investment selection criteria, then Advisor  
may execute the investment transaction and so advise the Chairman of the  
Investment Committee as soon thereafter as possible.  
  
 Investment Portfolio  
  
 The Company's investment portfolio consists of funds allocated and invested  
in one of two (2) basic forms of investment:  
  
 (A) Money market and analogous cash equivalent funds, awaiting permanent  
 investment into equities securities.  
  
 (B) Equity issues including common and preferred stocks, units of  
 beneficial interest, American Depository Receipts, and convertible  
 securities.  
  
  
  
 The Company shall establish percentage allocation ranges for each category,  
which shall be monitored on a regular, periodic basis and which may be changed  
from time to time.  
  
 Investment Objectives  
  
 1. The Company's investment portfolio is to be managed in a conservative,  
risk adverse style with the objective of achieving long-term performance  
superior to the widely followed market averages.  
  
 2. Primary investment emphasis shall be placed upon consistency of  
performance, i.e., the achievement of investment objectives in such a manner as  
to protect the Company's assets from excessive volatility in market value from  
year to year.  
  
 3. Significant investment emphasis shall also be placed upon the  
preservation of the purchasing power of the assets.  
  
 4. Sufficient liquidity shall be maintained to fund any possible corporate  
outflows related to the property and casualty insurance business.  
  
 Investment Policv Guidelines  
  
 Assets are to be managed with a view toward achieving the specific  
investment objectives previously described. Consistency of performance,  
protection of principal as well as purchasing power and the maintenance of  
sufficient liquidity, should be the overriding guidelines for the investment  
portfolio.  
  
 To underscore these considerations, as well as to recognize the fiduciary  
responsibilities associated with the management of the Company's assets, there  
are certain characteristics which are expected to be associated with the  
portfolio and which shall be viewed as guidelines in formulating investment  
strategies.  
  
 A. Equity Issues  
  
 1. Allocation. The target range of investments in equity issues is up to  
thirty three and 1/3 percent (33 1/3%) of the value of the Company's capital  
surplus.  
  
 2. Types of Securities. Equity securities shall mean common and preferred  
stocks or equivalents (e.g., units of beneficial interest, American Depository  
Receipts, plus issues convertible into common stock).  
  
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 3. Cash Equivalents. At the discretion of the Investment Manager, short  
term money market funds and/or investments may represent a material portion of  
the equity issues. However, if commercial paper is used, it must have a minimum  
quality rating of A-2 or P-2 as established by Moody's or Standard & Poor's. In  
addition, bankers' acceptances or certificates of deposit must be issued by  
banks incorporated in the United States.  
  
 4. Diversification. Without prior approval of the Company, additions to a  
single security may not be made once the market value of the security exceeds  
five percent (5%) of the total portfolio (at market value). Other than these  
constraints, there are no quantitative guidelines suggested as to insurer,  
industry or individual security diversification. However, prudent  
diversification standards should be developed and maintained by the Investment  
Manger.  
  
 Exclusions  
  
The following categories of securities are not permissible for investment in the  
Company's portfolio without prior written approval:  
  
 (a) Unregistered or restricted stock;  
  
 (b) Commodities, including gold or currency futures;  
  
 (c) Conditional sales contracts;  
  
 (d) Options, including the purchase, sale or writing of options;  
  
 (e) Margin buying;  
  
 (f) Short selling;  
  
 (g) Leasebacks; and  
  
 (h) Fixed income securities.  
  
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Regulatory Considerations  
  
 \* Risk Based Capital  
  
 The Company, as an insurance entity, is regulated by various state  
insurance departments, NAIC and A.M. Best. One element of the regulation is risk  
based capital which has a RBC component related to the investment portfolio.  
There are three factors which are evaluated by RBC: quality of invested assets,  
mixed of invested assets and affiliate risk. Manager should be aware of the  
RBC's current factors at all times when evaluating appropriate investment  
consideration and not participate in any investment decision which would be  
detrimental to the client's Risk Based Capital.  
  
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 Addendum B  
 INVESTMENT PLAN  
 OF  
 PENN STAR INSURANCE COMPANY  
  
 Investment Portfolio- Objectives and Guidelines  
  
 The Board of Directors of PENN-STAR INSURANCE COMPANY (the "Company")  
authorizes the Company's officers to engage the services of an Investment  
Manager who possesses the necessary personnel and research facilities to manage  
the Company's investment portfolio. The portfolio consists of common stocks,  
preferred stocks and cash equivalents.  
  
 The policy guidelines for the Investment Portfolio shall be as stated  
herein, and are subject to modification with Board approval from time to time by  
the Company after consideration of the advice and recommendations of the  
Investment Manager.  
  
 Execution of All Trades: It is hereby understood that all investment  
transactions must have prior approval either written or verbal, of the Chairman  
of the Investment Committee, Xxxxx Xxxxxxxx, prior to their initiation by the  
investment manager, provided, however, that if the Chairman of the Investment  
Committee is not available to give such approval and Advisor, in the exercise of  
its fiduciary responsibility, believes the investment transaction should be  
executed promptly, and the investment is within Client's Investment Objectives  
and Policy Guidelines and Advisor's investment selection criteria, then Advisor  
may execute the investment transaction and so advise the Chairman of the  
Investment Committee as soon thereafter as possible.   
  
 Investment Portfolio  
  
 The Company's investment portfolio consists of funds allocated and invested  
in one of two (2) basic forms of investment:  
  
 (A) Money market and analogous cash equivalent funds, awaiting permanent  
 investment into equities securities.  
  
 (B) Equity issues including common and preferred stocks, units of  
 beneficial interest, American Depository Receipts, and convertible  
 securities.  
  
  
  
 The Company shall establish percentage allocation ranges for each category,  
which shall be monitored on a regular, periodic basis and which may be changed  
from time to time.  
  
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 1. The Company's investment portfolio is to be managed in a conservative,  
risk adverse style with the objective of achieving long term performance  
superior to the widely followed market averages.  
  
 2. Primary investment emphasis shall be placed upon consistency of  
performance, i.e., the achievement of investment objectives in such a manner as  
to protect the Company's assets from excessive volatility in market value from  
year to year.  
  
 3. Significant investment emphasis shall also be placed upon the  
preservation of the purchasing power of the assets.  
  
 4. Sufficient liquidity shall be maintained to fund any possible corporate  
outflows related to the property and casualty insurance business.  
  
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 Assets are to be managed with a view toward achieving the specific  
investment objectives previously described. Consistency of performance,  
protection of principal as well as purchasing power and the maintenance of  
sufficient liquidity, should be the overriding guidelines for the investment  
portfolio.  
  
 To underscore these considerations, as well as to recognize the fiduciary  
responsibilities associated with the management of the Company's assets, there  
are certain characteristics which are expected to be associated with the  
portfolio and which shall be viewed as guidelines in formulating investment  
strategies.  
  
 A. Equity Issues  
  
 1. Allocation. The target range of investments in equity issues is up to  
thirty three and 1/3 percent (33 1/3%) of the value of the Company's capital  
surplus.  
  
 2. Types of Securities. Equity securities shall mean common and preferred  
stocks or equivalents (e.g., units of beneficial interest, American Depository  
Receipts, plus issues convertible into common stock).  
  
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 3. Cash Equivalents. At the discretion of the Investment Manager, short  
term money market funds and/or investments may represent a material portion of  
the equity issues. However, if commercial paper is used, it must have a minimum  
quality rating of A-2 or P-2 as established by Moody's or Standard & Poor's. In  
addition, bankers' acceptances or certificates of deposit must be issued by  
banks incorporated in the United States.  
  
 4. Diversification. Without prior approval of the Company, additions to a  
single security may not be made once the market value of the security exceeds  
five percent (5%) of the total portfolio (at market value). Other than these  
constraints, there are no quantitative guidelines suggested as to insurer,  
industry or individual security diversification. However, prudent  
diversification standards should be developed and maintained by the Investment  
Manger.  
  
 Exclusions  
  
 The following categories of securities are not permissible for investment  
in the Company's portfolio without prior written approval:  
  
  
 (a) Unregistered or restricted stock;  
  
 (b) Commodities, including gold or currency futures;  
  
 (c) Conditional sales contracts;  
  
 (d) Options, including the purchase, sale or writing of options;  
  
 (e) Margin buying;   
  
 (f) Short selling;  
  
 (g) Leasebacks; and  
  
 (h) Fixed income securities.  
  
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Regulatory Considerations  
  
 \* Risk-Based Capital  
  
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insurance departments, NAIC and A.M. Best. One element of the regulation is risk  
based capital which has a RBC component related to the investment portfolio.  
There are three factors which are evaluated by RBC: quality of invested assets,  
mixed of invested assets and affiliate risk. Manager should be aware of the  
RBC's current factors at all times when evaluating appropriate investment  
considerations and not participate in any investment decision which would be  
detrimental to the client's overall Risk-Based Capital.  
  
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 ADDENDUM C  
  
COMPENSATION AND EXPENSES The Client shall compensate the Advisor for its  
services by the payment of an annual fee, calculated monthly, billed and payable  
quarterly in arrears, based on the market value of the Account, including cash  
or its equivalents, at the following rates.  
  
Balanced Assets Annual Rate   
First $ 1,000,000 .75%  
Next $ 2,000,000 .563%  
Up to $50,000,000 .375%  
 Over $50,000,000 \*  
  
\* To be negotiated on a case by case basis.  
  
  
/s/ RF initial as acknowledgement of fee schedule  
  
 The Advisor's fee shall be computed by applying 1/12th of the annual  
percentage rate to the market value of the account computed on the last day of  
each month. In computing the value of the assets in the Account, securities  
listed on any national securities exchange shall be valued at the last quoted  
sale price on the principal exchange in which the security is traded on the  
valuation date. Any other asset shall be valued in a manner determined in good  
faith by or as directed by the Advisor to reflect its fair market value. Advisor  
shall exclude from the calculation of its fee any securities placed in the  
account by Client which Advisor does not supervise and regarding which advisor  
exercises no investment discretion and assumes no liability. Client shall inform  
Advisor, in writing, when Client places any such securities in the Account.  
  
 The Client's execution of this Agreement shall constitute authorization by  
the Client to the Independent Custodian of Client's funds to deduct the  
Management Fee from the Client's Account when due, in accordance with the  
following procedures:  
  
 1. Client provides authorization permitting Advisor's fees to be  
 paid directly from Client's account held by an independent  
 custodian,  
  
 2. Advisor sends Client and custodian, at least seven days prior to  
 the request for payment, a xxxx showing the amount of fee, the  
 value of Client's assets on which it was based, and the specific  
 manner in which Advisor's fee was calculated,  
  
 3. Custodian sends Client a statement, at least quarterly,  
 indicating all amounts disbursed from the account, including the  
 amount of the advisory fees paid directly to Advisor.  
  
 4. This billing arrangement may be terminated at any time by written  
 notice from Client to Advisor and custodian.