

REPORT OF EXAMINATION
OF THE
SAN DIEGO INSURANCE COMPANY
AS OF
DECEMBER 31, 2018

Filed on June 18, 2020

TABLE OF CONTENTS

	<u>PAGE</u>
SCOPE OF EXAMINATION	1
COMPANY HISTORY	2
MANAGEMENT AND CONTROL:.....	3
Management Agreements.....	5
TERRITORY AND PLAN OF OPERATION.....	6
REINSURANCE:	7
Quota Share Reinsurance Agreement	7
Assumed.....	7
Ceded Insurance.....	7
FINANCIAL STATEMENTS:	8
Statement of Financial Condition as of December 31, 2018.....	9
Underwriting and Investment Exhibit for the Year Ended December 31, 2018	10
Reconciliation of Surplus as Regards to Policyholders from December 31, 2014 through December 31, 2018.....	11
COMMENTS ON FINANCIAL STATEMENT ITEMS:.....	12
Aggregate Write-ins for Liabilities – Deposit Liability	12
SUMMARY OF COMMENTS AND RECOMMENDATIONS:	12
Current Report of Examination	12
Previous Report of Examination	12
ACKNOWLEDGMENT	13

Los Angeles, California
June 10, 2020

Honorable Ricardo Lara
Insurance Commissioner
California Department of Insurance
Sacramento, California

Dear Commissioner:

Pursuant to your instructions, an examination was made of the

SAN DIEGO INSURANCE COMPANY

(hereinafter also referred to as the Company). The Company's home office is located at 1615 Murray Canyon Road, San Diego, California 92108.

SCOPE OF EXAMINATION

We have performed our single-state examination of the Company. The previous examination of the Company was as of December 31, 2013. This examination covered the period from January 1, 2014 through December 31, 2018.

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

All accounts and activities of the Company were considered in accordance with the risk-focused examination process. This may include assessing significant estimates made by management and evaluating management's compliance with Statutory Accounting

Principles. The examination does not attest to the fair presentation of the financial statements included herein. If, during the course of the examination, an adjustment is identified, the impact of such adjustment will be documented separately following the Company's financial statements.

This examination report includes findings of fact and general information about the Company and its financial condition. There might be other items identified during the examination that, due to their nature (e.g., subjective conclusions, proprietary information, etc.), were not included within the examination report but separately communicated to other regulators and/or the Company.

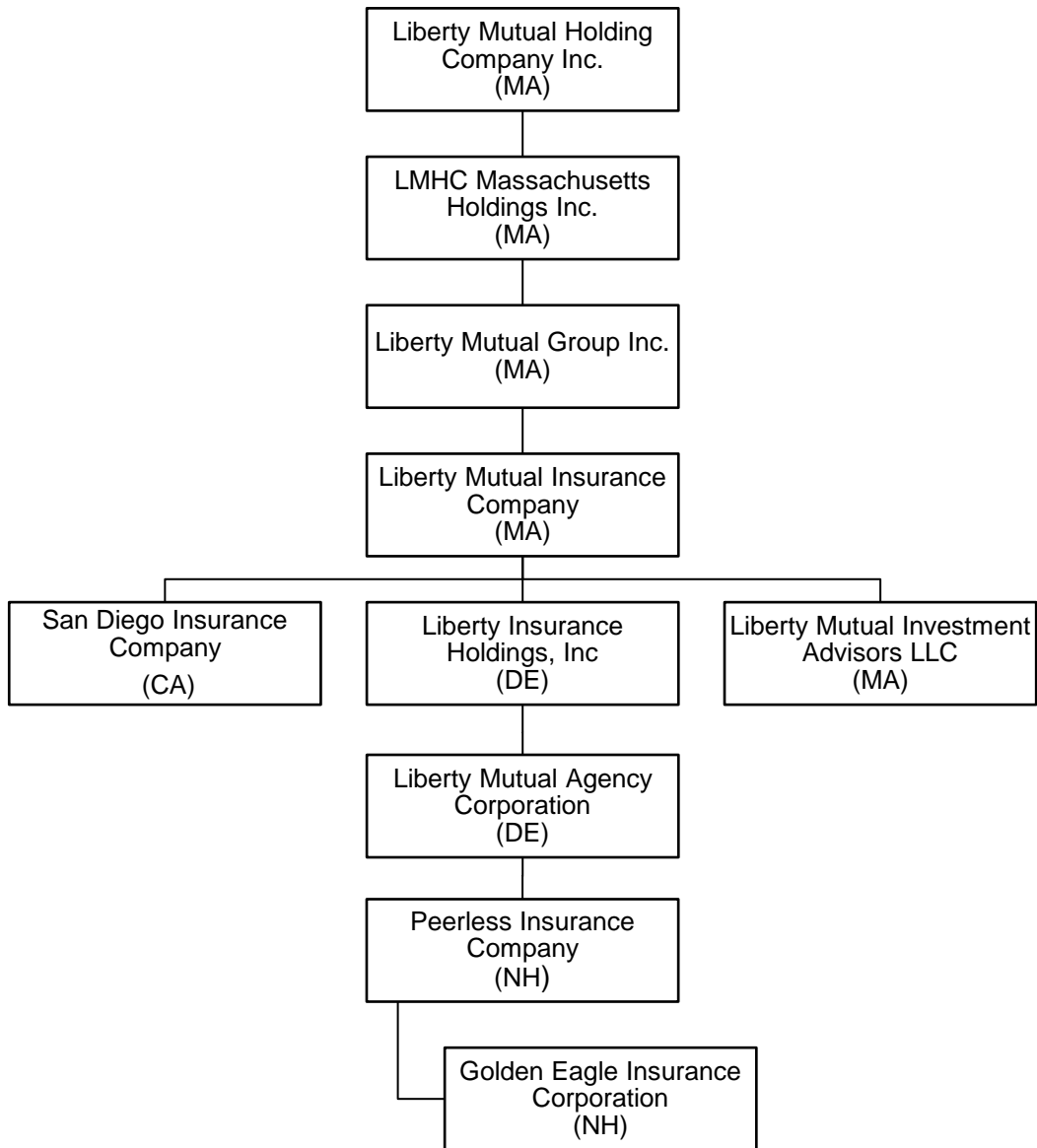
This was a coordinated examination with Massachusetts as the lead state of the Liberty Mutual Insurance Group. It was conducted concurrently with other insurance entities in the holding company group, 58 total legal entities. The following states participated in the examination: Arizona, California, Illinois, Indiana, Minnesota, New Hampshire, Oregon, Texas, and Wisconsin.

COMPANY HISTORY

The Company was incorporated under the laws of the state of California on July 19, 1997 and commenced business on August 22, 1997. The Company was formed as part of the rehabilitation plan of the Golden Eagle Insurance Company, which was placed under conservation on March 1, 1997 by the Insurance Commissioner of the State of California. The Company was incorporated as a wholly-owned subsidiary of Golden Eagle Insurance Corporation (GEIC). On December 31, 2008, GEIC contributed 100% of the Company to its higher tiered parent, Liberty Mutual Insurance Company.

MANAGEMENT AND CONTROL

The Company is a member of an insurance holding company system of which Liberty Mutual Holding Company Inc., (LMHC), is the ultimate controlling entity. LMHC is incorporated in the Commonwealth of Massachusetts. Following is an abridged organizational chart. All ownership is 100%.



The five members of the board of directors, who are elected annually, manage the business and affairs of the Company. Following are members of the board and principal officers of the Company serving at December 31, 2018:

Directors

<u>Name and Location</u>	<u>Principal Business Affiliation</u>
Neeti Bhalla Johnson Chestnut Hill, Massachusetts	Executive Vice President and Chief Investment Officer Liberty Mutual Group Inc.
James F. Kelleher Belmont, Massachusetts	Executive Vice President and Chief Legal Officer Liberty Mutual Group Inc.
David H. Long Dover, Massachusetts	Chief Executive Officer and President Liberty Mutual Group Inc.
Christopher L. Peirce North Attleboro, Massachusetts	Executive Vice President and Chief Financial Officer Liberty Mutual Group Inc.
Mark T. Touhey Scituate, Massachusetts	Senior Vice President, Corporate Secretary, and Chief of Staff to the Chief Executive Officer Liberty Mutual Group Inc.

Principal Officers

<u>Name</u>	<u>Title</u>
David H. Long	President and Chief Executive Officer
Christopher L. Peirce	Executive Vice President and Chief Financial Officer
Neeti Bhalla Johnson	Executive Vice President and Chief Investment Officer
James F. Kelleher	Executive Vice President and Chief Legal Officer
Laurance H.S. Yahia	Senior Vice President and Treasurer
Alison B. Erbig	Senior Vice President and Comptroller
Mark C. Touhey	Senior Vice President and Secretary

Management Agreements

Management Service Agreement: The Company is a party to a Management Services Agreement with its direct parent, Liberty Mutual Insurance Company (LMIC), effective August 21, 1997. LMIC provides investment management and administrative services to the Company. Under the terms of this agreement, fees are settled on a quarterly basis, however no fees were charged to the Company during the examination period. The California Department of Insurance (CDI) approved this agreement on June 2001.

Consolidated Federal Income Tax Agreement: The Company and its affiliates are part of a Consolidated Federal Income Tax Agreement with the ultimate parent, Liberty Mutual Holding Company, Inc., amended effective September 22, 2008. The allocation of taxes is based upon the separate return calculations with intercompany balances settled in the quarter subsequent to the filing of the consolidated return. The CDI approved the amendment to the agreement on September 5, 2008. For 2014, 2015, 2016, 2017, and 2018, the Company paid federal income taxes of \$563,000, \$517,000, \$550,000, \$460,000, and \$304,000, respectively.

Management Services Agreement: The Company entered into a Management Services Agreement with its affiliate, Golden Eagle Insurance Corporation (GEIC), effective August 21, 1997. Under the terms of this agreement, GEIC provides the Company with accounting, tax and auditing services, as well as services related to claim administration. GEIC also provides the Company with personnel, office space, equipment, and supplies in order for the Company to conduct its operations. Under this agreement, the net amount owed shall be determined not less frequently than quarterly. Payment is made upon the presentation of invoices covering the specific period to which the expenses apply. During the examination period, no services were provided by GEIC to the Company, consequently no payment was made by the Company. The agreement was approved by the CDI on December 4, 2007.

Investment Services Agreement: The Company entered into an Investment Management Agreement with Liberty Mutual Group Asset Management Inc. (LMGAMI), effective July 1, 2011. Under this agreement, LMGAMI is the Company's investment advisor and its

agent and attorney-in-fact to exercise the investment discretion per the agreement. The CDI approved this agreement on June 24, 2011. The Company pays LMGAMI a monthly fee, calculated by taking the sum of the US Generally Accepted Accounting Procedures market value of all cash and securities in the Company's account on the first day of each month and on the last day of that same month, divided by two, and multiplied by 0.00015. For 2014, 2015, 2016, 2017, and 2018, the fees paid by the Company to LMIC were \$121,466, \$124,287, \$125,979, \$123,436, and \$125,643, respectively.

Cash Management Agreement: The Company entered into a Cash Management Agreement with its parent, LMIC, effective January 1, 2016. Under the terms of this agreement, LMIC provides the Company with short term cash liquidity pool management services. The CDI approved this agreement on November 6, 2015. The Company pays LMIC a monthly fee, calculated by taking the sum of the US Generally Accepted Accounting Procedures market value of all cash and securities in the Company account on the first day of each month and on the last day of that same month, divided by two, and multiplied by .00015. The fees are included in the previously mentioned Investment Management Agreement calculation.

TERRITORY AND PLAN OF OPERATION

The Company is licensed in the state of California as a multiple-line property and casualty insurer. The Company was formed to run-off pre-March 31, 1997 insurance policies and surety bond liabilities of Golden Eagle Insurance Company, an unaffiliated insurer that was under conservation. The Company agreed that it would only transact the run-off liabilities assumed under the reinsurance agreement approved by the Conservation Court of the state of California on February 1, 1998, and would not transact any other business without prior written approval by the California Department of Insurance.

REINSURANCE

Quota Share Reinsurance Agreement

The Company entered into a Quota Share Reinsurance Agreement with Liberty Mutual Insurance Company, effective November 30, 2006. Under the terms of this agreement, the Company ceded 100% of its losses and loss adjustment expenses under the Conservation Court approved reinsurance agreement with Golden Eagle Insurance Company. The agreement was approved by the California Department of Insurance on March 19, 2007. Due to the nature of the agreement, it was determined that the Company was required to use deposit accounting. As of December 31, 2018, the Company had a liability deposit balance of \$3,209,897.

Assumed

The Company has no reinsurance assumed.

Ceded Insurance

The Company has no reinsurance ceded.

FINANCIAL STATEMENTS

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

Statement of Financial Condition as of December 31, 2018

Underwriting and Investment Exhibit for the Year Ended December 31, 2018

Reconciliation of Surplus as Regards Policyholders from December 31, 2013
through December 31, 2018

Statement of Financial Condition
as of December 31, 2018

<u>Assets</u>	<u>Ledger and Nonledger Assets</u>	<u>Assets Not Admitted</u>	<u>Net Admitted Assets</u>	<u>Notes</u>
Bonds	\$ 66,744,701	\$	\$ 66,744,701	
Cash, cash equivalents, and short-term investments	3,122,506		3,122,506	
Securities lending reinvested collateral assets	5,138,275		5,138,275	
Investment income due and accrued	<u>391,164</u>	<u> </u>	<u>391,164</u>	
Total assets	<u>\$ 75,396,646</u>	<u>\$</u>	<u>\$ 75,396,646</u>	
 <u>Liabilities, Surplus and Other Funds</u>				<u>Notes</u>
Current federal and foreign income taxes			\$ 73,394	
Net deferred tax liability			20,000	
Payable for parent, subsidiaries and affiliates			191,792	
Payable for securities			5,138,275	
Aggregate write-ins for liabilities			<u>3,209,897</u>	(1)
Total liabilities			8,633,358	
Common capital stock		\$ 2,600,000		
Gross paid in and contributed surplus		52,800,000		
Unassigned funds (surplus)		<u>11,363,288</u>		
Surplus as regards policyholders			<u>66,763,288</u>	
Total liabilities, surplus, and other funds			<u>\$ 75,396,646</u>	

Underwriting and Investment Exhibit
for the Year Ended December 31, 2018

State of Income

Underwriting Income

Premium earned	\$	0
Deductions:		
Other underwriting expenses incurred	\$	<u>9,742</u>
Total underwriting deductions		<u>9,742</u>
Net underwriting loss		(9,742)

Investment Income

Net investment income earned	1,498,121	
Net realized capital losses	<u>(10,229)</u>	
Net investment gain		1,487,892
Net income before dividends to policyholders, after capital gains tax, and before all other federal and foreign income taxes		1,478,150
Federal and foreign income taxes incurred		<u>306,719</u>
Net income		<u>\$ 1,171,431</u>

Capital and Surplus Account

Surplus as regards policyholders, December 31, 2017		\$ 65,585,859
Net income	\$ 1,171,431	
Dividends to stockholders	<u>6,000</u>	
Change in surplus as regards policyholders for the year		<u>1,177,431</u>
Surplus as regards policyholders, December 31, 2018		<u>\$ 66,763,290</u>

Reconciliation of Surplus as Regards to Policyholders
from December 31, 2013 through December 31, 2018

Surplus as regards policyholders, December 31, 2013			\$ 61,577,517
	<u>Gain in Surplus</u>	<u>Loss in Surplus</u>	
Net income	\$ 5,166,773	\$	
Change in net deferred income tax	<u>19,000</u>	<u></u>	
Total gains and losses	\$ 5,185,773	\$	
Net increase in surplus as regards policyholders			<u>5,185,773</u>
Surplus as regards policyholders, December 31, 2018			<u>\$ 66,763,290</u>

COMMENTS ON FINANCIAL STATEMENT ITEMS

(1) Aggregate Write-ins for Liabilities – Deposit Liability

The Company was formed as part of the rehabilitation plan of the Golden Eagle Insurance Company, which was placed under conservation on March 1, 1997, by the Insurance Commissioner of the state of California. Due to the nature of the reinsurance agreement, it was determined that the Company was required to use deposit accounting. As of December 31, 2018, the Company has a liability deposit balance of \$3,209,897.

SUMMARY OF COMMENTS AND RECOMMENDATIONS

Current Report of Examination

None.

Previous Report of Examination

None.

ACKNOWLEDGMENT

The courtesy and cooperation extended by the Company's officers and parent's employees during the course of this examination are hereby acknowledged.

Respectfully submitted,

/S/

Cuauhtémoc Beltrán, CFE
Examiner-In-Charge
Senior Insurance Examiner
Department of Insurance
State of California

/S/

Grace Asuncion, CFE
Senior Insurance Examiner, Supervisor
Department of Insurance
State of California