

REPORT OF EXAMINATION
OF THE
CALIFORNIA GENERAL UNDERWRITERS
INSURANCE COMPANY, INC
AS OF
DECEMBER 31, 2021

A handwritten signature in blue ink, appearing to be 'D. DeLa...' with a stylized flourish at the end.

Filed on May 30th, 2023

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Los Angeles, California
April 28, 2023

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

Dear Commissioner:

Pursuant to your instructions, an examination was made of the

CALIFORNIA GENERAL UNDERWRITERS INSURANCE COMPANY, INC.

(hereinafter also referred to as the Company). Its primary location of its books and records is located at 4484 Wilshire Boulevard, Los Angeles, California, 90010. The Company's statutory home office and main administrative office is located at 555 West Imperial Highway, Brea, California 92821.

SCOPE OF EXAMINATION

We have performed our multi-state examination of the Company. The previous examination of the Company was made as of December 31, 2017. This examination covers the period from January 1, 2018, through December 31, 2021.

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. The examination also included identifying and evaluating significant risks that could cause the Company'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 includes 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.

The examination was a coordinated examination of the Mercury Insurance Group with California as the lead state, and conducted concurrently with the Florida, Georgia, Illinois, Oklahoma, and Texas Departments of Insurance. The insurance entities reviewed as part of this examination are identified below by state of domicile:

<u>Company</u>	<u>State</u>
California Automobile Insurance Company	California
California General Underwriters Insurance Company, Inc.	California
Mercury Casualty Company	California
Mercury Insurance Company	California
Orion Indemnity Company (fka Workmen's Auto Insurance Company)	California
Mercury Indemnity Company of America	Florida
Mercury Insurance Company of Florida	Florida
Mercury Indemnity Company of Georgia	Georgia
Mercury Insurance Company of Georgia	Georgia
Mercury Insurance Company of Illinois	Illinois
American Mercury Insurance Company	Oklahoma
Mercury County Mutual Insurance Company	Texas
American Mercury Lloyds Insurance Company	Texas

COMPANY HISTORY

The Company was incorporated in the state of California on April 15, 1985 as Mercury General Insurance Company. The name was changed to California General Underwriters Insurance Company, Inc. on December 29, 1988. The Company is a wholly-owned subsidiary of Mercury Casualty Company (MCC). MCC in turn, is a wholly-owned subsidiary of Mercury General Corporation (MGC).

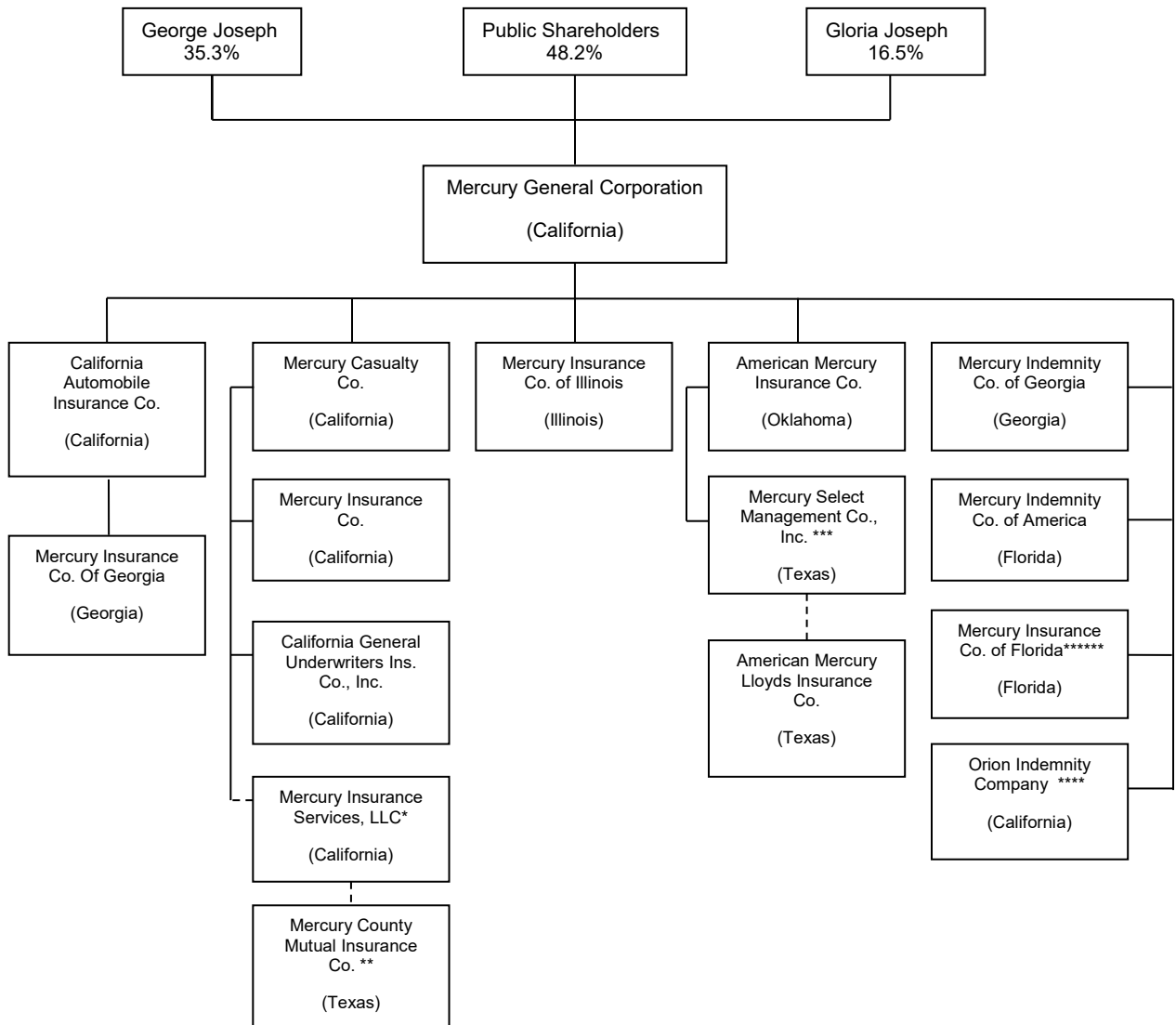
Capitalization

The Company has 200,000 shares of \$100 par value common stock authorized and 40,000 shares issued and outstanding.

MANAGEMENT AND CONTROL

The Company is a member of an insurance holding company system of which Mr. George Joseph is the ultimate controlling person. Mercury General Corporation (MGC) is a publicly traded insurance holding company. As of December 31, 2021, the controlling stockholders, George Joseph and Gloria Joseph, own 35.3% and 16.5%, respectively, of MGC's stock with the remaining 48.2% held by public shareholders, none of whom own 10% or more interest.

The following organizational chart depicts the Company's relationship within the holding company system. All ownership is 100% unless otherwise indicated.



* Mercury Insurance Services, LLC, is controlled by its sole and managing member, Mercury Casualty Company, through a management agreement.

** Mercury County Mutual Insurance Company is managed and controlled by Mercury Insurance Services, LLC, through a management agreement.

*** Mercury Select Management Company, Inc. is Attorney-in-fact for American Mercury Lloyds Insurance Company, a Texas Lloyds Plan Insurer.

****Orion Indemnity Company, a California insurer, was formerly named Workmen's Auto Insurance Company.

*****Mercury National Insurance Company, an Illinois domiciled insurance company and 100% owned subsidiary of MICIL, was dissolved.

*****Mercury Insurance Company of Florida was dissolved effective November 30, 2022.

The seven members of the Company's 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 on December 31, 2021:

Directors

<u>Name and Location</u>	<u>Principal Business Affiliation</u>
George G. Braunegg Los Angeles, California	Advisor and Investor Terafina Inc
Ramona L. Cappello Los Angeles, California	Principal The Cappello Group
James G. Ellis San Marino, California	Retired
George Joseph Los Angeles, California	Chairman of the Board Mercury General Corporation
Joshua E. Little St. George, Utah	Shareholder Durham Jones & Pinegar, P.C.
Martha E. Marcon Glendale, California	Retired
Gabriel Tirador Tustin, California	President and Chief Executive Officer Mercury General Corporation

Principal Officers

<u>Name</u>	<u>Title</u>
Gabriel Tirador	President and Chief Executive Officer
Theodore R. Stalick	Senior Vice President, Chief Financial Officer, and Treasurer
Judith A. Walters	Secretary
Christopher W. Graves	Vice President and Chief Investment Officer

Management Agreements

Tax Allocation Agreement: Since January 1, 1983, the Company and various affiliates have been parties to a Tax Allocation Agreement with the ultimate parent, MGC. Under the terms of this agreement, the tax liability of the Company and its affiliates are computed as if each entity filed a separate stand-alone return, with current credit for net losses incurred by the insurance subsidiaries to the extent it can be used in the current consolidated return. In 2015, the agreement was amended to: 1) add affiliate Workmen's Auto Insurance Company (now Orion Indemnity Company (Orion)), 2) delete dissolved entities, and 3) include several technical provisions required by the California Department of Insurance (CDI), which did not alter or affect existing practices. The amendment was approved by the CDI on June 5, 2015. Taxes paid or (recovered) by the Company totaled \$61,843, \$(57,914), \$103,343, and \$65,987 for the years 2018, 2019, 2020, and 2021, respectively.

Management Agreement: Since January 1, 2001, the Company has been a party to a Management Agreement with Mercury Insurance Services, LLC (MIS), a subsidiary of Mercury Casualty Company (MCC). Approval of the agreement was granted by the CDI on December 27, 2001. Under the terms of this agreement, MIS performs underwriting and loss adjustment services for the MGC group of companies. The management fee is based on actual incurred expenses. The underwriting portion of the management fee is allocated between the Company and its affiliates based upon their proportionate share of direct premiums written. The fee for allocated loss adjustment expenses is based on actual payments by MIS for claims on policies issued by the Company. The unallocated loss adjustment expenses portion of the management fee is allocated between the Company and its affiliates based upon their proportionate share of net losses incurred. In 2013, the agreement was amended: 1) authorizing MIS to pay certain expense items that were previously reserved to the insurers, including agent commissions and audit fees and 2) adding a 60-day due date for the payment of management fees, to comply with Statement of Statutory Accounting Principles No. 96. The amendment was approved by the CDI on September 25, 2013. In 2015, the agreement was amended again to allow MIS to pursue salvage and subrogation claims on behalf of the insurers, with MIS

remitting the recoveries to the insurers. This amendment was approved by the CDI on June 11, 2015. The Company paid management fees of \$55,248, \$55,098, \$3,718,865, and \$10,999,704 during the years 2018, 2019, 2020, and 2021, respectively.

Service Agreement: Effective December 1, 2019, the Company was added as a party to an existing Services Agreement with MCC, California Automobile Insurance Company (CAIC) and Mercury Insurance Company (MIC). Under the terms of this agreement, MCC collects premiums on behalf of the Company, CAIC and MIC. The amendment adding the Company was approved by the CDI on December 20, 2019. There are no fees or costs paid by any affiliates under this agreement.

Multiple-Cedents Reinsurance Allocation Agreement: Effective July 1, 2013, the Company, American Mercury Insurance Company (AMIC), CAIC, MIC, and MCC entered into a Multiple-Cedents Reinsurance Allocation Agreement, providing for the allocation of premiums and recoveries in connection with external reinsurance treaties covering all the parties at a single rate, as required by Statement of Statutory Accounting Principles No. 62R. The Agreement approval was granted by the Oklahoma Department of Insurance (ODI) and the CDI, on March 28, 2014 and June 26, 2014, respectively.

Effective July 1, 2018, the agreement was amended to add affiliate Orion as a party. The amendment also renewed the Agreement for three years until June 30, 2022. The amendment was approved by the ODI on June 11, 2019 and by the CDI on September 4, 2019. There were no premiums or recoveries allocated to the Company during the examination period. The Multiple-Cedents Reinsurance Allocation Agreement was renewed effective July 1, 2022, and will automatically renew for consecutive one-year terms until June 30, 2025.

TERRITORY AND PLAN OF OPERATION

The Company is licensed solely in California and did not write business on a direct basis until mid-2020. Effective June 1, 2020, the Company began directly transacting commercial multi-peril class of insurance covering commercial property policies primarily for apartment and residential condominium association and lessors risk, restaurants, and

small business. For the year ended December 31, 2021, the Company wrote \$26.7 million of direct premiums. As discussed in further detail in the Reinsurance section below, all business directly written by the Company is 100% ceded to Mercury Casualty Company under a 100% quota share reinsurance agreement.

REINSURANCE

Intercompany

Effective January 1, 2015, the Company entered into a 100% Reinsurance Agreement with California Automobile Insurance Company (CAIC), under which the Company assumed the fleet automobile policies written by CAIC for substantially all vehicles owned by affiliates. The agreement was terminated effective January 1, 2021, and notice was provided to the California Department of Insurance (CDI).

Effective January 1, 2020, the Company entered into a Quota Share Reinsurance Agreement with Mercury Casualty Company (MCC), under which MCC reinsures 100% of the direct business written by the Company. The agreement was approved by the CDI on December 20, 2019. The agreement was amended, effective January 1, 2021, making technical changes that had no material financial impact on either company. The amendment was approved by the CDI on December 8, 2020. The Company ceded \$17,587,290 in premium and \$30,313,882 in losses in calendar year 2021.

Assumed

Other than the assumed intercompany reinsurance agreement discussed in the Intercompany section above, the Company did not assume reinsurance during the period covered by this examination.

Ceded

The Company is party to a Catastrophe Reinsurance Treaty (2021 Treaty) with affiliated companies that are under the ownership, control or management of Mercury General

Corporation. The 2021 Treaty covers a wide range of perils that is effective from July 1, 2021 through June 30, 2022. The 2021 Treaty provides \$792 million of coverage on a per occurrence basis after covered catastrophe losses exceed the \$40 million combined company retention limit. The 2021 Treaty specifically excludes coverage for any Florida business and for California earthquake losses on fixed property policies, such as homeowners, but does cover losses from fires following an earthquake. In addition, the 2021 Treaty provides for one full reinstatement of coverage limits and excludes losses from wildfires on certain coverage layers of the 2021 Treaty.

Coverage on individual catastrophes provided for the 12 months ended June 30, 2022 under the 2021 Treaty is presented below in various layers.

	<u>Catastrophe Loss and LAE</u>		<u>Percentage of Coverage</u>
	<u>In Excess of</u>	<u>Up to</u>	
	(Amounts in Millions)		
Layer of Coverage (1)	\$ 40	\$ 100	70
Layer of Coverage (2)	100	400	100
Layer of Coverage (2)(3)(4)	400	792	100

- (1) The 2021 Treaty covers 70% placement for the layer of \$40 million to \$100 million.
- (2) Layer of Coverage represents multiple actual treaty layers that are grouped for presentation purposes.
- (3) 13.4% of this layer covers only California wildfires and fires following an earthquake in California and is not subject to reinstatement.
- (4) 14% of this layer includes a territorial restriction covering California, Arizona, and Nevada only.

ACCOUNTS AND RECORDS

Annual Statement Instructions

Pursuant to the National Association of Insurance Commissioners (NAIC) Annual Statements Instructions, Note to Financial Statements, 14D, Claims Related Extra Contractual Obligation and Bad Faith Losses Stemming from Lawsuits, the Company shall disclose the dollar amount paid (for the extra contractual and bad faith portion of the total claim amount) for claims related extra contractual obligations and bad faith losses stemming from lawsuits, in the current reporting period on a direct basis. The Company's 2021 Annual Statement Note to Financial Statements 14D was not prepared in accordance to the NAIC's Annual Statement Instructions and did not disclose the potential risk and/or uncertainties related to lawsuits in the manner or format required by the NAIC. The Company should compile its bad faith/extra contractual litigation settlements arising from claims and disclose it annually in the Notes to Financial Statements 14D in accordance with the NAIC Annual Statement Instructions. It is recommended the Company implement procedures to ensure compliance with the National Association of Insurance Commissioners Annual Statement Instructions for Note 14D to the Financial Statements, Claims related extra contractual obligations and bad faith losses stemming from lawsuits. The Company has subsequently updated its reporting procedures to ensure Note 14D is in compliance with the NAIC Annual Statement Instructions.

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 the financial condition of the Company for the period ending December 31, 2021. The accompanying comments to the amounts reported in the annual statements should be considered an integral part of the financial statements. No adjustments were made to the statutory financial statements filed by the Company.

Statement of Financial Condition as of December 31, 2021

Underwriting and Investment Exhibit for the Year Ended December 31, 2021

Reconciliation of Surplus as Regards Policyholders from December 31, 2017 through December 31, 2021

Statement of Financial Condition
as of December 31, 2021

<u>Assets</u>	<u>Ledger and Nonledger Assets</u>	<u>Assets Not Admitted</u>	<u>Net Admitted Assets</u>	<u>Notes</u>
Bonds	\$ 19,623,865	\$	\$ 19,623,865	
Cash and short-term investments	2,408,029		2,408,029	
Investment income due and accrued	253,069		253,069	
Premiums and agents' balances in course of collection	136,495	24,813	111,682	
Premiums, agents' balances and installments booked but deferred and not yet due (including \$0 earned but unbilled premiums.	3,068,951		3,068,951	
Amounts recoverable from reinsurers	516,223		516,223	
Net deferred tax asset	38,608		38,608	
Receivables from parent, subsidiaries and affiliates	<u>2,332,463</u>		<u>2,332,463</u>	
Total assets	<u>\$ 28,377,703</u>	<u>\$ 24,813</u>	<u>\$ 28,352,890</u>	
 <u>Liabilities, Surplus and Other Funds</u>			<u>Current Year</u>	<u>Notes</u>
Losses			0	(1)
Loss adjustment expenses			0	(1)
Commissions payable, contingent commissions and other similar charges			135,000	
Taxes, licenses and fees			494,742	
Current federal and foreign income taxes			3,923	
Advance premiums			756,845	
Ceded reinsurance premiums payable			2,000,059	
Remittances and items not allocated			264,455	
Payable for parent, subsidiaries and affiliates			<u>597,681</u>	
Total liabilities			4,252,705	
Common capital stock			4,000,000	
Gross paid-in and contributed surplus			3,500,000	
Unassigned funds (surplus)			<u>16,600,185</u>	
Surplus as regards policyholders			<u>24,100,185</u>	
Total liabilities, Surplus, and other funds			<u>\$ 28,352,890</u>	

Underwriting and Investment Exhibit
for the Year Ended December 31, 2021

State of Income

	<u>Underwriting Income</u>	<u>Current Year</u>
Premium earned		\$ 0
Deductions:		
Losses incurred		\$ (11,463)
Loss adjustment expenses incurred		<u>(2,715)</u>
Total underwriting deductions		<u>(14,178)</u>
Net underwriting gain		14,178
	<u>Investment Income</u>	
Net investment income earned		\$ 534,385
Net realized capital loss		<u>(1,212)</u>
Net investment gain		533,173
	<u>Other Income</u>	
Aggregate write-ins for miscellaneous income		<u>4,692</u>
Total other income		<u>4,692</u>
Net income after dividends to policyholders, after capital gains tax and before federal and foreign income taxes		552,043
Federal and foreign income taxes incurred		<u>38,984</u>
Net income		<u>\$ 513,059</u>

Capital and Surplus Account

Surplus as regards policyholders, December 31, 2020		\$ 23,602,971
Net income	\$ 513,059	
Change in net deferred income tax	4,702	
Change in nonadmitted assets	<u>(20,547)</u>	
Change in surplus as regards policyholders for the year		<u>497,214</u>
Surplus as regards policyholders, December 31, 2021		<u>\$ 24,100,185</u>

Reconciliation of Surplus as Regards to Policyholders
from December 31, 2017 through December 31, 2021

Surplus as regards policyholders, December 31, 2017					\$ 21,330,677
	<u>Gain in Surplus</u>	<u>Loss in Surplus</u>			
Net income	\$ 2,757,058	\$			
Change in net deferred income tax	37,263				
Change in nonadmitted assets			<u>24,813</u>		
Total gains and losses	<u>\$ 2,794,321</u>	<u>\$</u>	<u>24,813</u>		
Net increase in surplus as regards policyholders				<u>2,769,508</u>	
Surplus as regards policyholders, December 31, 2021					<u>\$ 24,100,185</u>

COMMENTS ON FINANCIAL STATEMENT ITEMS

(1) Losses and Loss Adjustment Expenses

Based on an analysis by a Senior Casualty Actuary from the California Department of Insurance, the Company's loss and loss adjustment expense reserves as of December 31, 2021 were found to be reasonably stated and have been accepted for the purpose of this examination. As of December 31, 2021, the Company reported zero net loss and loss adjustment expense reserves (LAE) because one hundred percent of its losses and LAE expenses were ceded to Mercury Casualty Company.

SUMMARY OF COMMENTS AND RECOMMENDATIONS

Current Report of Examination

Accounts and Records – Annual Statement Instructions (Page 10): It is recommended the Company implement procedures to ensure compliance with the National Association of Insurance Commissioners Annual Statement Instructions for Note 14D to the Financial Statements, Claims related extra contractual obligations and bad faith losses stemming from lawsuits.

Previous Report of Examination

None

ACKNOWLEDGMENT

Acknowledgment is made of the cooperation and assistance extended by the Company's officers and employees during the course of this examination.

Respectfully submitted,

Elizabeth Nielson, CFE, CPA
Examiner-In-Charge
Contract Examiner
Department of Insurance
State of California

Anjanette Briggs, CFE
Senior Insurance Examiner, Supervisor
Department of Insurance
State of California