

REPORT OF EXAMINATION
OF THE
CENTURY-NATIONAL INSURANCE COMPANY
AS OF
DECEMBER 31, 2010

Participating State
and Zone:

California

Filed August 18, 2011

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Los Angeles, California
July 1, 2011

Honorable Joseph Torti, III
Chairman of the NAIC Financial
Condition Subcommittee
Superintendent of Business Regulation
Division of Insurance
Cranston, Rhode Island

Honorable Linda S. Hall
Secretary, Zone IV-Western
Director of Insurance
Alaska Division of Insurance
Anchorage, Alaska

Honorable Dave Jones
Insurance Commissioner
California Department of Insurance
Sacramento, California

Dear Chairman, Secretary, and Commissioner:

Pursuant to your instructions, an examination was made of the

CENTURY-NATIONAL INSURANCE COMPANY

(hereinafter also referred to as the Company) at the primary location of its books and records at 12200 Sylvan Street, North Hollywood, California 91606. The Company's statutory home office is located at 16600 Sherman Way, Van Nuys, California 91406.

SCOPE OF EXAMINATION

The previous examination of the Company was made as of December 31, 2007. This examination covers the period from January 1, 2008 through December 31, 2010. The examination was conducted in accordance with the National Association of Insurance Commissioners' Financial Condition Examiners' Handbook. The Handbook requires the planning and performance of the examination to evaluate the Company's financial condition, to identify prospective risks, and to obtain information about the Company, including corporate governance, identification and assessment of inherent risks, and the evaluation of the system controls and procedures used to

mitigate those risks. The examination also included an assessment of the principles used and the significant estimates made by management, as well as an evaluation of the overall financial statement presentation, and management's compliance with Statutory Accounting Principles and annual statement instructions. All accounts and activities of the Company were considered in accordance with the risk-focused examination process.

In addition to those items specifically commented upon in this report, other phases of the Company's operations were reviewed including the following areas that require no further comment: fidelity bonds and other insurance; pensions, stock ownership and insurance plans; growth of company; loss experience; accounts and records; and statutory deposits.

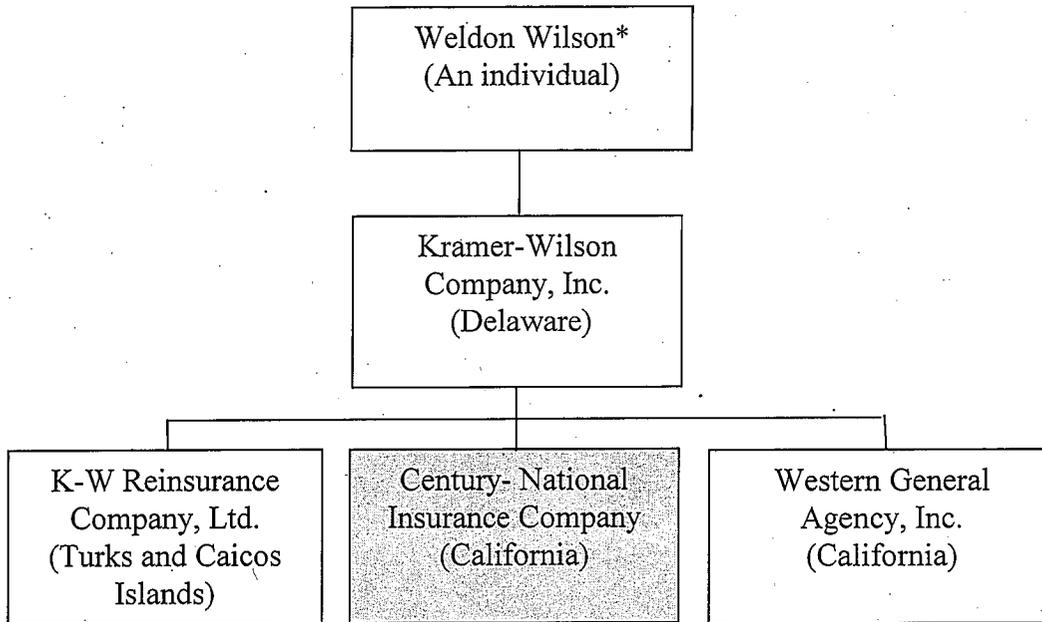
COMPANY HISTORY

The Company was incorporated in California on June 23, 1955, and commenced transacting property and casualty business on December 21, 1956. All outstanding shares of the Company are owned by its parent, Kramer-Wilson, Inc., a Delaware non-insurance company, whose principle operation is the management of the Company.

The Company paid ordinary cash dividends to its parent, Kramer-Wilson Company, Inc. of \$13.0 million, \$7.0 million, and \$11.0 million for 2008, 2009, and 2010, respectively.

MANAGEMENT AND CONTROL

The Company is a member of a holding company system of which Weldon Wilson is the ultimate controlling person. The following organizational chart depicts the interrelationship of the Company within the holding company system:



* Weldon Wilson's (43%) is the largest stockholder. All other ownership is 100%.

Management of the Company is vested in a three-member board of directors elected annually. A listing of the members of the board and principal officers serving on December 31, 2010 follows:

Directors

Name and Residence

Principal Business Affiliation

Weldon Wilson
Sherman Oaks, California

Chairman of the Board and Chief Executive Officer
Century-National Insurance Company and
Kramer-Wilson Company, Inc.

Kevin Wilson
Westlake Village, California

President
Century-National Insurance Company and
Kramer-Wilson Company, Inc.

Marie Balicki
Winnetka, California

Secretary
Century-National Insurance company

Principal Officers

<u>Name</u>	<u>Title</u>
Weldon Wilson	Chairman of the Board and Chief Executive Officer
Kevin Wilson	President
Judith Osborn	Treasurer
Marie Balicki	Secretary

Management Agreements

Management Agreement: The Company is party to a management agreement with its parent, Kramer-Wilson Company, Inc. (K-W), effective since 1972. Under the terms of the agreement, K-W produces business and provides management, labor, facility space, equipment, and other services required to enable the Company to engage in the insurance business. The Company retains responsibility for the payment of premium taxes, losses, loss adjustment expenses, investment expenses, and income taxes.

Noted within the management agreement is the provision that K-W remit to the Company all premiums written, regardless of whether they have been collected from the insured or from the producing agent, subagent, broker or solicitor. In addition, K-W is authorized to, among other things, appoint and terminate agents, subagents, solicitors and brokers, and perform all underwriting functions and adjust claims. For compensation, the Company reimburses K-W for all costs incurred in the performance of such services.

The agreement was initially approved by the California Department of Insurance in 1972 and again in 1986 with an addendum that changed the compensation from a percentage of earned premiums to a cost-reimbursement basis.

Western General Agency, Inc. (WGA) is a wholly-owned subsidiary of K-W and produces business exclusively for the Company. In 1992, WGA was added as a party to the management agreement between the Company and K-W. WGA is compensated on a cost reimbursement basis.

The following chart depicts the expenses paid to the above affiliated entities for the examination period:

Year	Expenses Paid to K-W	Expenses Paid to WGA
2008	\$31,891,513	\$28,990,646
2009	\$32,174,077	\$28,975,710
2010	\$32,578,777	\$31,526,668
Total	\$96,644,367	\$89,493,024

Tax Allocation Agreement: Effective since 1987, the Company and all of its affiliates file a consolidated federal income tax return under the terms of a Tax Allocation Agreement. The Company's tax liability, under the terms of this agreement, is the same as if it had filed on a separate stand-alone basis. The Company paid the following taxes during the examination period:

Year	Amount
2008	\$9,375,943
2009	\$15,054,968
2010	\$16,130,499
Total	\$40,561,410

CORPORATE RECORDS

Pursuant to California Insurance Code (CIC) Section 735, the Company is required to inform the board members of the receipt of the examination report. In addition, an entry that the examination report was presented to the board should be disclosed within the board minutes. A review of the board minutes disclosed the presentation of the receipt of the examination report was not entered in the minutes. It is recommended that the Company implement procedures to ensure future compliance with CIC Section 735.

TERRITORY AND PLAN OF OPERATION

As of December 31, 2010, the Company was licensed as a multiple line fire and casualty insurer. The following is a listing of the states in which the Company is licensed:

Alaska	Louisiana	Oklahoma
Arizona	Maryland	Oregon
Arkansas	Minnesota	Pennsylvania
California	Mississippi	South Carolina
Colorado	Missouri	South Dakota
Delaware	Montana	Tennessee
Florida	Nebraska	Texas
Georgia	Nevada	Utah
Idaho	New Jersey	Virginia
Illinois	New Mexico	Washington
Indiana	North Carolina	Wisconsin
Iowa	North Dakota	Wyoming
Kentucky	Ohio	

In 2010, the Company had direct written premiums of \$135,933,514. The following reflects the four largest premium producing states:

State	Direct Written Premium	% of Total
California	\$112,664,050	82.9%
Nevada	\$12,530,146	9.2%
Arizona	\$5,418,017	4.0%
Illinois	\$2,033,302	1.5%

The Company writes both commercial and personal lines insurance coverage throughout the western region of the United States. The Company specializes in providing collateral protection to financial institutions with large portfolios and commercial automobile and homeowners policies to consumers.

The major lines written during 2010 were homeowners multiple peril (48.9%), commercial automobile liability (18.5%), and fire (8.5%).

The Company employs a variety of distribution systems, including independent agents, brokers, and lender affiliated agents. Homeowners, fire, and earthquake policies are distributed through lender affiliated agents while commercial automobile liability and physical damage coverage are marketed through brokers. In addition, direct mail response is used to solicit mobile home insurance and personal automobile coverage.

REINSURANCE

Assumed

There is no material assumed business other than the Company's mandatory participation in the California Commercial Automobile Insurance Procedure Pool.

Ceded

The Company maintains a catastrophe reinsurance program to help mitigate the effects of a catastrophic event on its exposure to risk in the homeowners market. The Company retains the first \$2 million while reinsurance covers 95% of the next \$4 million, 100% of the next \$34 million, 95% of the next \$15 million, and 100% of the next \$45 million.

The following is a schedule of the principal ceded reinsurance contracts in-force as of the examination date:

Type of Contract	Reinsurer's Name	Company's Retention	Coverage
Underlying Property Catastrophe Excess of Loss	K-W Reinsurance Company, Ltd., an Unauthorized Affiliate	\$2 million in addition to 5% of each excess net loss for which claim is made under this contract	95% of \$4 million in excess of \$2 million for each and every loss occurrence not to exceed 95% of \$8 million in the aggregate during the term of this contract

Type of Contract	Reinsurer's Name	Company's Retention	Coverage
Master Property Catastrophe Excess of Loss	Munich Reinsurance Company, an Unauthorized Reinsurer		80% of \$20 million in excess of \$6 million for each and every loss occurrence not to exceed 80% of \$60 million in the aggregate during the 12 month period from July 1, 2010
Second Property Catastrophe Excess of Loss	Munich Reinsurance Company, an Unauthorized Reinsurer		<p><u>Section A:</u> 100 % of \$14 million in excess of \$26 million for each and every loss occurrence not to exceed 100% of \$42 million in the aggregate during the 12 month period from July 1, 2010</p> <p><u>Section B:</u> 20% of \$20 million in excess of \$6 million for each and every loss occurrence not to exceed 20% of \$60 million in the aggregate for the Master Property Catastrophe Excess of Loss listed above during the 12 month period from July 1, 2010</p>
Fourth Property Catastrophe Excess of Loss	Various Authorized, Unauthorized and Underwriters at Lloyds	5% of each excess net loss for which claim is made under this contract	95% of \$15 million in excess of \$40 million for each and every loss occurrence not to exceed 95% of \$30 million in the aggregate during the term of this contract
Fifth Property Catastrophe Excess of Loss	Various Authorized, Unauthorized and Underwriters at Lloyds		\$45 million in excess of \$55 million for each and every loss occurrence not to exceed \$90 million in the aggregate during the term of this contract

Effective June 30, 2003, the Company entered into a 40% quota-share treaty with K-W Reinsurance Company, Ltd., an affiliated company, for the automobile physical damage line of business.

As of December 31, 2010, reinsurance recoverables, for all ceded reinsurance totaled \$319,555 or 0.1% of surplus as regards policyholders.

FINANCIAL STATEMENTS

The financial statements prepared for this examination report include:

Statement of Financial Condition as of December 31, 2010

Underwriting and Investment Exhibit for the Year Ended December 31, 2010

Reconciliation of Surplus as Regards Policyholders from December 31, 2007
through December 31, 2010

Reconciliation of Examination Changes as of December 31, 2010

Statement of Financial Condition
as of December 31, 2010

<u>Assets</u>	<u>Ledger and Nonledger Assets</u>	<u>Assets Not Admitted</u>	<u>Net Admitted Assets</u>	<u>Notes</u>
Bonds	\$ 340,589,149	\$	\$ 340,589,149	
Preferred stocks	9,051,518		9,051,518	
Common stocks	127,708,849		127,708,849	
Cash, cash equivalent, and short-term investments	20,349,020		20,349,020	(1)
Receivable for securities	2,526,797		2,526,797	
Investment income due and accrued	4,415,981		4,415,981	
Uncollected premiums and agents' balances in course of collection	948,739	86,753	861,986	
Deferred premiums, agents' balances and installments booked but deferred and not yet due	10,910,498	50,985	10,859,513	
Amount recoverable from reinsurers	319,555		319,555	
Net deferred tax asset	13,256,196	7,081,153	6,175,043	
Aggregate write-ins for other than invested assets	<u>900,255</u>		<u>900,255</u>	
Total assets	<u>\$ 530,976,557</u>	<u>\$ 7,218,891</u>	<u>\$ 523,757,666</u>	
 <u>Liabilities, Surplus and Other Funds</u>				
Losses and loss adjustment expenses			\$ 94,197,789	(2)
Commissions payable, contingent commissions and other similar charges			4,114,434	
Other expenses			1,079,188	
Taxes, licenses and fees			24,512	
Current federal and foreign income taxes			183,207	
Unearned premiums			67,323,861	
Ceded reinsurance premiums payable			(155,239)	
Amounts withheld or retained by company for account of others			42,365	
Payable for securities			4,545,813	
Aggregate write-ins for liabilities			<u>28,000,000</u>	(3)
Total liabilities			199,355,930	
Common capital stock	\$ 5,000,000			
Gross paid in and contributed surplus	24,135,420			
Unassigned funds (surplus)	<u>295,266,316</u>			
Surplus as regards policyholders			<u>324,401,736</u>	
Total liabilities, surplus and other funds			<u>\$ 523,757,666</u>	

Underwriting and Investment Exhibit
for the Year Ended December 31, 2010

Statement of Income

Underwriting Income

Premiums earned		\$ 123,866,979
Deductions:		
Losses and loss expenses incurred	\$ 63,064,263	
Other underwriting expenses incurred	45,650,244	
Aggregate write-ins for underwriting deductions	<u>2,000</u>	
Total underwriting deductions		<u>108,716,507</u>
Net underwriting gain		15,150,472

Investment Income

Net investment income earned	\$ 16,341,592	
Net realized capital gain	<u>13,238,070</u>	
Net investment gain		29,579,662

Other Income

Finance and service charges not included in premiums	\$ <u>233,665</u>	
Total other income		<u>233,665</u>
Net income before federal income taxes		44,963,799
Federal income taxes incurred		<u>6,813,867</u>
Net income		<u>\$ 38,149,932</u>

Capital and Surplus Account

Surplus as regards policyholders, December 31, 2009		\$ 288,614,315
Net income	\$ 38,149,932	
Change in net unrealized capital gains	6,064,008	
Change in net deferred income tax	(1,831,788)	
Change in nonadmitted assets	4,405,269	
Dividends to stockholders	<u>(11,000,000)</u>	
Change in surplus as regards policyholders for the year		<u>35,787,421</u>
Surplus as regards policyholders, December 31, 2010		<u>\$ 324,401,736</u>

Reconciliation of Surplus as Regards Policyholders
from December 31, 2007 through December 31, 2010

Surplus as regards policyholders, December 31, 2007 per Examination			\$ 255,870,134
	<u>Gain in Surplus</u>	<u>Loss in Surplus</u>	
Net income	\$ 100,925,528	\$	
Net unrealized capital gains	503,314		
Change in net deferred income tax		6,655,581	
Change in nonadmitted assets	4,604,070		
Change in provision for reinsurance	154,271		
Dividends to stockholders	<u> </u>	<u>31,000,000</u>	
Total gains and losses	<u>\$ 106,187,183</u>	<u>\$ 37,655,581</u>	
Net increase in surplus as regards policyholders			<u>68,531,602</u>
Surplus as regards policyholders, December 31, 2010, per Examination			<u>\$ 324,401,736</u>

Reconciliation of Examination Changes
as of December 31, 2010

	<u>Per Company</u>	<u>Per Examination</u>	<u>Surplus Increase (Decrease)</u>	<u>Notes</u>
<u>Assets</u>				
Cash, and cash equivalents, and short-term investments	\$ 26,442,764	\$ 20,349,020	\$ (6,093,744)	(1)
<u>Liabilities</u>				
Draft outstanding	6,093,744	0	<u>6,093,744</u>	(1)
Net change to surplus			0	
Surplus as regards policyholders, December 31, 2010, per Company			<u>324,401,736</u>	
Surplus as regards policyholders, December 31, 2010, per Examination			<u>\$ 324,401,736</u>	

COMMENTS ON FINANCIAL STATEMENT ITEMS

(1) Cash, Cash Equivalents, and Short-term Investments

The Company, in its 2010 Annual Statement, incorrectly classified \$6,093,744 of outstanding check balances as “drafts outstanding” rather than as a reduction from “cash”. It is recommended that the Company follow the classification methodology for cash as presented in the National Association of Insurance Commissioners Annual Statement Instructions and Statements of Statutory Accounting Principles No. 2, paragraphs 6 and 7.

(2) Losses and Loss Adjustment Expenses

The December 31, 2010 loss and loss adjustment expense reserves were evaluated by a Casualty Actuary from the California Department of Insurance (CDI). Based on the analysis performed, the Company’s reserves for losses and loss adjustment expenses were deemed reasonable.

(3) Aggregate Write-ins for Liabilities

On November 8, 1988, the California voters passed an initiative known as Proposition 103. The proposition provided, among other things, that rates on new and renewal policies issued during the period of November 8, 1988, through November 7, 1989, be reduced to a level 20% below those in effect on November 8, 1987. On May 4, 1989, the California Supreme Court substantially upheld the provision of Proposition 103. The court’s decision permits an exemption from the rate rollback if an insurance company can demonstrate that its rates are justified and that the rollback would prevent the company from earning a fair rate of return.

In August 1991, the CDI issued regulations prescribing a method for computing Proposition 103 mandated rate rollbacks on premiums written for the period November 8, 1988 through November 7, 1989. Based on these regulations, the Company received a rollback calculation and filed for an exemption from the 20% rate rollback requirement. The California Insurance

Commissioner denied the Company's request for an exemption and ordered a \$21,572,137 rollback plus 10% simple interest accruing from May 8, 1989.

Pursuant to an agreement with the CDI, the Company agreed to establish a liability of \$28 million (\$42.4 million net of federal income tax) and pledge \$42.4 million of its assets in lieu of providing an appeal bond until a final decision is made.

On October 25, 2010, the Insurance Commissioner adopted the administrative law judge's decision reducing the rollback amount to \$9,387,107 plus interest.

The Company's management believes that under the criteria established by the 20th Century Insurance Company decision, it has no rollback liability and has petitioned the Superior Court for the State of California County of Sacramento for a Writ of Mandamus seeking judicial review of the Insurance Commissioner's rollback order.

SUMMARY OF COMMENTS AND RECOMMENDATIONS

Current Report of Examination

Corporate Records (Page 5): It is recommended that the Company implement procedures to ensure future compliance with California Insurance Code Section 735.

Comments on Financial Statement Items - Cash, Cash Equivalents, and Short-term Investments (Page 15): It is recommended that the Company follow the classification methodology for cash as presented in the National Association of Insurance Commissioners Annual Statement Instructions and Statements of Statutory Accounting Principles No. 2, paragraphs 6 and 7.

Comments on Financial Statement Items - Aggregate Write-ins for Liabilities (Page 15): The Company has had a Proposition 103 liability since 1989. In October 2010, the Insurance Commissioner adopted the administrative law judge's decision reducing the rollback amount. However, the Company's management believes that under the criteria established by the 20th

Century Insurance Company decision, it has no rollback liability and has petitioned the Superior Court for the State of California County of Sacramento for a Writ of Mandamus seeking judicial review of the Insurance Commissioner's rollback order.

Previous Report of Examination

Accounts and Records (Page 9): It was recommended that the Company evaluate and make appropriate changes to strengthen its information system controls. The Company has complied with this recommendation.

Comments on Financial Statement Items - Losses and Loss Adjustment Expenses (Page 13): The Company was audited by the Internal Revenue Service (IRS) for tax years 2004, 2005, and 2006. In 2008, the Company received a Notice of Proposed Adjustment from the IRS examiner for these tax years asserting that the Company's loss reserves were overstated in the audited tax years. As a result of this IRS audit, the Company reached a settlement with the IRS which called for deferral of a portion of loss reserve deductions originally claimed in tax years 2004, 2005, and 2006. Under the terms of the settlement agreement, the Company made a tax settlement payment to the IRS of approximately of \$2.0 million. During 2010, the IRS completed its audit of the Company's 2007 tax return. As a result of this audit, the IRS concluded the Company's December 31, 2007 reserves were reasonably stated. Further, loss reserves deductions disallowed in tax years 2004 through 2006 were allowed in full in tax year 2007. This conclusion by the IRS resulted in a \$2.0 million refund of 2007 federal income taxes.

Comments on Financial Statement Items - Aggregate Write-ins for Liabilities (Page 13): The Company has had a Proposition 103 liability since 1989. In October 2010, the Insurance Commissioner adopted the administrative law judge's decision reducing the rollback amount. However, the Company's management believes that under the criteria established by the 20th Century Insurance Company decision, it has no rollback liability and has petitioned the Superior Court for the State of California County of Sacramento for a Writ of Mandamus seeking judicial review of the Insurance Commissioner's rollback order.

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,

/S/

Sayaka T. Dillon, CFE
Examiner-In-Charge
Associate Insurance Examiner
Department of Insurance
State of California