

REPORT OF EXAMINATION  
OF THE  
FIREMAN'S FUND INSURANCE COMPANY  
AS OF  
DECEMBER 31, 2007

Participating State  
and Zone:

California

Filed June 19, 2009

## TABLE OF CONTENTS

	<u>PAGE</u>
SCOPE OF EXAMINATION.....	1
SUMMARY OF SIGNIFICANT FINDINGS .....	2
SUBSEQUENT EVENTS .....	2
COMPANY HISTORY: .....	3
Capitalization.....	3
Dividends Paid to Parent .....	5
MANAGEMENT AND CONTROL: .....	5
Management Agreements .....	8
Related Party Transactions .....	9
TERRITORY AND PLAN OF OPERATION.....	11
REINSURANCE: .....	12
Intercompany Reinsurance Agreement.....	12
Other Intercompany Reinsurance .....	13
Assumed .....	14
Crop Insurance.....	14
Loss Portfolio Transfer.....	15
Ceded.....	15
ACCOUNTS AND RECORDS: .....	20
Information Systems Controls .....	20
Federal Income Taxes.....	20
FINANCIAL STATEMENTS: .....	21
Statement of Financial Condition as of December 31, 2007 .....	22
Underwriting and Investment Exhibit for the Year Ended December 31, 2007.....	23
Reconciliation of Surplus as Regards Policyholders from December 31, 2003 through December 31, 2007 .....	24
Reconciliation of Examination Changes as of December 31, 2007 .....	25
COMMENTS ON FINANCIAL STATEMENT ITEMS: .....	26
Common Stocks.....	26
Aggregate Write-ins for Other Than Invested Assets:	
Keep Well Commitment Receivable .....	25
Losses and Loss Adjustment Expenses .....	26
Aggregate Write-ins for Liabilities: Excess of Statutory Reserves over Statement Reserves.....	27
SUMMARY OF COMMENTS AND RECOMMENDATIONS: .....	28
Current Report of Examination .....	28
Previous Report of Examination.....	29
ACKNOWLEDGMENT.....	33

San Francisco, California  
June 15, 2009

Honorable Alfred W. Gross  
Chairman of the NAIC Financial  
Condition Subcommittee  
Commissioner of Insurance  
Virginia Bureau of Insurance  
Richmond, Virginia

Honorable Morris Chavez  
Secretary, Zone IV-Western  
Superintendent of Insurance  
New Mexico Department of Insurance  
Santa Fe, New Mexico

Honorable Steve Poizner  
Insurance Commissioner  
California Department of Insurance  
Sacramento, California

Dear Chairman, Secretary and Commissioner:

Pursuant to your instructions, an examination was made of the

#### FIREMAN'S FUND INSURANCE COMPANY

(hereinafter also referred to as the Company) at its home office located at 777 San Marin Drive, Novato, California 94998.

#### SCOPE OF EXAMINATION

The previous examination of the Company was made as of December 31, 2003. This examination covers the period from January 1, 2004 through December 31, 2007. The examination was made pursuant to the National Association of Insurance Commissioners' (NAIC) plan of examination. The examination included a review of the Company's practices and procedures, an examination of management records, tests and analyses of detailed transactions within the examination period, and an evaluation of the assets and a determination of liabilities as of December 31, 2007, as deemed necessary under the circumstances.

The Company is the lead insurer in an intercompany reinsurance agreement with eight of its affiliates (the participants). Under the terms of this agreement, the participants cede, and the Company assumes, 100% of the participants' business generated from underwriting operations. The cessions from the participants are combined with the Company's business, resulting in the pooled balance to be allocated to each participant. In order to examine the Company's assets and liabilities that resulted from pooling, it was necessary to review this pooled balance. Each company in the pool was examined concurrently by its respective state of domicile.

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: corporate records; fidelity bonds and other insurance; officers', employees' and agents' welfare and pension plans; growth of company; business in force by states; loss experience; and sales and advertising.

#### SUMMARY OF SIGNIFICANT FINDINGS

As a result of this examination, surplus as regards policyholders as of December 31, 2007 has been reduced by \$363,453,000 to \$2,530,756,152. Adjustments were due to net increases in the Company's losses and loss adjustment expense reserves, after Keep Well Commitments receivable related to asbestos and environmental reserves, as well as minimum reserve amounts for loss and loss adjustment expenses as required by California Insurance Code Section 11558.

#### SUBSEQUENT EVENTS

The Company and its insurance subsidiaries (Group) underwent significant restructuring in August 2008. The Executive Committee of the Company's upstream parent, Allianz of America, Inc., made the decision to decentralize support services by aligning these services more closely with the operating companies. As a result, business functions that included Legal, Information Technology, Compliance and Marketing were realigned so that these functions would be managed independently by the Company and Allianz Life Insurance Company of North America.

Additionally, specialty marine business was combined with Allianz Global Corporate & Specialty's (AGCS) global marine business into a new Allianz unit, AGCS Marine Insurance Company (AMIC), that will be managed by AGCS. Agribusiness, a major contributor to the Company's profitability in the last few years, is now operated as a dedicated unit. The other portions of Specialty Insurance were combined with Commercial Business to form a new commercial and specialty risks organization. As a result, the Group currently has two primary business units: Personal and Commercial.

### COMPANY HISTORY

On January 2, 1991, Allianz of America, Inc. (AZOA), a U.S. subsidiary of Allianz SE, purchased 100% of the capital stock of the Company. Allianz SE (formerly Allianz Aktiengesellschaft, or Allianz AG) is a European Company incorporated in the Federal Republic of Germany and the European Union. Allianz SE is the ultimate parent of the Allianz Group. It was incorporated as Allianz Versicherungs Aktiengesellschaft in Berlin, Germany on February 5, 1890 and converted to a European Company on October 13, 2006. Allianz SE operates on a worldwide basis through branch offices, subsidiaries and affiliated companies.

Effective November 1, 1997, the Company and its subsidiaries became a wholly owned subsidiary of Allianz Insurance Company, a subsidiary of AZOA. Allianz Insurance Company changed its name to Allianz Global Risks US Insurance Company (AGR US) in 2003.

### Capitalization

The Company is authorized to issue 1 million shares of Class A voting common stock with a par value of \$15 per share. As of December 31, 2007, there were 280 thousand shares outstanding.

In May 2003, Allianz SE issued two Keep Well Commitments, in which Allianz SE agreed to contribute capital to the Company up to certain specified maximum amounts if the 2003 accident year combined loss ratio exceeds the planned combined ratio of 102%, and for any adverse

development up to \$1 billion for accident years 2002 and prior. The terms of the commitments commenced on January 1, 2003 and terminated on December 31, 2005. On January 6, 2005, Allianz SE issued a new Keep Well Commitment in favor of the Company, beginning calendar year 2006, in which Allianz SE agreed to contribute capital to the Company, up to \$800,000,000, to the extent of adverse development of reserves for accident years 2003 and prior years in excess of \$150,000,000 of the balances reported for such reserves as of December 31, 2005. The initial term of the Commitment commenced on January 1, 2006, terminated on December 31, 2008 and is deemed automatically extended for successive one-year terms thereafter, unless Allianz SE provides at least 12 months prior notice of termination. Pursuant to these commitments, the following surplus adjustments were recorded during the examination period:

1. On April 27, 2004, the Company recorded a surplus contribution and intercompany receivable in the amount of \$62,548,000.
2. On March 31, 2005, the Company recorded a surplus contribution and intercompany receivable in the amount of \$92,984,000.
3. On March 31, 2006, the Company recorded a surplus contribution and intercompany receivable in the amount of \$110,149,000.
4. As of December 31, 2007, \$190,707,000 in additional adverse development in excess of \$150,000,000 occurred related to accident years 2003 and prior, triggering a contribution due from Allianz SE to the Company in accordance with the terms of the commitments. Subject to regulatory approval, the contribution may take the form of a secured commitment, which would be converted to cash as the relevant losses are paid.

### Dividends Paid to Parent

In November 2004, the California Department of Insurance (CDI) approved the Company's request for a non-cash extraordinary dividend to its sole shareholder, Allianz Global Risks US Insurance Company (AGR US) totaling \$495 million in the form of promissory notes from Allianz SE or its subsidiaries.

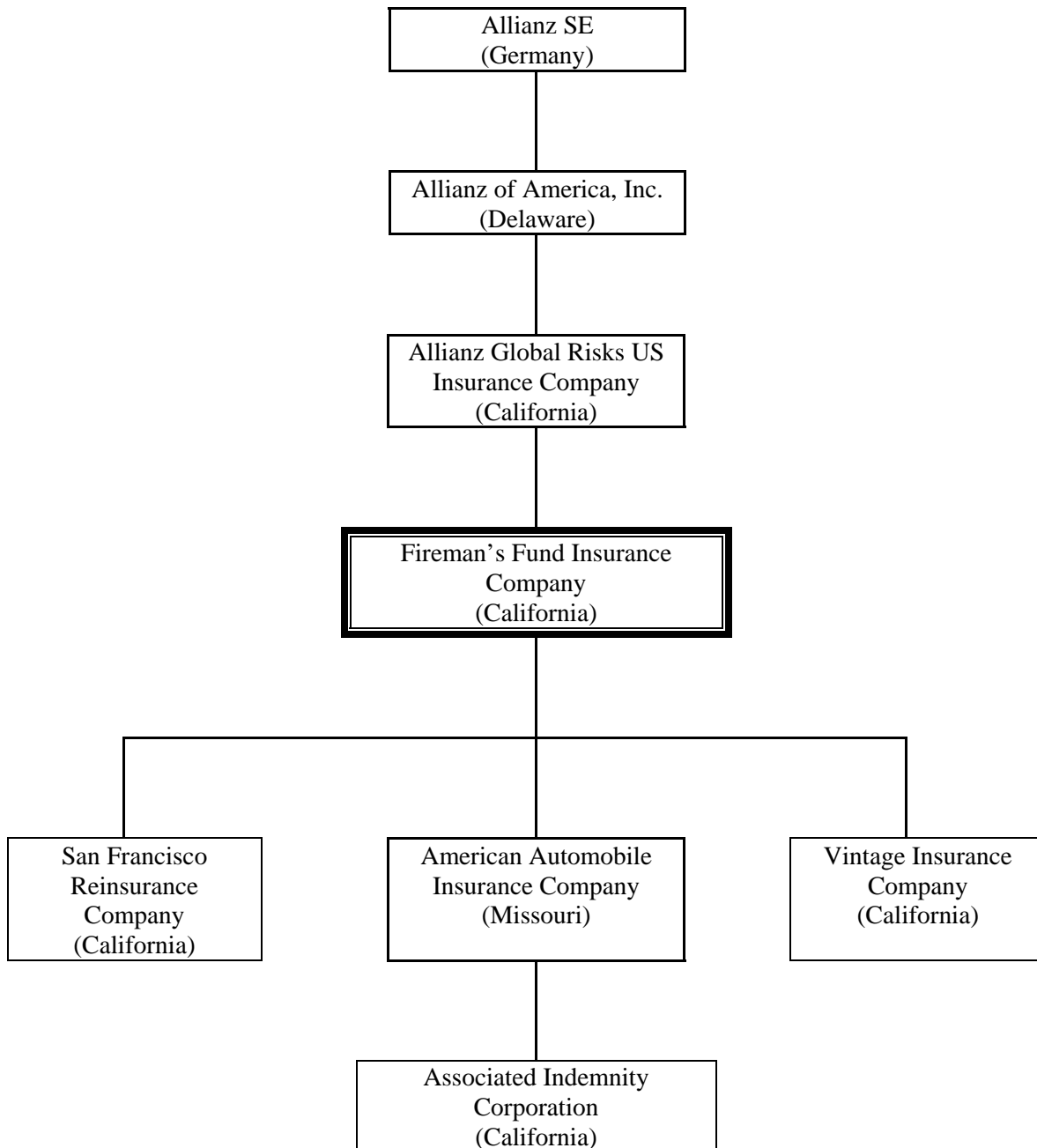
In November 2005, the CDI approved the Company's request for a non-cash extraordinary dividend to AGR US totaling \$720 million in the form of four promissory notes from Allianz SE or its subsidiaries.

In December 2006, the Company paid an extraordinary cash dividend to AGR US totaling \$725 million. The CDI approved this transaction in October 2006.

In December 2007, the Company paid an extraordinary cash dividend to AGR US totaling \$750 million. The CDI approved this transaction in October 2007.

### MANAGEMENT AND CONTROL

The Company is a member of an insurance holding company system. Allianz SE, formerly Allianz Aktiengesellschaft, is a European Company incorporated in the Federal Republic of Germany and the European Union. Allianz SE is the ultimate controlling entity. The following chart depicts the interrelationship of the Company and its California subsidiaries within the holding company system (all ownership is 100%):



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, 2007:

## Directors

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Gary C. Bhojwani Excelsior, Minnesota	President and Chief Executive Officer Allianz Life Insurance Company of North America
Jan R. Carendi Munich, Germany	Chairman of the Board Member of the Board of Management Allianz SE
Peter Huehne Tiburon, California	Executive Vice President and Chief Financial Officer Allianz Deutschland AG
Charles M. Kavitsky <sup>(a)</sup> Tiburon, California	President Allianz of America Corporation
Jill E. Paterson Tiburon, California	Executive Vice President and Chief Financial Officer Allianz of America Corporation
Dr. Helmut Perlet Paehl/Aidenried, Germany	Member of the Board of Management Allianz SE

## Principal Officers

<u>Name</u>	<u>Title</u>
Charles M. Kavitsky <sup>(a)</sup> Jill E. Paterson <sup>(b)</sup>	President and Chief Executive Officer Executive Vice President and Chief Financial Officer
Cynthia L. Pevehouse <sup>(c)</sup> Linda E. Wright <sup>(d)</sup>	Senior Vice President and Secretary Senior Vice President and Treasurer

The following changes in management occurred subsequent to the examination date:

<sup>(a)</sup> Charles Kavitsky was elected as Chairman of the Board effective January 1, 2008. In January 2009 the Company announced that Mr. Kavitsky will retire effective July 31, 2009. Michael LaRocco was named President and CEO effective March 17, 2008.

- (b) Jill Paterson was elected Treasurer effective October 28, 2008. Her current title is Executive Vice President, Chief Financial Officer and Treasurer.
- (c) Cynthia Pevehouse was elected Executive Vice President, General Counsel and Secretary at Allianz of America Corporation. Sally Narey replaced Ms. Pevehouse as Senior Vice President, General Counsel and Secretary effective September 8, 2008.
- (d) Linda Wright was replaced as Treasurer by Jill Paterson effective October 28, 2008. Ms. Wright is no longer employed by the Company.

### Management Agreements

Tax Reimbursement Agreement: Effective December 17, 1999, the Company entered into a Tax Reimbursement Agreement for the purpose of clarifying an agreement that was in effect since 1991. The Tax Reimbursement Agreement was between Allianz of America, Inc. (AZOA), the Company, and its subsidiaries. Under the terms of this agreement, the tax liability of the Company and its subsidiaries will be computed as if each member filed a separate stand-alone return. AZOA is the party primarily responsible for filing and making all tax payments on behalf of the Company and its subsidiaries.

Service Agreement: Effective March 6, 2006, a Service Agreement was executed between AZOA, the Company, Allianz of America Corporation, Allianz Global Risks US Insurance Company, and Allianz Life Insurance Company of North America (the Group Members). Each Group Member agrees to provide services for any requesting Group Member necessary for that Group Member's continuing operation. Any Group Member can decline to provide requested services if it would interfere with a Group Member's ability to meet its obligations to its policyholders or would otherwise adversely affect the performing Group Member. Each Group Member must reimburse other Group Members for direct and directly allocable expenses attributable to recipient Group Member, plus a reasonable charge for overhead. Services eligible to be provided among the Group Members include: Managerial, Investment, Treasury, Accounting, Legal, Tax, Risk Management, Audit, Information Technology, Underwriting, and Claims Handling services. The agreement was approved by the California Department of Insurance (CDI) in March 2006.

Agency Securities Lending Agreement: Effective March 2005, an Agency Securities Lending

Agreement was executed between Dresdner Bank AG (Dresdner), the Company, and Allianz Global Risks US Insurance Company (AGR US), acting through AZOA, as investment advisor. The agreement allows Dresdner to act as agent for securities lending purposes for the Company and AGR US.

The Company has other management and service agreements with its affiliated companies at December 31, 2007. The principal agreements were reviewed and found to be materially compliant with the California Insurance Code (CIC) and were filed with the CDI as required.

#### Related Party Transactions

(1) The Company guarantees the obligations of certain affiliates comprising the Interstate Insurance Group under an Agency Agreement with Bertholon-Rowland. Obligations included under the agreement relate to policies or certificates of insurance and any extensions or modifications.

(2) The Company, in accordance with the requirements of the State of Connecticut, authorized a guarantee for San Francisco Reinsurance Company (SFRe) as follows: as long as the Company controls SFRe, the combined capital and surplus will be maintained at or above \$4,000,000.

(3) The Company, in compliance with the requirements of the State of Connecticut, authorized a guarantee for Interstate Indemnity Company (IIC) as follows: as long as the Company controls IIC, the combined Capital and Surplus of IIC will be maintained at or above \$4,000,000.

(4) The Company sold 100% of its interest in Parkway Insurance Company, a New Jersey domiciled insurance subsidiary of Progressive Insurance effective December 1, 2006.

(5) On December 14, 2006, the Company received \$576,402,430 from AZOA, as payment for secured promissory notes in the amount of \$540,000,000 which were acquired from AZOA in 1994, 1995, 2001 and 2003. The payment consisted of \$540,000,000 in principal, \$14,722,350 in accrued interest, and a make whole payment of \$21,680,080.

(6) Fireman's Fund Insurance Company of Missouri was merged into American Automobile Insurance Company on November 1, 2007.

(7) The issued and outstanding common stock of Midway Insurance Company of Illinois was sold effective November 30, 2007. The Company sold Midway to Darwin National Underwriters on December 1, 2007.

(8) The American Insurance Company was re-domesticated from Nebraska to Ohio as of December 17, 2007.

(9) The Company sold Fireman's Fund Insurance Company of Nebraska on October 18, 2006 which merged with Pegasus Insurance Company, an Oklahoma domiciled insurer.

(10) The Company received dividends from its subsidiaries as shown in the schedule below:

<u>Subsidiary</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>
American Automobile Insurance Company	\$	\$ 15,700,000	\$
Fireman's Fund Insurance Company of Missouri	600,000		
Fireman's Fund Insurance Company of Nebraska		33,594,785	
Fireman's Fund Insurance Company of Texas	34,906,118		
Interstate Fire & Casualty Corporation		24,000,000	
Midway Insurance Company of Illinois	600,000		63,083
National Surety Corporation		24,000,000	
Parkway Insurance Company		33,152,046	
San Francisco Reinsurance Company		181,000,000	
The American Insurance Company		70,000,000	
All other	<u>                    </u>	<u>8,975,000</u>	<u>1,105,320</u>
Totals	<u>\$ 36,106,118</u>	<u>\$390,421,831</u>	<u>\$ 1,168,403</u>

The Company did not consistently report dividends received from affiliates on Schedule D, Part 2, Section 2, Common Stocks Owned December 31 of Current Year, or Schedule D, Part 4, Bonds and Stocks Sold, Redeemed or Otherwise Disposed of During Current Year, or Schedule BA, Parts 1 and

## 2, Long-Term Invested Assets.

The Company did not report a dividend payment received from its wholly owned subsidiary, International Film Guarantors, Inc. in the amount of \$8,975,000 in the Notes to Financial Statements, Note 10. Transactions concerning parents, subsidiaries and affiliates are required to be reported in the annual statement notes.

### TERRITORY AND PLAN OF OPERATION

The Company's operations are conducted jointly with its subsidiaries at its home office in Novato, California. As of December 31, 2007, the underwriting operations of the Company's group of insurance companies (Group) were conducted through four business units: Commercial, Personal, Specialty (includes Marine, Specialty Casualty and Crop), and Resolution Services, previously called Discontinued Operations (businesses deemed unprofitable or non-strategic).

The Company is the lead company in an intercompany reinsurance pooling agreement with eight of its affiliates. The Group operates throughout the United States and Puerto Rico through approximately 2,650 agent/broker locations. The Company is licensed in all 50 states and the District of Columbia.

For the period ending December 31, 2007, approximately one quarter of the Group's direct business was generated in California. Commercial line business generated a large portion of the Group's total business with approximately 34% of gross premium. Personal lines business represented 24% of gross premium. Specialty lines business produced the largest percentage representing approximately 42% of total gross premium in 2007. Specialty lines included marine, specialty casualty, and crop insurance coverages. With the acquisition of William H. McGee, the Group has become the largest cargo insurer in the United States and has a strong position in the inland marine market. The Group's Crop Insurance program offers products tailored to the specific needs of the agricultural sector, including multi-peril crop insurance (MPCI), crop hail, and livestock coverages. The Company and Rural Community Insurance Services, Inc. (RCIS), an unaffiliated multi-peril crop

MGA, are in a partnership whereby RCIS administers MPCCI business with 80% of the writings ceded back to the Company. The Company then retrocedes 37.5% to Empire Fire and Marine.

In August 2008, the Group underwent significant restructuring. Specialty marine business was combined with Allianz's Global Corporate Specialty's (AGCS) global marine business into a new Allianz unit, AGCS Marine Insurance Company (AMIC), that will be managed by AGCS. Agribusiness, a major contributor to the Group's profitability in the last few years, will be run as a dedicated unit. The other portions of the Specialty Insurance will be combined with Commercial Business to form a new commercial and specialty risks organization. As a result, the Group will have two primary business units: Personal and Commercial.

## REINSURANCE

### Intercompany Reinsurance Agreement

The Company is the lead insurer in an intercompany reinsurance pooling agreement with eight of its affiliates (hereinafter also referred to as the participants). Under the terms of this agreement dated January 1, 1999 and amended January 1, 2003, the participants cede and the Company assumes 100% of the participants' business generated from underwriting operations. The cessions from the participants are combined with the Company's business, resulting in the pooled balance to be allocated to each company in the pool. The following table illustrates each participant's pooled share as of December 31, 2007:

<u>Company</u>	<u>State of Domicile</u>	<u>Pooling Share</u>
Fireman's Fund Insurance Company	CA	75.0%
The American Insurance Company	OH	11.5%
National Surety Corporation	IL	4.0%
Interstate Fire & Casualty Company	IL	3.5%
American Automobile Insurance Company	MO	2.5%
Chicago Insurance Company	IL	1.5%
Associated Indemnity Corporation	CA	1.0%
Interstate Indemnity Company	IL	0.8%
Fireman's Fund Insurance Company of Ohio	OH	<u>0.2%</u>
Pool Total		<u><u>100.0%</u></u>

The agreement authorizes and empowers the Company to (1) collect and receive all premiums, (2) adjust and pay all losses, (3) reinsure or cancel any and all policies and contracts of insurance, and (4) act as though the policies and contracts of insurance and reinsurance were issued by the Company. It further provides for the complete sharing of all income and expenses of the pooled business with the exception of the investment operations, liabilities for federal income tax or other items not relating to the underwriting operations of the parties. Accounts are required to be settled quarterly.

Other companies within the Fireman's Fund Group, referred to as Specialty Companies, cede 100% to the pool, but do not assume any portion of the pooled balances. These companies receive a commission from the Company, and also pay the Company a management fee, resulting in minimal income. Three companies in the pool, Interstate Fire & Casualty Company, Interstate Indemnity Company, and Chicago Insurance Company, submit business to the pool net of external reinsurance arrangements with third parties.

#### Other Intercompany Reinsurance

Prior to the pooling of business among the participating companies, certain other business is assumed and/or ceded between the Company and other affiliated companies. These companies contribute to the pool but do not receive a percentage back from the pool. Instead, these affiliates

receive a 3.25% commission fee and reimbursement of expenses. The Company assumes all business written by the following subsidiaries:

Fireman's Fund County Mutual Insurance Company  
Fireman's Fund Indemnity Corporation  
Fireman's Fund Insurance Company of Georgia  
Fireman's Fund Insurance Company of Hawaii, Inc.  
Fireman's Fund Insurance Company of Louisiana

In addition, the Company has a variety of reinsurance arrangements other than pooling with the following affiliates:

Allianz Global Risks US Insurance Company  
San Francisco Reinsurance Company  
Vintage Insurance Company

The Company also provides reinsurance facilities to American Standard Lloyd's Insurance Company, acting by and through its Attorney-in-Fact, Standard General Agency, Inc. All business underwritten or assumed by American Standard Lloyd's Insurance Company is ceded 100% to Associated Indemnity Corporation and then to the intercompany pool.

#### Assumed

In addition to intercompany agreements, the Company assumes business from pools and associations and from various companies under several reinsurance agreements.

#### Crop Insurance

The Company participates in a crop insurance program where it fronts for a carrier in states in which the carrier is not admitted. 100% of this business is ceded to the carrier who performs all issuing and servicing of the policies. The Company then assumes approximately 80% of all risks from that same carrier and retrocedes 37.5% to a third insurer.

## Loss Portfolio Transfer

On September 30, 2002 the Company entered into a loss portfolio transfer agreement with Allianz Aktiengesellschaft (AZAG) in which AZAG agreed to assume losses associated with asbestos and environmental claims for accident years 1987 and prior for a maximum of \$2,158,000,000. In lieu of having the Company pay the full premium of \$1,276,000,000, AZAG dismissed \$1.1 billion of premium payment through the assignment of premiums. AZAG assigned the \$1.1 billion premium payment to Allianz of America, Inc. (AZOA), which in turn, assigned the payment to Allianz Global Risks US Insurance Company (AGR), formerly Allianz Insurance Company. AGR then assigned the payment back to the Company as a capital contribution. Therefore, no cash was actually exchanged for the \$1.1 billion premium payment. A trust account was established and the Company placed the remaining \$176,000,000 in securities in a trust account.

The prospective treatment of the contract was approved by the California Department of Insurance as it met the requirements for a prospective agreement defined under Statement of Statutory Accounting Principles (SSAP) No. 62, paragraph 30(d). During 2007, the maximum limit of \$2,158,000,000 was reached. The Company is now establishing reserves for all losses in excess of that amount.

## Ceded

Other than intercompany agreements, reinsurance is placed through the Company for the Fireman's Fund Insurance Company Group (Group). All members of the Group, either individually or collectively, may utilize the reinsurance of the various contracts that are in effect. For the major principal treaties, coverages, retentions and limits in effect for the exam period, see below.

The Company utilizes the facultative market, as needed, to increase its capacity. Senior management provides a list of acceptable facultative markets to the field underwriting staff.

<b>Line of Business and Type of Contract</b>	<b>Reinsurer's Name</b>	<b>Company's Retention</b>	<b>Reinsurer's Limit</b>
<b><u>Casualty:</u></b>			
<b><u>Per Risk Excess of Loss</u></b>			
First Layer	9 domestic, foreign and alien companies	\$15 million each and every occurrence, each and every risk	\$10 million excess \$15 million, each and every occurrence, each and every risk, not to exceed \$10 million each and every occurrence, each and every risk . Acts of Terrorism only \$60 million aggregate
Second Layer	9 domestic, foreign and alien companies	\$25 million per occurrence, each and every risk	\$25 million excess \$25 million, each and every occurrence, each and every risk, not to exceed \$25 million each and every occurrence, each and every risk. Acts of Terrorism only \$50 million in aggregate
<b><u>Property:</u></b>			
<b><u>Property – Per Risk XOL</u></b>			
First layer	Various domestic, foreign and alien companies led by Allianz and Axis Specialty Limited	\$15 million each and every loss/risk	\$10 million excess \$15 million, each and every loss/risk, not to exceed \$30 million per occurrence; limited to \$50 million
Second layer	Various domestic, foreign and alien companies led by Allianz and Allied World Assurance	\$25 million each and every loss/risk	\$25 million excess \$25 million, each and every loss/risk, not to exceed \$50 million per occurrence; limited to \$100 million
Third layer	Various domestic, foreign and alien companies led by Allianz and Axis Specialty Limited	\$50 million each and every loss/risk	\$50 million excess \$50 million, each and every loss/risk, not to exceed \$100 million per occurrence, limited to \$150 million
Fourth Layer	Various domestic, foreign and alien companies led by Allianz and Hannover Ruckversicherung	\$100 million each and every loss/risk	\$50 million excess \$100 million, each and every loss/risk, not to exceed \$100 million per occurrence; limited to \$100 million
Fifth Layer	Various domestic, foreign and alien companies led by Allianz and Axis Specialty Limited	\$150 million each and every loss/risk	\$50 million excess \$150 million, each and every loss/risk, not to exceed \$100 million per occurrence; limited to \$150 million
First Layer – Certified Terrorism only		\$15 million	\$10 million excess \$15 million, each and every loss/risk, not to exceed \$10 million per occurrence; limited to \$20 million
Second Layer- Certified Terrorism only		\$25 million	\$25 million excess \$25 million, each and every loss/risk, not to exceed \$25 million occurrence; limited to \$50 million
Third Layer Certified Terrorism only		\$50 million	\$50 million excess \$50 million, each and every loss/risk, not to exceed \$50 million occurrence; limited to \$100 million
Fourth Layer Certified Terrorism only		\$100 million	\$50 million excess \$100 million, each and every loss/risk, not to exceed \$50 million occurrence; limited to \$100 million

<b>Line of Business and Type of Contract</b>	<b>Reinsurer's Name</b>	<b>Company's Retention</b>	<b>Reinsurer's Limit</b>
Fifth Layer Certified Terrorism only		\$150 million	\$50 million excess \$150 million, each and every loss/risk, not to exceed \$50 million occurrence; limited to \$100 million
<u>Property Catastrophe Excess of Loss</u>			
First layer	21 domestic, foreign and alien companies led by Allianz SE	\$300 million plus 20% of \$100 million excess of \$300 million	80% of \$100 million excess \$300 million, loss/losses/one event, not to exceed \$100 million per occurrence; limited to \$200 million
Second Layer	29 domestic, foreign and alien companies led by Allianz SE	\$400 million plus 20% of \$150 million excess of \$400 million	80% of \$150 million excess \$400 million, loss/losses/one event, not to exceed \$150 million per occurrence; limited to \$300 million
Third Layer	25 domestic, foreign and alien companies led by Allianz SE	\$550 million plus 20% of \$250 million excess of \$550 million	80% of \$250 million excess \$550 million, loss/losses/one event, not to exceed \$250 million per occurrence; limited to \$500 million
Fourth Layer	27 domestic, foreign and alien companies led by Allianz SE	\$800 million plus 20% of \$400 million excess of \$800 million	80% of \$400 million excess \$800 million, loss/losses/one event, not to exceed \$400 million per occurrence; limited to \$800 million
Mega Catastrophe	Allianz SE	\$1,482 million	\$1,201 million excess \$1,482 million each and every loss occurrence with two or more risks involved
<u>Aggregate Excess of Loss</u>			
Terrorism	Allianz SE and National Indemnity	\$250 million plus 33.4% of \$150 million in excess of \$250 million	66.6% of \$150 million in excess of \$250 million. The retention and risks combine Allianz Global Risk US Insurance Company, the Company, and subsidiaries
<u>Inland Marine and Property Per Risk and Occurrence Excess of Loss</u>			
Sub-First Layer	SwissRe America only	\$10 million	100% of \$5 million excess \$10 million, each and every loss/occurrence(s)/one event; no more than \$30 million
First Layer	4 domestic, foreign and alien companies led by AxisRe	\$15 million plus 50% of \$10 million excess of \$15 million each and every loss/occurrence(s)/one event	50% of \$10 million excess \$15 million, each and every loss/occurrence(s)/one event; no more than 50% of \$30 million
Second Layer	11 domestic, foreign and alien companies led by AxisRe	\$25 million plus 10% of \$10 million excess of \$25 million each and every loss/occurrence(s)/one event	90% of \$10 million excess \$25 million, each and every loss/occurrence(s)/one event; no more than 90% of \$20 million
Third Layer	11 domestic, foreign and alien companies led by AxisRe	\$35 million plus 20% of \$15 million excess of \$35 million each and every loss/occurrence(s)/one event	80% of \$15 million excess \$35 million, each and every loss/occurrence(s)/one event; no more than 80% of \$30 million

<b>Line of Business and Type of Contract</b>	<b>Reinsurer's Name</b>	<b>Company's Retention</b>	<b>Reinsurer's Limit</b>
<b><u>Marine - Excess of Loss</u></b>			
First layer	13 domestic, foreign and alien companies led by PlatinumRe	\$10 million each and every loss / occurrence(s) /one event	\$5 million excess \$10 million, each and every loss/occurrence(s)/one event; no more than \$15 million
Second Layer	13 domestic, foreign and alien companies led by PlatinumRe	\$15 million each and every loss / occurrence(s) /one event	\$10 million excess \$15 million, each and every loss/occurrence(s)/one event, no more than \$30 million
Third Layer	13 domestic, foreign and alien companies led by PlatinumRe	\$25 million each and every loss / occurrence(s) /one event	\$15 million excess \$25 million, each and every loss/occurrence(s)/one event, no more than \$30 million
<b><u>Marine Whole - Excess of Loss (Ocean, Inland and Property)</u></b>			
First layer	12 domestic, foreign and alien companies led by Everest Reinsurance Company	\$10 million marine and \$15 million inland marine, each and every loss/occurrences(s)/one event	\$10 million excess retention, each and every loss/occurrence(s)/one event; no more than \$20 million
Second Layer	12 domestic, foreign and alien companies led by Everest Reinsurance Company	\$20 million marine and \$25 million inland marine, each and every loss/occurrences(s)/one event	\$10 million excess retention, each and every loss/occurrence(s)/one event; no more than \$20 million
Third Layer	12 domestic, foreign and alien companies led by Everest Reinsurance Company	\$30 million marine and \$35 million inland marine, each and every loss/occurrences(s)/one event	\$10 million excess retention, each and every loss/occurrence(s)/one event; no more than \$20 million
Fourth Layer	12 domestic, foreign and alien companies led by Everest Reinsurance Company	\$40 million marine and \$45 million inland marine, each and every loss/occurrences(s)/one event	\$20 million excess retention, each and every loss/occurrence(s)/one event; no more than \$40 million
<b><u>Entertainment:</u></b> (film and completion guarantee)			
Entertainment Excess of Loss Underlayer	Allianz - Dublin	\$12 million each and every loss / occurrence(s) /one event	\$3 million excess \$12 million, each and every loss/occurrence(s)/one event, no more than \$12 million / \$12.5 million Foreign Acts of Terrorism
Entertainment-Excess of Loss First Layer	Lloyds and 6 domestic, foreign and alien companies	\$15 million plus 10% of \$10 million excess \$15 million each and every loss / occurrence(s) /one event	90% of \$10 million excess \$15 million, each and every loss/occurrence(s)/one event, no more than \$40 million
Second Layer	Lloyds and 6 domestic, foreign and alien companies	\$25 million plus 10% of \$25 million excess \$25 million each and every loss / occurrence(s) /one event	90% of \$25 million excess \$25 million, each and every loss/occurrence(s)/one event, no more than \$50 million

Line of Business and Type of Contract	Reinsurer's Name	Company's Retention	Reinsurer's Limit
Third Layer	Lloyds and 6 domestic, foreign and alien companies	\$50 million plus 10% of \$50 million excess \$50 million each and every loss / occurrence(s) /one event	90% of \$50 million excess \$50 million, each and every loss/occurrence(s)/one event, no more than \$100 million

## ACCOUNTS AND RECORDS

### Information Systems Controls

During the course of the examination, a review was made of the Company's general controls over its information systems. As a result of this review, several low risk findings were noted in controls over logical security. These findings were presented to the Company along with recommendations to strengthen its controls. The Company should evaluate the recommendations and make appropriate changes to strengthen its information system controls.

### Federal Income Taxes

Currently the methodology being used for measuring temporary book/tax differences is not in compliance with Statement of Statutory Accounting Principles (SSAP) No. 10, paragraph 6.a. which states "Temporary differences are identified and measured using a balance sheet approach whereby statutory and tax basis balance sheets are compared." The Company currently uses an income statement approach where the current year non-taxable amounts are added/subtracted from last year's cumulative timing difference. The updated cumulative timing difference is used to support the deferred tax asset or liability. The balance sheet approach is preferred in order to assure completeness and accuracy of the deferred tax inventories, particularly where the tax basis calculations are complicated and are developed over several years. It is recommended that the Company identify and measure temporary differences using a balance sheet approach in compliance with SSAP No. 10, paragraph 6.a.

## FINANCIAL STATEMENTS

The financial statements prepared for this examination report include:

Statement of Financial Condition as of December 31, 2007

Underwriting and Investment Exhibit for the Year Ended December 31, 2007

Reconciliation of Surplus as Regards Policyholders from December 31, 2003  
through December 31, 2007

Reconciliation of Examination Changes as of December 31, 2007

Statement of Financial Condition  
as of December 31, 2007

<u>Assets</u>	<u>Ledger and Nonledger Assets</u>	<u>Assets Not Admitted</u>	<u>Net Admitted Assets</u>	<u>Notes</u>
Bonds	\$ 5,351,174,782	\$	\$ 5,351,174,782	
Preferred stocks	55,002,896		55,002,896	
Common stocks	1,770,110,400	28,372,616	1,741,737,784	(1)
Mortgage loans on real estate	109,759,728		109,759,728	
Cash and short-term investments	(132,862,290)		(132,862,290)	
Other invested assets	166,627,330	55,429,484	111,197,846	
Receivable for securities	1,297,617		1,297,617	
Investment income due and accrued	88,454,000	33,212,916	55,241,084	
Premiums and agents' balances in course of collection	1,493,540,385	59,691,310	1,433,849,075	
Premiums, agents' balances and installments booked but deferred and not yet due (including \$11,974,363 earned but unbilled premiums)	373,205,782	1,334,470	371,871,312	
Accrued retrospective premiums	1,658,194	104,910	1,553,284	
Amount recoverable from reinsurers	146,464,072		146,464,072	
Funds held by or deposited with reinsured companies	4,429,474		4,429,474	
Current federal and foreign income tax recoverable and interest thereon	24,191,188		24,191,188	
Net deferred tax asset	494,289,680	321,795,187	172,494,493	
Guaranty funds receivable or on deposit	3,518,496		3,518,496	
Electronic data processing equipment and software	151,364,610	151,171,319	193,291	
Furniture and equipment, including health care delivery assets	44,204,641	44,204,641	0	
Aggregate write-ins for other than invested assets	<u>790,827,671</u>	<u>17,839,882</u>	<u>772,987,789</u>	(2)
Total assets	<u>\$ 10,937,258,656</u>	<u>\$ 713,156,735</u>	<u>\$ 10,224,101,921</u>	
<u>Liabilities, Surplus and Other Funds</u>				
Losses and loss adjustment expenses			\$ 4,808,434,634	(3)
Reinsurance payable on paid loss and loss adjustment expenses			114,907,641	
Commissions payable, contingent commissions and other similar charges			101,150,665	
Other expenses			255,215,268	
Taxes, licenses and fees			37,172,772	
Unearned premiums			1,472,259,900	
Advance premiums			1,078,462	
Dividends declared and unpaid: Policyholders			1,442,887	
Ceded reinsurance premiums payable			599,600,304	
Funds held by company under reinsurance treaties			2,764,187	
Amounts withheld or retained by company for account of others			(3,261,384)	
Provision for reinsurance			58,137,377	
Payable to parent, subsidiaries and affiliates			44,149,021	
Payable for securities			1,764,454	
Aggregate write-ins for liabilities			<u>198,529,581</u>	(4)
Total liabilities			7,693,345,769	
Common capital stock	\$ 4,200,000			
Gross paid in and contributed surplus		2,231,476,897		
Unassigned funds (surplus)		<u>295,079,255</u>		
Surplus as regards policyholders			<u>2,530,756,152</u>	
Total liabilities, surplus and other funds			<u>\$ 10,224,101,921</u>	

Underwriting and Investment Exhibit  
for the Year Ended December 31, 2007

Statement of Income

Underwriting Income

Premiums earned		\$ 3,486,013,408
Deductions:		
Losses and loss expenses incurred	\$ 2,611,901,564	
Other underwriting expenses incurred	<u>1,065,734,880</u>	
Total underwriting deductions		<u>3,677,636,444</u>
Net underwriting loss		(191,623,036)

Investment Income

Net investment income earned	\$ 332,665,228	
Net realized capital gain	<u>11,416,872</u>	
Net investment gain		344,082,100

Other Income

Net loss from agents' or premium balances charged off (amount recovered \$453,079 amount charged off \$4,421,236)	\$ (3,968,157)	
Aggregate write-ins for miscellaneous income	<u>(3,233,386)</u>	
Total other income		<u>(7,201,543)</u>
Net income before dividends to policyholders, after capital gains tax and before federal and foreign income taxes		145,257,521
Dividends to policyholders		<u>4,521,429</u>
Net income after dividends to policyholders, after capital gains tax and before federal and foreign income taxes		140,736,092
Federal and foreign income taxes incurred		<u>176,949,485</u>
Net income		<u>\$ (36,213,393)</u>

Capital and Surplus Account

Surplus as regards policyholders, December 31, 2006		\$ 3,032,630,953
Net income	\$ (36,213,393)	
Change in net unrealized capital gains	153,922,555	
Change in net unrealized foreign exchange capital gain	240,029	
Change in net deferred income tax	21,900,007	
Change in nonadmitted assets	(73,210,812)	
Change in provision for reinsurance	51,166,327	
Surplus adjustments:		
Paid in	(296,020,000)	
Aggregate write-ins for losses in surplus	<u>(323,659,514)</u>	
Change in surplus as regards policyholders for the year		<u>(501,874,801)</u>
Surplus as regards policyholders, December 31, 2007		<u>\$ 2,530,756,152</u>

Reconciliation of Surplus as Regards Policyholders  
from December 31, 2003 through December 31, 2007

Surplus as regards policyholders, December 31, 2003 per Examination			\$ 2,201,044,279
	<u>Gain in Surplus</u>	<u>Loss in Surplus</u>	
Net income	\$ 2,047,656,886	\$	
Net unrealized capital gains	365,213,975		
Change in net foreign exchange capital losses		1,168,951	
Change in net deferred income tax		370,526,590	
Change in nonadmitted assets	102,394,521		
Change in provision for reinsurance	60,047,650		
Cumulative effect of changes in accounting principles		119,995	
Surplus adjustments: Paid-in		1,942,339,006	
Aggregate write-ins for gains and losses in surplus	<u>68,553,383</u>		
Total gains and losses	<u>\$ 2,643,866,415</u>	<u>\$ 2,314,154,542</u>	
Net decrease in surplus as regards policyholders			<u>(329,711,873)</u>
Surplus as regards policyholders, December 31, 2007, per Examination			<u>\$ 2,530,756,152</u>

Reconciliation of Examination Changes  
as of December 31, 2007

	<u>Per</u> <u>Company</u>	<u>Per</u> <u>Examination</u>	<u>Surplus</u> <u>Increase</u> <u>(Decrease)</u>	<u>Notes</u>
<u>Assets</u>				
Common Stocks	\$ 1,954,076,784	\$ 1,741,737,784	\$ (212,339,000)	(1)
Aggregate write-ins for other than invested assets:				
Keep Well Commitment Receivable	319,007,789	772,987,789	453,980,000	(2)
<u>Liabilities</u>				
Losses and loss adjustment expenses	4,356,760,634	4,808,434,634	(451,674,000)	(3)
Aggregate write-ins for liabilities:				
Excess of Statutory Reserves Over Statement Reserves	45,109,581	198,529,581	<u>(153,420,000)</u>	(4)
Net decrease to surplus			(363,453,000)	
Surplus as regards policyholders, December 31, 2007, per Company			<u>2,894,209,152</u>	
Surplus as regards policyholders, December 31, 2007, per Examination			<u>\$ 2,530,756,152</u>	

## COMMENTS ON FINANCIAL STATEMENT ITEMS

### (1) Common Stocks

The captioned asset was determined to be \$1,741,737,784 per examination, a decrease of \$212,339,000. This decrease is due to adjustments of \$157,900,000 to the statutory value of subsidiaries of the Company. These adjustments were the result of loss and loss adjustment expense reserve deficiencies noted by the California Department of Insurance (CDI)'s consulting actuary in the actuarial analysis of the intercompany reinsurance pool. In addition, adjustments totaling \$54,439,000 were made to the Company's subsidiaries for the minimum reserve amounts for loss and loss adjustment expenses as required by California Insurance Code (CIC) Section 11558.

### (2) Aggregate Write-ins for Other Than Invested Assets: Keep Well Commitment Receivable

Pursuant to provisions in the Keep Well commitment between the Company and Allianz SE, Allianz SE agreed to contribute capital to the Company to the extent of adverse development on accident year 2003 and prior reserves. As of December 31, 2007, \$800,000,000 in Keep Well coverage was available to the Company. As an offset to the consolidated reserve deficiency per examination, surplus relief amounting to \$453,980,000 is available as a capital contribution to the Company. The offset represents the total reserve deficiency of \$609,575,000 less adjusting and other expense (ULE) reserve deficiencies of \$155,595,000, which are not covered in the Keep Well Commitment. The capital contribution would be payable entirely to the Company, with no intercompany balances due to the subsidiaries.

### (3) Losses and Loss Adjustment Expenses

The CDI retained an independent Consulting Actuary to evaluate the loss and loss adjustment expense reserves (loss reserves) as of December 31, 2007. In addition, a Senior Casualty Actuary with the CDI reviewed the work of our Consulting Actuary, and performed additional analysis as deemed appropriate. Based on the analyses performed by the CDI's Consulting Actuary and in-house Senior Casualty Actuary, the CDI has determined its best estimate of loss reserves to be

\$6,411,246,000 for all companies participating in the intercompany reinsurance pooling agreement. The Company's share of this deficiency totals \$451,674,000. The reserve deficiency primarily relates to adverse development on asbestos and environmental reserves (A&E), which triggered amounts due from Allianz SE under a Keep Well Commitment. Refer to Note (2) above. Refer to the table below for the carried vs. estimated reserves for each company in the pool.

The CDI understands that the Company has retained an actuarial firm to perform a full ground-up analysis of its A&E reserves. The CDI will closely monitor the development of the Company's A&E reserves and will be reviewing the results of the A&E reserve study.

<u>Company</u>	<u>Pool Percentage</u>	<u>Indicated Per Department (000)</u>	<u>Carried Per Company (000)</u>	<u>Deficiency (000)</u>
<b>Fireman's Fund Insurance Company</b>	<b>75.0%</b>	<b>\$ 4,808,435</b>	<b>\$ 4,356,761</b>	<b>\$ (451,674)</b>
The American Insurance Company	11.5%	737,293	668,037	(69,256)
National Surety Corporation	4.0%	256,450	232,361	(24,089)
Interstate Fire & Casualty Company	3.5%	224,394	203,315	(21,078)
American Automobile Insurance Company	2.5%	160,281	145,225	(15,056)
Chicago Insurance Company	1.5%	96,169	87,135	(9,033)
Associated Indemnity Corporation	1.0%	64,112	58,090	(6,022)
Interstate Indemnity Company	0.8%	51,290	46,472	(4,818)
Fireman's Fund Insurance Company of Ohio	0.2%	12,822	11,618	(1,204)
<b>Total Pooled Companies</b>	<b>100.00%</b>	<b>\$ 6,411,246</b>	<b>\$ 5,809,014</b>	<b>\$ (602,232)</b>
Vintage Insurance Company	N/A	33	33	0
San Francisco Reinsurance Company	N/A	32,810	25,467	(7,343)
<b>Total All Companies</b>	<b>N/A</b>	<b>\$ 6,444,089</b>	<b>\$ 5,834,514</b>	<b>\$ (609,575)</b>

(4) Aggregate Write-ins for Liabilities: Excess of Statutory Reserves over Statement Reserves

The Company did not include a minimum reserve requirement for loss and loss adjustment expenses in its aggregate write-ins for liabilities as required by California Insurance Code (CIC) Section 11558. The additional reserve amount was calculated to be \$153,420,000. The additional reserve did not include a minimum reserve for workers compensation lines, as the statute no longer requires

this calculation effective January 1, 2008. The workers' compensation additional reserve would have amounted to \$4,891,450.

The minimum reserve requirement applies to all insurers licensed in California. As such, a calculation was made of the additional reserve for the Company's subsidiaries, which resulted in an additional \$54,439,000 adjustment (Schedule D, Part 2, Section 2: Common Stocks). The total adjustment to policyholder surplus amounted to \$207,859,000. It is recommended the Company calculate the minimum schedule P reserve liability in accordance with CIC Section 11558.

## SUMMARY OF COMMENTS AND RECOMMENDATIONS

### Current Report of Examination

Accounts and Records – Information System Controls (Page 19): As the result of the review of the Company's information systems controls, recommendations for improving these controls were presented to the Company. The Company should evaluate these recommendations and make appropriate changes to strengthen its controls over its information systems.

Accounts and Records – Federal Income Taxes (Page 19): It is recommended that the Company identify and measure temporary differences using a balance sheet approach in accordance with Statement of Statutory Accounting Principles (SSAP) No. 10, paragraph 6.a.

Comment on Financial Statement Items – Excess of Statutory Reserves over Statement Reserves (Page 26) – It is recommended the Company comply with California Insurance Code Section 11558.

## Previous Report of Examination

Management and Control – Related Party Transactions (Page 9): The following recommendations related to the \$1 billion surplus contribution made to the Company in September, 2001 by Allianz Global Risks US Insurance Company (AGR) were made:

- 1) It was recommended the share pledge agreements be amended to require that the market value of pledged securities be at least 120% of the principal balance of the note. The Company has complied with this recommendation.
  
- 2) It was recommended the Company implement controls to ensure that legally binding agreements between affiliates are enforced. Additionally, pursuant to California Insurance Code (CIC) Section 1215.5(b), it was recommended that the Company notify the California Department of Insurance (CDI) at least 30 days prior to entering into agreements with its affiliates. The Company has complied with these recommendations.
  
- 3) The following three recommendations related to the Securities and Securities Account Pledge Agreement were made:
  - a) Pursuant to CIC Section 1215.5(b), it was recommended that the Company notify the CDI at least 30 days prior to entering into agreements with its affiliates. The Company has complied with this recommendation.
  - b) It was recommended this agreement be amended to require the market value of pledged securities be at least 120% of the principal balance of the note. The Company has complied with this recommendation.
  - c) It was recommended the Company eliminate collateral deficiencies and establish monitoring procedures to ensure the collateral is at least 120% of the principal balance of the notes. The Company has complied with this recommendation.

Management and Control – Related Party Transactions (Page 9): It was recommended that the Company abide by the terms of all current and future intercompany sale agreements and account for

the sale transactions in accordance with SSAP No. 42 of the National Association of Insurance Commissioners (NAIC) Accounting Practices and Procedures Manual. The Company has implemented procedures to ensure adherence to the terms of all current and future intercompany sale agreements and to ensure accounting for sale transactions are in accordance with SSAP No.42 of the NAIC Accounting Practices and Procedure Manual.

Management and Control – Related Party Transactions (Page 9): It was recommended the Company disclose all material related party transactions in accordance with SSAP No. 25, paragraphs 17-18, of the NAIC Accounting Practices and Procedures Manual. The Company disclosed the guaranty made by Allianz of America, Inc. (AZOA) beginning with the first quarter 2005 financial statements.

Reinsurance - Intermediary Clause (Page 21): It was recommended that the Company modify the intermediary clause of the marine reinsurance treaties as well as the broker authorization agreement to include Guy Carpenter as an intermediary-broker. The Company modified the agreements as recommended with the April 1, 2005 renewals.

Reinsurance - Letters of Credit (Page 22): It was recommended the Company remove the references letters of credit that had expired from the letters of credit upon their renewal. The Company has complied with this recommendation.

Accounts and Records – Information System Controls (Page 22): The Company should evaluate the recommendations from the information systems controls review and make appropriate changes to strengthen its controls over its information systems. The Company has implemented changes to strengthen its controls over information systems.

Accounts and Records – Notes to Financial Statements (Page 22): It was recommended that the Company provide full disclosure in the Annual Statement of any accounting practices that depart from the NAIC accounting practices and procedures in accordance with SSAP No.1 paragraph 7 of the NAIC Accounting Practices and Procedures Manual. The Company provided full disclosure in its 2004 Annual Statement.

Accounts and Records – Reconciliation of General Ledger Accounts (Page 23): It was recommended that the Company implement controls to ensure that general ledger accounts are reconciled to the system from which the data feeding the general ledger resides. The Company has implemented controls to strengthen the reconciliation processes.

Comments on Financial Statement Items – Bonds (Page 29): It was recommended the Company revise its Custodial Agreement with Mellon Trust of California to include provisions recommended by the NAIC Financial Examiners Handbook. It was also recommended the Company submit the revised Agreement to the CDI for approval. The Company included the provisions and submitted the Agreement to the CDI for approval as recommended. The revised agreement was approved by the CDI on January 25, 2006.

Comments on Financial Statement Items – Common Stocks (Page 30): It was recommended that the Company classify Allianz Cash Pool, LLC as Other Invested Assets and report it in Schedule BA. The Company classified the Allianz Cash Pool, LLC as Other Invested Assets and reported it in Schedule BA in its 2004 Annual Statement.

Comments on Financial Statement Items – Other Invested Assets (Page 30): It was recommended the Company non-admit assets that are unavailable due to encumbrances or other third party interests. The Company began non-admitting assets as recommended starting with the 2004 Annual Statement.

Comments on Financial Statement Items – Other Invested Assets (Page 30): It was recommended the Company value other invested assets in accordance with SSAP No. 46 and SSAP No. 48 of the NAIC Accounting Practices and Procedures Manual. The Company has complied with this recommendation.

Comments on Financial Statement Items – Uncollected Premiums and Agents' Balances in Course of Collection (Page 32): It was recommended that the Company implement procedures to ensure that

over ninety balances due can be supported by the underlying policy level detail. The Company has implemented procedures to provide underlying policy level detail for over ninety balances due.

Comments on Financial Statement Items – Deferred Premiums, Agents’ Balances, and Installments Booked but Deferred and not yet Due (Page 32): It was recommended the Company implement controls to ensure that all accounts subject to pooling are properly pooled and allocated to each member. The Company has implemented controls to ensure that all accounts subject to pooling are properly pooled and allocated to each member.

Comments on Financial Statement Items – Amounts Recoverable from Reinsurers (Page 32): It was recommended the Company implement procedures and controls to ensure that reinsurance premiums payable are not offset against reinsurance recoverables on paid losses. The Company has complied with this recommendation.

Comments on Financial Statement Items – Dividends Declared and Unpaid – Policyholders (Page 33): It is recommended that the Company record policyholder dividends payable in the period in which they are declared. The Company has implemented a process to ensure timely notification and recording of dividends declared.

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/\_\_\_\_\_  
Gordon M. Curtis, CFE, CISA  
Examiner-In-Charge  
Department of Insurance  
State of California