

REPORT OF EXAMINATION
OF THE
SAN FRANCISCO REINSURANCE COMPANY
AS OF
DECEMBER 31, 2010

Filed: June 8, 2012

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San Francisco, California
May 16, 2012

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

Dear Commissioner:

Pursuant to your instructions, an examination was made of the

SAN FRANCISCO REINSURANCE COMPANY

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

SCOPE OF EXAMINATION

This is a multi-state examination of the Company. The previous multi-state 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.

The examination was a coordinated examination and was conducted concurrently with other insurance entities in the holding company group and included participation from the following States: Illinois, Louisiana, Missouri, New Jersey, and Ohio.

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; pensions, stock ownership and insurance plans; growth of company; statutory deposits; and sales and advertising .

COMPANY HISTORY

The Company began business in 1964 as National Surety Corporation of California. In 1980, the Company's name was changed to San Francisco Insurance Company and to its present name in 1981. Effective January 1, 1997, the Company ceased its underwriting operations, except for renewals, and is proceeding with the runoff of its existing business.

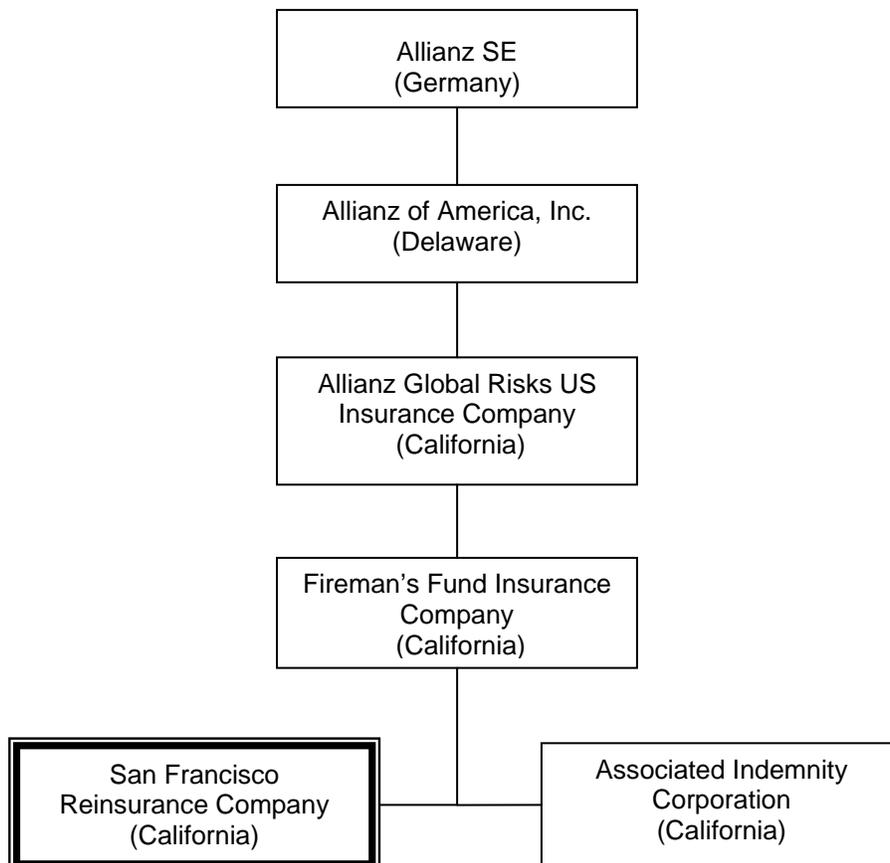
The Company is authorized to issue 60,000 shares of common stock with a par value of \$100. As of December 31, 2010, there were 39,215 shares outstanding. All outstanding shares of the Company are owned by its parent, Fireman's Fund Insurance Company (FFIC), a subsidiary of Allianz Global Risks US Insurance Company, which is wholly owned by Allianz of America, Inc. The ultimate parent of the Allianz Group is Allianz SE. Allianz SE operates on a worldwide basis through branch offices, subsidiaries and affiliated companies.

On December 14, 2009 the Company paid an ordinary dividend to FFIC as a cash distribution from gross paid-in and contributed surplus in the amount of \$14 million.

On December 14, 2010 the Company paid an ordinary dividend to FFIC as a cash distribution from gross paid-in and contributed surplus in the amount of \$8 million.

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, oversee management of the business and affairs of the Company. Following are members of the board and principal officers of the Company serving at December 31, 2010:

Directors

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Bruce F. Friedberg ^(a) Novato, California	Senior Vice President Fireman's Fund Insurance Company
Jeffery F. Johnson San Anselmo, California	Vice President and Controller Fireman's Fund Insurance Company
Michael E. LaRocco ^(b) Sonoma, California	Chairman, President and Chief Executive Officer Fireman's Fund Insurance Company
Sally B. Narey Larkspur, California	Senior Vice President, General Counsel and Secretary Fireman's Fund Insurance Company
Jill E. Paterson ^(c) Tiburon, California	Executive Vice President, Chief Financial Officer and Treasurer Fireman's Fund Insurance Company

Principal Officers

<u>Name</u>	<u>Title</u>
Michael E. LaRocco ^(b)	President and Chief Executive Officer
Jill E. Paterson ^(c)	Executive Vice President, Chief Financial Officer, and Treasurer
Sally B. Narey	Senior Vice President, General Counsel, and Secretary
Jeffery F. Johnson	Vice President and Controller

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

- (a) Effective March 9, 2012, David M. Zona was elected to the Board, replacing Bruce F. Friedberg.
- (b) Effective July 6, 2011, Lori D. Fouché, formerly President of Commercial Insurance replaced Michael LaRocco as the Company's President and Chief Executive Officer.
- (c) Effective September 19, 2011, Kevin E. Walker became the Company's Senior Vice President, Chief Financial Officer, Treasurer, and Director, replacing Jill E. Paterson.

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 affiliates. Under the terms of this agreement, the tax liability of the Company and its affiliates would 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 affiliates.

Service Agreement (Staff Support and Investment): Effective January 1, 1982, the Company entered into a services agreement with FFIC. The agreement has been amended on numerous occasions, with the most recent amendment effective September 30, 1994 was relating to investment fees only.

TERRITORY AND PLAN OF OPERATION

The Company is a professional reinsurance company, which wrote pro-rata and excess reinsurance in both the domestic and foreign markets. In October 2006, the Company's parent, FFIC, announced that the Company would cease underwriting new and renewal

risks, effective January 1, 1997. Following the parent's decision to place the Company into run-off, the renewal rights to the Company's book of business were sold to Hartford Fire Insurance Company.

REINSURANCE

The Company had no assumed or ceded premium written during the period covered by this examination. The reported liability for losses and loss adjustment expenses were for years prior to the examination period.

ACCOUNTS AND RECORDS

Information Systems Controls

During the course of the examination, a review was conducted of the Company's general controls over its information systems. As a result of this review, weaknesses were noted in the following areas: logical security, change management and vendor management. The weaknesses noted 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 systems controls.

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

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	\$ 83,855,316	\$	\$ 83,855,316	
Cash	1,032,575		1,032,575	
Receivable for securities	38,407		38,407	
Investment income due and accrued	1,013,857		1,013,857	
Amount recoverable from reinsurers	225,376		225,376	
Funds held by or deposited with reinsured companies	96,068		96,068	
Net deferred tax asset	<u>628,906</u>	<u>400,959</u>	<u>227,947</u>	
 Total assets	 <u>\$ 86,890,505</u>	 <u>\$ 400,959</u>	 <u>\$ 86,489,546</u>	
 <u>Liabilities, Surplus and Other Funds</u>				
Losses and loss adjustment expenses			\$ 6,278,652	(1)
Reinsurance payable on paid loss and loss adjustment expenses			(536,491)	
Other expenses			(152,529)	
Taxes, licenses and fees			38,037	
Current federal and foreign income taxes			3,525,613	
Funds held by company under reinsurance treaties			247,123	
Provision for reinsurance			1,381,494	
Payable to parent, subsidiaries and affiliates			<u>488,355</u>	
 Total liabilities			 11,270,254	
Common capital stocks	\$ 3,921,500			
Gross paid in and contributed surplus	10,633,647			
Unassigned funds (surplus)	<u>60,664,145</u>			
 Surplus as regards policyholders			 <u>75,219,292</u>	
 Total liabilities, surplus and other funds			 <u>\$ 86,489,546</u>	

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

Statement of Income

Underwriting Income

Premiums earned		\$ -
Deductions:		
Losses incurred	\$ (1,332,876)	
Other underwriting expenses incurred	<u>342,191</u>	
Total underwriting deductions		<u>(990,685)</u>
Net underwriting gain		990,685

Investment Income

Net investment income earned	\$ 4,497,225	
Net realized capital loss	<u>(16,392)</u>	
Net investment gain		<u>4,480,833</u>
Net income before federal and foreign income taxes		5,471,518
Federal and foreign income taxes incurred		<u>1,323,316</u>
Net income		<u>\$ 4,148,202</u>

Capital and Surplus Account

Surplus as regards policyholders, December 31, 2009		\$ 80,184,227
Net income	\$ 4,148,202	
Change in net unrealized foreign exchange capital loss	(6,778)	
Change in net deferred income tax	(514,659)	
Change in nonadmitted assets	425,170	
Change in provision for reinsurance	(1,016,870)	
Dividends to stockholders	<u>(8,000,000)</u>	
Change in surplus as regards policyholders for the year		<u>(4,964,935)</u>
Surplus as regards policyholders, December 31, 2010		<u>\$ 75,219,292</u>

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

Surplus as regards policyholders, December 31, 2007 per Examination			\$ 70,176,512
	Gain in Surplus	Loss in Surplus	
Net income	\$ 27,497,959	\$	
Net unrealized capital gains			
Change in net foreign exchange capital losses		35,749	
Change in net deferred income tax		574,845	
Change in nonadmitted assets	802,791		
Change in provision for reinsurance		647,376	
Dividends to stockholders		22,000,000	
Total gains and losses	\$ 28,300,750	\$ 23,257,970	
Net increase in surplus as regards policyholders			5,042,780
Surplus as regards policyholders, December 31, 2010, per Examination			\$ 75,219,292

COMMENTS ON FINANCIAL STATEMENT ITEMS

(1) Losses and Loss Adjustment Expenses

The California Department of Insurance (CDI) retained an independent Consulting Actuary pursuant to the authority granted in California Insurance Code (CIC) Section 733, to evaluate the loss and loss adjustment expense reserves (loss reserves) as of December 31, 2010. In addition, a Senior Casualty Actuary with the CDI reviewed the work of the Consulting Actuary, and performed additional analysis as deemed appropriate. Based on the analyses performed by the Consulting Actuary and CDI's Senior Casualty Actuary, the CDI has determined that the loss and loss adjustment expense reserves as reported by the Company are reasonable and have been accepted for the purposes of this examination.

SUMMARY OF COMMENTS AND RECOMMENDATIONS

Current Report of Examination

Accounts and Records – Information Systems Controls (Page 6): 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.

Previous Report of Examination

Accounts and Records - Information Systems Controls (Page 7): It was recommended that the Company evaluate the recommendations from the Information Systems review and make appropriate changes to strengthen its information system controls. The

Company has implemented changes to strengthen some of its controls over information systems.

Accounts and Records – Federal Income Taxes (Page 7): It was recommended that the Company identify and measure temporary differences using a balance sheet approach in compliance with Statement of Statutory Accounting Principles No. 10, paragraph 6.a. The Company has complied with this recommendation.

ACKNOWLEDGEMENT

Acknowledgement 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
Contract Examiner
Department of Insurance
State of California