

REPORT OF EXAMINATION
OF THE
WAWANESA GENERAL INSURANCE COMPANY
AS OF
DECEMBER 31, 2011

Filed August 24, 2012

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Los Angeles, California
July 13, 2012

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

Dear Commissioner:

Pursuant to your instructions, an examination was made of the

WAWANESA GENERAL INSURANCE COMPANY

(hereinafter also referred to as the Company) at its home office located at 9050 Friars Road, San Diego, California 92108.

SCOPE OF EXAMINATION

We have performed a multi-state examination of the Company. 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, 2011. The examination was conducted in accordance with the National Association of Insurance Commissioners' Financial Condition Examiners' Handbook (Handbook). The Handbook requires the planning and performance of the examination to evaluate the Company's financial condition, 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: corporate records; fidelity bonds and other insurance; pensions, stock ownership and insurance plans; growth of company; accounts and records; and sales and advertising.

COMPANY HISTORY

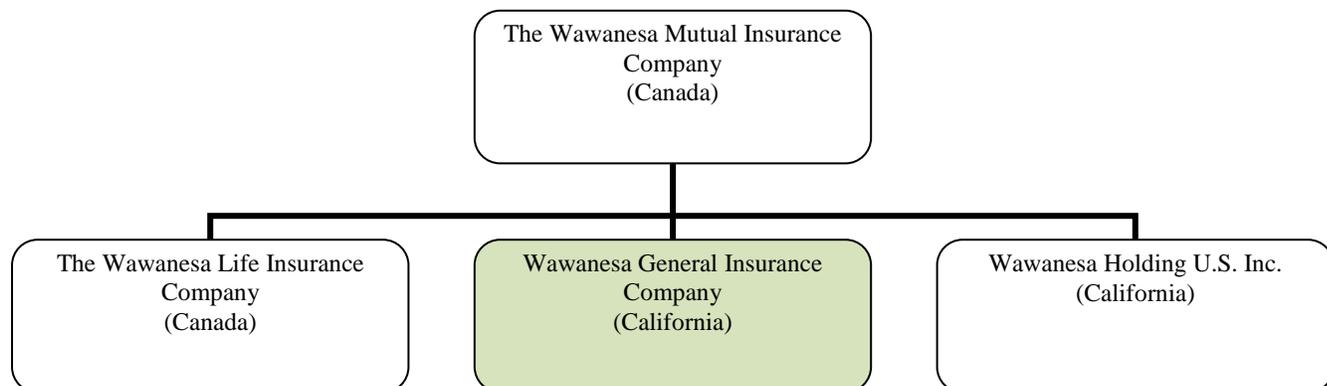
Effective July 1, 2011, the California Department of Insurance approved the withdrawal of the Company's parent, The Wawanesa Mutual Insurance Company (WMIC), United States of America Branch (U.S. Branch), as an admitted California insurer. The WMIC U.S. Branch operation was consolidated into the Company. As part of the consolidation, WMIC entered into an Assumption Reinsurance Agreement with the Company, whereby WMIC U.S. Branch ceded its outstanding liabilities and policy obligations.

Further, WMIC U.S. Branch transferred approximately \$52.7 million in securities and other assets to the Company to match the outstanding liabilities, plus an additional capital contribution of approximately \$102.7 million, for a total amount of approximately \$155.4 million. Of the total outstanding liabilities, \$23.3 million and \$18.1 million represented the unearned premium, and loss and loss adjustment expense reserves, respectively, carried for the policies transferred. As a ceding commission, the Company paid \$2.5 million to WMIC in consideration for the assumed business of the WMIC U.S. Branch (i.e., related to in-force policies and renewal rights).

During 2008 and 2011, the Company received respectively from its parent, WMIC, capital contributions of \$10 million cash and \$102.7 million consisting primarily of securities.

MANAGEMENT AND CONTROL

The Company is wholly-owned by The Wawanesa Mutual Insurance Company. The following is an organization chart depicting the relationship of the Company within the holding company system:



All ownership is 100%.

Management of the Company is vested in a ten-member board of directors elected annually. A listing of the members of the board and principal officers serving at December 31, 2011 follows:

Directors

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Richard Ramsay Bracken Manitoba, Canada	Chairman and Director Royal Canadian Securities Limited
Elizabeth Jane Beale Nova Scotia, Canada	President and Chief Executive Officer Atlantic Provinces Economic Council
Delmore Clair Crewson Manitoba, Canada	Retired
Gregory Joseph Hanson Manitoba, Canada	Retired
Robert Orville Landry Ontario, Canada	Retired
Kenneth Leslie Matchett Manitoba, Canada	Retired
John Stuart McCallum Manitoba, Canada	Professor, University of Manitoba
Kenneth Ernest McCrea Manitoba, Canada	President and Chief Executive Officer The Wawanesa Group of Companies

Directors - Continued

Margot Elizabeth Northey
Ontario, Canada

Retired

David Gerhard Unruh
British Columbia, Canada

Retired

Principal Officers

<u>Name</u>	<u>Title</u>
Kenneth Ernest McCrea	President and Chief Executive Officer
George Nicholas Bass	Vice President, General Counsel, and Secretary
David Gerald Fitzgibbons	Vice President U.S. Operations
Brett Alexander MacKinnon	Vice President and Chief Actuary
Gary John Timlick	Vice President and Treasurer
William Gin Saung	Chief Financial Officer

Management Agreements

Affiliated Management Agreement: The Company is party to a management agreement dated July 11, 1996 with its parent, The Wawanesa Mutual Insurance Company (WMIC). Under the terms of the agreements, WMIC provides the following services to the Company: management, office space, information systems, data processing services, telecommunications, administration, financial services, accounting services, investment services, accounting and financial reports, actuarial services, human resources services, legal services, marketing and solicitation of potential insureds, investigation of the applicants, policy forms, underwriting, rating and claims services. WMIC is reimbursed for some expenses on actual cost basis, while certain expenses are paid on a mutually agreed upon allocation basis. For 2008, 2009, 2010, and 2011 the Company paid \$37,824,629, \$39,692,040, \$41,739,239, and \$2,776,936, respectively, in fees to WMIC under the terms of this agreement. The California Department of Insurance (CDI) approved this agreement on July 25, 1996. This agreement has been subsequently replaced by the Services and Cost Allocation Agreement dated June 30, 2011.

Services and Cost Allocation Agreement: The Company is party to services and cost allocation agreement, effective June 30, 2011, with its parent, WMIC. This agreement replaces the Management Agreement dated July 11, 1996. WMIC provides the following services to the Company: actuarial and related services, information technology, computer and communication services, and additional services. WMIC is reimbursed based on the actual cost paid and accrued based on appropriate time studies, activity count expense sharing, or other appropriate methods of allocation. For 2011, the Company paid \$2,361,223 in fees to WMIC under the terms of this agreement. The CDI approved this agreement on June 30, 2011.

Office Lease Agreement: The Company is party to an office lease agreement, effective July 1, 2011 with its affiliate, Wawanesa Holdings U.S. Inc. (Wawanesa Holdings). Rent is calculated at \$1.74 per rentable square foot. For 2011, the Company paid \$872,643 in rent to Wawanesa Holdings under the terms of the lease agreement. The CDI approved this agreement on June 30, 2011.

Capital Maintenance Agreement: The Company is party to a capital maintenance agreement effective January 1, 2007 with its parent, WMIC. Under the terms of the agreement, WMIC agrees to contribute additional capital to the Company, if at any time the Company's total capital as shown on any regulatory quarterly or annual statement is less than 50% of the Company's net premiums written. Additional contributions are limited to a maximum of \$50 million within any 12-month period. Additional capital shall be received by the Company within sixty days of the Company's quarterly or annual statutory reporting deadline.

TERRITORY AND PLAN OF OPERATION

As of December 31, 2011, the Company was licensed to transact multiple lines of property and casualty insurance in the states of California and Oregon. The Company is a direct writer of private passenger auto liability and physical damage coverage, insuring preferred risks. The Company also offers preferred homeowners and condominium insurance, including earthquake coverage. All policies are issued for a 12-month term.

In 2011, direct premiums written were \$292.5 million of which 98% was written in California. The lines of business written in California were private passenger auto liability (51.3%), auto physical damage (40.2%), homeowners multiple peril (7.5%), and the remainder in fire, earthquake, and allied lines.

LOSS EXPERIENCE

The Company reported operating losses in all year under examination as follows:

Year	Net Operating (Loss)	Net Income or (Loss)
2008	\$ (18,543,444)	\$ (3,306,306)
2009	(11,613,989)	1,643,737
2010	(18,448,535)	(887,066)
2011	(21,603,637)	2,082,650

The Company has maintained its reported surplus position primarily through investment income. In 2008, the Company received a capital contribution from its parent, The Wawanesa Mutual Insurance Company (WMIC) in the amount of \$10 million in order to strengthen the Company's capital position.

In 2011, the Company received an additional \$102.7 million capital contribution from WMIC as part of a planned consolidation of the U.S. Branch operations.

REINSURANCE

Assumed

The Company does not assume any reinsurance.

Ceded

The Company is covered under its parent's reinsurance program including a catastrophe excess of loss contract, aggregate excess of loss contract and a casualty excess of loss contract. The

business covered under the parent's program includes personal, farm, commercial property and automobile physical damage. The following is a summary of the reinsurance program in-force as of December 31, 2011.

Layer	Reinsurance Limit
<u>Six Layer Catastrophe Excess of Loss</u>	
1 st Catastrophe Cover	100% of \$40 million excess of \$30 million
2 nd Catastrophe Cover	100% of \$30 million excess of \$70 million
3 rd Catastrophe Cover	100% of \$75 million excess of \$100 million
4 th Catastrophe Cover	100% of \$150 million excess of \$175 million
5 th Catastrophe Cover	100% of \$175 million excess of \$325 million
6 th Catastrophe Cover	100% of \$700 million excess of \$500 million
<u>Two Layer Aggregate Excess of Loss</u>	
First Aggregate	100% of \$25 million excess aggregate deductible of \$100 million
Second Aggregate	100% of \$50 million excess aggregate deductible of \$125 million
<u>Casualty Excess of Loss</u>	
First Excess	100% of \$15 million excess a deductible of \$5 million

Note: The above limits are in Canadian dollars.

The reinsurance program utilizes the services of Guy Carpenter & Company, Inc., as a reinsurance intermediary. The above program is primarily reinsured with Underwriters at Lloyd's of London.

FINANCIAL STATEMENTS

The financial statements prepared for this examination report include:

Statement of Financial Condition as of December 31, 2011

Underwriting and Investment Exhibit for the Year Ended December 31, 2011

Reconciliation of Surplus as Regards Policyholders from December 31, 2007
through December 31, 2011

Statement of Financial Condition
as of December 31, 2011

<u>Assets</u>	<u>Ledger and Nonledger Assets</u>	<u>Assets Not Admitted</u>	<u>Net Admitted Assets</u>	<u>Notes</u>
Bonds	\$ 441,076,244	\$	\$ 441,076,244	
Cash and short-term investments	15,791,341		15,791,341	
Aggregate write-in for invested assets	5,966		5,966	
Receivable for securities				
Investment income due and accrued	3,318,735		3,318,735	
Premiums and considerations:				
Premiums and agents' balances in course of collection	10,280,429	130,035	10,150,394	
Premiums, agents' balances and installments booked but deferred and not yet due	46,929,118		46,929,118	
Current federal and foreign income tax recoverable and interest thereon	1,115,331		1,115,331	
Net deferred tax asset	16,206,145	858,022	15,348,123	
Electronic data processing equipment and software	227,979		227,979	
Furniture and equipment, including health care delivery assets	424,139	424,139		
Aggregate write-ins for other than invested assets	<u>170,670</u>	<u>44,020</u>	<u>126,650</u>	
Total assets	<u>\$ 535,546,097</u>	<u>\$ 1,456,216</u>	<u>\$ 534,089,881</u>	
 <u>Liabilities, Surplus and Other Funds</u>				
Losses			\$ 106,918,496	(1)
Loss adjustment expenses			18,209,849	(1)
Other expenses			2,195,990	
Taxes, licenses and fees			183,673	
Unearned premiums			152,132,169	
Advance premiums			2,719,681	
Ceded reinsurance premiums payable			1,799,495	
Amounts withheld or retained by company for account of others			2,475,606	
Remittances and items not allocated			87	
Drafts outstanding			15,959,311	
Payable to parent, subsidiaries and affiliates			<u>3,527,095</u>	
Total liabilities			306,121,452	
Common capital stock		\$ 2,600,000		
Gross paid in and contributed surplus		218,106,778		
Unassigned funds (surplus)		<u>7,261,651</u>		
Surplus as regards policyholders			<u>227,968,429</u>	
Total liabilities, surplus and other funds			<u>\$ 534,089,881</u>	

Underwriting and Investment Exhibit
for the Year Ended December 31, 2011

Statement of Income

Underwriting Income

Premiums earned		\$ 287,640,827
Deductions:		
Losses and loss expenses incurred	\$ 278,024,625	
Other underwriting expenses incurred	<u>31,219,839</u>	
Total underwriting deductions		<u>309,244,464</u>
Net underwriting loss		(21,603,637)

Investment Income

Net investment income earned	\$ 14,563,940	
Net realized capital gain	<u>5,656,525</u>	
Net investment gain		20,220,465

Other Income

Net loss from agents' or premium balances charged off	\$ 274	
Finance and charges not included in premiums	<u>4,001,097</u>	
Total other income		<u>4,001,371</u>
Net income before federal income taxes		2,618,199
Federal income taxes incurred		<u>535,549</u>
Net income		<u>\$ 2,082,650</u>

Capital and Surplus Account

Surplus as regards policyholders, December 31, 2010		\$ 120,410,431
Net income	\$ 2,082,650	
Change in net unrealized capital loss	(46,890)	
Change in net deferred income tax	3,149,808	
Change in nonadmitted assets	(334,348)	
Surplus adjustments: Paid in	<u>102,706,778</u>	
Change in surplus as regards policyholders for the year		<u>107,557,998</u>
Surplus as regards policyholders, December 31, 2011		<u>\$ 227,968,429</u>

Reconciliation of Surplus as Regards Policyholders
from December 31, 2007 through December 31, 2011

Surplus as regards policyholders, December 31, 2007 per Examination			\$ 110,914,310
	<u>Gain in Surplus</u>	<u>Loss in Surplus</u>	
Net loss	\$	\$ 466,985	
Net unrealized capital loss		306,187	
Change in net deferred income tax	5,390,300		
Change in nonadmitted assets		1,047,787	
Change in provision for reinsurance	778,000		
Surplus adjustments: Paid-in	<u>112,706,778</u>	<u> </u>	
Total gains and losses	<u>\$ 118,875,078</u>	<u>\$ 1,820,959</u>	
Net increase in surplus as regards policyholders			<u>117,054,119</u>
Surplus as regards policyholders, December 31, 2011, per Examination			<u>\$ 227,968,429</u>

COMMENTS ON FINANCIAL STATEMENT ITEMS

(1) Losses and Loss Adjustment Expenses

Based on an analysis by a Casualty Actuary from the California Department of Insurance, the Company's loss and loss adjustment expense reserves as of December 31, 2011 were found to be reasonably stated and have been accepted for purposes of this examination.

SUMMARY OF COMMENTS AND RECOMMENDATIONS

Current Report of Examination

None

Previous Report of Examination

Corporate Records (Page 4): It was recommended that the Company implement procedures to ensure compliance with California Insurance Code (CIC) Sections 1200 and 1201. The Company has complied with this recommendation

Taxes, Licenses and Fees (Page 11): It was recommended that the Company remit the amount due to California Department of Insurance and implement procedures to insure future compliance with CIC Section 1872.8(a). The Company has complied with these recommendations.

ACKNOWLEDGEMENT

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/_____
Cuauhtémoc Beltran, CFE
Examiner-In-Charge
Department of Insurance
State of California