

REPORT OF EXAMINATION
OF THE
SUTTER INSURANCE COMPANY
AS OF
DECEMBER 31, 2015

Filed on May 16, 2017

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San Francisco, California
April 20, 2017

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

Dear Commissioner:

Pursuant to your instructions, an examination was made of the

SUTTER INSURANCE COMPANY

(hereinafter also referred to as the Company) at its home office located at 1301 Redwood Way, Petaluma, California 94594.

SCOPE OF EXAMINATION

We have performed our multi-state examination of the Company. The previous examination of the Company was as of December 31, 2011. This examination covered the period from January 1, 2012 through December 31, 2015.

The examination was conducted in accordance with the National Association of Insurance Commissioners *Financial Condition Examiners Handbook (Handbook)*. The Handbook requires the planning and performance of the examination to evaluate the Company's financial condition, assess corporate governance, identify current and prospective risks, and evaluate system controls and procedures used to mitigate those risks. An examination also includes identifying and evaluating significant risks that could cause an insurer's surplus to be materially misstated both currently and prospectively.

All accounts and activities of the Company were considered in accordance with the risk-focused examination process. This may include assessing significant estimates made by management and evaluating management's compliance with Statutory Accounting Principles. The examination does not attest to the fair presentation of the financial statements included herein. If, during the course of the examination, an adjustment is identified, the impact of such adjustment will be documented separately following the Company's financial statements.

This examination report includes findings of fact and general information about the Company and its financial condition. There may be other items identified during the examination that, due to their nature (e.g., subjective conclusions, proprietary information, etc.), were not included within the examination report, but separately communicated to other regulators and/or the Company.

COMPANY HISTORY

Sutter Insurance Company (the Company) was incorporated on June 28, 1974 under the laws of California, and commenced business on January 25, 1975. The Company is a wholly owned subsidiary of Dibill, Inc., which is owned and controlled by the Kleinecke family.

Capitalization

The Company is authorized to issue 1,000,000 shares of a single class of common stock with a par value of \$50 per share. As of December 31, 2015, there were 60,000 shares issued and outstanding.

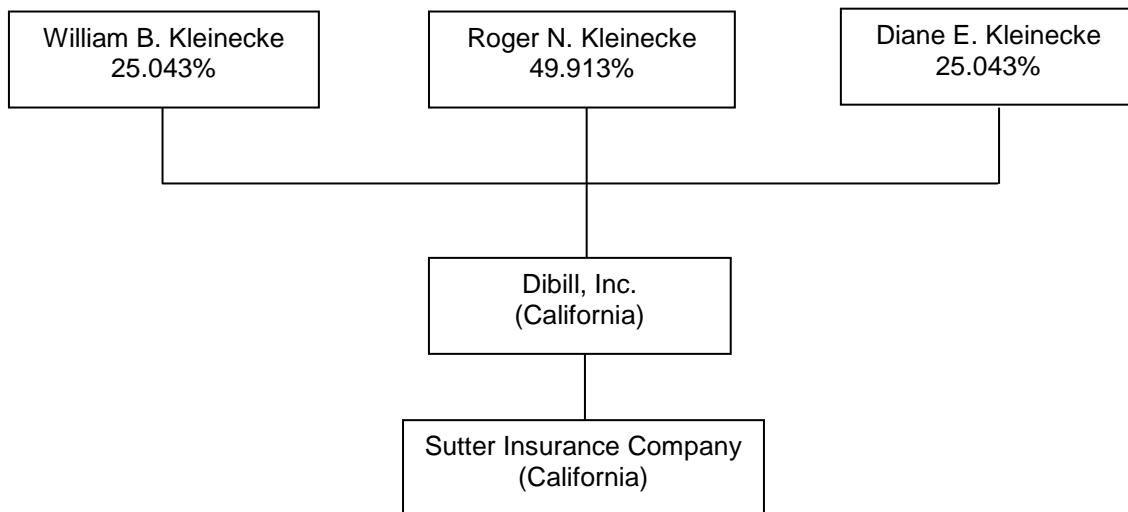
Dividends

The Company paid ordinary cash dividends of \$250,000 in 2012 and \$900,000 in 2015 to its immediate parent, Dibill, Inc.

MANAGEMENT AND CONTROL

The Company is a wholly owned subsidiary of Dibill, Inc., which is owned and controlled by members of the Kleinecke family as follows: Roger N. Kleinecke (49.913%), William B. Kleinecke (25.043%), and Diane E. Kleinecke (25.043%). The ultimate controlling person is Roger N. Kleinecke.

The following organizational chart depicts the Company's relationship within the holding company system at December 31, 2015. All ownership is 100% unless otherwise stated:



The Company is managed by a three-member board of directors, who are elected annually. Following are members of the board and principal officers of the Company serving at December 31, 2015:

Directors

<u>Name and Location</u>	<u>Principal Business Affiliation</u>
William B. Kleinecke Novato, California	President Sutter Insurance Company
Diane E. Kleinecke Santa Rosa, California	Secretary and Treasurer Sutter Insurance Company
Roger N. Kleinecke ^(a) Santa Rosa, California	Retired

Principal Officers

<u>Name</u>	<u>Title</u>
William B. Kleinecke	President
Diane E. Kleinecke	Secretary and Treasurer
George W. Lindh	Vice President of Claims

^(a) Roger N. Kleinecke relinquished his position as a member of the Board of Directors on December 31, 2015 and William Allan Kleinecke was elected to fill the position effective January 1, 2016.

Management Agreement

Tax Sharing Agreement: The Company and its immediate parent, Dibill, Inc. entered into an amended federal income tax sharing agreement dated August 26, 2013. This amended tax sharing agreement supersedes the tax sharing agreement dated January 5, 1999 to eliminate all reference to Anza Insurance Company, a 100% owned insurance subsidiary, which was sold in 2000. This agreement provides for allocation of year-end consolidated tax liability between the participants to the agreement. The year-end tax liability is computed on a consolidated basis; however, each participant's tax provision is calculated individually. This amendment was submitted to and approved by the California Department of Insurance (CDI) on October 22, 2013, pursuant to California Insurance Code Section 1215.5(b)(4).

TERRITORY AND PLAN OF OPERATION

The Company is licensed to transact property and casualty insurance in the states of California, Nevada, Oregon, and Washington. All operations are conducted out of its home office in Petaluma, California.

Direct premiums written in 2015 totaled \$15.9 million, and were written in California (89.9%), Washington (7.3%), Oregon (2.3%), and Nevada (0.5%). The Company's primary lines of business written in 2015 were commercial auto physical damage (45.5%) and commercial auto liability (34.7%). The remaining 19.8% of premiums written was comprised of fire, allied lines, homeowners multiple peril, inland marine, earthquake, other liability – occurrence, and warranty. Business was produced through approximately 28 general agents.

REINSURANCE

Assumed

The Company assumes minor amounts of reinsurance through mandatory insurance pools in California. As of the examination date, total reinsurance premiums assumed was \$52,000.

Ceded

The following is a summary of principal reinsurance agreements in-force as of December 31, 2015 (all reinsurers are authorized):

Line of Business and Type of Contract	Reinsurer's Name	Company's Retention	Reinsurer's Limit
<u>Property and Casualty:</u>			
Part 1A:			
Property Excess of Loss	QBE Reinsurance Corporation (50%) SCOR Reinsurance Company (50%)	\$300,000 per risk	\$800,000 excess of \$300,000 per risk, subject to a limit of \$1.6 million per occurrence
Part 1B:			
Casualty Excess of Loss	QBE Reinsurance Corporation (50%) SCOR Reinsurance Company (50%)	\$300,000 per occurrence	\$800,000 excess of \$300,000 per occurrence
Part II:			
Property Catastrophe	SCOR Reinsurance Company (100%)	\$500,000 per occurrence	\$1 million excess of \$500,000 per occurrence, subject to a term limit of \$2 million
Part III:			
Casualty Clash	QBE Reinsurance Corporation (60%) Swiss Re American Corp (40%)	\$1.1 million per occurrence	\$1 million excess of \$1.1 million per occurrence, subject to a term limit of \$2 million

ACCOUNTS AND RECORDS

Vehicle Fraud Assessment

California Insurance Code (CIC) Section 1872.8(a) requires each insurer doing business in California to pay an annual vehicle fraud assessment fee for each vehicle insured under an insurance policy issued in California. During the course of the examination, it was noted that the Company's vehicle counts were incorrect due to late

reporting by the general agents. This is not in compliance with California Code of Regulations (CCR), Title 10, Chapter 5, Subchapter 9, Article 4, Section 2698.62(b) which states that the vehicle fraud assessment shall be due on each vehicle, identified by its vehicle identification number for each quarter that a policy is in force on such vehicle and when a vehicle is added to or replaced one under an existing policy.

In addition, it was observed that some vehicles reported under policies produced by a general agent were counted twice in the vehicle fraud assessment reports. Furthermore, the vehicle counts also included vehicles insured under policies issued outside of California. It is recommended that the Company develop a methodology to ensure accurate counting of vehicles subject to the California Vehicle Fraud Assessment in accordance with CIC Section 1872.8(a) and CCR Title 10, Chapter 5, Subchapter 9, Article 4, Section 2698.62(b).

FINANCIAL STATEMENTS

The following financial statements are based on the statutory financial statements filed by the Company with the California Department of Insurance and present the financial condition of the Company for the period ending December 31, 2015. The accompanying comments to the amounts reported in the annual statements should be considered an integral part of the financial statements. There were no examination adjustments made to surplus as a result of the examination.

Statement of Financial Condition as of December 31, 2015

Underwriting and Investment Exhibit for the Year Ended December 31, 2015

Reconciliation of Surplus as Regards Policyholders from December 31, 2011 through December 31, 2015

Statement of Financial Condition
as of December 31, 2015

<u>Assets</u>	<u>Ledger and Nonledger Assets</u>	<u>Assets Not Admitted</u>	<u>Net Admitted Assets</u>	<u>Notes</u>
Bonds	\$ 34,620,077	\$	\$ 34,620,077	
Cash and short-term investments	770,337		770,337	
Investment income due and accrued	224,483		224,483	
Premiums and agents' balances in course of collection	985,773	16,477	969,296	
Premiums, agents' balances and installments booked but deferred and not yet due	925,639		925,639	
Amount recoverable from reinsurers	1,571		1,571	
Other amounts receivable from reinsurance contracts	76,770		76,770	
Current federal and foreign income tax recoverable and interest thereon	416,873		416,873	
Net deferred tax asset	1,920,752	361,595	1,559,157	
Receivables from parent, subsidiaries and affiliates	15,500		15,500	
Aggregate write-ins for other than invested assets	<u>266,689</u>		<u>266,689</u>	
 Total assets	 <u>\$ 40,224,464</u>	 <u>\$378,072</u>	 <u>\$ 39,846,392</u>	
 <u>Liabilities, Surplus and Other Funds</u>				
Losses			\$ 7,789,763	(1)
Loss adjustment expenses			1,009,822	(1)
Other expenses			170,482	
Unearned premiums			10,399,715	
Drafts Outstanding			<u>46,615</u>	
 Total liabilities			 19,416,397	
Common capital stock	\$ 3,000,000			
Gross paid-in and contributed surplus	2,800,000			
Unassigned funds (surplus)	<u>14,629,996</u>			
 Surplus as regards policyholders			 <u>20,429,996</u>	
 Total liabilities, surplus and other funds			 <u>\$ 39,846,393</u>	

Underwriting and Investment Exhibit
for the Year Ended December 31, 2015

Statement of Income

Underwriting Income

Premiums earned		\$ 19,883,137
Deductions:		
Losses incurred	\$ 13,351,094	
Loss adjustment expenses incurred	1,810,200	
Other underwriting expenses incurred	<u>5,358,989</u>	
Total underwriting deductions		<u>20,520,283</u>
Net underwriting loss		(637,146)

Investment Income

Net investment income earned	\$ 794,297	
Net realized capital gain	<u>3,138</u>	
Net investment gain		797,435

Other Income

Finance and Service charges not included in premiums	\$ <u>201,518</u>	
Total other income		<u>201,518</u>
Net income after dividends to policyholders, after capital gains tax and before federal and foreign income taxes		<u>361,807</u>
Net income		<u>\$ 361,807</u>

Capital and Surplus Account

Surplus as regards policyholders, December 31, 2014		\$ 21,321,749
Net income	\$ 361,807	
Change in net deferred income tax	(207,527)	
Change in nonadmitted assets	(146,034)	
Dividends to stockholders	<u>(900,000)</u>	
Change in surplus as regards policyholders for the year		<u>(891,754)</u>
Surplus as regards policyholders, December 31, 2015		<u>\$ 20,429,995</u>

Reconciliation of Surplus as Regards Policyholders
from December 31, 2011 through December 31, 2015

Surplus as regards policyholders, December 31, 2011			\$ 21,650,711
	<u>Gain in Surplus</u>	<u>Loss in Surplus</u>	
Net loss	\$	\$	453,072
Change in net deferred income tax	206,349		
Change in nonadmitted assets	176,007		
Dividends to stockholders	<u> </u>	<u>1,150,000</u>	
Total gains and losses	<u>\$ 382,356</u>	<u>\$ 1,603,072</u>	
Net decrease in surplus as regards policyholders			<u>(1,220,716)</u>
Surplus as regards policyholders, December 31, 2015			<u>\$ 20,429,995</u>

COMMENTS ON FINANCIAL STATEMENT ITEMS

(1) Losses and Loss Adjustment Expenses

A Casualty Actuary from the California Department of Insurance reviewed the Actuarial Report as of December 31, 2015 prepared by the Company's independent actuary and concurred with the independent actuary's conclusion that the Company's loss and loss adjustment expense reserves as of December 31, 2015 are reasonable and have been accepted for purposes of this examination.

SUBSEQUENT EVENTS

The Company paid ordinary cash dividends of \$450,000 to its immediate parent, Dibill, Inc., in 2016.

SUMMARY OF COMMENTS AND RECOMMENDATIONS

Current Report of Examination

Accounts and Records – Vehicle Fraud Assessment (Page 6): It is recommended that the Company develop a methodology to ensure accurate counting of vehicles subject to the California Vehicle Fraud Assessment in accordance with California Insurance Code (CIC) Section 1872.8(a) and California Code of Regulations (CCR), Title 10, Chapter 5, Subchapter 9, Article 4, Section 2698.62(b).

Previous Report of Examination

Management and Control – Intercompany Agreements – (Page 3): It was recommended that the Company amend its tax sharing agreement to remove Anza Insurance Company as a party and file the agreement with the California Department of Insurance

pursuant to California Insurance Code Section 1215.5(b)(4). The Company has complied with this recommendation.

Accounts and Records – Managing General Agent Act (Page 6): It was recommended that the Company ensure that the onsite reviews it performs on its managing general agents (MGA) include a review of the MGA's underwriting and claims practices in accordance with CIC Section 769.84(c). The Company has complied with this recommendation.

Comments on Financial Statement items – Taxes, Licenses and Fees (Page 10): It was recommended the Company implement procedures to ensure its vehicle count is accurate and comply with CIC Section 1872.8(a). The Company has not complied with this recommendation.

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/ _____

Sam Chiu, CFE
Examiner-In-Charge
Associate Insurance Examiner
Department of Insurance
State of California

/S/ _____

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