

REPORT OF EXAMINATION  
OF THE  
WESTERN MUTUAL INSURANCE COMPANY  
AS OF  
DECEMBER 31, 2018

Filed on April 23, 2020

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Los Angeles, California  
April 10, 2020

Honorable Ricardo Lara  
Insurance Commissioner  
California Department of Insurance  
Sacramento, California

Dear Commissioner:

Pursuant to your instructions, an examination was made of the

### WESTERN MUTUAL INSURANCE COMPANY

(hereinafter also referred to as the Company) at its home office located at 2172 Dupont Drive, Irvine, California 95612.

#### SCOPE OF EXAMINATION

We have performed our multi-state examination of the Company. The previous examination of the Company was as of December 31, 2014. This examination covered the period from January 1, 2015 through December 31, 2018.

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 might 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.

This was a coordinated examination with California as the lead state of the Western Mutual Insurance Group. It was conducted concurrently with other insurance entities in the holding company group, including Residence Mutual Insurance Company and Arizona Home Insurance Company. Arizona participated on the examination.

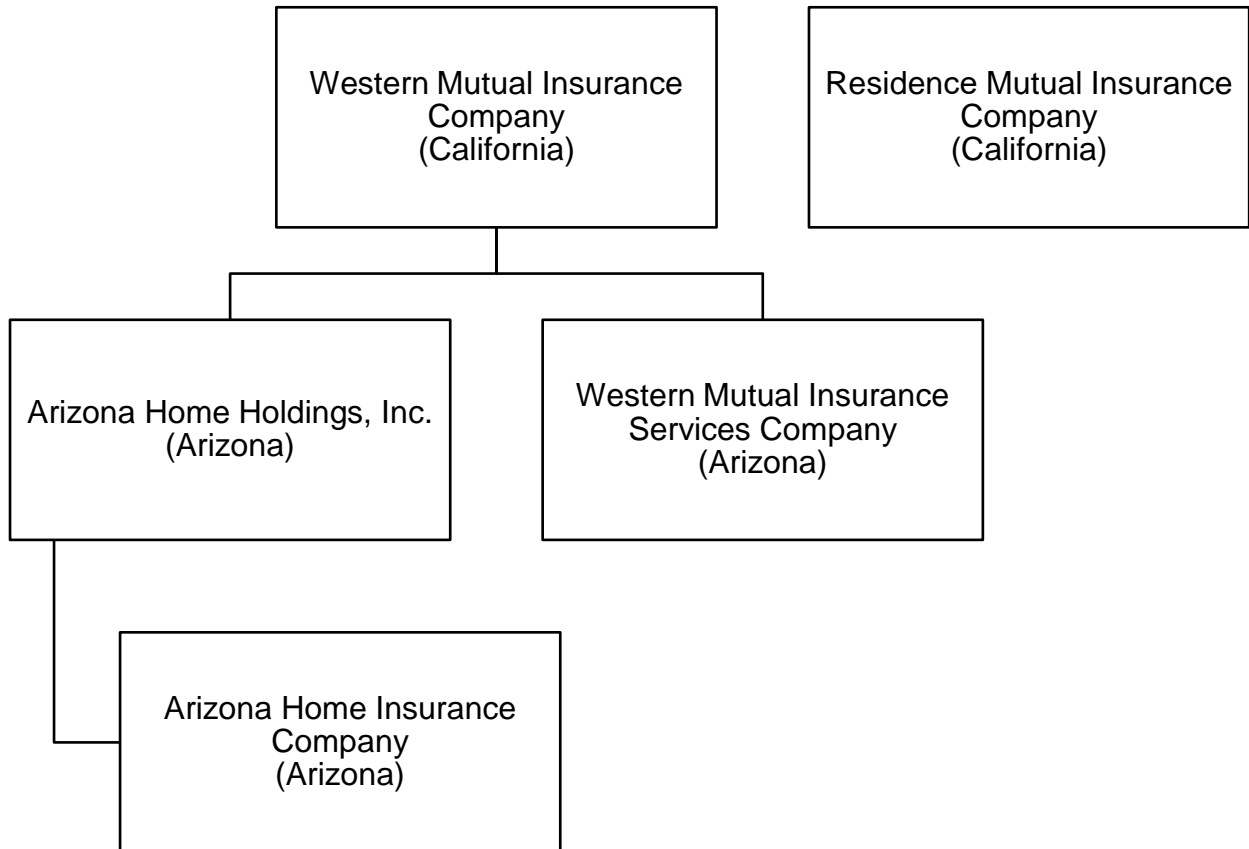
### COMPANY HISTORY

Western Mutual Insurance Group consists of three property and casualty insurance companies: The Company, Residence Mutual Insurance Company (RMIC), and Arizona Home Insurance Company (AHIC), which is 100% owned by Arizona Home Holdings, Inc. (AHH). The Company was incorporated in California on March 7, 1942 and commenced business on April 30, 1942.

The Company is a mutual insurance company and has no shareholders. On April 6, 2016, The Company acquired RMIC's 50% ownership of the Arizona Home Holdings, Inc. On October 26, 2018, the Company acquired the RMIC's 50% ownership of Western Mutual Insurance Services.

MANAGEMENT AND CONTROL

The following organizational chart depicts the Company's relationship with its affiliates as of December 31, 2018 (All ownership is 100%):



The six 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, 2018:

Directors

<u>Name and Location</u>	<u>Principal Business Affiliation</u>
James D. Anderson Newport Beach, California	Certified Public Accountant James D. Anderson, CPA
Michael D. Antonovich Glendale, California	Retired
John J. Barcal La Habra Heights, California	Attorney John J. Barcal, Inc.
Joe Crail Newport Coast, California	Chairman of the Board and President Western Mutual Insurance Group
Lucile Ann Crail Silverton, Oregon	Private Investor
Paul P. Rubincam <sup>(a)</sup> Palos Verdes Estates, California	Retired

Principal Officers

<u>Name</u>	<u>Title</u>
Joe Crail	President
Paul E. Calvet	Executive Vice President
Carmen Estrada	Secretary
Michael G. Hardy	Chief Financial Officer

<sup>(a)</sup> Kelly Ann Walker replaced Paul Rubincam as a director, effective on February 15, 2019.

## Management Agreements

Agency Agreement: Effective August 1, 1981, the Company and Residence Mutual Insurance Company (RMIC) entered into an Agency Agreement with Cardinal Insurance Agency (Cardinal). Under the terms of the agreement, Cardinal provides insurance agency services for the Company and RMIC, which includes soliciting, selling, and servicing insurance products. The Company pays a commission to Cardinal based on a commission rate that ranges from 5% to 25%. From 2015 to 2018, the Company paid Cardinal \$47,957, \$26,210, \$47,094, and \$51,882, respectively, for the services provided under the agreement.

Agency Agreement: Effective October 6, 1994, the Company and RMIC entered into an Agency Agreement with Western Mutual Insurance Services Company (WMISC), formerly known as Inland Southern Insurance Services, Inc. The Company did not amend the agreement to reflect the name change to WMISC. Under the terms of this agreement, WMISC provides insurance agency services for the Company and RMIC, which includes soliciting, selling, and servicing insurance products. The Company pays a commission to WMISC based on a commission rate that ranges from 5% to 22.5%. From 2015 to 2018, the Company paid WMISC \$94,018, \$89,056, \$83,428, and \$26,518, respectively, for services provided under this agreement. It is recommended that the Company amend the agreement to reflect the name change to WMISC.

Service Agreement: Effective January 1, 2006, the Company, RMIC, and Arizona Home Insurance Company (AHIC) entered into the Service Agreement (Agreement) whereby the participants cooperate in the performance of certain administrative and special services and share in the use of the day to day operations of certain property, equipment, and facilities. The California Department of Insurance approved this Agreement on February 8, 2008.

The shared functions provided by the participants include the following: accounting and auditing, premium collection, underwriting, claims, actuarial, data processing, legal, and payroll. Costs of the services are allocated at cost in accordance with the pooling

percentages; 35% to the Company, 53% to RMIC, and 12% to AHIC. The Agreement requires that the charges be settled within 45 days after each quarter. From 2015 through 2018, the Company's allocated shared costs were \$9.4 million, \$9.6 million, \$10.1 million, and \$10.5 million, respectively, under the terms of this Agreement.

## TERRITORY AND PLAN OF OPERATION

As of December 31, 2018, the Company was licensed to transact multiple lines of property and casualty insurance in the following seven states: Arizona, California, Colorado, Nevada, New Mexico, Texas, and Utah.

In 2018, the Company wrote \$18,183,937 of direct premiums of which \$9,207,475 (50.6%) was written in Texas, \$4,908,893 (27.0%) was written in Nevada, \$2,482,487 million (13.7%) was written in California, \$810,130 (4.5%) was written in New Mexico, \$592,596 (3.3%) was written in Colorado and \$182,356 (0.9%) was written in Utah. The lines of business written were homeowners multiple peril (98.2%), earthquake (1.1%), fire (0.4%), and allied lines (0.3%).

Policies are issued exclusively on residential properties. Business is produced on a direct basis as well as through agencies and brokers.

## REINSURANCE

### Intercompany Reinsurance Agreement

Intercompany Quota Share Pooling Agreement: Effective January 1, 2006, the Company, Residence Mutual Insurance Company (RMIC), and Arizona Home Insurance Company (AHIC) participate in the Intercompany Quota Share Pooling Agreement, whereby all business written by the pool participants is pooled and all premium, losses and expenses are reapportioned among the participants. Pool participation percentages are 53% for RMIC, 35% for the Company, and 12% for AHIC.



## Assumed Reinsurance

The Company does not assume any business except from the Intercompany Quota Share Pooling Agreement.

## Ceded Reinsurance

The following is a summary of the principal ceded reinsurance treaties as of December 31, 2018. All participating reinsurers are authorized.

<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>Property and Casualty</u></b>			
<b><u>Excess of Loss</u></b>			
First Layer	Transatlantic Reinsurance Company	\$ .4 million	\$ .6 million in excess of \$ .4 million of each and every loss occurrence with a maximum of \$1.8 million per loss occurrence
Second Layer	Transatlantic Reinsurance Company	\$1 million	\$2 million in excess of \$1 million of first layer of each and every loss occurrence with a maximum of \$6 million per occurrence
<b><u>Catastrophe:</u></b>			
First Layer	31.2% Various Lloyd's Syndicate 20.0% R+V Versicherung AG 8.0% American Agricultural Insurance Company 40.8% Various other reinsurers	\$2.5 million	\$5 million excess of \$2.5 million of each and every loss occurrence. Annual deductible \$2.5 million with a maximum of \$10 million for all loss occurrences during the term of the contract.

<b>Line of Business and Type of Contract</b>	<b>Reinsurer's Name</b>	<b>Company's Retention</b>	<b>Reinsurer's Limit</b>
Second Layer	26.0% Various Lloyd's Syndicate 20.0% R+V Versicherung AG 8.0% American Agricultural Insurance Company 46.0% Various other reinsurers	\$7.5 million	\$12.5 million in excess of \$7.5 million of each and every loss occurrence with a maximum of \$25 million for all loss occurrences during the term of the contract.
Third Layer	25.3% Various Lloyd's Syndicate 20.0% R+V Versicherung AG 8.0% American Agricultural Insurance Company 8.0% Mapfre Re, Compania De Reasegueros S.A. 38.7% Various other insurers	\$20 million	\$35 million in excess of 20 million of each and every loss occurrence with a maximum of \$70 million for all loss occurrences during the term of the contract.

As of the examination date, and under the terms of its external reinsurance agreements, the Company reported total net reinsurance recoverables of \$185 thousand.

### 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, 2018. The accompanying comments to the amounts reported in the annual statements should be considered an integral part of the financial statements. There were no adjustments made to the financial statements as a result of the examination.

Statement of Financial Condition as of December 31, 2018

Underwriting and Investment Exhibit for the Year Ended December 31, 2018

Reconciliation of Surplus as Regards Policyholders from December 31, 2014 through December 31, 2018

Statement of Financial Condition  
as of December 31, 2018

<u>Assets</u>	<u>Ledger and Nonledger Assets</u>	<u>Assets Not Admitted</u>	<u>Net Admitted Assets</u>	<u>Notes</u>
Bonds	\$ 55,102,041	\$	\$ 55,102,041	
Common stocks	29,929,193		29,929,193	
Real estate properties occupied by the company	2,159,634		2,159,634	
Cash and short-term investments	2,835,192		2,835,192	
Investment income due and accrued	228,116		228,116	
Premiums and agents' balances in course of collection	899,267	3,294	895,973	
Reinsurance amounts recoverable from reinsurers	2,309,448		2,309,448	
Current federal and foreign income tax recoverable and interest there on	77,215		77,215	
Electronic data processing equipment and software	260,368	260,368		
Furniture and equipment	62,162	62,162		
Receivable from parent, subsidiaries and affiliates	1,472,968		1,472,968	
Aggregate write-ins for other than invested assets	<u>506,072</u>	<u>491,494</u>	<u>14,578</u>	
Total assets	<u>\$ 95,841,676</u>	<u>\$ 817,318</u>	<u>\$ 95,024,358</u>	

Liabilities, Surplus and Other Funds

	<u>Current Year</u>	<u>Notes</u>
Losses and loss adjustment expenses	\$ 8,463,532	(1)
Reinsurance payable on paid loss and loss adjustment expenses	2,161,827	
Commissions payable, contingent commissions and other similar charges	253,893	
Other expenses	964,447	
Taxes, licenses and fees	123,494	
Net deferred tax liability	406,000	
Unearned premiums	14,856,630	
Advance premiums	518,804	
Ceded reinsurance premiums payable	75,483	
Funds held by company under reinsurance treaties	600,000	
Aggregate write-ins for liabilities	<u>63,529</u>	
Total liabilities	28,487,639	
Unassigned funds (surplus)	<u>66,536,719</u>	
Total liabilities, Surplus, and other funds	<u>\$ 95,024,358</u>	

Underwriting and Investment Exhibit  
for the Year Ended December 31, 2018

State of Income

	<u>Underwriting Income</u>	<u>Current Year</u>
Premium earned		\$ 27,273,069
Deductions:		
Losses and loss expenses incurred		\$ 18,995,414
Other underwriting expenses incurred		<u>6,345,536</u>
Total underwriting deductions		<u>25,340,950</u>
Net underwriting gain		1,932,119
	<u>Investment Income</u>	
Net investment income earned		\$ 820,026
Net realized capital gain		<u>38,918</u>
Net investment gain		858,944
	<u>Other Income</u>	
Finance and service charges not included in premiums		<u>\$ 23,671</u>
Total other income		<u>23,371</u>
Net income after dividends to policyholders, after capital gains tax and before federal and foreign income taxes		2,814,734
Dividends to policyholders		<u>599,839</u>
Net income		<u>\$ 2,114,895</u>

Capital and Surplus Account

Surplus as regards policyholders, December 31, 2017		\$ 62,530,376
Net income	\$ 2,214,895	
Change in net unrealized capital gains less capital gains tax	1,335,737	
Change in net deferred income tax	350,000	
Change in nonadmitted assets	<u>105,711</u>	
Change in surplus as regards policyholders for the year		<u>4,006,343</u>
Surplus as regards policyholders, December 31, 2018		<u>\$ 66,536,719</u>

Reconciliation of Surplus as Regards Policyholders  
from December 31, 2014 through December 31, 2018

Surplus as regards policyholders, December 31, 2014			\$ 50,255,873
	Gain in Surplus	Loss in Surplus	
Net income	\$ 8,443,549	\$	
Net unrealized capital gains	7,349,029		
Change in net deferred income tax	133,000		
Change in nonadmitted assets	<u>355,268</u>		
Total gains and losses	\$ 16,280,846	\$	
Net increase in surplus as regards policyholders			<u>16,280,846</u>
Surplus as regards policyholders, December 31, 2018			<u>\$ 66,356,719</u>

## COMMENTS ON FINANCIAL STATEMENT ITEMS

### (1) Losses and Loss Adjustment Expense

Based on an analysis by a Casualty Actuary for the California Department of Insurance, the Company's loss and loss adjustment expense reserves as of December 31, 2018, were found to be reasonably stated and have been accepted for purposes of this examination.

## SUMMARY OF COMMENTS AND RECOMMENDATIONS

### Current Report of Examination

Management and Control – Agency Agreement (Page 5): The Agency Agreement between the Company and Western Mutual Insurance Services Company (WMISC) still reflects WMISC's former name, Inland Southern Insurance Services, Inc. It is recommended that the Company amend the agreement to reflect the name change to WMISC.

### Previous Report of Examination

Accounts and Records – Information Systems Controls (Page 9): As a result of the review of the Company's information systems controls, recommendations for improving these controls were presented to the Company. The Company has implemented additional information system controls.

Accounts and Records – Related Party (Page 9): It was recommended that the Company comply with the Statements of Statutory Accounting Principles (SSAP) No. 25, paragraph 19 to disclose all related parties and relevant transactions. The Company acknowledged this recommendation and had included all related parties and transactions in its December 2015 Annual Statement, Schedule Y, Parts 1 and 2.

Accounts and Records – Reinsurance (Page 9): It was recommended that the Company comply with SSAP No. 63, paragraph 8, in regards to the recording and accounting of premiums, losses and expenses as a result of the Pooling Agreement. The Company acknowledged this recommendation and had reported in its December 31, 2015 Annual Statement gross of the Pooling Agreement.

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/\_\_\_\_\_

Thomas Podsiadlo, CFE  
Examiner-In-Charge  
Senior Insurance Examiner  
Department of Insurance  
State of California

/S/\_\_\_\_\_

Grace Asuncion, CFE  
Senior Insurance Examiner, Supervisor  
Department of Insurance  
State of California