

REPORT OF EXAMINATION
OF THE
CALIFORNIA CASUALTY COMPENSATION
INSURANCE COMPANY
AS OF
DECEMBER 31, 2017

FILED: MARCH 12, 2019

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San Francisco, California
January 28, 2019

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

Dear Commissioner:

Pursuant to your instructions, an examination was made of the

CALIFORNIA CASUALTY COMPENSATION INSURANCE COMPANY

(hereinafter referred to as the Company) at its home office located at 1875 South Grant Street, San Mateo, California 94402.

SCOPE OF EXAMINATION

We have performed our single state examination of the Company. The previous examination of the Company was made as of December 31, 2013. This examination covered the period from January 1, 2014 through December 31, 2017.

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. An examination also includes identifying and evaluating significant risks that could cause an insurer's surplus to be materially misstated, both currently and prospectively.

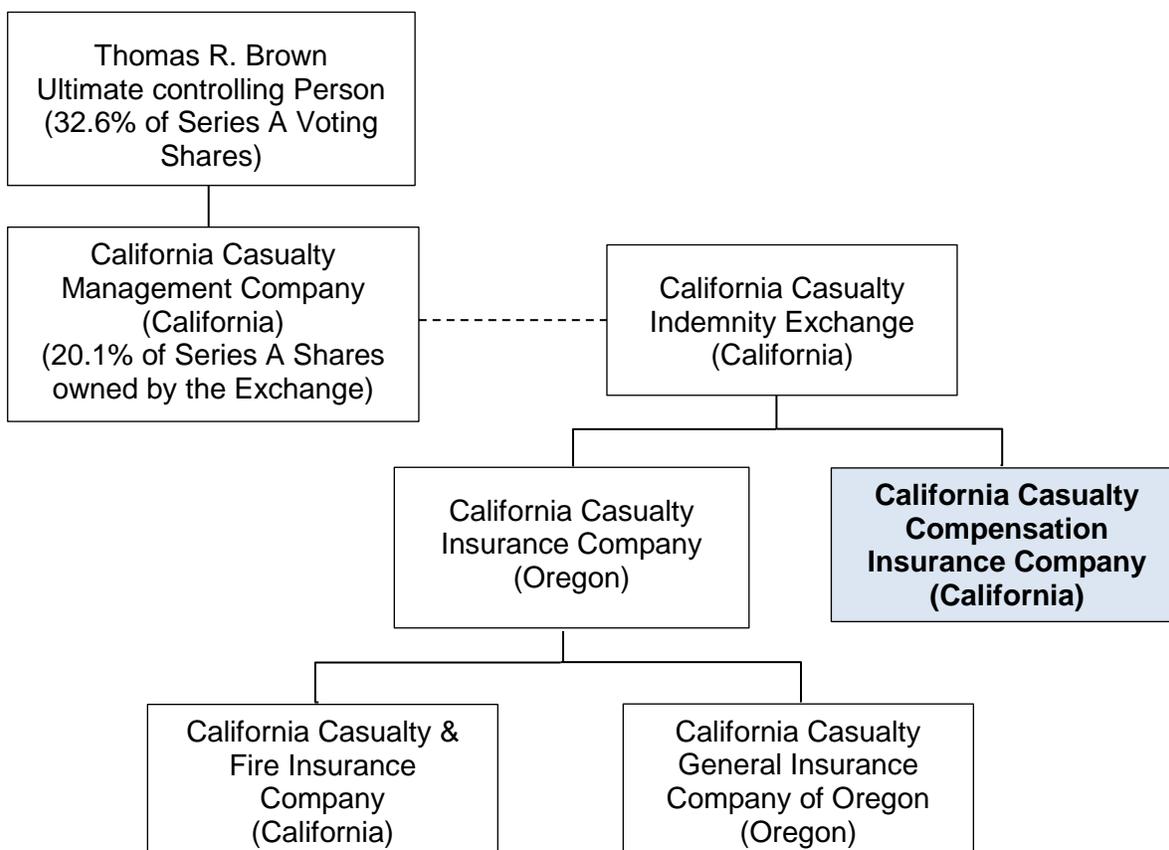
All accounts and activities of the Company were considered in accordance with the risk-focused examination process. This may include assessing significant estimates made by management and evaluating management's compliance with Statutory Accounting Principles. The examination does not attest to the fair 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.

This was a coordinated examination with California as the lead state of the California Casualty Group. The examination was conducted concurrently with the examinations of the Company's parent, California Casualty Indemnity Exchange, and its three affiliates: California Casualty Insurance Company (Oregon), California Casualty & Fire Insurance Company (California), and California Casualty General Insurance Company of Oregon (Oregon). The Oregon Department of Consumer and Business Services, Division of Financial Regulation participated in the examination.

MANAGEMENT AND CONTROL

The Company is a member of an insurance holding company system which is controlled by the California Casualty Management Company (CCMC) as the attorney-in-fact for California Casualty Indemnity Exchange (Exchange). As of December 31, 2017, Thomas Runnels Brown owned or controlled 32.6% of the Class A voting common stock of CCMC.



The fourteen members of the Board of Directors, who are elected annually, oversee the business and affairs of the Company. The following are members of the Board and principal officers of the Company serving at December 31, 2017:

Board of Directors

Name and Location

Principal Business Affiliation

Jonathan A. Brown ^(A)
Fair Oaks, California

Retired
Association of Independent Colleges and
Universities

Wayne S. Diviney
Clifton, Virginia

Retired
National Education Association

Carolyn E. Doggett ^(B)
Belmont, California

Retired
California Teachers Association

Board of Directors (continued)

<u>Name and Location</u>	<u>Principal Business Affiliation</u>
Jose A. Gomez San Marino, California	Educator, University Administrator California State University, Los Angeles
Jon H. Hamm El Dorado Hills, California	Labor Union Executive California Association of Highway Patrolmen
Mitchell E. Hornecker Portland, Oregon	Business Consultant Modoc Consulting
Barbara E. Kerr Riverside, California	Retired California Teachers Association
Leona S. Lindner Washington, D.C.	Chief Marketing Officer National Education Association's Member Benefits Corporation
Michael G. McPherson Silver Spring, Maryland	Chief Financial Officer National Education Association
Karen M. Padovese Fairfield, California	Chief Executive Officer GeoVera Holdings, Inc.
Edward G. Phoebus III Silver Spring, Maryland	President and Chief Executive Officer National Education Association Member Benefits Corporation
Heather S. Schafer Millersville, Maryland	Executive Director National Volunteer Fire Council
Thomas M. Tongue Portland, Oregon	Attorney Scheabe, Williamson, & Wyatt
Suzanne M. Zimmer ^(A) Golden, Colorado	Assistant Executive Director Colorado Education Association

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

- (A) Jonathan A. Brown and Suzanne M. Zimmer became emeritus members effective June 25, 2018, and October 12, 2018, respectively. The Company is in the process recruiting replacements.
- (B) Effective January 1, 2018, Karen B. Kyhn has been appointed as a member of the Advisory Board, replacing Carolyn E. Doggett.

Principal Officers

<u>Name</u>	<u>Title</u>
Carl B. Brown	President
Michael A. Ray	Chief Financial Officer
James R. Inglese	Secretary
Wayne S. Diviney	Chairman of the Board

Intercompany Agreements

Management Agreement: The Company is managed by California Casualty Management Company (CCMC) under a Management Agreement (Agreement), effective

January 1, 1994. Under the terms of the Agreement, CCMC has the power to conduct, control and supervise the complete insurance activities of the Company. As compensation for the services performed, CCMC is paid a monthly fee of up to 125% of expenses incurred on behalf of the Company. In addition, the Company pays CCMC an annual incentive fee not to exceed 10% of the group's calendar year pre-tax income. This Agreement was approved by the California Department of Insurance (CDI) on November 12, 1993 pursuant to California Insurance Code (CIC) Section 1215.5(b)(4). There was no incentive fee paid during the examination period. The total fees paid by the Company under this agreement were: \$354,610 in 2014, \$1,013,555 in 2015, \$658,662 in 2016, and \$537,280 in 2017.

Tax Allocation Agreement: Effective January 1, 1992, the Company entered into a tax allocation agreement entitled "California Casualty Group Tax Allocation Agreement" (Tax Agreement) with California Casualty Indemnity Exchange (Exchange), California Casualty Insurance Company, California Casualty & Fire Insurance Company, and

California Casualty General Insurance Company of Oregon. On January 1, 1999, this Tax Agreement was restated as the “Tax Allocation Agreement California Casualty Indemnity Exchange and Subsidiaries”, and was submitted to the CDI pursuant to CIC Section 1215.5(b)(4) on March 26, 2008. The CDI did not disapprove the agreement as of March 24, 2009. The review and determination was made pursuant to CIC Section 1215.5(b) only. Under the terms of this restated Tax Agreement, the consolidated federal income tax liability of the Exchange and its subsidiaries is allocated to each company in proportion to each company’s share of taxable income, computed on a separate company basis. The Exchange is responsible for filing and making all tax payments on behalf of its subsidiaries.

TERRITORY AND PLAN OF OPERATION

As of December 31, 2017, the Company is licensed to transact property and casualty insurance only in California. The Company did not write any direct business during the examination period.

All of the workers’ compensation and miscellaneous commercial business for the California Casualty Group has been in run-off since October 1997 and retroceded to the Company (See “REINSURANCE”).

The Company’s run-off business is managed by California Casualty Management Company (CCMC). In accordance with the terms of the retroactive reinsurance agreement with XL Re Ltd., (See “REINSURANCE”), in July 2001, a third-party claim adjuster, GAB Robins North America Inc. (GAB Robins NA), was contracted to handle the workers’ compensation claims in run-off. In 2010, GAB Robins NA was acquired by Gallagher Bassett Service Inc.

REINSURANCE

Pooling

A revised Intercompany Pooling Agreement (Agreement), effective January 1, 2011, was approved by the California Department of Insurance (CDI) on August 30, 2010 pursuant to California Insurance Code (CIC) Section 1215.5(b)(3). This revised Agreement was amended to clarify that only the Company's parent, California Casualty Indemnity Exchange (Exchange), may purchase non-affiliate reinsurance contracts and each subsidiary's direct premiums and direct paid loss and loss adjustment expenses are ceded to the Exchange. Under the terms of this Agreement, each participating insurer cedes 100% of its direct and assumed business to the Exchange. Personal lines of business are pooled separately from workers' compensation and miscellaneous commercial lines business, which are in run-off. Under this revised Agreement, personal lines business is retroceded to and assumed by California Casualty Insurance Company, California Casualty & Fire Insurance Company and California Casualty General Insurance Company of Oregon according to their respective pooling percentages of 8%, 10%, and 12%. The Exchange retains 70% of the pooled personal lines business. All workers' compensation and miscellaneous commercial lines direct and assumed business are retroceded 100% to the Company.

Assumed

The Company did not assume any reinsurance business other than from the pooling agreement discussed above.

Ceded

The Company entered into an Adverse Loss Development Retrocession Contract with XL Re, Ltd., of Hamilton, Bermuda (XL Re), effective January 1, 2001. The purpose of the agreement was to cede 100% of the ultimate net loss paid or payable by the Company on workers' compensation and employer's liability losses for policies with dates of injury on or before December 31, 1998 issued by the Company and all other

insurers through the Intercompany Pooling Agreement. The maximum limit to be ceded to XL Re was \$110 million, with a sub-limit of \$15 million for 1987 and prior injury dates. The arrangement called for California Casualty Management Company to contract with an acceptable third party administrator for claims handling of the subject losses. Pursuant to CIC Section 1011(c), the CDI approved the agreement on October 22, 2001.

The Company, together with its parent and its subsidiaries (the Group) entered into reinsurance agreements with Munich Reinsurance America Inc. (Munich Re), primarily covering workers' compensation claims from 1935 through 2001. A Commutation and Release Agreement was entered on March 28, 2017 with Munich Re to release Munich Re from assumed risks and liabilities on workers' compensation business in exchange for \$22.0 million. In accordance with the Intercompany Pooling Agreement, all workers' compensation direct and assumed business are retroceded 100% to the Company. As a result, the Company's loss and loss expense reserves increased by \$21.2 million, assets increased by \$21.7 million, and income and surplus increased by \$0.5 million.

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, 2017. The accompanying comments to the amounts reported in the financial statements should be considered an integral part of the financial statements. No examination adjustments were made to the financial statements as a result of the examination.

Statement of Financial Condition as of December 31, 2017

Underwriting and Investment Exhibit for the Year Ended December 31, 2017

Reconciliation of Surplus as Regards Policyholders from December 31, 2013
through December 31, 2017

Statement of Financial Condition
as of December 31, 2017

<u>Assets</u>	<u>Ledger and Nonledger Assets</u>	<u>Assets Not Admitted</u>	<u>Net Admitted Assets</u>	<u>Notes</u>
Bonds	\$ 88,269,642	\$	\$ 88,269,642	
Cash and cash equivalents	3,760,746		3,760,746	
Receivables for securities	601,000		601,000	
Investment income due & accrued	403,690		403,690	
Uncollected premiums and agents' balances in course of collection	10		10	
Amount recoverable from reinsurers	239		239	
Receivables from parent, subsidiaries and affiliates	3,316,975		3,316,975	
Aggregate write-ins for other than invested assets	<u>221,856</u>		<u>221,856</u>	
 Total assets	 <u>\$ 96,574,158</u>	 <u>\$</u>	 <u>\$ 96,574,158</u>	
 <u>Liabilities, Surplus and Other Funds</u>				
Losses			\$ 35,761,083	(1)
Reinsurance payable on paid losses and loss adjustment expenses			215,282	
Loss adjustment expenses			5,128,128	(1)
Other expenses (excluding taxes, licenses and fees)			10,493	
Taxes, licenses and fees (excluding federal and foreign income taxes)			66	
Current federal and foreign income taxes			14,334	
Net deferred tax liability			18,718	
Unearned premiums			20	
Payable to parent, subsidiaries and affiliates			3,232,333	
Aggregate write-ins for liabilities			<u>(19,552,103)</u>	(2)
 Total liabilities			 24,828,354	
Aggregate write-ins for special surplus funds		\$ 18,595,604		
Common capital stock		2,600,000		
Gross paid in and contributed surplus		26,800,000		
Unassigned funds (surplus)		<u>23,750,200</u>		
 Surplus as regards policyholders			 <u>71,745,804</u>	
 Total liabilities, surplus and other funds			 <u>\$ 96,574,158</u>	

Underwriting and Investment Exhibit
for the Year Ended December 31, 2017

Statement of Income

Underwriting Income

Premiums earned		\$ 38
Deductions:		
Losses incurred	\$ (1,499,566)	
Loss expenses incurred	1,876,911	
Other underwriting expenses incurred	<u>(427,024)</u>	
Total underwriting deductions		<u>(49,679)</u>
Net underwriting gain		49,717

Investment Income

Net investment income earned	\$ 1,373,591	
Net realized capital gains	<u>18,917</u>	
Net investment gain		1,392,508

Other Income

Aggregate write-ins for miscellaneous income	\$ <u>(200,000)</u>	
Total other income		<u>(200,000)</u>
Net income before federal and foreign income taxes		1,242,224
Federal and foreign income taxes incurred		<u>365,617</u>
Net income		<u>\$ 876,608</u>

Capital and Surplus Account

Surplus as regards policyholders, December 31, 2016		\$ 70,905,757
Net income	\$ 876,608	
Change in net deferred income tax	<u>(36,561)</u>	
Change in surplus as regards policyholders for the year		<u>840,047</u>
Surplus as regards policyholders, December 31, 2017		<u>\$ 71,745,804</u>

Reconciliation of Surplus as Regards Policyholders
from December 31, 2013 through December 31, 2017

Surplus as regards policyholders, December 31, 2013, per Examination			\$ 68,222,457
	<u>Gain in Surplus</u>	<u>Loss in Surplus</u>	
Net income	\$ 3,583,334	\$	
Change in net deferred income tax	<u> </u>	<u>59,987</u>	
Total gains and losses	<u>\$ 3,583,334</u>	<u>\$ 59,987</u>	
Net increase in surplus as regards policyholders			<u>3,523,347</u>
Surplus as regards policyholders, December 31, 2017, per Examination			<u>\$ 71,745,804</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, 2017 prepared by the Company's actuary and concurred with the actuary's conclusion that the Company's loss and loss adjustment expense reserves as of December 31, 2017 are reasonable and have been accepted for purposes of this examination.

(2) Aggregate Write-Ins for Liabilities

Aggregate write-ins for liabilities as of December 31, 2017 included \$19.6 million in ceded retroactive reinsurance reserves related to the retroactive reinsurance agreement with XL Re, Ltd., as mentioned in the "Reinsurance-Ceded" section of this examination report.

SUMMARY OF COMMENTS AND RECOMMENDATIONS

Current Report of Examination

None.

Previous Report of Examination

None.

ACKNOWLEDGMENT

Acknowledgment is made of the cooperation and assistance extended by the Company's officers and California Casualty Management Company's employees during the course of this examination.

Respectfully submitted,

_____/S/_____

Mei Gu, CFE
Examiner-In-Charge
Senior Insurance Examiner
Department of Insurance
State of California

_____/S/_____

Ber Vang, CFE, AES, CISA
Senior Insurance Examiner, Supervisor
Department of Insurance
State of California