

REPORT ON EXAMINATION

OF THE

UNITRIN PREFERRED INSURANCE COMPANY

AS OF

DECEMBER 31, 2013

DATE OF REPORT

April 23, 2015

EXAMINER

JOSEPH REVERS, CFE

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NEW YORK STATE
DEPARTMENT *of*
FINANCIAL SERVICES

Andrew M. Cuomo
Governor

Benjamin M. Lawsky
Superintendent

April 23, 2015

Honorable Benjamin M. Lawsky
Superintendent of Financial Services
Albany, New York 12257

Sir:

Pursuant to the requirements of the New York Insurance Law, and in compliance with the instructions contained in Appointment Number 31117 dated February 11, 2014, attached hereto, I have made an examination into the condition and affairs of Unitrin Preferred Insurance Company as of December 31, 2013, and submit the following report thereon.

Wherever the designation “the Company” appears herein without qualification, it should be understood to indicate Unitrin Preferred Insurance Company.

Wherever the term “Department” appears herein without qualification, it should be understood to mean the New York State Department of Financial Services.

The examination was conducted at the Company’s administrative office located at 12926 Gran Bay Parkway West, Jacksonville, Florida 32258.

1. SCOPE OF EXAMINATION

The Department has performed a coordinated group examination of the Company, a multi-state insurer. The previous examination was conducted as of December 31, 2010. This examination covered the three year period from January 1, 2011 through December 31, 2013. Transactions occurring subsequent to this period were reviewed where deemed appropriate by the examiner.

This examination was conducted as a coordinated examination of a number of property and casualty insurance companies ultimately owned by the Kemper Group. The coordinated examination was conducted by the State of Illinois as the lead state. Other states participating in this examination were: Texas, Oregon and Wisconsin.

The following insurers were included in the examination: Trinity Universal Insurance Company, Charter Indemnity Company, Unitrin Country Mutual Insurance, Kemper Independence Insurance Company, Financial Indemnity Company, Merastar Insurance Company, Response Insurance Company, National Merit Insurance Company, Response Worldwide Insurance Company, Response Worldwide Direct Auto Insurance, Warner Insurance Company, Unitrin Direct Insurance Company, Unitrin Direct Property & Casualty, Alpha Property & Casualty Insurance Company, Unitrin Safeguard Insurance Company, Valley Property & Casualty Insurance Company, United Casualty Insurance Company of America, Unitrin Auto & Home Insurance Company, and Unitrin Advantage Insurance Company.

This examination was conducted in accordance with the National Association of Insurance Commissioners (“NAIC”) Financial Condition Examiners Handbook (“Handbook”), which requires that we plan and perform the examination to evaluate the financial condition and identify prospective risks of the Company by obtaining information about the Company including corporate governance, identifying and assessing inherent risks within the Company and evaluating system controls and procedures used to mitigate those risks. This examination also includes assessing the principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation, management’s compliance with Statutory Accounting Principles and annual statement instructions when applicable to domestic state regulations.

All financially significant accounts and activities of the Company were considered in accordance with the risk-focused examination process. This examination also included a review and evaluation of the

Company's own control environment assessment. The examiners also relied upon audit work performed by the Company's independent public accountants when appropriate.

This examination report includes a summary of significant findings for the following items as called for in the Handbook:

- Significant subsequent events
- Company history
- Corporate records
- Management and control
- Fidelity bonds and other insurance
- Pensions, stock ownership and insurance plans
- Territory and plan of operation
- Growth of Company
- Loss experience
- Reinsurance
- Accounts and records
- Financial statements
- Summary of recommendations

This report on examination is confined to financial statements and comments on those matters that involve departures from laws, regulations or rules, or that are deemed to require explanation or description.

2. DESCRIPTION OF COMPANY

The Company was incorporated on September 28, 1942, under the laws of the State of New York as The Unity Fire Insurance Corporation to act as the successor to the United States Branch of The Union Fire, Accident & General Insurance Company of Paris, France. The Company was licensed and commenced business on October 13, 1942. In 1950, the Company adopted the name The Unity Fire and General Insurance Company.

Effective July 3, 1990, SCOR U. S. Corporation ("SCOR") acquired, and absorbed by merger, the Company's former parent, Rockleigh Management Corporation; therefore, the Company became a subsidiary of SCOR. On April 8, 1996, the Company changed its name to General Security Property and Casualty Company.

Effective December 31, 2002, Unitrin, Inc., which subsequently changed its name to Kemper Corporation, acquired 100% of the common stock of the Company from SCOR. As part of the acquisition, the Company ceded on an indemnity basis, all of its insurance related assets and liabilities in force on or before December 31, 2002 to General Security National Insurance Company, pursuant to an indemnity and assumption agreement. Additionally, the stock purchase agreement provided for the return of capital by the Company to SCOR in the amount of \$6,199,470, in order to reduce the net assets of the Company to the amount agreed to in the sale agreement. The acquisition was approved by the Department on December 23, 2002.

On February 18, 2003, the Company's name was changed to its current title. On December 29, 2003, the Company became a wholly-owned subsidiary of Trinity Universal Insurance Co. ("Trinity"), which is a wholly-owned subsidiary of Kemper Corporation, a Delaware corporation.

Capital paid in is \$3,900,000 consisting of 6,500 shares of \$600 par value per share common stock. Gross paid in and contributed surplus is \$2,526,285. There were no changes in capital paid in and contributed surplus from the prior examination date to the current examination date.

A. Management

Pursuant to the Company's charter and by-laws, management of the Company is vested in a board of directors consisting of not less than seven nor more than thirteen members. The board meets at least once during each calendar year. At December 31, 2013, the board of directors was comprised of the following seven members:

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
John Michael Boschelli Chicago, Illinois	Vice President and Chief Investment Officer, Unitrin Preferred Insurance Company
Patrick Brian Gillson Syracuse, New York	Vice President Casualty Claims, Unitrin Preferred Insurance Company
Andrea Elizabeth James Jacksonville, Florida	President, Unitrin Preferred Insurance Company
Denise Idell Lynch Chicago, Illinois	Property & Casualty Group Executive, Unitrin Preferred Insurance Company
Maxwell Thomas Mindak Chicago, Illinois	Vice President – Financial Planning and Analysis, Unitrin Preferred Insurance Company
Christopher Lamont Moses Chicago, Illinois	Vice President and Treasurer, Unitrin Preferred Insurance Company
Richard NMI Roeske Chicago, Illinois	Vice President and Chief Accounting Officer, Unitrin Preferred Insurance Company

A review of the minutes of the board of directors' meetings held during the examination period indicated that the meetings were generally well attended and each board member had an acceptable record of attendance.

As of December 31, 2013, the principal officers of the Company were as follows:

<u>Name</u>	<u>Title</u>
Andrea Elizabeth James	President
Kristine Ruth Azar	Vice President and Secretary
Brian Todd Sandlin	Treasurer

B. Territory and Plan of Operation

As of December 31, 2013, the Company was licensed to write business in twenty states and the District of Columbia.

As of the examination date, the Company was authorized to transact the kinds of insurance as defined in the following numbered paragraphs of Section 1113(a) of the New York Insurance Law:

<u>Paragraph</u>	<u>Line of Business</u>
3	Accident & health
4	Fire
5	Miscellaneous property
6	Water damage
7	Burglary and theft
8	Glass
9	Boiler and machinery
10	Elevator
11	Animal
12	Collision
13	Personal injury liability
14	Property damage liability
15	Workers' compensation and employers' liability
16	Fidelity and surety
17	Credit
19	Motor vehicle and aircraft physical damage
20	Marine and inland marine
21	Marine protection and indemnity

Based on the lines of business for which the Company is licensed and the Company's current capital structure, and pursuant to the requirements of Articles 13 and 41 of the New York Insurance Law, the Company is required to maintain a minimum surplus to policyholders in the amount of \$2,200,000.

The following schedule shows the direct premiums written by the Company both in total and in New York for the period under examination:

<u>Calendar Year</u>	<u>New York State</u>	<u>Total Premiums</u>	<u>Premiums Written in New York State as a Percentage of Total Premium</u>
2011	\$33,785,772	\$78,626,233	42.97%
2012	\$30,341,832	\$76,559,197	39.63%
2013	\$27,804,662	\$69,923,507	39.76%

The Company's predominant lines of business are homeowners multiple peril (40.33%), private passenger auto liability (31.25%), and auto physical damage (21.40%), which accounted for approximately 93% of the total direct written premiums in 2013. At December 31, 2013, the Company wrote business through approximately 236 independent agents.

C. Reinsurance

Assumed

Assumed reinsurance accounted for less than 1% of the Company's gross premium written at December 31, 2013 and consisted solely of business assumed from mandatory pools.

Ceded

100% Quota Share Reinsurance Agreement

Pursuant to a 100% quota share reinsurance agreement with its direct parent Trinity Universal Insurance Company ("Trinity"), the Company cedes 100% of its net liability, premiums, losses, and other expenses for existing, new, and renewal business, net of unaffiliated reinsurance to Trinity. This agreement became effective on January 1, 2009. Additionally, existing losses were retroactively transferred to Trinity as well. As a result of this agreement the Company retains no underwriting risk.

The quota-share agreement was filed and non-disapproved by the Department pursuant to the provisions of Section 1505(d) (2) of the New York Insurance Law. The agreement was reviewed and found to contain the required clauses, including an insolvency clause meeting the requirements of Section 1308 of the New York Insurance Law.

Examination review of the Schedule F data reported by the Company in its filed annual statement was found to accurately reflect its reinsurance transactions.

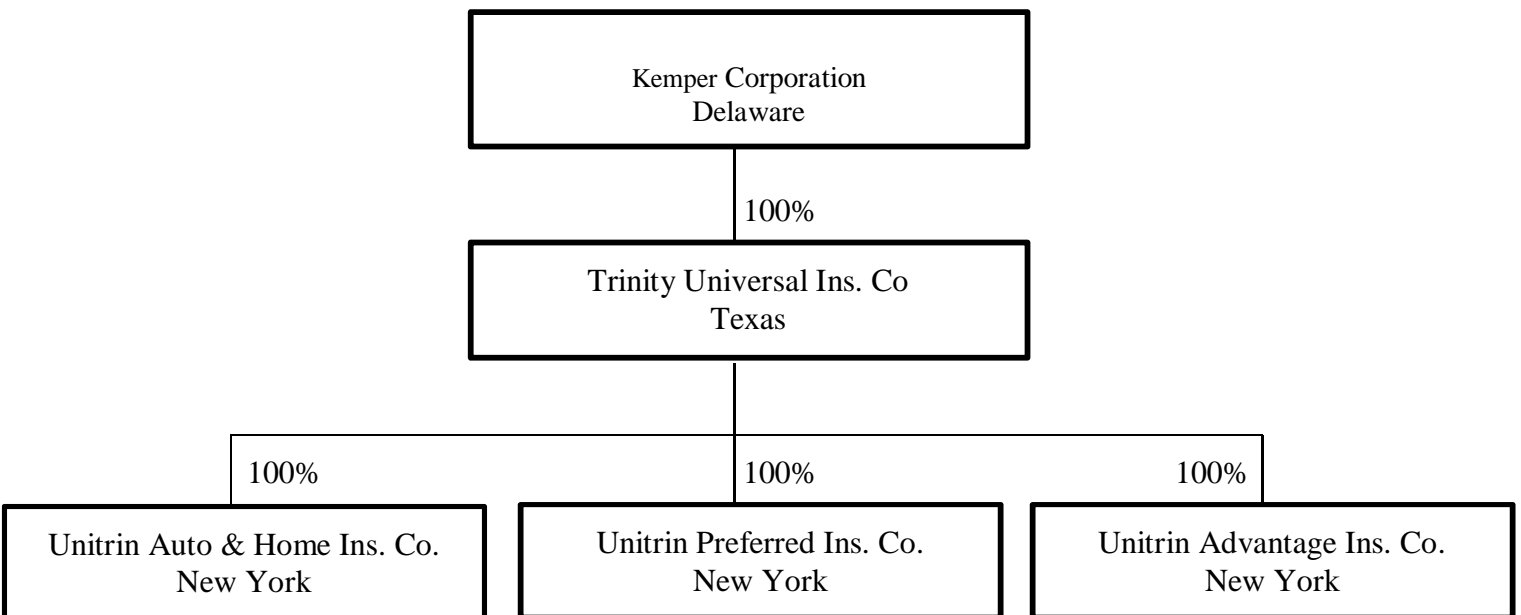
At December 31, 2013, the Company reported approximately \$71 million in reinsurance recoverables from Trinity. These reinsurance recoverables are the Company's most significant financial item and ultimately the Company's most significant financial risk is its ultimate ability to collect on these reinsurance recoverables. It is noted that Trinity was examined concurrently with the Company and there were no examination changes made to Trinity's balance sheet and income statement.

D. Holding Company System

The Company is a member of the Kemper Group. The Company is a wholly-owned subsidiary of Trinity Universal Insurance Company, a Texas domiciled corporation, which is ultimately controlled by Kemper Corporation, a Delaware corporation.

A review of the Holding Company Registration Statements filed with this Department indicated that such filings were complete and were filed in a timely manner pursuant to Article 15 of the New York Insurance Law and Department Regulation 52.

The following is an abridged chart of the holding company system at December 31, 2013:



At December 31, 2013, the Company was party to the following agreements with other members of its holding company system:

General Services - Policy Administration Agreement

Effective January 1, 2009, the Company and Merastar Insurance Company (“MIC”), a wholly owned subsidiary of Trinity, entered into a general service agreement whereby MIC shall administer the new and renewal property and casualty lines insurance business of the Company, including marketing, underwriting, subject to the Company’s written guidelines, and claims administration.

General Services Agreement

Effective July 1, 2010, Unitrin Services Company (“USC”), which subsequently changed its name to Kemper Corporate Services, provides the following services to the Company: trade execution and investment analysis; financial accounting and reporting; purchasing and accounts payable; investment accounting; tax return preparation; tax accounting and tax advice; maintenance and benefits plans; administration of post-retirement medical benefits; benefit plan regulatory reporting and support; risk management; automobile fleet management; internal audit; cash management and bank relations; financial planning and analysis of results of operations; capital project review and evaluation; real estate management; corporate secretarial functions; and legal support and advice. Effective December 21, 2012, the agreement was amended and restated.

Information Technology Services Agreement

Effective January 1, 2009, the Company and Unitrin Direct Property & Casualty Company (“UDPC”) entered into an information technology services agreement whereby UDPC shall provide information technology applications and consulting services on technology that is shared among Kemper Corporation property and casualty affiliates.

Computer Service Agreement

Effective July 1, 2010, the Company and USC entered into a computer service agreement whereby USC shall provide computer data processing services to the Company using computer systems maintained by USC including: mainframe, midrange and minicomputer and other central processors and controllers;

data storage devices, cartridges and tape drives; MVS, UNIX and other operating system software; database management software; CICS and other transaction processing software; groupware, middleware and network software; routers and other network and 10 telecommunications equipment and lines located at its data center facilities; and internet and intranet access software and systems.

All of the above agreements were submitted to and non-disapproved by the Department.

Tax Allocation Agreement

The Company is included in a consolidated federal income tax return with the Kemper Group. The tax allocation agreement states that each participant in the agreement shall be allocated tax as if they filed a separate company return. In 2009, the agreement was amended to include additional new affiliates. The amendment was filed with the Department and approved by the Company's board of directors pursuant to Department Circular Letter No.33 (1979).

E. Significant Operating Ratios

The following ratios have been computed as of December 31, 2013, based upon the results of this examination:

Net premiums written to surplus as regards policyholders	0%
Liabilities to liquid assets (cash and invested assets less investments in affiliates)	48%
Premiums in course of collection to surplus as regards policyholders	23%

The premium ratios reflected above are not meaningful given the Company's 100% cession to Trinity.

All of the above ratios fall within the benchmark ranges set forth in the Insurance Regulatory Information System of the National Association of Insurance Commissioners.

3. FINANCIAL STATEMENTS

A Balance Sheet

The following shows the assets, liabilities and surplus as regards policyholders as of December 31, 2013 as determined by this examination and as reported by the Company:

<u>Assets</u>	<u>Assets</u>	<u>Assets Not Admitted</u>	<u>Net Admitted Assets</u>
Bonds	\$10,760,308	\$ 0	\$10,760,308
Cash, cash equivalents and short-term investments	1,698,152	0	1,698,152
Investment income due and accrued	206,310	0	206,310
Uncollected premiums and agents' balances in the course of collection	2,038,022	1,749	2,036,273
Deferred premiums, agents' balances and installments booked but deferred and not yet due	13,372,372	0	13,372,372
Net deferred tax asset	56,616	0	56,616
Guaranty funds receivable or on deposit	13,361	0	13,361
Aggregate write-ins for other than invested assets	<u>67,422</u>	<u>51,861</u>	<u>15,561</u>
Total assets	<u>\$28,212,563</u>	<u>\$53,610</u>	<u>\$28,158,953</u>

Liabilities, Surplus and Other Funds

Examination

Losses and Loss Adjustment Expenses	\$ 0
Commissions payable, contingent commissions and other similar charges	1,333,598
Other expenses (excluding taxes, licenses and fees)	66,106
Taxes, licenses and fees (excluding federal and foreign income taxes)	956,285
Current federal and foreign income taxes	594,025
Advance premium	963,801
Ceded reinsurance premiums payable (net of ceding commissions)	15,413,616
Payable to parent, subsidiaries and affiliates	127,796
Aggregate write-ins for liabilities	<u>1,419</u>
Total liabilities	<u>\$19,456,645</u>
Common capital stock	\$3,900,000
Gross paid in and contributed surplus	2,526,285
Unassigned funds (surplus)	<u>2,276,024</u>
Surplus as regards policyholders	<u>8,702,308</u>
Total liabilities, surplus and other funds	<u>\$28,158,953</u>

Note: The examiner is unaware of any potential exposure of the Company to any tax assessment and no liability has been established herein relative to such contingency.

B. Statement of Income

Underwriting Income

Premiums earned		\$	0
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Investment Income

Net investment income earned	\$1,374,163		
Net realized capital gain	<u>24</u>		
Net investment gain or (loss)		\$	<u>1,374,187</u>
Net income before federal income taxes		\$	1,374,187
Federal and foreign income taxes incurred			<u>504,518</u>
Net Income		\$	<u>869,669</u>

C. Capital and Surplus

Surplus as regards policyholders increased \$412,791 during the three-year examination period January 1, 2011 through December 31, 2013, detailed as follows:

Surplus as regards policyholders per report on examination as of December 31, 2010			\$8,289,518
	Gains in <u>Surplus</u>	Losses in <u>Surplus</u>	
Net income	\$869,669		
Change in net deferred income tax	9,636		
Change in nonadmitted assets		\$ 7,515	
Dividends to stockholders	<u>0</u>	<u>459,000</u>	
Total Gains / Losses in Surplus	<u>\$879,305</u>	<u>\$466,515</u>	
Net increase (decrease) in surplus			<u>412,790</u>
Surplus as regards policyholders per report on examination as of December 31, 2013			<u>\$8,702,308</u>

4. LOSSES AND LOSS ADJUSTMENT EXPENSES

The examination liability for the captioned items of \$0 is the same as reported by the Company as of December 31, 2013. Effective January 1, 2009, 100% of the Company's insurance liabilities are ceded to Trinity Universal Insurance Company ('Trinity').

At the examination date, the Company has taken reinsurance reserve credit for losses ceded to Trinity of approximately \$38 million. The Company has additionally reduced its unearned premium reserve by approximately \$33 million.

5. **COMPLIANCE WITH PRIOR REPORT ON EXAMINATION**

The prior report on examination contained no recommendations.

6. **SUMMARY OF COMMENTS AND RECOMMENDATIONS**

This report contains no comments or recommendations.

Respectfully submitted,

Joseph Revers, CFE
Senior Insurance Examiner

STATE OF NEW YORK)
)ss:
COUNTY OF NEW YORK)

JOSEPH REVERS, being duly sworn, deposes and says that the foregoing report, subscribed by him, is true to the best of his knowledge and belief.

Joseph Revers

Subscribed and sworn to before me

this _____ day of _____, 2015.

APPOINTMENT NO. 31117

NEW YORK STATE

DEPARTMENT OF FINANCIAL SERVICES

I, BENJAMIN M. LAWSKY, Superintendent of Financial Services of the State of New York, pursuant to the provisions of the Financial Services Law and the Insurance Law, do hereby appoint:

Joseph Revers

as a proper person to examine the affairs of the

Unitrin Preferred Insurance Company

and to make a report to me in writing of the condition of said

COMPANY

with such other information as he shall deem requisite.

In Witness Whereof, I have hereunto subscribed by name
and affixed the official Seal of the Department
at the City of New York

this 11th day of February, 2014

BENJAMIN M. LAWSKY
Superintendent of Financial Services

By:



Rolf Kaumann
Deputy Chief Examiner

