

REPORT ON EXAMINATION
OF THE
NATIONAL CONTINENTAL INSURANCE COMPANY
AS OF
DECEMBER 31, 1998

DATE OF REPORT

AUGUST 31, 2000

EXAMINER

GILBERT W. DENTON

TABLE OF CONTENTS

<u>PAGE NO.</u>		<u>PAGE NO.</u>
1.	Scope of examination	2
2.	Description of Company	3
A.	Management	4
B.	Territory and plan of operation	6
C.	Reinsurance	8
D.	Holding company system	11
E.	Abandoned Property Law	16
F.	Accounts and records	16
G.	Significant operation ratios	19
3.	Financial statements	20
A.	Balance sheet	20
B.	Underwriting and investment exhibit	22
4.	Loss and loss adjustment expenses	24
5.	Compliance with prior report on examination	24
6.	Summary of comments and recommendations	29



STATE OF NEW YORK
INSURANCE DEPARTMENT
25 BEAVER STREET
NEW YORK, NEW YORK 10004

August 31, 2000

Honorable Neil Levin
Superintendent of Insurance
Albany, NY 12257

Sir:

Pursuant to the requirements of the New York Insurance Law, and in compliance with instructions contained in Appointment Number 21610, dated August 29, 2000, attached hereto, I have made an examination into the condition and affairs of the National Continental Insurance Company as of December 31, 1998 and submit the following report thereon.

The examination was conducted at the Company's administrative offices located at 6300 Wilson Mills Road, Mayfield Village, Ohio.

Wherever the designations "NCIC" or "the Company" appears herein without qualification, they should be understood to indicate the National Continental Insurance Company.

1. SCOPE OF EXAMINATION

The prior examination was conducted as of December 31, 1994. This examination covers the four-year period from January 1, 1995 through December 31, 1998 and was limited in its scope to a review or audit of only those balance sheet items considered by this Department to require analysis, verification or description, including: invested assets, inter-company balances, loss and loss adjustment expense reserves and the provision for reinsurance. The examination included a review of income, disbursements and company records deemed necessary to accomplish such analysis or verification, and utilized to the extent considered appropriate, work performed by the Company's independent public accountants. A review or audit was also made of the following items as called for in the Examiners Handbook of the National Association of Insurance Commissioners:

- History of the Company
- Management and control
- Corporate records
- Fidelity bonds and other insurance
- Territory and plan of operation
- Market conduct activities
- Growth of the Company
- Business in force by states
- Reinsurance
- Accounts and records
- Financial statements

A review was made to ascertain what action was taken by the Company with regard to comments and recommendations contained in the prior report on examination.

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

2. DESCRIPTION OF COMPANY

The Company was incorporated as a stock fire insurer on December 24, 1897 under the name Caledonian-American Insurance Company, and commenced business on March 24, 1898 under the laws of the State of New York.

Rathbone, King and Seeley, Inc. acquired control of the Company in 1958. At that time the Company's name was changed to American Star Insurance Company and its administrative office was moved to San Francisco, California. The Seibels Bruce Group, Inc. acquired 100% of the stock of Rathbone, King and Seeley, Inc. in 1981.

In November 1985, financial control of the Company was acquired by the Progressive Corporation which contributed the stock of American Star Insurance Company to its subsidiary, Progressive Casualty Insurance Company. The Company's name was changed to the National Continental Insurance Company and its administrative offices were moved to Cleveland, Ohio. In 1988, the Company's administrative offices were moved to Mayfield Heights, Ohio. Progressive Casualty Insurance Company transferred the Company's stock by means of a dividend to the Progressive Corporation on December 29, 1989. The Company's administrative offices were moved to Mayfield Village, Ohio in 1994. The relocations were

approved pursuant to Section 325(b) of the New York Insurance Law. The Company's statutory home office is in Hauppauge, New York.

The Company received a surplus contribution of \$20,077,005 from the Progressive Corporation in 1995. This surplus contribution was the return of cash forwarded to the Progressive Corporation pursuant to stock redemption and retirement of common shares on March 22, 1994. This transaction was a condition of the de-pooling agreement approved by the Department on December 20, 1995.

Pursuant to the de-pooling process from the Progressive Pool, beginning in January 1996, the Company primarily acts as a servicing carrier for the Commercial Auto Insurance Plans (CAIP) and Special Risk Distribution Plans (SRDP) for selected states.

As of December 31, 1998, paid in capital was \$7,912,500, which consisted of 316,500 shares at \$25 par value and gross paid in and contributed surplus was \$35,250,753.

The Company paid its parent, the Progressive Corporation, \$23,200,000 in dividends in December 1998. The dividend payment was approved by this Department.

A. Management

The board of directors, consisting of nine members, is elected annually by the sole shareholder, the Progressive Corporation, which exercises the corporate power of the Company. The Company's by-laws state that the directors are to be elected at an annual meeting of the shareholders.

The meetings and or actions of the board members during the examination period was executed by means of a “Shareholders’ Written Action Without Meeting in Lieu of Annual Meeting.”

At December 31, 1998, the Company’s board of directors consisted of the following members:

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Michael R. Beney Camillus, New York	Vice President, Progressive Northeastern Insurance Company
Charles C. Boucherle Chardon, Ohio	General Manager, Progressive Casualty Insurance Company
Timothy R. Case Waterford, New York	Claims Manager II, Progressive Casualty Insurance Company
Charles B. Chokel Pepper Pike, Ohio	Vice President, Progressive International Holdings Corporation
Margaret M. Dowd Valley Stream, New York	Branch Manager, Progressive Casualty Insurance Company
Robin A. Harbage Pittsford, New York	General Manager, Progressive Casualty Insurance Company
Peter B. Lewis Beachwood, Ohio	Director and Chairman, Progressive International Holdings Corporation
Victor Politzi Loudonville, New York	General Manager, Progressive Casualty Insurance Company
David M. Schneider Pepper Pike, Ohio	Director and Secretary, Progressive International Holdings Corporation

At December 31, 1994, the principal officers of the Company were as follows:

<u>Name</u>	<u>Title</u>
Charles C. Boucherle	President
Kathleen M. Ceerny	Vice President and Assistant Secretary
Janet A. Dolohanty	Assistance Vice President and Assistant Treasurer
Charles B. Chokel	Treasurer
David M. Schneider	Secretary

B. Territory and Plan of Operation

As of December 31, 1998, the Company was licensed to transact business in the District of Columbia and in all states except Vermont. The Company's business consists of policies written under state-mandated involuntary Commercial Auto Insurance Plans ("CAIP") and Special Risk Distribution Plans ("SRDP") and an immaterial amount of voluntary private passenger automobile insurance. The following 9 states CAIP programs were serviced by the Company: Arizona, California, Colorado, Montana, New Jersey, New York, Oregon, Utah and Washington. Under the guidelines of the service plans, the Company provides policy and claim processing services and retains no underwriting risk.

As of December 31, 1998, the Company was licensed to transact the kinds of business 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 and health
4	Fire
5	Miscellaneous property
6	Water damage
7	Burglary and theft
8	Glass
9	Boiler and machinery
12	Collision
13	Personal injury liability
14	Property damage liability

<u>Paragraph</u>	<u>Line of Business</u>
15	Workers' compensation and employers' liability
16	Fidelity and surety
19	Motor vehicle and aircraft physical damage
20	Marine
21	Marine protection and indemnity
26	Gap insurance

The Company is also licensed to write workers' compensation insurance as may be incidental to the coverages contemplated under paragraphs 20 and 21 of Section 1113(a), including insurances described in the Longshoremen's and Harbor Workers' Compensation Act.

Based upon 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, National Continental Insurance Company is required to maintain a minimum surplus to policyholders in the amount of \$2,700,000.

The following is a schedule of net direct business written countrywide and in New York State for the five-year period covered by this examination:

<u>Year</u>	<u>New York Net Direct Premiums Written</u>	<u>Countrywide Net Direct Premiums Written</u>	<u>Percentage of New York Net Direct Premiums Written to Countrywide</u>
1995	\$43,650,796	\$105,394,702	41.4%
1996	\$20,641,684	\$124,199,658	16.6%
1997	\$11,698,545	\$ 83,321,966	14.0%
1998	\$ 6,088,043	\$ 56,455,009	10.8%

Despite having a license in all states except Vermont, the Company has discontinued writing business, except for the limited amount of business it continues to renew in New York. Otherwise, all the

other business is derived from being a service carrier for the CAIP and SRDP business, where there is no underwriting of risk. The Company receives a service fee from the respective states.

C. Reinsurance

Following is a description of the Company's ceded reinsurance program in effect at December 31, 1998:

Commercial Automobile Insurance Plans ("CAIP")

These contracts cover commercial auto-related risk and call for 100% cession of all premiums and losses. Maximum gross exposures on casualty and property risks are \$10 million under combined single limits policies or \$5 million and \$1 million, respectively, under single limits policies. Physical damage limits on property-related claims are unlimited and vary according to the severity of the claim. There is no net exposure for these contracts. These agreements are continuous with no stated termination date.

Effective December 12, 1997, the Company entered in a 100% quota share agreement with United Financial Casualty Company. The agreement only covers certain policies issued or renewed by the Company under CAIP. Maximum gross exposures on casualty and property risks are \$10 million under combined single limits policy or \$5 million and \$1 million, respectively, under single limits policies. Physical damage limits on property-related claims are unlimited and vary according to the severity of the claim. These agreements are continuous with no stated termination date. There is no net exposure for this contract. This agreement would attach only if both the State and the Company were to become insolvent.

Environment, Asbestos, Product Liability

Prior to the acquisition by the Progressive Corporation in 1985, the Company ceded 100% of its business to an authorized insurer and other third party insurers. During 1994, the Progressive Corporation settled a dispute over the seller's refusal to pay certain pre-sale business written by American Star Insurance Company. The Agreement provided for a commutation by the South Carolina Insurance Company (reinsurer) of the first \$20 million of losses for a consideration of \$10.1 million. The rights to the third party reinsurance recoverables were assigned to the Company. The reinsurer was also obligated to fund out of 50% of its surplus in excess of \$20 million, 50% of the future loss payments in excess of \$20 million gross losses.

Effective July 1, 1995, as a condition of the de-pooling agreement approved by the Department, the Company and its affiliate, Progressive Casualty Insurance Company, entered into an aggregate excess of loss agreement, as follows:

<u>Subject Business</u>	<u>Coverage</u>
All insurance and reinsurance policies, contracts and binders and all other evidence of insurance or reinsurance liability issued or renewed by the Company on or before November 25, 1985	\$45,000,000 xs \$28,478,300

At December 31, 1999, the carried reserves on this business were approximately \$21 million.

Dealership Security Program

<u>Lines of Business</u>	<u>Type of Cessions</u>	<u>Limits</u>
Physical Damage only	Quota Share	90 % of \$10,000,000 each and every risk subject to \$11,700,000 loss occurrence
Physical Damage only	Excess of Loss	\$500,000 xs \$500,000 any one loss any one risk subject to limit of \$1,000,000 per loss occurrence and limit of \$1,500,000 annual aggregate

The examiner reviewed all ceded reinsurance contracts during the examination period to verify that the contracts contain standard clauses, including the insolvency clauses as per Section 1308 of the New York Insurance Law.

It was noted that selected reinsurance contracts were subject to the Laws of Ohio. It is recommended that the Company amend its reinsurance contracts to be governed under the Laws of New York State, its state of domicile.

Furthermore, the reinsurance contracts' arbitration clauses stipulated that the seat for arbitration shall be in Ohio. It is recommended that the Company amend the arbitration clauses contained in its reinsurance contracts to require that the seat for arbitration shall be in New York State, its state of domicile.

The Schedule F data as contained in the Company's filed annual statements filed for the years covered by the examination period appear to accurately reflect its reinsurance transactions.

D. Holding Company System

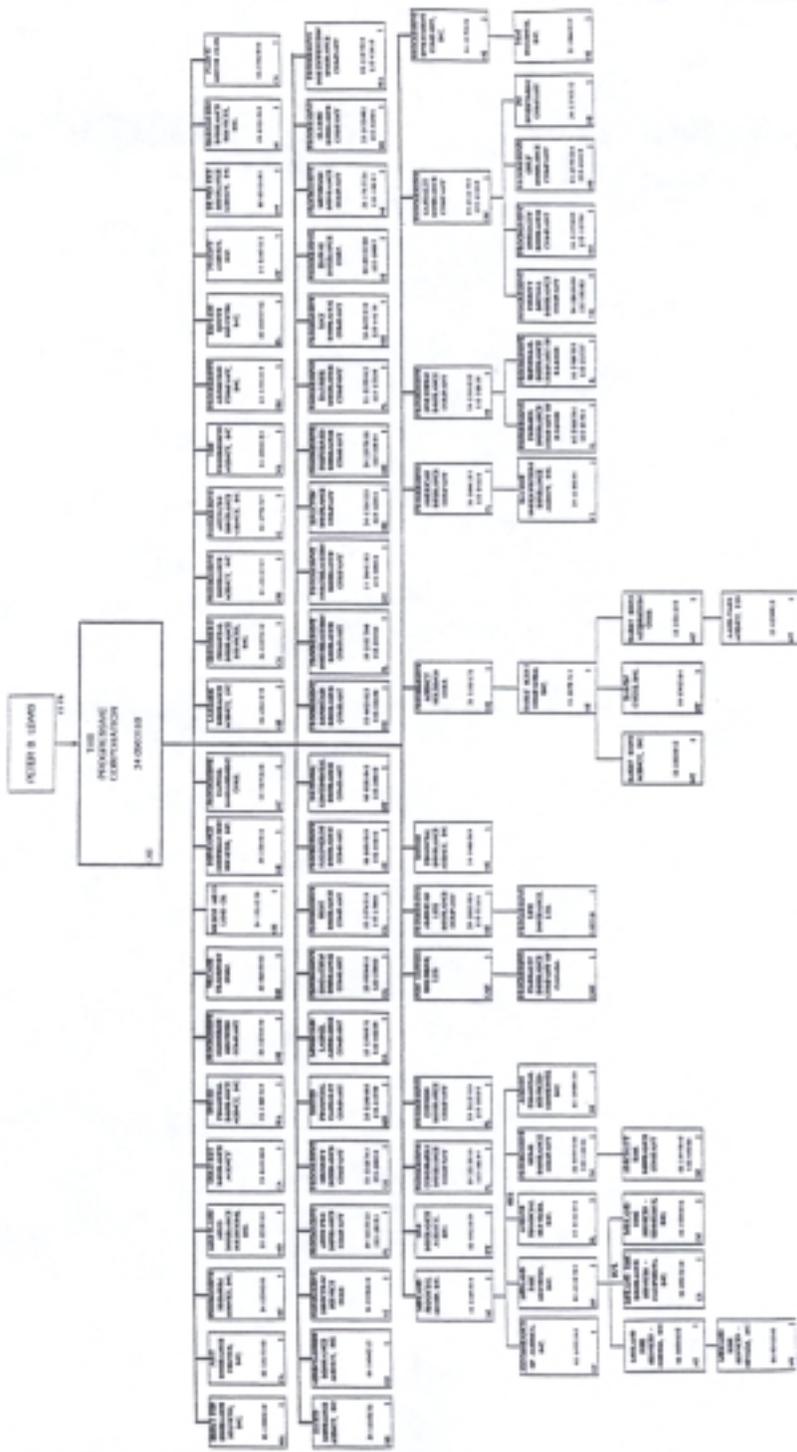
The Company is a wholly-owned subsidiary of the Progressive Corporation, an Ohio insurance holding company. At December 31, 1998, the Progressive Corporation holding company system consisted of over eighty (80) operating subsidiaries and or affiliates.

It is noted that the Company reported Peter B. Lewis, Chairman, President and Chief Executive Officer of the Progressive Corporation and the Progressive Corporation as ultimate controlling person in its Form B, Insurance Company System Annual Registration Statement dated March 27, 1998. The Registration Statement indicated Mr. Lewis as the owner of 14.2% of the voting securities of the Progressive Corporation. The Registration Statement, Item 3, contained the following wording:

“Because Mr. Lewis owns approximately 14.2% of the voting securities of the Progressive Corporation and has not filed a disclaimer of control, there is a statutory presumption that he is the ultimate controlling person. Mr. Lewis neither confirms nor denies that he is the ultimate controlling person.”

The following chart depicts the holding company system at December 31, 1998:

THE PROGRESSIVE GROUP
ORGANIZATION CHART



The Company has entered into the following agreements with members of its holding company system. The agreements have been approved by the Department pursuant to the provisions of Section 1505 of the New York Insurance Law.

1. Cash Management Agreement between Progressive Casualty Insurance Company and National Continental Insurance Company

This agreement, effective January 1, 1998, provides for the Company's participation in the Progressive Casualty Insurance Company's central cash management system (cashier account) in which all the cash of the Progressive Holding Company system's companies are deposited. Pursuant to the agreement, Progressive Casualty Insurance Company is responsible in a fiduciary capacity for the Company's cash, and performs all the Company's duties and operations as they pertain to cash, including the recording and payment of the Company's obligations. The balances in the cashier account are to be settled on a quarterly basis, with payment made within thirty (30) days of the end of each quarter.

2. Interest Agreement between Progressive Casualty Insurance Company and National Continental Insurance Company and Other Affiliates

The Company became a participant, effective November 25, 1985, to the existing Interest Agreement among the Progressive Casualty Insurance Company and members of the holding company system. Pursuant to the Agreement, the Company agrees to pay Progressive Casualty Insurance Company or to receive credit from Progressive Casualty Insurance Company for any balances owed to Progressive Casualty Insurance Company or owed by Progressive Casualty Insurance Company as a result of the activity in the cashier account per the Cash Management Agreement.

3. Investment Services Agreement between Progressive Partners, Inc. and National Continental Insurance Company and Other Affiliates

Pursuant to this agreement, effective July 16, 1992, Progressive Partners, Inc. provide investment management services to the Company as well as other affiliated members. Costs of the investment services are shared among the members of the holding company system.

4. Service Agreement between Progressive Casualty Insurance Company (“PCIC”) and National Continental Insurance Company

Effective January 1, 1996, the Company entered in a service agreement with Progressive Casualty Insurance Company. Pursuant to the Agreement, the Company utilizes the personnel, property and facilities of Progressive Casualty Insurance Company. PCIC also provides all services relating to the insurance operations, including administrative and record keeping functions for the Company. The Company reimburses PCIC for all its identifiable expenses. The expenses that are not identifiable, are allocated based on formulas and factors consistent with the provisions of Department Regulation 30.

5. General Agency Agreement between ProgNY Agency, Inc. and National Continental Insurance Company

Effective August 14, 1996, this agreement authorized ProgNY agency to sell insurance products for the Company.

6. Producer’s Agreement between United Financial Insurance Agency, Inc. and United Financial Insurance Agency of Washington, Inc. and National Continental Insurance Company

Pursuant to the Agreement, effective May 15, 1996, United Financial Insurance Agency,

Inc. and United Financial Insurance Agency of Washington, Inc. are authorized to sell selected insurance business for the Company in New York State.

7. Reinsurance Agreement between National Continental Insurance Company and United Financial Casualty Company

Effective December 31, 1997, this 100% quota share agreement with United Financial Casualty Company provides protection for the Company's CAIP business. The agreement is continuous with no termination date and only attach if both the Company and the state were to become insolvent.

8. Aggregate Excess of Loss Reinsurance Agreement between National Continental Insurance Company and Progressive Casualty Insurance Company

Effective July 1, 1995, as a condition of the de-pooling agreement approved by the Department, the Progressive Corporation provided an aggregate excess of loss reinsurance agreement, which was entered into by its subsidiary, Progressive Casualty Insurance Company

The following agreement was not filed with the Department in accordance with Section 1505(d) of the New York Insurance Law:

1. Allocation of Federal Income Taxes between the Progressive Corporation and National Continental Insurance Company and Certain Affiliates

Effective April 2, 1990, the Company has entered an income tax sharing agreement with the Progressive Corporation, as well as other members of its holding company system, whereby the companies file a consolidated federal income tax return. A review of the agreement revealed that it did not contain all the provisions required by the Department Circular Letter No. 33 (1979), including an escrow provision, a provision that any taxes payable by the Company shall not exceed any amounts that

would have been payable if the Company filed a separate income tax return, and a provision that any balance owing are to be settled within thirty (30) days.

It is recommended that the Company amend this agreement to comply with the provisions set forth in Department Circular Letter No. 33 (1979) and that said amended agreement be submitted to the Department for approval in accordance with Section 1505(d) of the New York Insurance Law.

E. Abandoned Property Law

A review was made of the information included in the Company's Report of Abandoned Property to the Office of the Comptroller of the State of New York during the period under examination. The Company has complied with Section 1316 of the New York Abandoned Property Law during the said period.

F. Accounts and Records

1. Custodial Agreement

The Company is party to a custodial agreement dated September 1, 1991, with Bankers Trust Company and other specified affiliates of the Progressive Corporation. The agreement was reviewed and found not to contain various provisions which meet the guidelines established by the Department for the contents of such agreement. In order to ensure appropriate safeguards and controls for its securities, it is recommended that the Company amend its custodial agreement so that it may contain the following protective covenants and provisions:

1. The agreement should contain a provision which indicates whether the custodian is covered by Bankers Blanket Bond Insurance of the broadest form available, that the

Company be notified in writing of any material change in the form of such bond, the amount of the bond or of the termination of coverage.

2. The agreement should contain a provision which express the custodian's duty to protect the Company's property with the same degree of care it employs to protect its own property.
3. The agreement should require the custodian to furnish to the Company, at least quarterly, a list completely describing the property held.
4. The agreement should require the custodian to maintain records sufficient to verify information reported in Schedule D of the Annual Statement Blank.

Furthermore, the review of the custodial agreement also revealed that it did not contain a provision that such written instructions and/or confirmation of oral and/or "any other means" transfer instructions are to be signed by any two persons authorized by the Company. Such persons are to be specified in a listing to be furnished to the bank from time to time, signed by the Company's treasurer or an assistant treasurer, and certified under the corporate seal by its secretary or assistant secretary. The inclusion of this provision is indicative of sound internal control and prudent business practice.

It is recommended that the custodial agreement be amended to contain the aforementioned provision.

It was noted that the custodial agreement provided for the transfer of funds by "any other means", including, but not limited to oral instructions and instructions received by computer, electronic instruction system or telecommunication terminals. However, the agreement did not indicate any limitations as to the amount of such transfers, nor did it specify to which accounts such funds could be transferred. In order to eliminate this potential internal control deficiency, it is recommended that the Company's board of

directors establish limitations as to the amount of funds that can be transferred via the methods described above, as well as specify those accounts to which funds could be transferred.

2. State Plan Liability

The Company reported its net participation in various state private passenger and commercial automobile residual market facilities under the above caption. Allocations of experience from the facilities' manager indicated that such allocation should be recorded as reinsurance assumed. The NAIC's Accounting Practices and Procedures Manual for Property/Casualty Insurance Companies makes a similar distinction relative to the respective premiums.

It is recommended that the Company properly report residual market premiums under the appropriate caption in future annual statement filings.

3. Claims

As stated in the report of the last examination, the Company has not designated a corporate officer with the responsibility to investigate and resolve complaints filed with the New York State Insurance Department. The corporate officer designee is a requirement of Regulation 64, Part 216.4(c) and Circular Letter No. 11 (1978).

It is recommended that the Company comply with Regulation 64, Part 216.4(c) and Circular Letter No. 11 (1978).

G. Significant Operating Ratios

Based upon the results of this examination, the following ratios have been computed as of December 31, 1998:

Net premiums written in 1998 to Surplus as regards policyholders	.13:1
Liabilities to liquid assets (cash and invested assets, less investments in affiliates)	65.0%
Premiums in course of collection to Surplus as regards policyholders	9.37%

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

The underwriting ratios presented below are on an earned-incurred basis and encompass the four-year period covered by this examination:

	<u>Amounts</u>	<u>Ratios</u>
Losses incurred	\$97,589,821	61.01%
Loss adjustment expenses incurred	32,559,787	20.35
Other underwriting expenses incurred	62,245,627	38.91
Net underwriting loss	<u>(32,440,009)</u>	<u>(20.28)</u>
Premiums earned	<u>\$159,955,226</u>	<u>100.00%</u>

3. FINANCIAL STATEMENTS

A. Balance Sheet

The following shows the assets, liabilities and surplus as regards policyholders as determined by this examination as of December 31, 1998. This statement is the same as the balance sheet filed by the Company:

<u>Assets</u>	<u>Ledger Assets</u>	<u>Non-Ledger Assets</u>	<u>Not-Admitted Assets</u>	<u>Admitted Assets</u>
Bonds	\$84,095,755		\$208,938	\$83,886,817
Preferred stocks	2,017,779		297,779	1,720,000
Cash	425,000			425,000
Premiums and agents' balances in course of collection	3,520,992		42,521	3,478,471
Premiums, agents' balances and installments booked but deferred and not yet due	1,430,281			1,430,281
Reinsurance recoverable on loss and loss adjustment expense payments	13,158,636			13,158,636
Interest, dividends and real estate income due and accrued		\$1,213,115		1,213,115
Receivables from parent, subsidiaries and affiliates	2,313,206			2,313,266
Aggregate write-ins for other assets	<u>569,024</u>	<u> </u>	<u>238,583</u>	<u>330,441</u>
Total assets	<u>\$107,530,733</u>	<u>\$1,213,115</u>	<u>\$787,821</u>	<u>\$107,956,027</u>

Liabilities

Losses	\$19,218,900
Reinsurance payable on paid losses and loss adjustment expenses	2,399
Loss adjustment expenses	12,947,189
Contingent commissions and other similar charges	10,738
Other expenses	175,859
Taxes, licenses and fees	255,896
Unearned premiums	2,763,001
Amounts withheld or retained by company for account of others	303,397
Remittances and items not allocated	685,953
Provision for reinsurance	7,313,848
Drafts outstanding	5,331,561
Other liabilities	2,763
Unearned fee reserve	3,874,896
State Plan Liability	2,643,939
Escheatable property	<u>18,615</u>
 Total liabilities	 <u>\$55,548,954</u>
 Common capital stock	 \$ 7,912,500
Gross paid in and contributed surplus	35,250,753
Unassigned funds	<u>9,243,820</u>
 Surplus as regards policyholders	 <u>\$52,407,073</u>
 Total liabilities and surplus	 <u>\$107,956,027</u>

NOTE: The Internal Revenue Service has completed its audits of the consolidated income tax returns filed on behalf of the Company for the years 1995 and 1996. All material adjustments, if any, made subsequent to the date of examination and arising from said audits, are reflected in the financial statements included in this report. Audits covering tax years 1997 and 1998 are currently in progress, while the audit covering tax year 1999 have yet to commence. The examiner is unaware of any potential exposure of the Company to any further tax assessment and no liability had been established herein relative to such contingency.

B. Underwriting and Investment Exhibit

Surplus as regards policyholders increased \$26,647,024 during the four-year examination period, January 1, 1995 to December 31, 1998, detailed as follows:

Statement of Income

Underwriting Income

Premiums earned		\$159,955,226
Deductions:		
Losses incurred	\$97,589,821	
Loss adjustment expenses incurred	32,559,787	
Other underwriting expenses incurred	<u>62,245,627</u>	
Total underwriting deductions		<u>192,395,235</u>
Net underwriting income		\$(32,440,009)

Investment Income

Net investment income earned	\$24,187,118	
Net realized capital gains	<u>3,679,326</u>	
Net investment gain		27,866,444

Other Income

Miscellaneous income	\$48,692,655	
Agents' balances charged off	<u>(989,887)</u>	
Total other income		<u>47,702,768</u>
Net income before federal income taxes		\$43,129,203
Federal income taxes incurred		<u>14,459,517</u>
Net income		<u>\$28,669,686</u>

Capital and Surplus Account

Surplus as regards policyholders December 31, 1994,
per report on examination \$25,760,049

	<u>Gains in Surplus</u>	<u>Losses in Surplus</u>	
Net income	\$28,669,686		
Change in not-admitted assets	462,420		
Change in provision for reinsurance	626,913		
Change in excess of statutory reserves over statement reserves	11,000		
Surplus paid-in	20,077,005		
Dividends to Stockholders	<u> </u>	<u>\$23,200,000</u>	
Total gains and losses	<u>\$49,847,024</u>	<u>\$23,200,000</u>	
Increase in surplus			<u>26,647,024</u>
Surplus as regards policyholders December 31, 1998, per report on examination			<u>\$52,407,073</u>

Summary of Surplus as Regards Policyholders

	<u>December 31, 1994</u>	<u>December 31, 1998</u>	<u>Change</u>
Capital paid in	\$7,912,500	\$7,912,500	
Gross paid in and contributed surplus	15,173,748	35,250,753	\$20,077,005
Unassigned funds (surplus)	<u>2,673,801</u>	<u>9,243,820</u>	<u>6,570,019</u>
Surplus as regards policyholders	<u>\$25,760,049</u>	<u>\$52,407,073</u>	<u>\$26,647,024</u>

4. LOSSES AND LOSS ADJUSTMENT EXPENSES

The examination liabilities for the above captioned accounts totaling \$19,218,900 and \$12,947,189 respectively, are the same as the amounts reported by the Company in its December 31, 1998 filed annual statement. The examination analysis was conducted in accordance with generally accepted actuarial principles and was based on statistical information contained in the Company's internal records and in its filed statements.

5. COMPLIANCE WITH PRIOR REPORT ON EXAMINATION

The prior report on examination contained the following recommendation as follows (page numbers refer to the prior report on examination):

<u>ITEM NO.</u>	<u>PAGE NO.</u>
1. <u>Execution of Reinsurance Contracts</u>	
It was recommended that the Company, within a reasonable length of time subsequent to effective date, maintain fully executed reinsurance contracts within its files.	11
The Company has complied with this recommendation.	
2. <u>Named Reinsureds</u>	
It was recommended that each reinsured be named individually within all reinsurance contracts.	11
The Company has not complied with this recommendation. However, due to the termination of the respective agreements this recommendation does not need to be repeated herein.	

<u>ITEM</u>	<u>PAGE NO.</u>
3. <u>Offset Clauses</u>	
It is recommended that all reinsurance contracts which contain broad offset clauses make specific reference to Section 7427 of the New York Insurance Law.	11
The Company has complied with this recommendation.	
4. <u>Trust Account Agreement</u>	
The following was recommended relative to the Company's Trust Account Agreement:	
a. It was recommended that the Company, as well as all other participating affiliates be specifically named in the applicable reinsurance and trust agreements.	12
b. It was recommended that said reinsurance and trust agreement be fully executed.	12
c. It was recommended that the trust agreement contain the provisions outlined in Department Regulation 114, Part 126.	12
The Company has complied with all of the recommendations of this section.	
5. <u>Affiliated Agreement Allocation of Federal Income Taxes</u>	
It was recommended that the Company include within the aforementioned agreement the appropriate provisions outlined in Department Circular Letter 33(1979) and that said amended agreement be submitted to this Department for approval pursuant to Section 1505(d) of the New York Insurance Law.	16
The Company has not complied with this recommendation and this recommendation is repeated herein.	

ITEM NO.PAGE NO.6. Internal Controls

The following recommendations are made relative to the Company's EDP Operations:

- | | | |
|----|---|----|
| a. | It was recommended that the disaster recovery plan listing of contract persons be periodically updated and that all internal contact and secondary contact person positions be filled by current Progressive Group employees. | 19 |
| b. | It was recommended that the Company maintain systems design and programming standards manuals. | 19 |
| c. | It was recommended that the Company include within its on-line claims network system controls which would prevent the possible inadvertent changing or deletion of data. | 19 |

The Company has complied with all of the recommendations of this section.

7. Securities' Custodial Agreement

The following recommendations are made relative to the Company's custodial agreement:

- | | | |
|----|--|----|
| a. | It was recommended that written instructions and/or confirmation of instructions relative to "any other means" transfers and transactions be signed by any two persons authorized by the Company. Such persons are to be specified in a listing to be furnished to the bank from time to time, signed by the Company's treasurer or assistant treasurer, and certified under the corporate seal by its secretary or assistant secretary. | 20 |
| b. | Specific "other means" (as described in the agreement) transfer limitations, as established by the Company's board of directors, should be included within the custodial agreement. Said limitations should include specified accounts to which said transfers could be made and specific amount limitations. | 20 |

The Company has not complied with any of the recommendations in this section and both recommendations are repeated herein.

ITEM NO.PAGE NO.8. Expense Allocation

It was recommended that the Company analyze its expenses in accordance with Department Regulation 30 and properly allocate amounts to the underwriting, loss adjustment and investment functions. In this regard, it is recommended that the Company allocate its expenses to expense items in accordance with Regulation 30. 21

The Company has complied with this recommendation.

9. Uncollected Premiums

It was recommended that the Company properly segregate premiums receivable between those that are in course of collection and those that are booked but deferred and not yet due when reporting this asset in future statement filings. 21

The Company has complied with this recommendation.

10. State Plan Liability

It was recommended that the Company report residual market premiums under the appropriate caption in future statement filings. 22

The Company has not complied with this recommendation and this recommendation is repeated herein.

11. Letters of Credit

The following was recommended in regards to the Company's letters of credit:

a. It was recommended that the Company be specifically named as beneficiary on all applicable letters of credit. 27

b. It was recommended that said letters of credit contain all the requirements for acceptable letters of credit as specified in Regulation 133, Part 79.1. 27

The Company has not complied with all the recommendations. However, due to an immaterial amount and runoff status, these recommendations are not repeated herein.

<u>ITEM NO.</u>	<u>PAGE NO.</u>
11. <u>Policy Forms</u>	
It was recommended that the Company comply with Section 2307(b) of the New York Insurance Law and obtain Department approval prior to use relative to all issued policy forms within the State of New York.	28
The Company has complied with this recommendation.	
12. <u>Mandatory Inspections of Private Passenger Automobiles</u>	
Pursuant to Regulation 79, Part 67(c)(1) & (2), it was recommended that documentation of verbal notice relative to mandatory inspection site location, the consequences of the insured's failure to obtain a timely inspection, the name of the person giving the notice and the identity of the site(s) provided be contained in the insured's policy records.	29
The Company has complied with this recommendation.	
13. <u>Claims Handling</u>	
Pursuant to Regulation 64, Part 216.4(c) and Circular Letter No. 11 (1978), it was recommended that the Company designate and furnish to the Superintendent of Insurance the name and title of the corporate officer responsible for its internal department specifically designated to investigate and resolve complaints filed with the New York Insurance Department.	29
The Company has not complied with this recommendation and this recommendation is repeated herein.	
14. <u>Subsequent Events</u>	
A plan for the de-pooling of the Company from the Progressive Group pool effective January 1, 1996 and other transactions was confirmed by this Department on September 10, 1995. Details of said de-pooling and other transactions are included in Item 7 of this report.	30

6. SUMMARY OF COMMENTS AND RECOMMENDATIONS

<u>ITEM</u>	<u>PAGE NO.</u>
A. <u>Reinsurance</u>	
i. It is recommended that the Company amend its reinsurance contracts to be governed under the Laws of New York State, its state of domicile.	10
ii. It is recommended that the Company amend the arbitration clauses contained in its reinsurance contracts to require that the seat for arbitration shall be in New York State, its state of domicile.	10
B. <u>Allocation of Federal Income Tax Agreement</u>	
It is again recommended that the Company amend this agreement to comply with the provisions set forth in Department Circular Letter No. 33 (1979) and that said amended agreement be submitted to the Department for approval in accordance with Section 1505(d) of the New York Insurance Law.	16
C. <u>Accounts and Records</u>	
i. It is recommended that the Company amend its custodial agreement to include the protective covenants and provisions which meet the guidelines established by the Department for the contents of such agreements.	17
ii. It is recommended that the custodial agreement be amended to contain the aforementioned provision.	17
iii. It is again recommended that the Company's board of directors establish limitations as to the amount of funds that can be transferred via the methods described above, as well as specify those accounts to which funds could be transferred.	17
iv. It is again recommended that the Company properly report residual market premiums under the appropriate caption in future annual statement filings.	18
v. It is again recommended that the Company comply with Regulation 64, Part 216.4(c) and Circular Letter No. 11 (1978).	18

STATE OF NEW YORK
INSURANCE DEPARTMENT

I, NEIL D. LEVIN, Superintendent of Insurance of the State of New York,
pursuant to the provisions of the Insurance Law, do hereby appoint:

Gilbert Denton

as proper person to examine into the affairs of the

National Continental Insurance Company

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

Company

with such other information as he shall deem requisite.

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

this 29th day of August, 2000




NEIL D. LEVIN
Superintendent of Insurance