REPORT ON EXAMINATION

OF

NATIONAL CONTINENTAL INSURANCE COMPANY

AS OF

DECEMBER 31, 2017

DATE OF REPORT	APRIL 16, 2019
EXAMINER	SHEIK H. MOHAMED

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June 28, 2019

Honorable Linda A. Lacewell
Superintendent
New York State Department of Financial Services
Albany, New York 12257

Madam:

Pursuant to the requirements of the New York Insurance Law, and in compliance with the instructions contained in Appointment Number 31698 dated December 27, 2017, attached hereto, I have made an examination into the condition and affairs of National Continental Insurance Company as of December 31, 2017, and submit the following report thereon.

Wherever the designation "the Company" appears herein without qualification, it should be understood to indicate National Continental 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 6300 Wilson Mills Road, Cleveland, OH 44143.

1. SCOPE OF EXAMINATION

The Department has performed an examination of the Company, a multi-state insurer. The previous examination was conducted as of December 31, 2012. This examination covered the five-year period from January 1, 2013 through December 31, 2017. Transactions occurring subsequent to this period were reviewed where deemed appropriate by the examiner.

The examination was conducted in conjunction with the State of Ohio, which was the lead state of the Progressive Group. The examination was performed concurrently with the examinations of the following insurers:

Company	State of Domicile
American Strategic Insurance Corp.	Florida
ASI Lloyds	Texas
ASI Assurance Corp.	Florida
ASI Select Insurance Corp.	Delaware
ASI Preferred Insurance Corp.	Florida
ASI Home Insurance Corp.	Florida
ASI Select Auto Insurance Corp.	California
Artisan and Truckers Casualty Company	Wisconsin
Blue Hill Specialty Insurance Company Inc.	Illinois
Drive New Jersey Insurance Company	New Jersey
Mountain Laurel Assurance Company	Ohio
Progressive Advanced Insurance Company	Ohio
Progressive American Insurance Company	Ohio
Progressive Bayside Insurance Company	Ohio
Progressive Casualty Insurance Company	Ohio
Progressive Choice Insurance Company	Ohio
Progressive Classic Insurance Company	Wisconsin
Progressive Commercial Casualty Company	Ohio
Progressive County Mutual Insurance Company	Texas
Progressive Direct Insurance Company	Ohio
Progressive Express Insurance Company	Ohio
Progressive Freedom Insurance Company	Ohio
Progressive Garden State Insurance Company	New Jersey
Progressive Gulf Insurance Company	Ohio
Progressive Hawaii Insurance Corp.	Ohio
Progressive Marathon Insurance Company	Michigan
Progressive Max Insurance Company	Ohio
Progressive Michigan Insurance Company	Michigan
Progressive Mountain Insurance Company	Ohio
Progressive Northern Insurance Company	Wisconsin

Company	State of Domicile
Progressive Northwestern Insurance Company	Ohio
Progressive Paloverde Insurance Company	Indiana
Progressive Preferred Insurance Company	Ohio
Progressive Premier Insurance Company of Illinois	Ohio
Progressive Property Insurance Company	Florida
Progressive Security Insurance Company	Louisiana
Progressive Select Insurance Company	Ohio
Progressive Southeastern Insurance Company	Indiana
Progressive Specialty Insurance Company	Ohio
Progressive Universal Insurance Company	Wisconsin
Progressive West Insurance Company	Ohio
United Financial Casualty Company	Ohio

Other states participating in this examination were California, Delaware, Florida, Illinois, Indiana, Louisiana, Michigan, New Jersey, Texas and Wisconsin.

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 current and 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 New York laws, statutory accounting principles, and annual statement instructions.

This examination report includes, but is not limited to, the following:

Company history
Management and control
Territory and plan of operation
Holding company description
Reinsurance
Financial statement presentation
Loss review and analysis
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 under the laws of the State of New York as a stock fire insurer on December 24, 1897 as the Caledonian-American Insurance Company. It became licensed on March 24, 1898 and commenced business on the same date. In 1958, the Company was acquired by Rathbone, King and Seeley, Inc., and its name was changed to American Star Insurance Company. In 1981, the stock of Rathbone, King and Seeley, Inc. was acquired by the Seibels Bruce Group, Inc.

In November 1985, financial control of the Company was acquired by The Progressive Corporation ("TPC"), a publicly-traded holding company, and the Company's name was changed to its current title. The Company is wholly-owned by Progressive Commercial Holdings, Inc., a Delaware holding company, which is in turn wholly-owned by TPC.

A. Corporate Governance

Pursuant to the Company's charter, management of the Company is vested in a board of directors consisting of nine members. At December 31, 2017, the board of directors was comprised of the following members:

Name and Residence	Principal Business Affiliation
Patricia O. Bemer Highland Heights, OH	Senior Human Resources Business Leader, The Progressive Corporation
Michael R. Beney Camillus, NY	Manager Claims Process, The Progressive Corporation
Michael W. Bissler Munson Township, OH	Senior Controller, The Progressive Corporation
Brian D. Courtney Concord Township, OH	Business Leader Commercial Automobile Insurance Plans, The Progressive Corporation
Thomas W. Flynn Smithtown, NY	Director Casualty, The Progressive Corporation
Jeanette L. Hisek Twinsburg, OH	Business Leader Commercial Lines, Regional Marketing, The Progressive Corporation

Name and Residence	Principal Business Affiliation
William R. Kampf Moreland Hills, OH	General Manager Small Business Insurance, The Progressive Corporation
Kevin P. Maher Westlake, OH	Business Leader Commercial Lines Operations, The Progressive Corporation
Christopher J. Rosati Shoreham, NY	Director Claims, The Progressive Corporation

During the period under examination, the board of directors held no annual board meetings. Instead, the Company made all its decisions through written consent with the approval/signature of all board members. These actions are contrary to the Company's by-laws, which state, in part:

> "A meeting of the board of directors shall be held in the month of March in each year following the annual meeting of stockholders, at such time and place of such meeting …"

It is recommended that the Company comply with its by-laws and hold annual meetings of its board of directors, or amend its by-laws to give the board of directors the option to act by unanimous consent in lieu of a meeting, if they so choose.

As of December 31, 2017, the principal officers of the Company were as follows:

Name	Title
Brian D. Courtney	President
Patricia M. Corwin	Secretary
Michael W. Bissler	Treasurer
Patricia O. Bemer	Vice President
Kevin P. Maher	Vice President
Sandra L. Rihvalsky	Vice President
Margaret A. Rose	Assistant Secretary

B. Territory and Plan of Operation

As of December 31, 2017, the Company was licensed to write business in all 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:

Paragraph	Line of Business
3	Accident & health
4	Fire
5	Miscellaneous property
6	Water damage
7	Burglary and theft
8	Glass
9	Boiler and machinery
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
26(A)	Motor vehicle lessor/creditor gap insurance
26(B)	Motor vehicle lessee/debtor gap insurance

The Company may also write such workers' compensation insurance as may be incidental to coverage contemplated under paragraphs 20 and 21 of Section 1113(a) of the New York Insurance Law including insurance described in the Longshoremen's and Harbor Workers' Compensation Act (Public Law No. 803, 69th Congress as amended; 33 USC Section 901 et seq. as amended).

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, the Company is required to maintain a minimum surplus to policyholders in the amount of $2,950,000.

The following schedule shows the direct and net premiums written by the Company for the period under examination:

Calendar Year	Direct Premiums Written	Net Premiums Written
2013	$ 62,781,098	$ 18,650,058
2014	$ 73,289,844	$ 16,912,073
2015	$ 93,327,827	$ 14,599,984
2016	$102,514,871	$ 13,290,559
2017	$122,512,358	$ 12,158,175

The Company did not assume any business during the examination period.

The Company has two business segments as follows:

1. The commercial lines insurance segment under which the Company assumes underwriting risk.
2. The service provider segment under which the Company retains no underwriting risk.

The commercial lines business consists primarily of liability, physical damage, and other auto-related insurance for automobiles and trucks owned by small businesses. The business is generated by independent insurance agencies.

The service provider segment consists of policy issuance and claim adjusting services. The Company places risks on its paper for Commercial Automobile Insurance Plans ("CAIP"), Special Risk Distribution Programs ("SRDP"), and the state-mandated voluntary New Jersey Special Automobile Insurance Plan ("SAIP"). CAIP and SRDP are state supervised plans serving the involuntary market in Massachusetts and New Jersey. The Company retains no underwriting risk in the service provider segment, as the ultimate payment obligations under these policies belong to the various state plans. However, the Company does have counterparty risk. The Company receives fee revenue for the underwriting and claims services it performs for these state plans.

C. Reinsurance Ceded

At December 31, 2017, the Company participated in 41 CAIPs, two SRDPs, and one SAIP. As part of these plans, the Company cedes 100% of its premiums and losses related to these plans, and in return, receives a fee for its policy issuance and claims adjustment services.

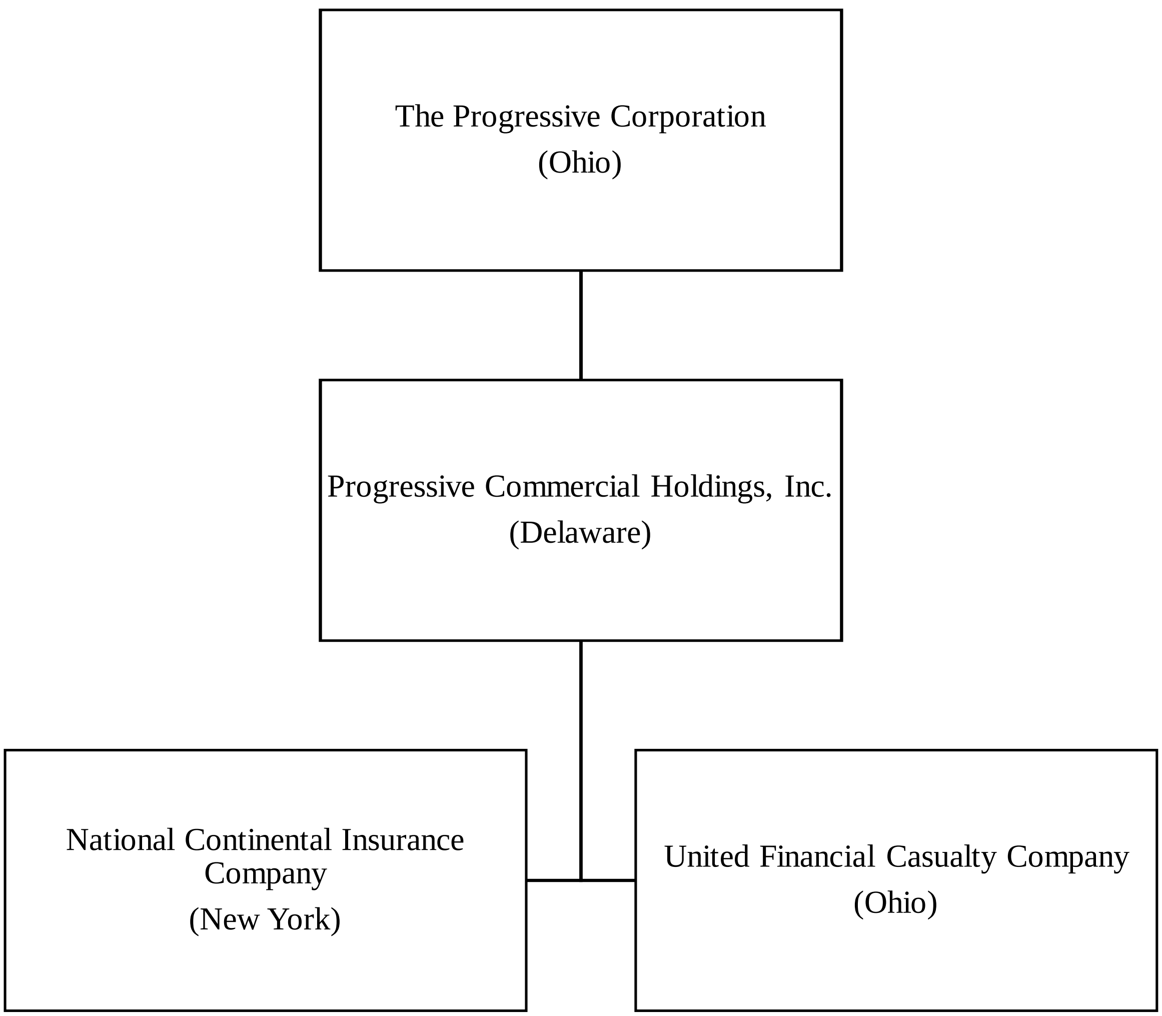
Examination review found that the Schedule F data reported by the Company in its filed annual statement accurately reflected its reinsurance transactions. Representations were supported by a reinsurance attestation from the Company's President and Treasurer. Additionally, examination review indicated that the Company was not a party to any finite reinsurance agreements.

D. Holding Company System

The Company is a member of the Progressive Group. The Company is wholly-owned by Progressive Commercial Holdings, Inc., a Delaware holding company, which is ultimately controlled by TPC, a publicly-traded holding company incorporated in Ohio. TPC, through its insurance subsidiaries, provides personal and commercial auto insurance, residential property insurance, and other specialty property and casualty insurance.

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, 2017:



Holding Company Agreements

At December 31, 2017, the Company was party to the following agreements with other members of its holding company system:

Cost Allocation Agreement

Effective January 1, 2005, the Company entered into a service agreement with United Financial Casualty Company ("UFCC"). Pursuant to the agreement, the Company utilizes the personnel, property and facilities of UFCC. UFCC also provides services relating to the insurance operations, including administrative and record keeping for the Company. The Company reimburses UFCC 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. The agreement was filed with this Department pursuant to Section 1505 of the New York Insurance Law. In 2017, a net amount of $22,355,242 was charged to the Company for services provided pursuant to the agreement.

Tax Allocation Agreement

Effective August 1, 2005, the Company and other members of its holding company system entered into an income tax sharing agreement with The Progressive Corporation, whereby the companies file a consolidated federal income tax return. The agreement was filed with this Department pursuant to Section 1505 of the New York Insurance Law.

The Company was also party to the following agreements which were not significant or not in use:

- Cash management agreement between the Company, Progressive Casualty Insurance Company and their affiliates;
- Interest agreement between the Company and its affiliates;
- Investment services agreement between the Company, Progressive Capital Management and their affiliates;
- Trademark and prorater plus license agreement between the Company, Progressive Casualty Insurance Company, Progressive American Insurance Company and The Progressive Corporation;
- General agency agreement between the Company, Progny Agency, Inc., Progressive Casualty Insurance Company, Progressive Northern Insurance Company, Progressive Northwestern Insurance Company, Progressive Specialty Insurance Company and United Financial Casualty Company;

- General agency agreement between the Company, Progressive Specialty Insurance Agency, Inc., Artisan and Truckers Casualty Company, Progressive Express Insurance Company, and United Financial Casualty Company;

- Non-exclusive patent licensing agreement between the Company, Progressive Casualty Insurance Company and their affiliates;

- Escrow agreement between the Company, The Progressive Corporation and Progressive Investment Company, Inc.;

- Agreement for periodic settlement of guaranty association amounts between the Company and Drive New Jersey Insurance Company; and

- Licensing agreement between the Company, Progressive Casualty Insurance Company and their affiliates.

E. Significant Ratios

The Company's operating ratios, computed as of December 31, 2017, fall within the benchmark ranges set forth in the Insurance Regulatory Information System of the NAIC.

Operating Ratios	Result
Net premiums written to policyholders' surplus	19%
Adjusted liabilities to liquid assets	78%
Two-year overall operating	0%

Underwriting Ratios

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

	Amounts	Ratios
Losses and loss adjustment expenses incurred	$ 89,585,707	76.84%
Other underwriting expenses incurred	77,550,967	66.51
Net underwriting gain (loss)	(50,543,862)	(43.35)
Premiums earned	$116,592,812	100.00%

The Company's reported risk-based capital score ("RBC") was 397.8% at December 31, 2017. The RBC is a measure of the minimum amount of capital appropriate for a reporting entity to support its overall business operations in consideration of its size and risk profile. An RBC of 200 or below can result in regulatory action. There were no financial adjustments in this report that impacted the Company's RBC score.

F. Accounts and Records

In 2017, the Company provided policy issuance and claim adjusting services to forty-one CAIPs, two SRDPs and one SAIP. The Company currently records the loss adjustment expenses and underwriting expenses associated with this business in the Statement of Income "underwriting income section" while reporting the fee revenue in the "other income section". This has resulted in a distortion of the Company's underwriting income with consistent underwriting losses given the inclusion of expenses not associated with the premiums earned. The expenses associated with generating fee revenue should not be included in the underwriting income section, as these expenses are not associated with an underwriting risk for which the Company has reported premiums earned.

Section 1610(a) of the New York Insurance Law allows a company to engage directly in ancillary business. Specifically, Section 1610(a) states, in part:

> "A domestic insurance company subject to this article may, provided that it maintains its books and records which separately accounts for such business, engage directly..."

Statutory accounting principles are designed to address the concerns of regulators. The NAIC Accounting Practices and Procedures Manual, Statements of Statutory Accounting Principles ("SSAP") currently do not specifically address profits or losses on ancillary business. However, it is noted that International Financial Reporting Standard 8, in addressing required disclosures relating to business segments, identifies information about the profit or loss of each business segment. The segment reporting requirements under International Financial Reporting Standards are essentially identical to the requirements noted under U.S. Generally Accepted Accounting Principles.

It is recommended that the Company allocate the expenses associated with the fee revenue from its service provider segment to the Statement of Income other income section, thereby allowing the reader a fair presentation on the financial performance of each segment, as well as a more accurate value of the Company’s combined ratio and other NAIC scoring system ratios.

3. FINANCIAL STATEMENTS

A. Balance Sheet

The following shows the assets, liabilities and surplus as regards policyholders as of December 31, 2017, as reported by the Company:

Assets	Assets	Assets Not Admitted	Net Admitted Assets
Bonds	$ 69,809,968	$ 0	$ 69,809,968
Cash, cash equivalents and short-term investments	4,399,682	0	4,399,682
Receivables for securities	7,000	0	7,000
Investment income due and accrued	349,857	0	349,857
Uncollected premiums and agents' balances in the course of collection	11,509,305	66,232	11,443,073
Deferred premiums, agents' balances and installments booked but deferred and not yet due	13,897,930	0	13,897,930
Amounts recoverable from reinsurers	25,561,310	0	25,561,310
Net deferred tax asset	438,982	7,435	431,547
Receivables from parent, subsidiaries and affiliates	6,028,898	0	6,028,898
New Jersey SAIP service carrier receivable	2,061,126	0	2,061,126
Alaska CAIP receivable	740,445	0	740,445
PLIGA receivable	275,449	0	275,449
PLIGA unearned surcharge recoverable	14,502	0	14,502
Prepaid expenses	39,638	39,638	0
Total assets	$135,134,092	$113,305	$135,020,787

Liabilities, Surplus and Other Funds

Liabilities		
Losses and loss adjustment expenses		$ 25,287,350
Commissions payable, contingent commissions and other similar charges		1,869
Other expenses (excluding taxes, licenses and fees)		39,003
Taxes, licenses and fees (excluding federal and foreign income taxes)		958,708
Current federal and foreign income taxes		1,661,556
Unearned premiums		6,138,483
Advance premium		45,590
Ceded reinsurance premiums payable (net of ceding commissions)		19,999,273
Provision for reinsurance		24,800
Drafts outstanding		5,616,625
Unearned fee revenue		9,552,840
State plan liability		2,836,858
PLIGA payable		127,129
Escheatable property		35,524
PLIGA unearned surcharge payable		14,502
Other liabilities		6,505
Total liabilities		$ 72,346,615
Surplus and Other Funds		
Common capital stock	$ 6,429,106	
Gross paid in and contributed surplus	29,542,125	
Unassigned funds (surplus)	26,702,941	
Surplus as regards policyholders		62,674,172
Total liabilities, surplus and other funds		$135,020,787

Note: The Internal Revenue Service has completed its audits of the Company's consolidated federal income tax returns through tax year 2016. 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 2017 and 2018 are currently under examination. 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

The net income for the examination period as reported by the Company was $67,803,264 as detailed below:

Underwriting Income		
Premiums earned		$116,592,812
Deductions:		
Losses and loss adjustment expenses incurred	$89,585,707	
Other underwriting expenses incurred	77,550,967	
Total underwriting deductions		167,136,674
Net underwriting gain or (loss)		$(50,543,862)
Investment Income		
Net investment income earned	$12,037,031	
Net realized capital gain	1,884,606	
Net investment gain or (loss)		13,921,637
Other Income		
Net gain or (loss) from agents' or premium balances charged off	$ (1,708,338)	
Finance and service charges not included in premiums	1,440,033	
Service business revenue	130,434,006	
Interest income on intercompany balances	72,160	
Miscellaneous other (expense) income	(9,938)	
Income from transferable state tax credit	11,875	
Total other income		130,239,798
Net income before federal income taxes		$ 93,617,573
Federal income taxes incurred		25,814,309
Net income		$ 67,803,264

C. Capital and Surplus

Surplus as regards policyholders increased $17,621,838 during the five-year examination period January 1, 2013 through December 31, 2017, as reported by the Company, detailed as follows:

Surplus as regards policyholders as reported by the Company as of December 31, 2012			$45,052,334
	Gains in Surplus	Losses in Surplus	
Net income	$67,803,264		
Change in net deferred income tax		$ 4,992,119	
Change in nonadmitted assets	835,493		
Change in provision for reinsurance		24,800	
Dividends to stockholders	0	46,000,000	
Total gains and losses	$68,638,757	$51,016,919	
Net increase (decrease) in surplus			17,621,838
Surplus as regards policyholders as reported by the Company as of December 31, 2017			$62,674,172

Capital paid in is $6,429,075 consisting of 257,163 shares of $25 par value per share common stock. Gross paid in and contributed surplus is $29,542,125. Gross paid in and contributed surplus did not change during the examination period.

4. LOSSES AND LOSS ADJUSTMENT EXPENSES

The examination liability for the captioned items of $25,287,350 is the same as reported by the Company as of December 31, 2017. The examination analysis of the loss and loss adjustment expense reserves was conducted in accordance with generally accepted actuarial principles and statutory accounting principles, including SSAP No. 55. The Company’s reserve is concentrated in the commercial automobile liability line of business.

5. COMPLIANCE WITH PRIOR REPORT ON EXAMINATION

The prior report on examination contained no comments or recommendations.

6. SUMMARY OF COMMENTS AND RECOMMENDATIONS

ITEM		PAGE NO.
A.	Corporate Governance	
	It is recommended that the Company comply with its by-laws and hold annual meetings of its board of directors, or amend its by-laws to give the board of directors the option to act by unanimous consent in lieu of a meeting, if they so choose.	5
B.	Accounts and Records	
	It is recommended that the Company allocate the expenses associated with the fee revenue from its service provider segment to the Statement of Income other income section, thereby allowing the reader a fair presentation on the financial performance of each segment, as well as a more accurate value of the Company’s combined ratio and other NAIC scoring system ratios.	11

Respectfully submitted,

____________/S/___________
Sheik H. Mohamed,
Associate Insurance Examiner

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

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

____________/S/___________
Sheik H. Mohamed

Subscribed and sworn to before me

this_________ day of __________________, 2019.

APPOINTMENT NO. 31698

NEW YORK STATE

DEPARTMENT OF FINANCIAL SERVICES

*I, **Maria T. Vullo**, 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:*

Sheik Mohamed

as a proper person to examine the affairs of the

National Continental 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 27th day of December, 2017

MARIA T. VULLO
Superintendent of Financial Services

By:

Joan Riddell
Deputy Bureau Chief