

Report of Examination of

**Infinity Preferred Insurance Company**  
Cincinnati, Ohio

As of December 31, 2011

## Table of Contents

<b>Subject</b>	<b>Page</b>
Salutation.....	1
Description of Company .....	1
Scope of Examination .....	1
Management and Control:	
Board of Directors.....	2
Officers.....	2
Insurance Holding Company System.....	3
Territory and Plan of Operations.....	3
Reinsurance:	
Intercompany Pooling Agreement .....	3
External Reinsurance Ceded .....	4
Significant Operating Results .....	5
Financial Statements:	
Statement of Assets, Liabilities, Surplus and Other Funds.....	6
Statement of Income .....	7
Statement of Changes in the Capital and Surplus Account.....	8
Notes to Financial Statements:	
Investments .....	8
Loss and Loss Adjustment Expense Reserves .....	8
Conclusion.....	9
Subsequent Events .....	9
Acknowledgement.....	9

Columbus, Ohio  
November 30, 2012

Honorable Mary Taylor  
Lt. Governor/Director  
State of Ohio  
Department of Insurance  
50 West Town Street  
3<sup>rd</sup> Floor – Suite 300  
Columbus, Ohio 43215

Dear Madam:

In accordance with Section 3901.07 of the Ohio Revised Code (“ORC”), the Ohio Department of Insurance (“Department”) conducted an examination of

**Infinity Preferred Insurance Company**

an Ohio domiciled, stock, property and casualty insurance company, hereinafter referred to as the “Company.”

**Scope of Examination**

The Department last examined the Company as of December 31, 2006. The Department’s current examination covers the period of January 1, 2007 to and including December 31, 2011.

Representatives of the Indiana Department of Insurance, as the coordinating state regulator of the insurance company affiliates of Infinity Property and Casualty Corporation, led the multi-state coordinated examination that included representatives from the states of Indiana, Ohio, and Texas. The examination was conducted in accordance with the National Association of Insurance Commissioners (“NAIC”) Financial Condition Examiners Handbook (“Handbook”). The Handbook requires that the Department plan and perform the examination to evaluate the Company’s financial condition and identify prospective risks including corporate governance, identify and assess inherent risks, and evaluate system controls and procedures used to mitigate those risks. An 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 accounts and activities of the Company were considered in accordance with the risk-focused examination process.

For all years under examination, the Certified Public Accounting firm of Ernst & Young LLP provided an unqualified opinion on the Company’s financial statements based on Statutory Accounting Principles. The audited financial reports were reviewed during the examination.

## Management and Control

### Board of Directors

Management of the Company is vested in its Board of Directors, which was comprised of the following members as of the examination date:

<b><u>Name</u></b>	<b><u>Principal Occupation</u></b>
James R. Gober	Chairman of the Board, President, and Chief Executive Officer, Infinity Property and Casualty Corporation
Glen N. Godwin	Senior Vice President – Business Development, Infinity Insurance Companies
Scott C. Pitrone	Senior Vice President – Product Management, Infinity Insurance Companies
Roger H. Prestridge	Vice President and Controller, Infinity Insurance Companies
Samuel J. Simon	Executive Vice President, General Counsel, Assistant Secretary, and Director, Infinity Property and Casualty Corporation
Roger Smith	Executive Vice President, Chief Financial Officer, Treasurer, and Director, Infinity Property and Casualty Corporation
Shelia H. Williams	Vice President – Human Resources, Infinity Insurance Companies

### Officers

As of the examination date, the following officers were serving in the designated position:

<b>Name</b>	<b>Title</b>
Glen N. Godwin	President and Chief Executive Officer
Mary L. Clark	Assistant Treasurer

Samuel J. Simon	Senior Vice President and Secretary
Roger H. Prestridge	Vice President and Treasurer
Roger Smith	Senior Vice President and Chief Financial Officer
James H. Romaker	Assistant Secretary
Troy P. Ballard	Assistant Treasurer
Shelia H. Williams	Vice President
Mitchell Silverman	Assistant Secretary
Vicki W. Daniell	Assistant Treasurer

### **Insurance Holding Company System**

The Company is a member of a holding company system as defined under Section 3901.32 of the ORC. The Company is wholly owned by Infinity Insurance Company (“IIC”), an Indiana domiciled insurance company. IIC is wholly owned by Infinity Property and Casualty Corporation, an Ohio domiciled holding company that, through its subsidiaries, provides personal automobile insurance with a concentration on nonstandard auto insurance.

### **Territory and Plan of Operations**

The Company is licensed to operate in the states of Ohio, Pennsylvania, and South Carolina. The Company is a part of the Infinity Insurance Group (“Group”) which provides personal automobile insurance nationwide with a concentration in nonstandard private passenger auto insurance. The Group markets its insurance products using a network of approximately 12,900 independent agents and brokers. While the Group does offer commercial auto and classic collector coverage, these products represented only 6% and 1% of gross written premiums for 2011, respectively. The remaining 93% of gross writings represents the private passenger auto market. Overall, the Group estimates that 76% of their personal auto insurance is concentrated in nonstandard personal auto coverage.

### **Reinsurance**

#### **Intercompany Pooling Agreement**

The Company is a member of the Group and participates in an inter-company reinsurance pool for which IIC acts as the lead pool reinsurer.

The pooling process is comprised of three steps. First, each company directly or indirectly cedes 100% of their direct and assumed business to IIC pursuant to the pooling agreement. In 2011 the Company ceded premiums totaling \$0.4 million and case loss and expense reserves totaling \$1.1 million to IIC in connection with pooling transactions.

Second, IIC then cedes excess of loss and catastrophe reinsurance to a group of unrelated open market reinsurers (external reinsurance) and various state-operated residual market reinsurance facilities. Any uncollected external reinsurance balances are ultimately shared amongst all pool members in proportion to each member's designated pooling percentage.

Third, in its capacity as lead pool insurer, IIC then cedes (or retrocedes) back to each participating pool member a specified percentage of the combined "pool" in accordance with each member's applicable pooling percentage. At December 31, 2011 IIC retained 98.8% of the total pool and ceded 1/10<sup>th</sup> of 1% (one-tenth of one percent) to each of twelve remaining pool members as shown below. In 2011 IIC ceded premiums totaling \$1.1 million to each remaining pool member and reported total reinsurance recoverables (consisting of paid, outstanding and IBNR loss and LAE reserves plus unearned premiums) of \$1.0 million due from each remaining pool member identified below.

<u>Company Name</u>	<u>Percentage</u>	
	<u>2011</u>	<u>2010</u>
Infinity Insurance Company (IN)	98.8%	98.6%
Infinity Assurance Insurance Company (OH)	0.1%	0.1%
Infinity Auto Insurance Company (OH)	0.1%	0.1%
Infinity Casualty Insurance Company (OH)	0.1%	0.1%
Infinity General Insurance Company (OH)	-	0.1%
Infinity Indemnity Insurance Company (IN)	0.1%	0.1%
Hillstar Insurance Company (IN)	0.1%	0.1%
Infinity Preferred Insurance Company (OH)	0.1%	0.1%
Infinity Premier Insurance Company (IN)	0.1%	0.1%
Infinity Reserve Insurance Company (OH)	0.1%	0.1%
Infinity Safeguard Insurance Company (OH)	0.1%	0.1%
Infinity Security Insurance Company (IN)	0.1%	0.1%
Infinity Select Insurance Company (IN)	0.1%	0.1%
Infinity Specialty Insurance Company (OH)	-	0.1%
Infinity Standard Insurance Company (IN)	<u>0.1%</u>	<u>0.1%</u>
Combined Group Totals	<u>100.0%</u>	<u>100.0%</u>

In addition to the above listed companies, one other affiliate, Infinity County Mutual Insurance Company (TX), cedes 100% of its business to IIC, but does not reassume any share of the combined pool results. IIC, in turn cedes all but a minor portion of its direct and assumed business to other pool companies where it is combined with other business in the Infinity Pool.

#### **External Reinsurance Ceded**

As noted above, IIC, as lead pool reinsurer, maintains a comprehensive "corporate" reinsurance program designed to limit both per-risk and catastrophe exposures to acceptable limits. The primary contracts and limits placed in this regard are as follows:

- Private passenger auto excess of loss - \$900k x/s \$100k – This contract was terminated in 2008 and is currently in run off servicing losses only.

- Commercial auto excess of loss - \$700k x/s \$300k
- Property (auto comprehensive) catastrophe excess of loss - \$15 million x/s \$5 million
- Contingency clash and excess of loss - \$10 million x/s \$5 million

These treaties are placed on behalf of all members of the Group by IIC in their capacity as lead pool reinsurer. The cost of each treaty is deducted from the combined pooled premium and the residual ceded to each pool member in proportion to their designated pool share.

### Significant Operating Results

The Company reported the following net underwriting results during the examination period, reported in thousands.

	<u>2011</u>	<u>2010</u>	<u>2009</u>	<u>2008</u>	<u>2007</u>
Premiums earned	<u>\$ 1,019</u>	<u>\$ 906</u>	<u>\$ 848</u>	<u>\$ 922</u>	<u>\$ 1,032</u>
Losses incurred	628	501	466	555	588
Loss adjustment expenses incurred	140	106	98	93	140
Underwriting expenses incurred	<u>303</u>	<u>273</u>	<u>236</u>	<u>250</u>	<u>281</u>
Net underwriting gain (loss)	<u>\$ (52)</u>	<u>\$ 26</u>	<u>\$ 48</u>	<u>\$ 24</u>	<u>\$ 23</u>

### Financial Statements

The financial condition and the results of its operations for the period under examination as reported and filed by the Company with the Department and audited by the Company's external auditors, are reflected in the following:

Statement of Assets, Liabilities, Surplus and Other Funds

Statement of Income

Statement of Changes in the Capital and Surplus Account

**Statement of Assets, Liabilities, Surplus and Other Funds  
December 31, 2011**

Bonds	\$ 4,469,128
Cash, cash equivalents and short-term investments	<u>62,237</u>
Subtotal, cash and invested assets	4,531,365
Investment income due and accrued	26,477
Uncollected premiums and agents' balances in course of collection	94,526
Net deferred tax asset	<u>43,544</u>
Total admitted assets	<u>\$ 4,695,912</u>
Losses	\$ 345,208
Reinsurance payable on paid losses and loss adjustment expenses	67,517
Loss adjustment expenses	135,375
Commissions payable, contingent commissions and other charges	3,051
Other expenses	20,276
Taxes, licenses and fees	4,298
Current federal income taxes	4,501
Unearned premiums	472,397
Payable to parent, subsidiaries and affiliates	18,060
Accounts payable and other liabilities	<u>150</u>
Total liabilities	1,070,833
Additional admitted deferred tax assets	1,729
Common capital stock	1,500,000
Gross paid in and contributed surplus	734,000
Unassigned funds (surplus)	<u>1,389,350</u>
Total surplus and other funds	<u>3,625,079</u>
Total liabilities, surplus and other funds	<u>\$ 4,695,912</u>

**Statement of Income**  
**As of December 31, 2011**

Premiums earned	<u>\$ 1,019,060</u>
Losses incurred	628,584
Loss adjustment expenses incurred	139,878
Other underwriting expenses incurred	<u>302,651</u>
Total underwriting deductions	<u>1,071,113</u>
Net underwriting loss	<u>(52,053)</u>
Net investment income earned	81,866
Net realized capital gains	<u>1,676</u>
Net investment gain	<u>83,542</u>
Net loss from agents' or premium balances charged off	(19,974)
Finance and service charges not included in premiums	61,992
Other fee income	20,692
Miscellaneous expense	<u>(630)</u>
Total other income	<u>62,080</u>
Net income before federal income taxes	93,569
Federal income taxes incurred	<u>35,884</u>
Net income	<u>\$ 57,685</u>

**Statement of Changes in the Capital and Surplus Account**  
(in thousands)

	<u>2011</u>	<u>2010</u>	<u>2009</u>	<u>2008</u>	<u>2007</u>
Capital and surplus, December 31 prior year	\$ 3,936	\$ 3,928	\$ 4,460	\$ 4,263	\$ 4,055
Net income	58	124	167	214	204
Change in net deferred income tax	4	4	15	(22)	8
Change in non-admitted assets	2	0	(2)	5	(4)
Surplus adjustments – Paid in	0	0	(266)	0	0
Dividends to stockholders	<u>(375)</u>	<u>(120)</u>	<u>(446)</u>	<u>0</u>	<u>0</u>
Change in surplus during the year	<u>(311)</u>	<u>8</u>	<u>(532)</u>	<u>197</u>	<u>208</u>
Capital and surplus, December 31 current year	<u>\$ 3,625</u>	<u>\$ 3,936</u>	<u>\$ 3,928</u>	<u>\$ 4,460</u>	<u>\$ 4,263</u>

**Notes to Financial Statements**

**Investments**

The Company's investments were in compliance with ORC Section 3925.08 and valued in accordance with the relevant Statements of Statutory Accounting Principles and the NAIC Securities Valuation Office.

**Loss and Loss Adjustment Expense Reserves**

The Company's Board of Directors appointed Martha A. Winslow, FCAS, MAAA, of Towers Watson, to render the Company's Statement of Actuarial Opinion ("Opinion"). Ms. Winslow prepared an Actuarial Report supporting the Opinion in connection with the preparation of the Company's December 31, 2011 Annual Statement.

David M. Shepherd, FCAS, MAAA, of Merlinos & Associates, Inc., was contracted by the Indiana Department of Insurance to review the reserves for the Group as of December 31, 2011. There were no actuarial adjustments from the review performed by Merlinos & Associates, Inc.

Thomas S. Botsko, ACAS, MAAA, Chief Property & Casualty Actuary of the Department, reviewed the work performed by Mr. Shepherd. Based on his review, Mr. Botsko determined that the loss and loss adjustment expense reserves presented in the Company's 2011 Annual Statement are reasonably stated.

### Conclusion

The balance sheet contained in this Report of Examination reflects the financial condition of the Company as of December 31, 2011, and is summarized as follows:

Total Assets	<u>\$ 4,695,912</u>
Liabilities	1,070,833
Capital and Surplus	<u>3,625,079</u>
Total Liabilities, Capital and Surplus	<u>\$ 4,695,912</u>

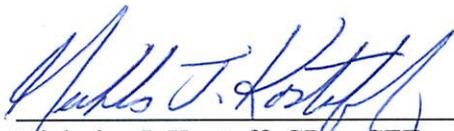
### Subsequent Events

There have been no events subsequent to the examination date which would have a material effect on the financial condition of the Company.

### Acknowledgement

In addition to the undersigned, David T. Finkler, CPA, CFE; Thomas S. Botsko, ACAS, MAAA; and Bradley J. Schroer, of the Department, participated in this examination.

Respectfully,

  
\_\_\_\_\_  
Nicholas J. Kostoff, CPA, CEE  
Examiner-In-Charge  
Office of Risk Assessment  
Ohio Department of Insurance

  
\_\_\_\_\_  
David A. Cook, CFE  
Assistant Chief Examiner  
Office of Risk Assessment  
Ohio Department of Insurance

**Verification**

As required by Section 3901.07 of the Ohio Revised Code, the undersigned hereby attest to the best of their knowledge and belief that the attached is a true Report of Examination as of December 31, 2011.

Nicholas J. Kostoff    4/8/13                      E. Chase                      4/8/13  
Examiner-In-Charge    Date                      Assistant Chief Examiner                      Date

State of Ohio

County of Franklin

Personally appeared before me the above named Nicholas J. Kostoff personally known to me, who executed the above instrument and that the statements and answers contained therein are true and correct to the best of his/her knowledge and belief.

Subscribed and sworn to before me this 8 day of April, 2013.

Elizabeth Chase  
(Notary Public)  
ELIZABETH CHASE  
NOTARY PUBLIC, STATE OF OHIO  
~~MY COMMISSION EXPIRES MAY 22, 2017~~  
My Commission Expires

State of Ohio

County of Franklin

Personally appeared before me the above named David A. Cook personally known to me, who executed the above instrument and that the statements and answers contained therein are true and correct to the best of his/her knowledge and belief.

Subscribed and sworn to before me this 8 day of April, 2013.

Elizabeth Chase  
(Notary Public)  
ELIZABETH CHASE  
NOTARY PUBLIC, STATE OF OHIO  
~~MY COMMISSION EXPIRES MAY 22, 2017~~  
My Commission Expires