

Report of Examination of

Progressive Northwestern Insurance Company
Mayfield Village, Ohio

As of December 31, 2012

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Columbus, Ohio
August 6, 2013

Honorable Mary Taylor
Lt. Governor/Director
Ohio Department of Insurance
50 West Town Street
3rd 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

Progressive Northwestern Insurance Company

an Ohio domiciled, stock, property and casualty insurance company, hereinafter referred to as the (“Company”). The Company is 100% owned by Drive Insurance Holdings, Inc. (“DIHI”) and DIHI is 100% owned by The Progressive Corporation. The examination was conducted at Progressive’s home office, located at 6300 Wilson Mills Road, Mayfield Village, Ohio.

Scope of Examination

The Department last examined the Company as of December 31, 2007. The current examination covers the period of January 1, 2008 through and including December 31, 2012.

The Department conducted the examination in accordance with the National Association of Insurance Commissioners (“NAIC”) Financial Condition Examiners 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.

The State of Ohio took the lead role to perform the coordinated exam of the Progressive insurance companies and the States of Indiana, Louisiana, Michigan, New Jersey, New York, Texas and Wisconsin were all participants on the group examination.

All accounts and activities of the Company were considered in accordance with the risk-focused examination process.

For years covered by the examination, the certified public accounting firm of PricewaterhouseCoopers (“PwC”) provided an unqualified opinion based on statutory accounting principles. Relevant work performed by PwC during its annual audit of the Company was reviewed during the examination and incorporated into the examination work papers.

In addition, the following items were reviewed during the course of this examination:

1. Company history;
2. fidelity bonds and other insurance;
3. officers’, employees’, and agents’ welfare and pension plans;
4. growth of Company;
5. loss experience;
6. pending litigation; and
7. Articles of Incorporation and Bylaws.

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.

<u>Name</u>	<u>Principal Occupation</u>
Thomas Hudson Hollyer	National Product Development Leader, Personal Lines – Progressive
Kathryn Margaret Lemieux	Customer Relation Management Systems Leader, Personal Lines - Progressive
Mark Donald Niehaus	Personal Lines Product Management General Manager – Progressive
David Lloyd Pratt	Business Leader Usage Based Insurance, Personal Lines – Progressive
David James Skove	Personal Lines Product Management General Manager – Progressive

Officers

As of the examination date, the following officers were elected and serving in accordance with the Company's Bylaws:

<u>Name</u>	<u>Title</u>
Mark Donald Niehaus	President
Peter James Albert	Secretary
Thomas Alfred King	Treasurer

Insurance Holding Company System

The Company is a member of a holding company system as defined in Section 3901.32 of the ORC. The Progressive Corporation is the ultimate controlling party of the insurance holding company system.

Territory and Plan of Operations

The Company is licensed to transact business in the District of Columbia and the following states:

Alaska	Arizona	Arkansas	California	Colorado
Connecticut	Delaware	Georgia	Hawaii	Idaho
Indiana	Iowa	Kansas	Kentucky	Louisiana
Maine	Maryland	Minnesota	Mississippi	Missouri
Montana	Nebraska	Nevada	New Jersey	New Mexico
New York	North Carolina	North Dakota	Ohio	Oklahoma
Oregon	Rhode Island	South Carolina	South Dakota	Tennessee
Texas	Utah	Virginia	Washington	West Virginia
Wisconsin				

The following schedule illustrates the Company's premium written in 2012 by line of business:

	Direct	Assumed	Ceded	Net	Percent
Private passenger auto liability	\$ 251,409,669	\$ 622,438,733	\$ 251,409,669	\$ 622,438,733	57.1%
Auto physical damage	174,968,012	370,986,841	174,968,012	370,986,841	34.1%
Commercial auto liability	26,667,632	66,670,527	26,667,632	66,670,527	6.1%
Inland marine	11,498,549	18,240,846	11,498,549	18,240,846	1.7%
Other liability – occurrence	6,657,724	7,577,129	6,657,724	7,577,129	0.7%
All other lines	_____	<u>3,377,295</u>	_____	<u>3,377,295</u>	<u>0.3%</u>
Totals	<u>\$ 471,201,586</u>	<u>\$ 1,089,291,371</u>	<u>\$ 471,201,586</u>	<u>\$ 1,089,291,371</u>	<u>100.0%</u>

Significant Operating Results

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

	2012	2011	2010	2009	2008
Premiums earned	\$ 1,068,807	\$ 1,002,920	\$ 971,982	\$ 977,179	\$ 974,862
Losses incurred	692,405	617,807	578,736	578,493	601,068
Loss adjustment expenses incurred	110,499	103,825	104,996	106,684	115,919
Other underwriting expenses incurred	230,829	223,321	221,897	213,837	212,587
Aggregate write-ins	-	-	<u>(185)</u>	<u>185</u>	-
Total underwriting deductions	<u>1,033,733</u>	<u>944,953</u>	<u>905,444</u>	<u>899,199</u>	<u>929,574</u>
Net underwriting gain	\$ 35,074	\$ 57,966	\$ 66,538	\$ 77,980	\$ 45,288
Loss ratio	64.8%	61.6%	59.5%	59.2%	61.7%
Loss adjustment expense ratio	<u>10.3%</u>	<u>10.4%</u>	<u>10.8%</u>	<u>10.9%</u>	<u>11.9%</u>
Loss and LAE ratio	75.1%	72.0%	70.3%	70.1%	73.6%
Other underwriting expense ratio	<u>21.2%</u>	<u>22.0%</u>	<u>22.6%</u>	<u>22.1%</u>	<u>22.0%</u>
Combined ratio	<u>96.3%</u>	<u>94.0%</u>	<u>92.9%</u>	<u>92.2%</u>	<u>95.6%</u>

Reinsurance

The Company is party to various reinsurance agreements including a pooling agreement with affiliated property casualty companies (“Agency Pool”). 100% of the underwriting business of each member company, net of external reinsurance, is ceded to Progressive Casualty Insurance Company, the pool manager and a pool participant. The combined premiums, losses, and expenses are then retroceded to each Agency Pool member based on pre-determined pooling percentages.

The companies participating in the Agency Pool are listed below, each with their respective pooling percentage:

Progressive Casualty Insurance Company	49%
Progressive Northern Insurance Company	12%
Progressive Northwestern Insurance Company	12%
Progressive Specialty Insurance Company	7%
Progressive Preferred Insurance Company	6%
Progressive Michigan Insurance Company	4%
Progressive Classic Insurance Company	3%
Progressive American Insurance Company	2%
Progressive Gulf Insurance Company	2%
Progressive Bayside Insurance Company	1%
Progressive Mountain Insurance Company	1%
Progressive Southeastern Insurance Company	1%
Progressive Hawaii Insurance Corp.	<u>0%</u>
	100%

The Agency Pool’s affiliated assumed reinsurance transactions are a result of (1) 90% quota-share reinsurance agreements with three of its non-pooled insurance affiliates, (2) a 100% quota-share reinsurance agreement with Progressive County Mutual Insurance Company, a managed but not owned insurance affiliate, and (3) aggregate stop loss reinsurance agreements with National Continental Insurance Company and Progressive Max Insurance Company, two affiliated insurance companies. The Agency Pool’s ceded premiums consist of “State Plans”. State Plans include (1) amounts ceded to state-provided reinsurance facilities, including the Michigan Catastrophic Claims Association and the North Carolina Reinsurance Facility, and (2) state-mandated involuntary CAIP, for which the Agency Pool retains no loss indemnity risk.

Effective April 11, 2011, the Company and thirty-two affiliates entered into an excess of loss agreement with Swiss Reinsurance America Corporation (“Swiss Re”), that applies to commercial vehicle policies with vehicle liability limits in excess of \$1 million, but not to exceed \$2 million. The companies cede to Swiss Re \$1 million in excess of \$1 million.

The examination noted that the Company has policies and procedures in place to comply with SSAP 62R and 63.

Financial Statements

The financial condition and the results of its operations for the five year 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, Capital and Surplus
- Statement of Income
- Statement of Changes in the Capital and Surplus Account

**Statement of Assets
December 31, 2012**

Admitted assets

Bonds	\$ 870,066,007
Common stocks	148,425,892
Cash equivalents and short-term investments	<u>79,522,082</u>
Total cash and invested assets	1,098,013,981
Investment income due and accrued	5,549,887
Uncollected premiums and agents' balances in the course of collection	(62,425)
Deferred premiums, agents' balances and installments booked but deferred and not yet due	62,315,381
Amounts recoverable from reinsurers	5,481,364
Net deferred tax asset	19,376,575
Receivables from parent, subsidiaries and affiliates	15,313,406
Aggregate write-ins for other than invested assets	
State tax credits	<u>1,227,684</u>
Total admitted assets	<u>\$1,207,215,853</u>

**Statement of Liabilities, Capital and Surplus
December 31, 2012**

Liabilities

Losses	\$ 372,252,858
Reinsurance payable on paid losses and loss adjustment expenses	8,534,570
Loss adjustment expenses	74,321,507
Commissions payable, contingent commissions and other similar charges	1,776,240
Other expenses	34,178,772
Taxes, licenses and fees	8,757,738
Current federal and foreign income taxes	8,885,881
Unearned premiums	324,200,664
Advance premium	3,201,558
Ceded reinsurance premiums payable	39,334
Drafts outstanding	19,977,627
Aggregate write-ins for liabilities	
State plan liability	3,516,328
Other liabilities	185,471
Escheatable property	46,806
Unearned fee reserve	<u>10,275</u>
Total liabilities	859,885,629

Capital and Surplus

Common capital stock	3,000,025
Gross paid in and contributed surplus	146,299,975
Unassigned funds	<u>198,030,224</u>
Surplus as regards policyholders	<u>347,330,224</u>
Total liabilities, capital and surplus	<u>\$ 1,207,215,853</u>

Statement of Income
As of December 31, 2012

Premiums earned	<u>\$ 1,068,807,082</u>
Losses incurred	692,405,366
Loss adjustment expenses incurred	110,498,667
Other underwriting expenses incurred	<u>230,829,165</u>
Net underwriting gain	35,073,884
Net investment income earned	27,588,471
Net realized capital gains less capital gains tax	<u>14,371,099</u>
Net investment gain	<u>41,959,570</u>
Net loss from agents' or premium balances charged off	(3,948,990)
Finance and service charges not included in premiums	9,948,141
Aggregate write-ins for miscellaneous income:	
Miscellaneous income	927,293
Service business revenue	93,996
Interest income on intercompany balances	<u>33,608</u>
Total other income	<u>7,054,048</u>
Net income, after dividends to policyholders, after capital gains tax and before all other federal and foreign income taxes	<u>84,087,502</u>
Federal and foreign income taxes incurred	<u>27,105,269</u>
Net income	<u>\$ 56,982,233</u>

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

<u>Capital and Surplus</u>	<u>2012</u>	<u>2011</u>	<u>2010</u>	<u>2009</u>	<u>2008</u>
Capital & surplus, prior year end	\$ 328,475	\$ 319,267	\$ 326,317	\$ 297,260	\$ 320,013
Net income	56,982	65,486	82,200	104,137	38,881
Change in net unrealized capital gain (loss)	2,327	(65)	6,580	11,737	(74,445)
Change in net deferred income tax	2,644	1,445	(9,387)	(1,974)	10,883
Change in non-admitted assets	(98)	342	157	5,957	(5,072)
Paid in surplus adjustment	-	-	-	15,000	7,000
Dividends to stockholders	(43,000)	(58,000)	(86,600)	(105,800)	-
Net change in capital and surplus	18,855	9,208	(7,050)	29,057	(22,753)
Capital and surplus, current year end	\$ 347,330	\$ 328,475	\$ 319,267	\$ 326,317	\$ 297,260

Notes to Financial Statements

Investments

The Company's investment portfolio primarily consists of investment grade bonds and is in compliance with Section 3925.08 of the ORC. The investments were 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 Gary S. Traicoff, FCAS, MAAA, of Progressive management to render a Statement of Actuarial Opinion ("Opinion") on the total reserves. Mr. Traicoff prepared an Actuarial Report supporting the Opinion in conjunction with the preparation of the Company's December 31, 2012 Annual Statement.

Thomas Botsko, ACAS, MAAA, the Department's Chief Property and Casualty Actuary, reviewed the Actuarial Report and performed other procedures as considered necessary to evaluate the loss and loss adjustment expense ("LAE") reserves. Mr. Botsko concluded the reserves fall within a reasonable range of reserve estimates at December 31, 2012.

Subsequent Events

There are no material subsequent events.

Conclusion

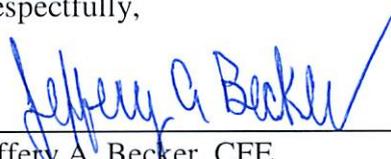
The balance sheet contained in this Report of Examination reflects the financial condition of the Company as of December 31, 2012, and is summarized as follows:

Total Admitted Assets	<u>\$ 1,207,215,853</u>
Liabilities	859,885,629
Surplus as Regards Policyholders	<u>347,330,224</u>
Total Liabilities and Surplus as Regards Policyholders	<u>\$ 1,207,215,853</u>

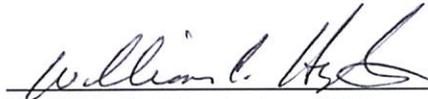
Acknowledgement

In addition to the aforementioned and undersigned, the following representatives of the Department participated in this examination: Mohammad Arif, AES, CISA, CPA; Edward Nagorny, CFE, CPA; Kim Somogyi, CPA; Bryan Radecky, CPA; and Bradley Schroer.

Respectfully,



Jeffery A. Becker, CFE
Examiner-In-Charge
Office of Risk Assessment
Ohio Department of Insurance



William C. Harrington, CFE
Chief Examiner
Office of Risk Assessment
Ohio Department of Insurance

Verification

As required by Section 3901.07 of the ORC, 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, 2012.

Jeffery A. Becker 8/6/13
Examiner-In-Charge Date

William C. Harrington 8/6/13
Chief Examiner Date

State of Ohio

County of Franklin

Personally appeared before me the above named, Jeffery A. Becker, 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 knowledge and belief.

Subscribed and sworn to before me this 6 day of August, 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, William C. Harrington, 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 knowledge and belief.

Subscribed and sworn to before me this 6 day of August, 2013.

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