

Report of Examination of

Progressive Casualty Insurance Company
Cleveland, Ohio

As of December 31, 2007

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Columbus, Ohio
February 12, 2009

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Commissioner
Chairman, Financial Condition (E) Committee
National Association of Insurance Commissioners
Division of Insurance
State of Virginia
1300 East Main Street
Richmond, Virginia 23219

Honorable Merle Scheiber
Director of Insurance
Secretary, Midwestern Zone
National Association of Insurance Commissioners
South Dakota Division of Insurance
Department of Revenue and Regulation
445 East Capitol Avenue, 1st Floor
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Honorable Thomas R. Sullivan
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Secretary, Northeastern Zone
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Honorable Morris Chavez
Superintendent of Insurance
Secretary, Western Zone
National Association of Insurance Commissioners
New Mexico Insurance Division
PO Drawer 1269
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Honorable Mary Jo Hudson
Director
State of Ohio
Department of Insurance
50 West Town Street
3rd Floor – Suite 300
Columbus, Ohio 43215

Dear Madams and Sirs:

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

Progressive Casualty Insurance Company

an Ohio domiciled, stock, property and casualty insurance company, hereinafter referred to as the “Company”. The examination was conducted at the Company’s home office, located at 6300 Wilson Mills Road, Cleveland, Ohio.

A report of this examination is hereby respectfully submitted.

Scope of Examination

The Department last examined the Company as of December 31, 2002. The current full scope association examination covers the intervening period to and including December 31, 2007.

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.

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

For each year during the period under examination, the Certified Public Accounting firm of PricewaterhouseCoopers, LLP (“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.

The Department's property and casualty actuary was retained to review the relevant work performed by the opining actuary, to report on the adequacy of the carried reserves, and to comment on any other statutory matters relating to reserves.

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.

Name	Principal Occupation
Karen M. Barone	Progressive Insurance Companies, Personal Lines General Manager
Richard R. Crawley	Progressive Insurance Companies, Direct Auto Product Research and Development Leader
Christopher J. Garson	Progressive Insurance Companies, Information Technology Business Leader
Steven B. Gellen	Progressive Insurance Companies, Customer Relationship Management Manager
Thomas H. Hollyer	Progressive Insurance Companies, National Product Development Leader
Mark D. Niehaus	Progressive Insurance Companies, Personal Lines General Manager
David J. Skove	Progressive Insurance Companies, Personal Lines General Manager

Officers

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

Name	Title
David J. Skove	President
Thomas A. King	Treasurer
Dane A. Shrallow	Secretary

Insurance Holding Company System

The Company is a member of a holding company system as defined in Section 3901.32 of the ORC. The following displays the chain of ownership of the insurance companies as of December 31, 2007:

The Progressive Corporation – Ohio

Progressive RSC, Inc. – Ohio

Pacific Motor Club – California

Progressive Capital Management Corp. – New York

Progressive Investment Company, Inc. – Delaware

Progressive Insurance Agency, Inc. – Ohio

Progressive Adjusting Company, Inc. – Ohio

Progressive Premium Budget, Inc. – Ohio

Wilson Mills Land Company – Ohio

Village Transport Corp. – Delaware

Progressive Corporate Support, Inc. – Ohio

Silver Key Insurance Agency, Inc. – Nevada

Garden Sun Insurance Services, Inc. – Hawaii

Progn Agency, Inc. – New York

Progressive Vehicle Service Company – Ohio

Progressive Direct Holdings, Inc. – Delaware

Progressive Freedom Insurance Company – New Jersey

Progressive Specialty Insurance Agency, Inc. – Ohio

Progressive Auto Pro Insurance Agency, Inc. – Florida

Progressive Choice Insurance Company – Ohio

Mountain Laurel Assurance Company – Ohio

Progressive Marathon Insurance Company – Michigan

Midland Financial Group, Inc. – Ohio

Midland Risk Services, Inc. – Tennessee

Progressive Advanced Insurance Company – Ohio

Progressive Direct Resources Services Company – Ohio

Progressive Select Insurance Company – Florida

Progressive Max Insurance Company – Ohio

Progressive Paloverde Insurance Company – Indiana
Progressive Premier Insurance Company of Illinois – Ohio
Progressive Universal Insurance Company – Wisconsin
Progressive Direct Insurance Company – Ohio
 Gadsden, Al, LLC – Ohio
Progressive Garden State Insurance Company – New Jersey
Progressive Commercial Holdings, Inc. – Delaware
 National Continental Insurance Company – New York
 Progressive Express Insurance Company – Florida
 Commercial Resource Services Company – Ohio
 Artman and Truckers Casualty Company – Wisconsin
 United Financial Casualty Company – Ohio
 Progressive Commercial Casualty Company – Ohio
Drive Insurance Holdings, Inc. – Delaware
 Progressive West Insurance Company – Ohio
 Progressive Mountain Insurance Company – Ohio
 Progressive Preferred Insurance Company – Ohio
 Progressive Classic Insurance Company – Wisconsin
 Progressive Bayside Insurance Company – Florida
 Progressive Hawaii Insurance Corp. – Ohio
 Progressive Southeastern Insurance Company – Indiana
 Progressive Northeastern Insurance Company – New York
 Drive Resource Services Company – Ohio
 Progressive Michigan Insurance Company – Michigan
 Progressive Northern Insurance Company – Wisconsin
 Bayside Underwriters Insurance Agency, Inc. – Florida
 Progressive Security Insurance Company – Louisiana
 Progressive Northwestern Insurance Company – Ohio
 Progressive American Insurance Company – Florida
 Progressive DLP Corp. – Ohio
 Progressive Casualty Insurance Company – Ohio
 Progressive Specialty Insurance Company – Ohio
 Trussville/Cahaba, AL., LLC - Ohio
 Progressive Gulf Insurance Company – Ohio
 PC Investment Company – Delaware
Progressive Alliance Insurance Agency, Inc – Washington
Drive New Jersey Insurance Company – New Jersey

Reinsurance

The Company is a 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 the Company, the Agency Pool manager. 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 Northwestern Insurance Company	12%
Progressive Northern 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 Southeastern Insurance Company	1%
Progressive Mountain Insurance Company	1%
Progressive Hawaii Insurance Corp.	0%
United Financial Casualty Company	0%
National Continental Insurance Company	0%
	<hr/>
	100%

The Agency Pool's affiliated assumed reinsurance transactions are a result of (1) 90% quota-share reinsurance agreements with four of its non-pooled insurance affiliates, (2) a 100% quota-share reinsurance agreement with Progressive County Mutual Insurance Company, a managed but not owned affiliate, and (3) an aggregate excess of loss reinsurance agreement with National Continental Insurance Company and Progressive Max Insurance Company, two affiliated companies. The Agency Pool's ceded non-affiliated reinsurance transactions are primarily a result of business written under state-mandated involuntary Commercial Auto Insurance Plans/Procedures ("CAIP"), for which the Agency Pool retains no indemnity risk, and state-provided reinsurance facilities. The Agency Pool's remaining reinsurance primarily arises from its non-auto programs.

The Company has policies and procedures in place to comply with Statements of Statutory Accounting Principles 62 and 63.

All contracts contained an insolvency clause, errors and omission clause and an arbitration clause, which meet the guidelines prescribed by the NAIC.

Territory and Plan of Operations

The Company was licensed to transact business in all states, Guam, Puerto Rico, and the provinces of Canada.

Percentage of Net Business Written by Line

<u>Description</u>	<u>2007</u>
Private passenger auto liability	54.1%
Auto physical damage	37.8%
Commercial auto liability	5.5%
All other	2.6%
Total	<u>100.0%</u>

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, Surplus and Other Funds
Statement of Operations
Statement of Changes in the Capital and Surplus Account

Statement of Assets, Liabilities, Surplus and Other Funds

December 31, 2007

Admitted assets	
Cash and invested assets:	
Bonds	\$1,017,583,854
Preferred stocks	300,536,916
Common stocks:	
Affiliated companies	1,281,717,089
Unaffiliated companies	650,914,414
Properties occupied by the company	530,072,667
Properties held for sale	5,549,424
Cash and short term investments	188,540,346
Other invested assets	249,500
Receivable for securities	306,436
Total cash and invested assets	3,975,470,646
Investment income due and accrued	21,364,921
Uncollected premiums and agents' balances in course of collection	117,208,664
Deferred premiums, agents' balances and installments booked but deferred and not yet due	493,327,048
Accrued retrospective premiums	459
Amounts recoverable from reinsurers	41,707,783
Net deferred tax asset	37,288,448
Electronic data processing equipment and software	20,193,369
Receivables from parent, subsidiaries and affiliates	64,272,440
Aggregate write-ins for other than invested assets:	
State unearned surcharge recoverable	1,364,203
State tax credits	223,125
PLIGA Receivable	106,046
State plan refund	67,036
Total admitted assets	\$4,772,594,188

December 31, 2007

Liabilities, capital and surplus

Liabilities:

Losses	\$1,382,650,715
Reinsurance payable on paid losses and loss adjustment expenses	263,059,792
Loss adjustment expenses	340,191,291
Commissions payable, contingent commissions and other charges	10,696,982
Other expenses	134,776,616
Taxes, licenses and fees	35,800,384
Current federal and foreign income taxes	21,063,598
Unearned premiums	1,206,822,255
Advance premiums	5,140,893
Ceded reinsurance premiums payable	7,006,220
Amounts withheld or retained by company for account of others	27,490
Drafts outstanding	71,850,721
Aggregate write-ins for liabilities:	
Other liabilities	29,759,339
State plan liability	9,432,393
Escheatable property	245,621
Unearned fee reserve	202,789
Total liabilities	<u>3,518,727,099</u>

Capital and surplus:

Common capital stock	3,000,000
Gross paid in and contributed surplus	550,360,228
Unassigned funds	700,506,861
Total capital and surplus	<u>1,253,867,089</u>
Total liabilities, capital and surplus	<u>\$4,772,594,188</u>

Statement of Operations

December 31, 2007

Premiums earned	\$4,160,829,416
Losses incurred	2,477,798,879
Loss expenses incurred	491,506,301
Other underwriting expenses incurred	894,312,670
2002 Private passenger auto escrow	1
Net underwriting gain	<u>297,211,565</u>
Net investment income earned	119,170,903
Net realized capital gains	71,562,518
Net investment gain	<u>190,733,421</u>
Net gain (loss) from agents' or premium balances charged off	(38,340,343)
Finance and service charges not included in premiums	15,489,765
Aggregate write-ins for miscellaneous income:	
Finance and service charge revenue assumed	21,829,926
Miscellaneous income	1,940,134
Service business revenue	1,021,605
Interest expense on intercompany balances	(35,964,141)
Total other income (expense)	<u>(34,023,054)</u>
Net income before federal and foreign income taxes	453,921,932
Federal and foreign income taxes incurred	96,586,237
Net income	<u>\$357,335,695</u>

Statement of Changes in the Capital and Surplus Account

(In thousands)

	2003	2004	2005	2006	2007
Capital and surplus December 31, previous year	<u>\$1,619,438</u>	<u>\$2,218,108</u>	<u>\$1,773,858</u>	<u>\$1,653,980</u>	<u>\$1,592,701</u>
Net income	579,784	727,575	537,340	660,980	357,336
Net unrealized capital gains	303,973	196,725	146,392	120,879	50,345
Change in net unrealized foreign exchange capital gain	1,220	-0-	-0-	-0-	-0-
Change in net deferred income tax	(11,518)	(24,889)	(9,260)	(8,516)	(97,816)
Change in nonadmitted assets	14,111	(42,850)	(18,770)	(21,495)	13,613
Change in provision for reinsurance	930	(16)	(782)	645	309
Cumulative effect of changes in accounting principles	11,982	-0-	-0-	-0-	-0-
Surplus paid in	8,188	19,205	(484)	11,031	1,432
Dividends to stockholders	(310,000)	(1,320,000)	(775,400)	(805,000)	(662,200)
Aggregate write-ins for gains and losses in surplus	-0-	-0-	1,086	(19,803)	(1,853)
Net change in capital and surplus	<u>598,670</u>	<u>(444,250)</u>	<u>(119,878)</u>	<u>(61,279)</u>	<u>(338,834)</u>
Capital and surplus December 31, current year	<u>\$2,218,108</u>	<u>\$1,773,858</u>	<u>\$1,653,980</u>	<u>\$1,592,701</u>	<u>\$1,253,867</u>

Summary of Examination Changes

There were no changes made as a result of this examination.

Notes to Financial Statements

Investments

At December 31, 2007, the Company's investments, as measured by statement valuations, were composed of:

<u>Invested Assets</u>	<u>Ratio to Total</u>	
	<u>Investments</u>	<u>Assets</u>
Common stocks	48.6%	40.5%
Bonds	25.6%	21.3%
Properties occupied by the company	13.3%	11.1%
Preferred stocks	7.6%	6.3%
All other	<u>4.9%</u>	<u>4.1%</u>
Totals	<u>100.0%</u>	<u>83.3%</u>

The bond portfolio included 12.4% of United States, Canadian, state, and local government issues, 13.3% special revenue and 74.3% industrial and miscellaneous. The NAIC Securities Valuation Office (SVO) and/or a NAIC Acceptable Rating Organization (ARO) rated 94.4% of the bond portfolio as Class 1, 3.6% Class 2, 1.3% Class 3, and 0.7% Class 4. Cash includes demand deposits.

The Company's investments were in compliance with Section 3925.08 of the ORC.

Loss and Loss Adjustment Expense Reserves

The Company's corporate actuary, Allan R. Neis, FCAS, MAAA, certified the total reserves for the years covered by the examination. The Department's actuary, Mary D. Miller, FCAS, MAAA, reviewed the detailed calculations for the reserves of the major lines of business as of December 31, 2007.

On the basis of the above-mentioned analysis, it was determined that the loss and loss adjustment expense reserves were reasonable as of December 31, 2007.

Subsequent Event

During 2008, results included write-downs of securities determined to have had an other-than-temporary decline in fair value of \$195,120,665 related to the financial sector. The Company properly accounted for these transactions.

Conclusion

The balance sheet contained in this Report of Examination reflects the financial condition of the Company as of December 31, 2007, and is summarized as follows:

Total Admitted Assets	<u>\$4,772,594,188</u>
Liabilities	\$3,518,727,099
Surplus as Regards Policyholders	<u>1,253,867,089</u>
Total Liabilities and Surplus as Regards Policyholders	<u>\$4,772,594,188</u>

Acknowledgement

Appreciation is expressed for the assistance extended by the officers and employees of the Company during the course of this examination.

In addition to the undersigned, the following representatives of the Department participated in this examination: William C. Harrington, CFE, CPA (inactive), Chief Examiner, David T. Finkler, CPA; Methuselah E. Nyangoro, CPA; Richard J. Mack, CFE; Vicky L. Hugo, CPA; Louis F. Radecky, CPA (inactive); Edward J. Nagorny, CPA, CFE; Mark W. Boston, CPA; C. Cameron Piatt, CPCU, CFE; Bradley J. Schroer; Mary D. Miller, FCAS, MAAA; William H. Ward, CPA, CFE; Floyd D. Meeks, AES; and Dominik R. Ilc, AES.

Respectfully,



Jeffrey A. Becker, CFE
Examiner-In-Charge
Ohio Department of Insurance



Jeffrey K. Ebert, CFE
Assistant Chief Examiner
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, 2007.

Jeffery A. Becker
Jeffery A. Becker, CFE
Examiner-In-Charge

2/12/09
Date

Jeffrey K. Ebert
Jeffrey K. Ebert, CFE
Assistant Chief Examiner

2/12/09
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/her knowledge and belief.

Subscribed and sworn to before me this 12 day of February, 2009.

Elizabeth Chase
(Notary Public)
ELIZABETH CHASE
NOTARY PUBLIC, STATE OF OHIO
MY COMMISSION EXPIRES MAY 22, 2012

State of Ohio

County of Franklin

Personally appeared before me the above named, Jeffrey K. Ebert, 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 12 day of February, 2009.

Elizabeth Chase
(Notary Public)
ELIZABETH CHASE
NOTARY PUBLIC, STATE OF OHIO
MY COMMISSION EXPIRES MAY 22, 2012