

**REPORT ON EXAMINATION**  
**OF**  
**MERCURY INSURANCE COMPANY OF**  
**FLORIDA**  
**CLEARWATER, FLORIDA**

**AS OF**  
**DECEMBER 31, 2009**

**BY THE**  
**OFFICE OF INSURANCE REGULATION**

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**TALLAHASSEE, FLORIDA**

November 11, 2010

Kevin M. McCarty  
Commissioner  
Office of Insurance Regulation  
State of Florida  
Tallahassee, Florida 32399-0326

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34 State House Station  
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Dear Sir and Madam:

Pursuant to your instructions, in compliance with Section 624.316, Florida Statutes, and in accordance with the practices and procedures promulgated by the National Association of Insurance Commissioners (NAIC), we have conducted an examination as of December 31, 2009, of the financial condition and corporate affairs of:

**MERCURY INSURANCE COMPANY OF FLORIDA  
1901 ULMERTON ROAD, SIXTH FLOOR  
CLEARWATER, FLORIDA 33762-2307**

Hereinafter referred to as, the "Company". Such report of examination is herewith respectfully submitted.

## **SCOPE OF EXAMINATION**

This examination covered the period of January 1, 2005, through December 31, 2009. The Company was last examined by representatives of the Florida Office of Insurance Regulation (Office) as of December 31, 2004. This examination commenced with planning at the Office on July 21, 2010. The fieldwork commenced on July 26, 2010, and concluded as of November 11, 2010.

This financial examination was an association zone statutory financial examination conducted in accordance with the Financial Condition Examiners Handbook, Accounting Practices and Procedures Manual and annual statement instructions promulgated by the NAIC as adopted by Rules 69O-137.001(4) and 69O-138.001, Florida Administrative Code, with due regard to the statutory requirements of the insurance laws and rules of the State of Florida.

The Financial Condition Examiners Handbook requires that the examination be planned and performed to evaluate the financial condition and identify 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. An examination also includes assessing the principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation and 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.

This report of examination is confined to significant adverse findings, a material change in the financial statements or other information of regulatory significance or requiring regulatory action. The report comments on matters that involved departures from laws, regulations or rules, or which were deemed to require special explanation or description.

## **SUMMARY OF SIGNIFICANT FINDINGS**

### **Current Exam Findings**

There were no material findings or exceptions noted during the examination as of December 31, 2009.

### **Prior Exam Findings**

The following is a summary of significant adverse findings contained in the Office's prior examination report as of December 31, 2004, along with resulting action taken by the Company.

#### **Lines of business**

The Company did not write insurance coverage in Commercial multi peril and Other liability during 2004. **Resolution:** The above noted lines of business have been removed from the Certificate of Authority. Commercial multi peril was removed on May 24, 2006 and Other liability was placed in withdrawn status on April 24, 2006 as required by Section 624.430, Florida Statutes.

### **Agents' Balances**

The Company did not properly age its agents' balances. The Company did not provide an aging of this amount on a policy-by-policy basis as required by Rule 69O-138.024, Florida Administrative Code. **Resolution:** The Company properly aged its agents' balances on a policy by policy basis as required by Rule 69O-138.024, Florida Administrative Code for the period under review.

## **HISTORY**

### **General**

The Company was incorporated in Florida on August 27, 2001, and commenced business on January 2, 2002, as Mercury Insurance Company of Florida.

The Company was authorized to transact the following insurance coverage in Florida on December 31, 2009:

Private Passenger Auto Liability  
Commercial Auto Liability

PPA Physical Damage  
Commercial Auto Physical Damage

The Articles of Incorporation and the Bylaws were not amended during the period covered by this examination.

### **Dividends to Stockholders**

The Company did not declare nor pay any dividends to stockholders during the period of this examination.

## **Capital Stock and Capital Contributions**

As of December 31, 2009, the Company's capitalization was as follows:

Number of authorized common capital shares	1,200,000
Number of shares issued and outstanding	1,200,000
Total common capital stock	\$1,200,000
Par value per share	\$1.00

Control of the Company was maintained by its parent, Mercury General Corporation (MGC), a California Corporation, who owned 100% of the stock issued by the Company, and was in turn owned by controlling stockholders George Joseph and Gloria Joseph, who owned 34.3% and 16.7%, respectively. The remaining 49.0% was owned by public stockholders and traded on the New York Stock Exchange.

## **Surplus Debentures**

The Company did not have any surplus debentures during the period of this examination.

## **Acquisitions, Mergers, Disposals, Dissolutions, and Purchase or Sales Through Reinsurance**

The Company was not party to any acquisitions, mergers, disposals, dissolutions and/or purchases or sales through reinsurance for the period covered by this examination.

## **CORPORATE RECORDS**

The recorded minutes of the shareholder, Board of Directors (Board), and certain internal committees were reviewed for the period under examination. The recorded minutes of the Board adequately documented its meetings and approval of Company transactions and events in

accordance with Section 607.1601, Florida Statutes, including the authorization of investments as required by Section 625.304, Florida Statutes.

### **Conflict of Interest**

The Company adopted a policy statement requiring annual disclosure of conflicts of interest in accordance with the NAIC Financial Condition Examiners Handbook adopted by Rule 69O-138.001, Florida Administrative Code.

## **MANAGEMENT AND CONTROL**

### **Management**

The annual shareholder meeting for the election of directors was held in accordance with Sections 607.1601 and 628.231, Florida Statutes. Directors serving as of December 31, 2009, were:

### **Directors**

<b>Name and Location</b>	<b>Principal Occupation</b>
Bruce Bunner Winter Park, FL	Retired; President, Financial Structures Ltd.
Richard Grayson Murietta, CA	Retired; Senior Vice President Union Bank
George Joseph Los Angeles, CA	Chairman of the Board Mercury General Corporation
Donald Newell Pinehurst, NC	Retired; Senior Vice President The SCPIE Companies
Gabriel Tirador Tustin, CA	President & CEO Mercury General Corp.
Judith Walters Oxnard, CA	Secretary Mercury General Corp. & Subsidiaries

The Board in accordance with the Company's bylaws appointed the following senior officers:

### Senior Officers

<b>Name</b>	<b>Title</b>
Gabriel Tirador	President & CEO
Theodore Stalick	VP/CFO & Treasurer
Judith Walters	Secretary

The Company's Board appointed several internal committees in accordance with Section 607.0825, Florida Statutes. Following were the principal internal board committees and their members as of December 31, 2009:

<b>Audit Committee</b>	<b>Investment Committee</b>	<b>Compensation Committee</b>	<b>Corp. Gov Committee</b>
Nathan Bessin *	George Joseph *	Donald Spuehler *	Nathan Bessin *
Donald Newell	Gabriel Tirador	Bruce Bunner	Donald Newell
Donald Spuehler	Richard Grayson		Donald Spuehler
Martha Marcon			

\* Chairman

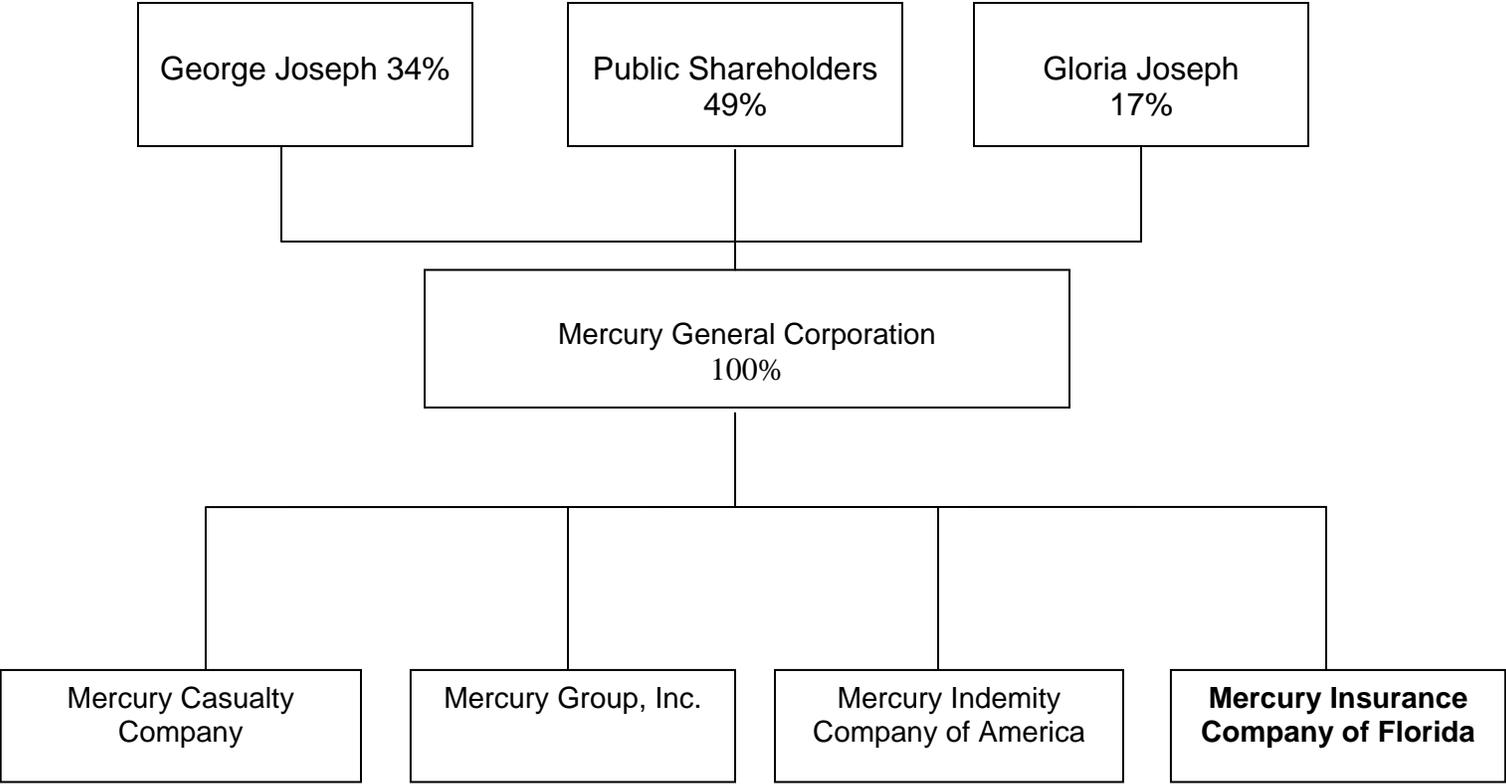
### Affiliated Companies

The Company was a member of an insurance holding company system as defined by Rule 69O-143.045(3), Florida Administrative Code. The latest holding company registration statement was filed with the State of Florida on April 28, 2010, as required by Section 628.801, Florida Statutes, and Rule 69O-143.046, Florida Administrative Code.

A simplified organizational chart as of December 31, 2009, reflecting the holding company system, is shown below. Schedule Y of the Company's 2009 annual statement provided a list of all related companies of the holding company group.

MERCURY INSURANCE COMPANY OF FLORIDA  
ORGANIZATIONAL CHART

DECEMBER 31, 2009



The following agreements were in effect between the Company and its affiliates:

### **Tax Allocation Agreement**

The Company, along with its parent and other affiliated corporations, filed a consolidated federal income tax return. On December 31, 2009, the method of allocation of tax liability between the companies was based upon calculations on a separate return basis.

### **Management Agreement**

The Company had a management agreement with Mercury Insurance Services, LLC (MIS). Pursuant to the agreement, MIS provided all employees and performed underwriting and loss adjustment services on behalf of the Company for the period under review. The Company utilized independent agents to produce the business and MIS was responsible for the underwriting process and ultimate decisions on binding risk based upon previously established guidelines provided by the Company. MIS was also responsible for adjusting and settling all losses the Company was liable for. The loss adjustments and settlements were performed by MIS and settled out of the Company bank accounts. The fees for the services rendered were billed to the Company at the actual incurred expenses.

## **FIDELITY BOND AND OTHER INSURANCE**

The Company maintained fidelity bond coverage up to \$3,000,000 with a deductible of \$100,000, which reached the suggested minimum recommended by the NAIC.

The Company also maintained Directors and Officers insurance coverage in the amount of \$30,000,000, with a retention point of \$500,000. The policy was maintained at the holding company level, but applied to all companies within the group.

## **PENSION, STOCK OWNERSHIP AND INSURANCE PLANS**

The Company did not have any employees.

## **TERRITORY AND PLAN OF OPERATIONS**

The Company was authorized to transact insurance in the following states:

Florida  
Pennsylvania

### **Treatment of Policyholders**

The Company established procedures for handling written complaints in accordance with Section 626.9541(1) (j), Florida Statutes.

The Company maintained a claims procedure manual that included detailed procedures for handling each type of claim in accordance with Section 626.9541(1) (i) 3a, Florida Statutes.

## **COMPANY GROWTH**

### **Profitability of Company**

The following table shows the profitability trend (in dollars) of the Company for the period of examination, as reported in the filed annual statements.

	<b>2009</b>	<b>2008</b>	<b>2007</b>	<b>2006</b>	<b>2005</b>
Premiums Earned	0	0	0	0	0
Net Underwriting Gain/(Loss)	(21,427)	(239,961)	13,089	(75,438)	(82,413)
Net Income	937,151	108,445	500,160	528,775	645,131
Total Assets	59,756,884	59,186,136	59,089,336	59,870,464	71,889,078
Total Liabilities	22,358,412	22,461,750	22,784,674	24,490,636	36,946,312
Surplus As Regards Policyholders	37,398,472	36,724,386	36,304,662	35,379,830	34,942,766

As outlined above, the Company had zero Premiums Earned for the entire period under review. This was due to the 100 percent quota share agreement with their affiliate Mercury Casualty Company (MCC), whereas all earned premiums were ceded to the affiliate in conjunction with all losses and reserve liabilities. Because the Company did not earn any premiums, but was still responsible for the Underwriting Expenses, the Company had a Net Underwriting Loss for all years, except 2007, under review. The Net Income amounts were primarily attributed to the Net Investment Income earned.

### **LOSS EXPERIENCE**

The Company did not experienced net losses for the entire period under review. The Company entered into a 100 percent (%) quota share reinsurance agreement with their affiliate, Mercury Casualty Company (MCC), whereas 100 percent (%) of all losses were ceded to the assuming affiliate, MCC.

## **REINSURANCE**

The reinsurance agreements reviewed complied with NAIC standards with respect to the standard insolvency clause, arbitration clause, transfer of risk, reporting and settlement information deadlines.

### **Assumed**

The Company did not assume risk.

### **Ceded**

The Company ceded risk on a quota share basis to MCC, an affiliate. The Company ceded 100 percent of the ultimate net loss arising out of each occurrence for all private passenger and commercial automobile and automobile physical damage business written by the Company.

The reinsurance contracts were reviewed during the examination to verify transfer of risk was evident and the contracts were in force for the entire period under review.

## **ACCOUNTS AND RECORDS**

The Company maintained its principal operational offices in Clearwater, Florida. The examination was primarily conducted in the corporate headquarters of the parent in Los Angeles, California.

An independent CPA firm audited the Company's statutory basis financial statements annually for the years 2005, 2006, 2007, 2008 and 2009, in accordance with Section 624.424(8), Florida Statutes. Supporting work papers were prepared by the CPA as required by Rule 69O-137.002, Florida Administrative Code.

The Company's accounting records were maintained on the FlexiLedger accounting system. This system had direct interfaces with various premiums and claims systems.

The Company and non-affiliates had the following agreements:

### **Custodial Agreement**

The Company maintained a custodial agreement with the Bank of New York Trust Company. The agreement was in compliance with Rule 69O-143.042, Florida Administrative Code.

### **Independent Auditor Agreement**

The Company maintained an agreement with KPMG LLP to perform an annual audit, in compliance with Section 624.424(8), Florida Statutes.

### **Information Technology Report**

ParenteBeard LLC performed an evaluation of the information technology and computer systems of the Company. Results of the evaluation were noted in the Information Technology Report provided to the Company.

### **STATUTORY DEPOSITS**

The following securities were deposited with the State of Florida as required by Section 624.411, Florida Statutes:

STATE	Description	Par Value	Market Value
FL	US T-NOTE, 5.00 %, 08/15/11	350,000	369,180
TOTAL FLORIDA DEPOSITS		<u>\$350,000</u>	<u>\$369,180</u>

## **FINANCIAL STATEMENTS PER EXAMINATION**

The following pages contain financial statements showing the Company's financial position as of December 31, 2009, and the results of its operations for the year then ended as determined by this examination. Adjustments made as a result of the examination are noted in the section of this report captioned, "Comparative Analysis of Changes in Surplus."

**MERCURY INSURANCE COMPANY OF FLORIDA**  
**Assets**

**DECEMBER 31, 2009**

	Per Company	Examination Adjustments	Per Examination
Bonds	\$16,355,266		\$16,355,266
Cash:	9,169,278		9,169,278
Investment Income Due & Accrued	135,629		135,629
Agents' Balances:			
Uncollected premium	4,735,487		4,735,487
Deferred premium	16,520,707		16,520,707
Reinsurance recoverable	12,093,570		12,093,570
Current federal and foreign income tax recoverable and tax thereon	114,832		114,832
Net deferred tax asset	632,108		632,108
Receivable from parents, subsidiaries and affiliates	7		7
Totals	\$59,756,884	\$0	\$59,756,884

**MERCURY INSURANCE COMPANY OF FLORIDA**  
**Liabilities, Surplus and Other Funds**

**DECEMBER 31, 2009**

	<b>Per Company</b>	<b>Examination Adjustments</b>	<b>Per Examination</b>
Commissions Payable	\$4,545,747		\$4,545,747
Other expenses	70,983		70,983
Taxes, licenses and fees	992,843		992,843
Advanced Premium	1,813,520		1,813,520
Ceded reinsurance premiums payable	10,851,286		10,851,286
Remittances and items not allocated	22,705		22,705
Payable to parent, subsidiaries and affiliates	4,061,318		4,061,318
<b>Total Liabilities</b>	<b>\$22,358,412</b>		<b>\$22,358,412</b>
Common capital stock	\$1,200,000		\$1,200,000
Gross paid in and contributed surplus	32,300,000		32,300,000
Unassigned funds (surplus)	3,898,472		3,898,472
<b>Surplus as regards policyholders</b>	<b>\$37,398,472</b>		<b>\$37,398,472</b>
<b>Total liabilities, surplus and other funds</b>	<b>\$59,756,884</b>		<b>\$59,756,884</b>

**MERCURY INSURANCE COMPANY OF FLORIDA**  
**Statement of Income**

**DECEMBER 31, 2009**

**Underwriting Income**

Premiums earned			-
	<b>Deductions:</b>		
Losses incurred			-
Loss expenses incurred			-
Other underwriting expenses incurred		21,427	
Aggregate write-ins for underwriting deductions			-
Total underwriting deductions		<u>21,427</u>	
Net underwriting gain or (loss)			(\$21,427)

**Investment Income**

Net investment income earned			\$950,261
Net realized capital gains or (losses)			-
Net investment gain or (loss)			<u>\$950,261</u>

**Other Income**

Net gain or (loss) from agents' or premium balances charged off			-
Finance and service charges not included in premiums			-
Aggregate write-ins for miscellaneous income			-
Total other income			<u>\$0</u>
Net income before dividends to policyholders and before federal & foreign income taxes			\$928,834
Dividends to policyholders			-
Net Income, after dividends to policyholders, but before federal & foreign income taxes			<u>\$928,834</u>
Federal & foreign income taxes			<u>(8,317)</u>

Net Income \$937,151

**Capital and Surplus Account**

Surplus as regards policyholders, December 31 prior year			\$36,724,386
Net Income			\$937,151
Net unrealized capital gains or losses			-
Change in net deferred income tax		(255,756)	
Change in non-admitted assets		(7,309)	
Change in provision for reinsurance			-
Surplus adjustments: Paid in			-
Aggregate write-ins for gains and losses in surplus examination adjustment			-
Change in surplus as regards policyholders for the year			<u>\$674,086</u>
Surplus as regards policyholders, December 31 current year			<u><u>\$37,398,472</u></u>

A comparative analysis of changes in surplus is shown below.

**MERCURY INSURANCE COMPANY OF FLORIDA**  
**Comparative Analysis of Changes In Surplus**

**DECEMBER 31, 2009**

The following is a reconciliation of Surplus as regards policyholders between that reported by the Company and as determined by the examination.

Surplus as Regards Policyholders  
December 31, 2009, per Annual Statement \$37,398,472

	<u>PER</u> <u>COMPANY</u>	<u>PER</u> <u>EXAM</u>	<u>INCREASE</u> <u>(DECREASE)</u> <u>IN SURPLUS</u>
ASSETS:			
No Adjustments			
LIABILITIES:			
No Adjustments			
Net Change in Surplus:			<u>0</u>
Surplus as Regards Policyholders December 31, 2009, Per Examination			<u><u>\$37,398,472</u></u>

## COMMENTS ON FINANCIAL STATEMENTS

### Liabilities

**Losses and Loss Adjustment Expenses** \$0

The Company did not report any losses or loss adjustment expense reserves on the balance sheet for the year ending December 31, 2009. This was due to the 100% quota share agreement in place with their affiliate.

### Capital and Surplus

The amount reported by the Company of \$37,398,472, exceeded the minimum of \$4,000,000 required by Section 624.408, Florida Statutes.

## CONCLUSION

The insurance examination practices and procedures as promulgated by the NAIC have been followed in ascertaining the financial condition of **Mercury Insurance Company of Florida** as of December 31, 2009, consistent with the insurance laws of the State of Florida.

Per examination findings, the Company's Surplus as regards policyholders was \$37,398,472, which exceeded the minimum of \$4,000,000 required by Section 624.408, Florida Statutes

In addition to the undersigned, Michael Brennan, CPA, Examiner In Charge, Phil Schmoyer, Participating Examiner, Jennifer Cox, Participating Examiner, Caner Ozsoy, Participating Examiner, and Andrew Wittig, IT Specialist representing ParenteBeard LLC participated in the examination.

Respectfully submitted,

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Kethessa Carpenter, CPA  
Financial Examiner/Analyst Supervisor  
Florida Office of Insurance Regulation

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Mary James, CFE, CPM  
Chief Examiner  
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