



THE COMMONWEALTH OF MASSACHUSETTS
OFFICE OF CONSUMER AFFAIRS AND BUSINESS
REGULATION
DIVISION OF INSURANCE

REPORT OF EXAMINATION OF THE
ENCOMPASS INSURANCE COMPANY OF MASSACHUSETTS

Northbrook, Illinois

As of December 31, 2008

NAIC GROUP CODE 0008

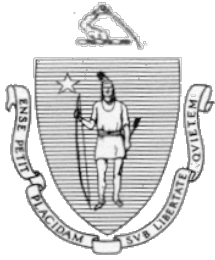
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ENCOMPASS INSURANCE COMPANY OF MASSACHUSETTS

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COMMONWEALTH OF MASSACHUSETTS
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April 30, 2010

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Honorable Commissioners;

Pursuant to your instructions and in accordance with Massachusetts General Laws, Chapter 175, Section 4, an examination has been made of the financial condition and affairs of

ENCOMPASS INSURANCE COMPANY OF MASSACHUSETTS
Northbrook, Illinois

at its administrative office located at 3075 Sanders Road, Northbrook, Illinois 60062-7127. The following report thereon is respectfully submitted.

SCOPE OF EXAMINATION

This is the first examination of Encompass Insurance Company of Massachusetts hereinafter referred to as "the Company" or "Encompass". The current National Association of Insurance Commissioners ("NAIC") association plan examination covers the period from September 1, 2004 through December 31, 2008, and any material transactions and/or events occurring subsequent and noted during the examination.

The current examination was conducted at the direction of, and under the overall management and control of the examination staff of the Massachusetts Division of Insurance (the "Division") representing the NAIC Northeastern Zone. The statutory examination was performed at the Company's primary location of books and records in Northbrook, Illinois. Representatives from RSM McGladrey, Inc. were engaged by the Division to assist in the examination by performing certain examination procedures. The current examination was conducted concurrent with, and as part of the examination of the Allstate Insurance Group ("Group") of companies with Illinois as the lead state. RSM McGladrey, Inc. was also retained by the Illinois Department of Insurance to assist in conducting its examination of the Illinois domiciled insurers in the Group. The Illinois Department of Insurance also retained the actuarial services of Insurance Regulatory Services, Inc., ("INS") Consultants to review the actuarially determined loss and loss adjustment expense reserves of the Group. The Division has relied on Illinois for all of the work performed in the planning phase of the risk focused examination and INS Consultants for the work performed on the loss reserves.

The examination was conducted in accordance with standards established by the NAIC Financial Condition (E) Committee as well as with the requirements of the NAIC Financial Condition Examiner's Handbook, the examination standards of the Division and Massachusetts General Laws. The principal focus of the examination was 2008 activity; however, transactions both prior and subsequent thereto were reviewed as deemed appropriate. The examination was conducted following the NAIC Risk Focused Examination model.

In addition to a review of the financial condition of the Company, the examination included a review of the Company's business policies and practices, corporate records, reinsurance treaties, conflict of interest disclosure statements, fidelity bonds and other insurance, disaster recovery plan and other pertinent matters to provide reasonable assurance that the Company was in compliance with applicable laws, rules and regulations. In planning and conducting the examination, consideration was given to the concepts of materiality and risk and examination efforts were directed accordingly.

The Company is audited annually by Deloitte & Touche LLP ("D&T"), an independent certified public accounting firm, in accordance with 211 CMR 23.00. The firm expressed unqualified opinions on the Company's financial statements for the calendar years 2005 through 2008. A review and use D&T's work papers were made to the extent deemed appropriate and effective.

HISTORY

On September 1, 2004, Continental Casualty Company ("CCC") acquired the common stock of Encompass, a corporate shell formerly known as New England Fidelity Insurance Company ("NEFIC"), from the Division which was acting in its capacity as permanent receiver of NEFIC. The

Certificate of Authority for Encompass to write personal lines insurance in Massachusetts was issued on October 10, 2004 with an effective date of September 1, 2004. The Company did not begin writing substantial business in Massachusetts until 2005.

CCC was a wholly owned subsidiary of The Continental Corporation, which was wholly owned by CNA Financial Corporation, which in turn was approximately 91% owned by Loews Corporation. CCC and certain of its insurance affiliates sold their personal lines insurance business to a subsidiary of The Allstate Corporation ("TAC") on October 1, 1999. In connection with that transaction, Allstate was granted an option to purchase five designated insurance companies of CCC with Encompass designated as one of them. In anticipation of Allstate's option being exercised, all of the future personal lines insurance business written by Encompass was ceded to the Allstate Insurance Company ("AIC") under an indemnity reinsurance agreement dated December 2, 2002. Effective October 1, 2005, Allstate exercised its option to purchase the common stock of Encompass.

Capital Stock

As of December 31, 2008, the Company had 50,000,000 shares of \$5 par value common stock authorized and 190,000 shares outstanding with an aggregate stated value of \$950,000. All of the common stock was owned by AIC.

Dividends to Stockholders

There were no dividends paid during the examination period.

Growth of the Company

The growth of the Company for the years 2005 through 2008 is shown in the following schedule, which was prepared from the Company's annual statements, including any changes as a result of the examination. All amounts are in thousands.

<u>Year</u>	<u>Admitted Assets</u>	<u>Liabilities</u>	<u>Surplus</u>	<u>Direct Premiums Written</u>	<u>Net Premiums Written</u>
2008	\$ 6,144,860	\$ 117,648	\$ 6,027,212	\$ 93,377,139	\$ 0
2007	6,023,955	93,673	5,930,282	111,484,407	0
2006	5,900,607	144,359	5,756,248	118,573,583	0
2005	5,595,789	15,656	5,580,133	127,220,763	0

MANAGEMENT

Annual Meeting of Stockholders

The annual meeting of the stockholders was held each year during the examination period. At any meeting of the stockholders, a majority in interest of all stock issued and outstanding and entitled to vote upon a question to be considered at the meeting shall constitute a quorum for the consideration of such question.

Board of Directors

The by-laws provide that the business and affairs of the Company shall be managed by the Board of

Directors except as otherwise provided by the Articles of Incorporation or by a valid shareholder agreement. The Board of Directors shall consist of not less than three or more than eight directors with the number determined at each annual meeting by resolution of the shareholders. Each director holds office for a term of one year.

The by-laws do not specify the number of meetings to be held during a year. The minutes of the Board of Directors meetings indicated that meetings were held four times per year during the examination period. At any meeting of the Board, a majority of directors shall constitute a quorum. The minutes indicated that a quorum was obtained at all meetings of the Board of Directors held during the examination period.

At December 31, 2008 the board was comprised of three directors. Directors duly elected and serving at December 31, 2008, with business affiliations, were as follows:

<u>Director</u>	<u>Business Affiliation</u>
Cynthia H. Young	Chairman of the Board and President Encompass Insurance Company of Massachusetts
Mark L. Thompson	Senior Vice President Encompass Insurance Company of Massachusetts
Laura R. Dunne	Senior Vice President Allstate Insurance Company

Officers

The by-laws of the Company provide that the officers of the Company shall be a president, one or more vice presidents, a secretary, and a treasurer and other officers as deemed necessary. Pursuant to the by-laws, the officers of the Company are elected by the Board of Directors. Vacancies among the officers shall be filled by the Board of Directors.

The elected officers and their respective titles at December 31, 2008 were as follows:

<u>Name</u>	<u>Title</u>
Cynthia H. Young	President
Samuel H. Pilch	Acting Chief Financial Officer, Group Vice President and Controller
Terrance J. Kelaher	Vice President
Mark L. Thompson	Vice President
Karen C. Gardner	Vice President
Mary J. McGinn	Vice President and Secretary
Steven C. Verney	Vice President and Treasurer

Conflict of Interest Procedures

The Company has adopted a policy statement pertaining to conflict of interest. The Company has an established procedure for the disclosure to the Board of Directors of any material interest or affiliation on the part of any officer or director, which is in or is likely to conflict with his/her official duties.

Annually, each officer, director and responsible employee completes a questionnaire disclosing any material conflicts of interest. The completed questionnaires were reviewed, and no discrepancies were noted in the responses to the General Interrogatories regarding conflicts of interest as reflected in the Company's 2008 Annual Statement.

Management Continuity and National Emergency

The Company provides for the continuity of management in the event of a catastrophe or other emergency in accordance with sections 180M through 180Q of Chapter 175 of the Massachusetts General Laws.

Corporate Records

Articles of Incorporation and By-laws

The bylaws and Articles of Incorporation and amendments thereto were read. The bylaws were filed with the Division in November 2005.

Corporate Governance

TAC is a publicly traded company listed on the New York Stock Exchange ("NYSE"). As such, TAC is subject to the rules and regulations of the Sarbanes-Oxley Act of 2002, the Securities Exchange Commission and the NYSE. The Group has ultimate fiduciary responsibilities for the Company's operations, corporate actions, and treatment of constituents, particularly, policyholders, claimants, employees, shareholders, etc.

It should be noted that TAC has an audit committee of its Board of Directors that is comprised of "independent" directors; it meets four times a year, appears to have a financially sound acumen within its outside directors composition; is ultimately responsible to the full Board for outside external auditor selection (CPA firm) and for review of such services, for the financial reporting, accounting and disclosure environment, for the internal control environment from which the corporation operates, and for control of selection of other consulting firms services as to "independence" from a "sound practices" perspective.

Transactions and Agreements with Subsidiaries and Affiliates

Investment Management Agreement

Effective January 1, 2007, the Company entered into an Investment Management Agreement with Allstate Investments, LLC ("AILLC") whereby AILLC provides investment management services and advice.

Tax Sharing Agreement

The agreement covers the allocation and settlement of current federal income taxes among companies included in the consolidated income tax return of TAC and its subsidiaries.

Service and Expense Agreement

Effective October 1, 2005, the Company became a party to the Amended and Restated Service and Expense Agreement between AIC, TAC and certain affiliates pursuant to which AIC furnishes a variety of services. The agreement provides for the cost sharing and allocation of operating expenses among the parties.

AFFILIATED COMPANIES

Per Form B, as filed with the Division, the Company is a member of a holding company system and is subject to the registration requirements of Chapter 175, Section 206C of the Massachusetts General Laws. The Company is a wholly owned subsidiary of AIC; an Illinois domiciled insurance company, which is a wholly owned subsidiary of Allstate Insurance Holdings, LLC, a Delaware limited liability company. Allstate Insurance Holdings, LLC is a wholly-owned subsidiary of TAC.

The “ultimate controlling person” of the Company is TAC, as indicated on the Organization Chart within this report.

ORGANIZATION CHART

The following listing shows the identities and interrelationships of subsidiary companies within the Allstate Insurance holding company system, including the Company. (Jurisdiction of domicile is in parenthesis)

The Allstate Corporation (DE)

 Allstate Insurance Holdings, LLC (DE)

 Allstate Insurance Company (IL)

 Allstate New Jersey Insurance Company (IL)

 Allstate New Jersey Property and Casualty Insurance Company (IL)

 Encompass Insurance Company of New Jersey (IL)

 Encompass Property and Casualty Insurance Company of New Jersey (IL)

 Allstate Floridian Insurance Company (IL)

 Allstate Floridian Indemnity Company (IL)

 Encompass Floridian Indemnity Company (IL)

 Encompass Floridian Insurance Company (IL)

 Allstate Life Insurance Company (IL)

 Allstate Assurance Company (IL)

 Charter National Life Insurance Company (IL)

 Allstate Life Insurance Company of New York (NY)

 IntramERICA Life Insurance Company (NY)

 Lincoln Benefit Life Company (NE)

 Surety Life Insurance Company (NE)

 ALIC Reinsurance Company (SC)

 Allstate Fire and Casualty Insurance Company (IL)

Allstate Indemnity Company (IL)
Allstate North American Insurance Company (IL)
Allstate Property and Casualty Insurance Company (IL)
Northbrook Indemnity Company (IL)
Deerbrook Insurance Company (IL)
Encompass Home and Auto Insurance Company (IL)
Encompass Indemnity Company (IL)
Encompass Independent Insurance Company (IL)
Encompass Insurance Company (IL)
Encompass Insurance Company of America (IL)
Encompass Property and Casualty Company (IL)
Encompass Insurance Company of Massachusetts (MA)
Allstate County Mutual Insurance Company (TX)
Allstate Texas Lloyd's (TX)
North Light Specialty Insurance Company (IL)
American Heritage Life Investment Corporation (DE)
American Heritage Life Insurance Company (FL)
First Colonial Insurance Company (FL)
Concord Heritage Life Insurance Company, Inc. (NH)

FIDELITY BOND AND OTHER INSURANCE

The Company maintains fidelity coverage with an authorized Massachusetts insurer, consistent with Massachusetts General Laws, Chapter 175, Section 60. The aggregate limit of liability exceeds the NAIC suggested minimum.

The Company has further protected its interests and property by policies of insurance covering other insurable risks. Coverage was in force as of December 31, 2008.

INSURANCE PRODUCTS AND RELATED PRACTICES

Territory and Plan of Operation

The Company is licensed and authorized to transact business only in the state of Massachusetts and sells primarily private passenger automobile and homeowner's coverage through Encompass independent agents. As a writer of Massachusetts private passenger automobile insurance, the Company participates in Commonwealth Automobile Insurers, the states reinsurance facility for high risk drivers. All net underwriting business is 100% reinsured by AIC.

Massachusetts Automobile Business and Regulatory Reform

As noted, a principal line of business written by the Company is Massachusetts private passenger automobile business. Until April 1, 2008, the private passenger automobile insurance market in Massachusetts was heavily regulated and the Massachusetts Commissioner of Insurance (the "Commissioner") was responsible for setting premium rates on an annual basis. In July of 2007, the Massachusetts Division of Insurance issued its "Opinion, Findings and Decision on the Operation of Competition in Private Motor Vehicle Insurance in 2008", in which it determined that competition in

the Massachusetts private passenger motor vehicle insurance market was sufficient such that the Commissioner cannot “fix-and-establish” premium rates for 2008. Accordingly, effective April 1, 2008, each insurer, including the Company, was permitted to file and use its own rates subject to disapproval by the Commissioner.

Also in July of 2007, the Division issued a decision approving rules that will implement an assigned risk plan, the Massachusetts Automobile Insurance Plan (“MAIP”), to provide private passenger insurance for those individuals unable to obtain insurance voluntarily. This new assigned risk plan will ultimately replace the current facility for high risk drivers, Commonwealth Automobile Reinsurers (“CAR”). The effect of these two decisions was to introduce “managed competition” to the Massachusetts private passenger automobile insurance market. This regulatory reform is significant to the industry as a whole. During the first year of managed competition, nine new automobile insurers entered the Massachusetts market, including the Company’s parent, AIC. The Company asserts that currently, this event will not impact its current business plan or operations.

REINSURANCE

As noted above, the Company has in place a quota share reinsurance agreement with AIC effective October 1, 2005 pursuant to which AIC indemnifies the Company for 100 percent of its net underwriting results (direct business plus assumed, less ceded to third parties) ceded to AIC. This agreement was effective October 1, 2005 and is essentially the same treaty which was in place prior to AIC’s actual acquisition of the Company.

ACCOUNTS AND RECORDS

The Company’s internal control structure was discussed with management through questionnaires and through a review of the work performed by the Company’s independent certified public accountants, D&T, including work performed on behalf of AIC generated to support the requirements of the Sarbanes-Oxley Act of 2002. As part of its engagement for the Illinois Department of Insurance, RSM McGladrey Inc. performed a review and evaluation of the control environment of the Group’s IT systems. The NAIC’s Information Systems Questionnaire (“ISQ”) completed by the Company was reviewed and interviews with Company management and IT staff were conducted to gather supplemental information and corroborate the Company’s responses to the ISQ. Included was a review of the documentation supporting management and organization controls, application systems development and maintenance controls, operating and processing controls, logical and physical security controls, contingency planning controls, personal computers, Local Area Network, Wide Area Network and internet controls. The control environment of the Company’s information systems was found to have in place sufficient internal controls.

No material internal control weaknesses were noted in connection with the examination, nor were any such matters reported in the CPA firm’s filings with the Division.

The Company uses an automated general ledger system. Trial balances were traced from the general ledger and supporting documents to the 2008 Annual Statement. No material exceptions were noted.

FINANCIAL STATEMENTS

The following financial statements are presented on the basis of accounting practices prescribed or permitted by the Division of Insurance of the Commonwealth of Massachusetts and by the National Association of Insurance Commissioners, as of December 31, 2008.

Statement of Assets, Liabilities, Surplus and Other Funds as of December 31, 2008

Summary of Income for the Year Ended December 31, 2008

Statement of Capital and Surplus as of December 31, 2008

Reconciliation of Capital and Surplus for the Four Year Period Ended December 31, 2008

For Information Purposes Only

Encompass Insurance Company of Massachusetts
Statement of Assets, Liabilities, Surplus and Other Funds
As of December 31, 2008

	As Reported by the Company	Examination Changes	Per Statutory Examination
Assets			
Bonds	\$5,794,145	\$0	\$5,794,145
Cash and short-term investments	247,615		247,615
Subtotals, cash and invested assets	6,041,761		6,041,761
Investment income due and accrued	28,272		28,272
Net deferred tax asset	3,691		3,691
Aggregate write-ins for other than invested assets	71,135	0	71,135
Total Assets	<u>\$6,144,860</u>	<u>\$0</u>	<u>\$6,144,860</u>

For Information Purposes Only

Encompass Insurance Company of Massachusetts
Statement of Assets, Liabilities, Surplus and Other Funds (Continued)
As of December 31, 2008

	As Reported by the Company	Examination Changes	Per Statutory Examination
Liabilities			
Current federal and foreign income taxes	\$46,513	\$0	\$46,513
Payable to parent, subsidiaries and affiliates	65,416		65,416
Aggregate write ins for liabilities	5,719		5,719
Total Liabilities	117,648	0	117,648
Common capital stock	950,000	0	950,000
Gross paid in and contributed surplus	4,514,255		4,514,255
Unassigned funds (surplus)	562,956		562,956
Surplus as regards policyholders	6,027,212	0	6,027,212
Total Liabilities, Capital and Surplus	\$6,144,860	\$0	\$6,144,860

Encompass Insurance Company of Massachusetts
Statement of Income
As of December 31, 2008

	As Reported by the Company	Examination Changes	Per Statutory Examination
Net investment income	\$141,947	\$0	\$141,947
Net realized capital gains	971		971
Net investment gain	142,918	0	142,918
Net income before dividends to policyholders and before federal and foreign income taxes	142,918	0	142,918
Federal and foreign income taxes incurred	(45,990)		(45,990)
Net Income	\$96,928	\$0	\$96,928

Encompass Insurance Company of Massachusetts
Capital and Surplus
For the Year Ended December 31, 2008

	As Reported by the Company	Examination Changes	Per Statutory Examination
Capital and Surplus, December 31, prior year	\$5,930,282	\$0	\$5,930,282
Net Income	96,928		96,928
Change in net deferred income tax	(3,692)		(3,692)
Change in nonadmitted assets	3,693		3,693
Change in surplus	96,929	0	96,929
Capital and Surplus, December 31, current year	\$6,027,212	\$0	\$6,027,212

For Information Purposes Only

Encompass Insurance Company of Massachusetts
Reconciliation of Capital and Surplus
For the Four Year Period Ended December 31, 2008

	2008	2007	2006	2005
Capital and Surplus, December 31, prior year	\$5,930,282	\$5,756,247	\$5,580,132	\$5,462,603
Net Income	96,928	174,035	176,117	99,582
Change in deferred tax	(3,692)	(3,692)	(3,692)	54,453
Change in nonadmitted assets	3,693	3,692	3,690	(50,761)
Paid in surplus adjustments	0	0	0	14,255
Change in surplus as regards policyholders	96,929	174,035	176,115	117,529
	<u>\$6,027,212</u>	<u>\$5,930,282</u>	<u>\$5,756,247</u>	<u>\$5,580,132</u>

For Information Purposes Only

ACKNOWLEDGEMENT

Acknowledgment is made of the cooperation and courtesies extended by the officers and employees of the Company to all examiners during the course of the examination.

John M. Curran, CFE
Supervising Examiner and Examiner-in-Charge
Commonwealth of Massachusetts
Division of Insurance
Representing Northeastern Zone, NAIC

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