

STATE OF UTAH INSURANCE DEPARTMENT

REPORT OF FINANCIAL EXAMINATION

OF

WESTERN NATIONAL TITLE INSURANCE COMPANY

OF

SALT LAKE CITY, UTAH

AS OF

DECEMBER 31, 2003



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June 14, 2004

Honorable Merwin U. Stewart, Commissioner
Utah Insurance Department
3110 State Office Building
Salt Lake City, Utah 84114-6901

In accordance with your instructions and in compliance with Utah Code Annotated (UCA) Title 31A, an examination was conducted as of December 31, 2003, of the financial condition and business affairs of

WESTERN NATIONAL TITLE INSURANCE COMPANY
of
Salt Lake City, Utah

a stock title insurance company, hereinafter referred to as the Company, and the following report of examination is respectfully submitted.

Scope of Examination

Period Covered by Examination

The Company was last examined as of December 31, 1999, by a representative of the State of Utah Insurance Department. The current examination covers the intervening period from January 1, 2000, through December 31, 2003, including any material transactions and/or events occurring subsequent to the examination date noted during the course of the examination.

Examination Procedures Employed

The examination was conducted to determine compliance with accounting practices and procedures in conformity with the applicable laws of the state of Utah, insurance rules promulgated by the state of Utah Insurance Department (Department), and Statements of Statutory Accounting Principles (SSAPs) contained within the Accounting Practices and Procedures Manual promulgated by the National Association of Insurance Commissioners (NAIC).

The examination included a general review and analysis of the Company's operations, the manner in which its business was conducted during the examination period and a determination of its financial condition as of December 31, 2003. Assets were verified and valued, and liabilities were determined or estimated. The Company retained the services of a certified public accounting firm to audit its financial records for the years under examination. Copies of audit confirmations were made available for the examiner's use.

Status of Adverse Findings, Material Changes in the Financial Statement, and Other Significant Regulatory Information Disclosed in the Previous Examination

Important points and recommendations noted in the prior examination report have been addressed by the Company or have received further comment in this report.

History

General

A certificate of authority authorizing the Company to transact the business of title insurance, as defined in Utah Code Annotated (UCA) § 31A-01-301(150) was issued by the Utah Insurance Department effective November 5, 1987.

There were no amendments to the articles of incorporation or the bylaws during the years under review.

Capital Stock

Article IV of the articles of incorporation stated the initial authorized capitalization at one million (1,000,000) shares of common stock having no par value. One hundred thousand three hundred fifty (100,350) shares of the stock were issued on November 5, 1987. The amount paid for the shares, \$1,003,500, served as the Company's initial capitalization.

In January 2002, The First American Corporation purchased thirty thousand six hundred and twenty-five (30,625) shares of stock, which represents one hundred percent (100%) ownership of the Company.

The Company repurchased a major portion of its common stock from its shareholder as follows:

<u>Period</u>	<u>Number of Shares</u>	<u>Dollar Amount</u>
October 31, 1988	50,000	\$ 500,000
February 9, 1990	5,000	50,000
March 27, 1991	4,725	47,250
April 1, 1992	5,000	50,000
April 1, 1993	5,000	50,000
	<u>69,725</u>	<u>\$ 697,250</u>

The net capital stock outstanding was \$306,250 (\$1,003,500 - \$697,250) as of December 31, 2003.

Dividends to Stockholders

No dividends were declared or paid during the examination period.

Management

Article III of the Company's bylaws states, "The business and affairs of the corporation shall be managed by its board of directors ... The number of directors of the corporation shall vary from not less than three (3) to a maximum of nine (9) directors as the board may itself from time to time determine."

Name and Residence

Principle Occupation

Brian Joseph Coe
Scottsdale, Arizona

South West Regional Vice President
First American Title Insurance Company

William M. Wirthlin Jr.
Salt Lake City, Utah

State Manager
First American Title Insurance Agency, LLC
Associated Title Insurance Agency, LLC

Ray Bill Whitney
Sandy, Utah

Chief Operations Officer
First American Title Insurance Agency, LLC

Blake Taggart Heiner
Salt Lake City, Utah

Claims Counsel
First American Title Insurance Company

Ronald Raymond Beliveau
Cave Creek, Arizona

South West Regional Chief Financial Officer
First American Title Insurance Company

Gary Lewis Kermott
Dana Point, California

President
The First American Corporation

Gary Lewis Kermott was elected as a director of the Company on September 22, 2003. However, the Company did not immediately notify the Commissioner of his election, nor was biographical information submitted to the Department as required by UCA § 31A-5-410(1)(a). Mr. Kermott's biographical affidavit was submitted to the Department during the course of the examination.

Officers:

Office

Officer

President
Secretary
Treasurer
Vice President

William M. Wirthlin Jr.
Blake Taggart Heiner
Ronald Raymond Beliveau
Brian Joseph Coe

Vice President
Vice President
Vice President
Vice President
Vice President

Ray Bill Whitney
Blake Taggart Heiner
Ronald Raymond Beliveau
Michael H. Muir
Gary Lewis Kermott

Conflict of Interest Procedure

Although the general interrogatories for all years under review indicated that directors and officers of the Company had a conflict of interest procedure in place, no conflict of interest statements were provided to the examination.

Corporate Records

The records generated for and during the period covered by the examination were reviewed. The records consisted of the minutes of the meetings of the board of directors and shareholder.

The Company did not provide evidence of board of directors or shareholder meeting minutes from January 1, 2000 through December 31, 2000. The Company's 2000 Annual Statement filed with the Department answered, "Yes" as the reporting entity keeping complete permanent records of the proceedings of its board of directors and all subordinate committees thereof. UCA § 16-10a-1601(1)(a) requires a corporation to keep permanent records of all shareholders and board of director meeting minutes.

The prior examination report as of December 31, 1999, was distributed to the board in March 2001.

Acquisitions, Mergers, Disposals, Dissolutions, and Purchase or Sales through Reinsurance

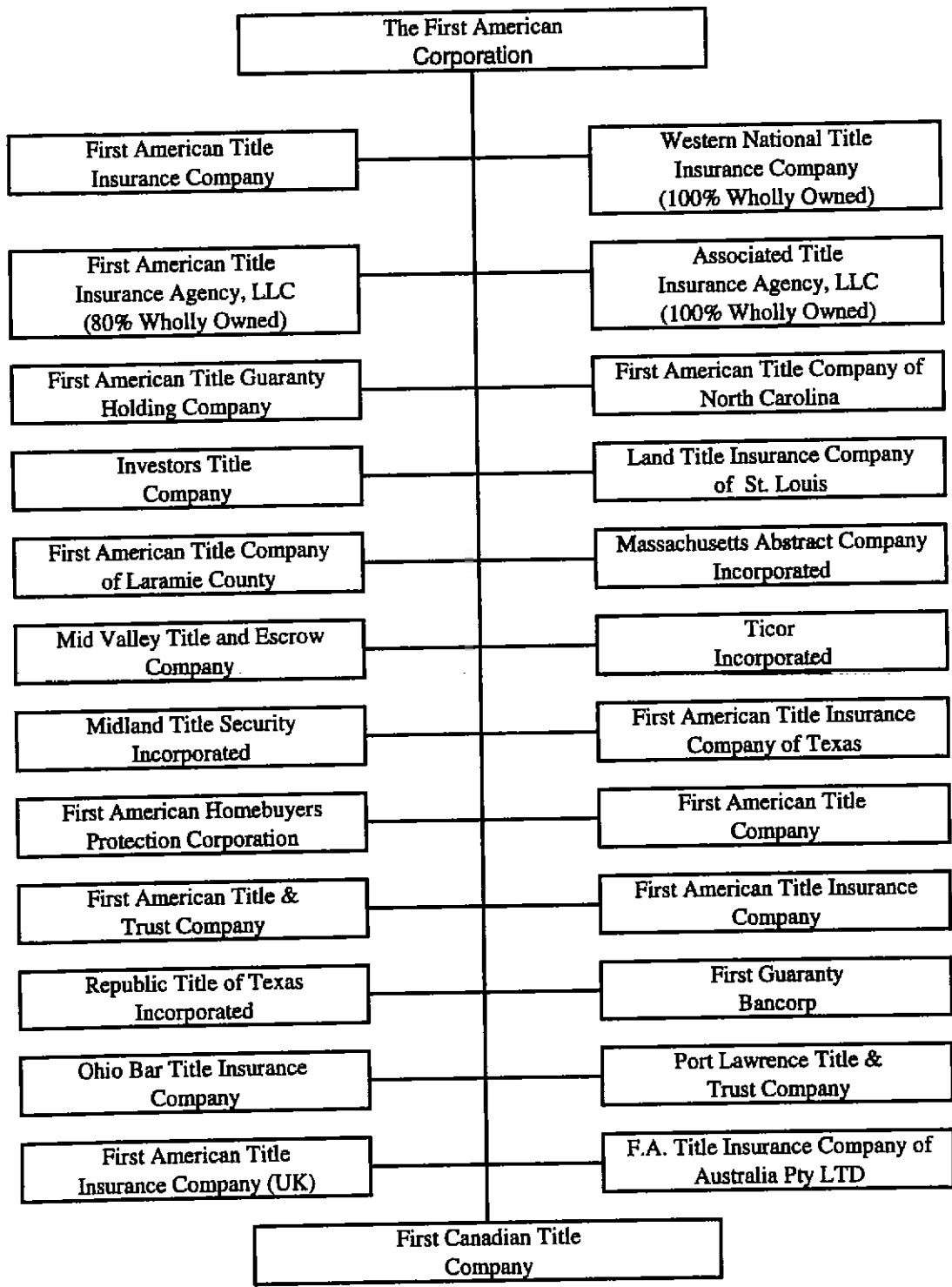
The Company was not a party to any acquisitions, mergers, disposals, dissolutions and purchase or sales through reinsurance during the examination period.

Surplus Debentures

No surplus notes were outstanding, retired or issued during the examination period.

Affiliated Companies

The Company is a member of a holding company system. The First American Corporation is the ultimate controlling person in the system. Through common control, the Company is affiliated with numerous entities within the holding company system. Following is an organizational chart of significant other companies within the holding company system.



Cost-Sharing Agreements and Significant Regulatory Information Concerning Parent, Subsidiaries, and Affiliates

On September 1, 2002, the Company entered into a management agreement with First American Title Insurance Agency, LLC. Under the agreement, First American Title Insurance Agency, LLC agreed to provide the following services including, but not limited to, the following for \$7,500.00 per month:

- Underwriting analysis and decisions, claims administration;
- Title training for employees for both companies, marketing, accounting;
- Legal consultation including coordination with outside counsel;
- General management services, office space and equipment.

On September 10, 2002, the Company entered into a title insurance underwriting agreement with Associated Title Insurance Agency, LLC (ATIA). Under the agreement, the Company authorized ATIA to issue commitments and policies of title insurance on its behalf within the State of Utah. However, ATIA is not allowed to issue any commitment or policy for liability in excess of \$2,000,000 without the prior written consent of the Company. ATIA pays the first \$3,500 of any claim made on pre-existing residential or commercial structure. ATIA submits 7.5% of the gross premium billed and retains the remaining 92.5%.

On September 10, 2002, the Company entered into a title insurance underwriting agreement with First American Title Insurance Agency, LLC (FATIA). Under the agreement, the Company authorized FATIA to issue commitments and policies of title insurance on its behalf within the State of Utah. However, FATIA is not allowed to issue any commitment or policy for liability in excess of \$2,000,000 without the prior written consent of the Company. FATIA pays the first \$3,500 of any claim made on pre-existing residential or commercial structure. FATIA submits 7.5% of the gross premium billed and retains the remaining 92.5%.

The First American Financial Corporation and some of its subsidiaries, including the Company, filed taxes on an allocation basis for the tax years 2002 and 2003. However, the Company did not enter into a written tax allocation agreement specifying the terms of the arrangement, including the rights and obligations of the participants. The absence of a tax allocation agreement is not in compliance with UCA § 31A-16-106(1)(a)(vi). In April 2004, the Company signed and executed a tax allocation agreement with The First American Financial Corporation.

Fidelity Bond and Other Insurance

The Company was a named insured on a joint endorsement attached to the fidelity bond policy of its parent, The First American Corporation. The minimum fidelity coverage suggested by the NAIC for an organization of the Company's size and premium volume is not less than \$125,000. As of December 31, 2003, the Company participated in fidelity bond coverage of \$15,000,000.

Pension, Stock Ownership and Insurance Plans

The Company did not offer any pension, stock ownership or insurance plans during the examination period.

Statutory Deposit

UCA § 31A-4-105 requires the Company to maintain a deposit in the amount of its required capital. According to UCA § 31A-5-211(2), the Company's minimum capital requirement was \$200,000. As of December 31, 2003, the book and market values of the statutory deposit were \$200,000 and \$200,093 respectively.

Insurance Products and Related Practices

Policy Forms and Underwriting

The policy forms issued by the Company consisted primarily of an owner's policy of title insurance for residential property and a lender's policy of title insurance for second mortgages, refinancing, home equity loans, and first mortgages on existing structures. The Company issued a limited number of owners and lenders' policy of title insurance concerning new structures on residential property and to residential builders/developers. As of December 31, 2003, the Company also had underwritten limited amounts of commercial properties.

The policy forms issued during the examination period were consistent with Department approved forms. The Company's single risk retention limit was \$750,000 and over \$2,000,000 in the aggregate.

Territory and Plan of Operations

During the examination period the Company was authorized to conduct title insurance business in the State of Utah and did not operate in any other jurisdictions.

Four agencies sold title insurance on behalf of the Company.

Advertising and Sales Material

The Company's marketing efforts relied heavily upon the agencies with which it contracted to sell its products. Most of its advertising was done by these agencies through direct contact with banks, mortgage companies, other lenders, and real estate persons.

Treatment of Policyholders

There were no complaints registered with the Utah Insurance Department for the period covered by this examination.

Reinsurance

Assumed

The Company did not assume any insurance risk during the examination period.

Ceded

During the period January 2, 2002, through July 20, 2003, the Company was without reinsurance coverage since the agreement with Fidelity National Title Insurance Company was terminated on January 2, 2002. However, the Company entered into a reinsurance agreement with its parent, First American Title Insurance Company on July 21, 2003, with an effective date of January 2, 2002. First American Title Insurance Company reinsured risks over \$750,000 or \$2,000,000 in the aggregate. The primary retention is \$750,000. The premium paid for reinsurance coverage was \$0.25 per \$1,000 of reinsurance risk over \$750,000.

The Company's reinsurer did not submit to the jurisdiction of the courts of Utah with regards to a reinsurance agreement. The Company did not claim credit against reserves for reinsurance ceded.

Accounts and Records

Employees who were contracted from First American Title Insurance Agency, LLC performed the Company's accounting procedures and financial reporting functions. The accounting system consisted of a general ledger, journals, registers, statistical records and other related records. Many of the records were maintained on local area network electronic data processing systems, personal computers, and in hard copy form.

Accounts and records deficiencies included the following:

- The Company reported in its annual statements that its special deposits were not being held for the benefit of all policyholders, claimants, and creditors. However, deposits being held were held for the benefit of all policyholders, claimants and creditors.

- The Common Capital Stock reported on the 2003 Annual Statement was erroneously stated. The reporting error was not considered material for examination purposes and an adjustment was not made. The Company's surplus as regards policyholders was correctly stated.
- As stated on the signature card for the Company's checking account two (2) signatures are required on all checks issued. However, many of the checks issued by the Company had only one (1) signatory's signature.
- Several securities purchased and sold during the year 2003 were not disclosed on the Schedule D – Part 5. It is recommended that the Company disclose securities purchased and sold during the same year in accordance with NAIC Annual Statement Instructions.

UCA §31A-4-113 requires each authorized insurer to file a true statement of its financial condition and affairs as of December 31 of the preceding year in accordance with the annual statement instructions and the accounting practices and procedures published by the NAIC. According to the NAIC annual statement instructions, a statement is not considered filed unless the information therein is complete and accurate.

Financial Statements

The following financial statements were prepared from the Company's accounting records and the valuations and determinations made during the examination:

Balance Sheet as of December 31, 2003

Summary of Operations -
for the Period Ended December 31, 2003

Reconciliation of Capital and Surplus Account -
January 1, 2000 through December 31, 2003

The accompanying Notes to Financial Statements are an integral part of the financial statements.

Western National Title Insurance Company
Balance Sheet as of December 31, 2003

QUALIFIED ASSETS

	<u>Amount</u>	<u>Notes</u>
Bonds	\$ 3,350,810	(1)
Cash, Cash Equivalents and Short-Term Investments	1,343,381	(2)
Investment Income Due and Accrued	22,564	
Uncollected Premiums and Agent's Balances in the Course of Collection	17,973	
Net Deferred Tax Asset	12,237	
Total Qualified Assets	\$ 4,746,965	

LIABILITIES, CAPITAL AND SURPLUS

Known Claims Reserve	\$ 334,106	
Statutory Premium Reserve	1,376,863	
Other Expenses	5,899	
Taxes, Licenses and Fees Due or Accrued	4,107	
Current Federal and Foreign Income Taxes	47,033	
Total Liabilities	1,768,008	
Common Capital Stock	1,070,167	
Unassigned Funds (Surplus)	2,606,040	
Treasury Stock	(697,250)	
Surplus as regards Policyholders	2,978,957	(3)
Total Liabilities, Capital and Surplus	\$ 4,746,965	

Western National Title Insurance Company
Summary of Operations
for the Period Ended December 31, 2003

Operating Income

Title Insurance Premiums Earned \$ 7,445,158

Deduct:

Losses and Loss Adjustment Expenses Incurred 120,469

Operating Expenses Incurred 7,164,211

Total Operating Deductions 7,284,680

Net Operating Gain 160,478

Investment Income

Net Investment Income Earned 66,794

Other Income

Net Income, Before Federal Income Taxes 227,272

Federal and Foreign Income Taxes Incurred (111,342)

Net Income \$ 115,930

Western National Title Insurance Company
Reconciliation of Capital and Surplus Account
January 1, 2000 through December 31, 2003

	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>Per Exam 2003</u>
Reserves and Unassigned Funds December 31 Previous Year	\$ 2,076,583	\$ 2,390,590	\$ 2,588,367	\$ 2,807,762
Net Gain or (Loss)	263,923	181,317	209,353	115,930
Change in Net Deferred Income Tax				188,440
Change in Nonadmitted Assets				(176,203)
Prior Year Federal Income Tax Adjustment				43,028
Reserve Adjustment	(16,583)	16,460	10,042	
Release Contingent Liability	<u>66,667</u>			
Net Change in Reserves and Unassigned Funds	<u>314,007</u>	<u>197,777</u>	<u>219,395</u>	<u>171,195</u>
Reserves and Unassigned Funds	<u>\$ 2,390,590</u>	<u>\$ 2,588,367</u>	<u>\$ 2,807,762</u>	<u>\$ 2,978,957</u>

Notes to Financial Statements

(1) Bonds

\$3,350,810

As of December 31, 2003, the Company reported Bonds of \$3,250,000.

A certificate of deposit of \$100,810 was reclassified to Bonds from Cash pursuant to SSAP No. 26. SSAP No. 26 states that certificates of deposits with a maturity date in excess of one year shall be classified as a bond.

(2) Cash, Cash Equivalents and Short-Term Investment Investments

\$1,343,381

As of December 31, 2003, the Company reported Cash of \$1,444,191. The Company did not report any Cash Equivalents or Short-Term Investments.

Pursuant to the Purposes and Procedures Manual of the NAIC Securities Valuation Office Part Four and Part Eleven, the examination reclassified a Dreyfus cash management fund of \$200,000 from Cash to Short-Term Investments.

Pursuant to SSAP No. 26 the examination reclassified a certificate of deposit of \$100,810 to Bonds since the investment maturity was in excess of one-year.

(3) Surplus as Regards Policyholders

\$2,978,957

Adjustments made to balances reported by the Company are identified below:

<u>Description</u>	<u>Annual Statement Dr (Cr)</u>	<u>Per Examination</u>	<u>Change in Surplus Inc. (Dec.)</u>	<u>Notes</u>
Bonds	\$ 3,350,810	\$ 3,250,000	\$ 100,810	(1)
Cash, Cash Equivalents and Short-Term Investments	1,343,381	1,444,191	<u>(100,810)</u>	(2)
Total Examination Changes			<u>-</u>	
Surplus as Regards Policyholders			<u>2,978,957</u>	
Surplus as Regards Policyholders			<u>\$ 2,978,957</u>	

The Company's minimum adjusted capital requirement, pursuant to UCA § 31A-17-609, was \$813,516. Its surplus as regards policyholders was determined to be \$2,978,957. The Company's excess surplus pursuant to UCA § 31A-1-301(120)(c) was \$1,758,683.

Summary


Items of significance or special interest contained in this report are summarized below:

1. The Company did not provide evidence to the examination of its shareholder and board of directors meeting minutes from January 2000, through December 2000. U.C.A. §16-10a-1601 requires a corporation to keep as permanent records all actions taken on behalf of the corporation by its shareholder and board of directors. (**History - Corporate Records**)
2. The Company did not execute a tax allocation agreement, which is not in compliance with UCA § 31A-16-106(1)(a)(iv). In 2004, the Company signed and executed a tax allocation agreement with The First American Financial Corporation. (**Affiliated Companies - Cost-Sharing Agreements and Significant Regulatory Information Concerning Parent, Subsidiaries and Affiliates**)
3. The Company did not provide evidence that the directors and officers signed and executed conflict of interest procedures on an annual basis. It is recommended that the directors and officers sign and execute conflict of interest statements on an annual basis. (**History - Conflict of Interest Procedure**)
4. Accounts and records deficiencies were noted during the examination. (**Accounts and Records**)
5. The Company's minimum adjusted capital requirement, pursuant to UCA § 31A-17-609, was \$813,516. Its surplus as regards policyholders was determined to be \$2,978,957. The Company's excess surplus pursuant to UCA § 31A-1-301(120)(c) was \$1,758,683. (**Notes to Financial Statements**)

Conclusion

The assistance and cooperation extended during the course of the examination by officers, employees and representatives of the Company is acknowledged.

Respectfully submitted,



Allen J. Hart, CFE
Audit Manager
Utah Insurance Department