

REPORT OF EXAMINATION
OF THE
COMPWEST INSURANCE COMPANY
AS OF
DECEMBER 31, 2018

Filed on May 12, 2020

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Oakland, California
April 30, 2020

Honorable Ricardo Lara
Insurance Commissioner
California Department of Insurance
Sacramento, California

Dear Commissioner:

Pursuant to your instructions, an examination was made of the

COMPWEST INSURANCE COMPANY

(hereinafter also referred to as the Company) at the primary location of its books and records at 200 North Grand Avenue, Lansing, Michigan 48933. The Company's statutory home office is located at 3 Hutton Centre Drive, Suite 550, Santa Ana, California 92707.

SCOPE OF EXAMINATION

We have performed our multi-state examination of the Company. The previous examination of the Company was as of December 31, 2015. This examination covered the period from January 1, 2016 through December 31, 2018.

The examination was conducted in accordance with the National Association of Insurance Commissioners *Financial Condition Examiners Handbook (Handbook)*. The Handbook requires the planning and performance of the examination to evaluate the Company's financial condition, assess corporate governance, identify current and prospective risks, and evaluate system controls and procedures used to mitigate those risks. An examination also includes identifying and evaluating significant risks that could cause an insurer's surplus to be materially misstated both currently and prospectively.

All accounts and activities of the Company were considered in accordance with the risk-focused examination process. This may include assessing significant estimates made by management and evaluating management's compliance with Statutory Accounting Principles. The examination does not attest to the fair presentation of the financial statements included herein. If, during the course of the examination, an adjustment is identified, the impact of such adjustment will be documented separately following the Company's financial statements.

This examination report includes findings of fact and general information about the Company and its financial condition. There might be other items identified during the examination that, due to their nature (e.g., subjective conclusions, proprietary information, etc.), were not included within the examination report but separately communicated to other regulators and/or the Company.

This was a coordinated examination with Michigan as the lead state. It was conducted concurrently with other insurance entities in the holding company group, including Accident Fund Insurance Company of America, Accident Fund General Insurance Company, Accident Fund National Insurance Company, United Wisconsin Insurance Company, and Third Coast Insurance Company. The following states participated on the examination: California and Wisconsin.

COMPANY HISTORY

Capitalization

As of December 31, 2018, the Company had 10,000 shares of \$300 par value common stock authorized, issued and outstanding.

MANAGEMENT AND CONTROL

The Company is part of an insurance holding group owned by Accident Fund Holdings, Inc. (AFHI). The AFHI group primarily provides workers compensation insurance. It is ultimately owned by Blue Cross Blue Shield of Michigan Mutual Insurance Company (BCBSMMIC). Following is an abridged organizational chart reflecting the ownership structure at December 31, 2018. All ownership is 100%:

Blue Cross Blue Shield of Michigan Mutual Insurance Company (Michigan)
Emergent Holdings, Inc. (Michigan)
 Accident Fund Holdings, Inc. (Michigan)
 Accident Fund Insurance Company of America (Michigan)
 Accident Fund General Insurance Company (Michigan)
 Accident Fund National Insurance Company (Michigan)
 CompWest Insurance Company (California)
 United Wisconsin Insurance Company (Wisconsin)
 Third Coast Insurance Company (Wisconsin)

The five members of the board of directors, who are appointed annually, oversee the business and affairs of the Company. Following are members of the board and principal officers of the Company serving at December 31, 2018:

Directors

<u>Name and Location</u>	<u>Principal Business Affiliation</u>
Lisa M. Corless Okemos, Michigan	President and Chief Executive Officer Accident Fund Holdings, Inc.
Alan G. Gileczek Gregory, Michigan	President CompWest Insurance Company
Elizabeth R. Haar Dexter, Michigan	President and Executive Vice President Blue Cross Blue Shield of Michigan Mutual Insurance Company and Emerging Markets
Anthony G. Phillips Howell, Michigan	Executive Vice President, Chief Risk Officer, and Chief Actuary Emerging Markets

Name and Location

Principal Business Affiliation

Steven E. Reynolds^(a)
Milford, Michigan

Vice President and Secretary
Accident Fund Holdings, Inc.

Principal Officers

Name

Title

Alan G. Gileczek

President

Steven E. Reynolds^(a)

Secretary

Anthony G. Phillips

Treasurer

^(a) Steven E. Reynolds, Director and Secretary, retired on July 2, 2019. John S. Roberts was appointed as a Director, effective June 6, 2019. Bobbi J. Elliott was appointed Secretary, effective June 6, 2019.

Management Agreements

Intercompany Tax Sharing Agreement: Effective October 3, 2017, the Company entered into an Intercompany Tax Sharing Agreement with its parent, Blue Cross Blue Shield of Michigan Mutual Insurance Company (BCBSMMIC), which was approved by the California Department of Insurance (CDI) on October 3, 2017. The agreement provides for BCBSMMIC and its subsidiaries to participate in the consolidated tax return. Income tax liability is settled between the parties based on the difference between each party's consolidated and separate return calculations, with payments due or receivable within 30 days of calculation. This agreement replaced an earlier agreement, effective October 15, 2013. Changes were made to consolidate previous tax sharing agreements and more plainly specify the duties of BCBSMMIC. Taxes payable/(receivable) under this agreement for 2016, 2017, and 2018 were \$6,170,082, (\$816,000), and \$240,000, respectively.

Inter-Company Services Agreement: Effective February 15, 2010, the Company entered into an Inter-Company Services Agreement with its parent, BCBSMMIC, which was approved by the CDI on February 12, 2010. The agreement allows the Company to receive and/or provide various administrative services. Services include but are not limited to: financial accounting, underwriting, communications, marketing, claims administration, information systems, and general and administrative services. A First Amendment to the Inter-Company Services Agreement was effective February 15, 2018, and approved by the CDI on February 15, 2018. This amendment provides for the addition/removal of Group members, prohibiting the advancement of funds to Group members and adding an insolvency clause. The amounts paid by the Company were: \$9,198,343, \$10,817,818 and \$13,406,509 for these services in 2016, 2017, and 2018, respectively.

TERRITORY AND PLAN OF OPERATION

The Company writes workers' compensation with a focus on the western states. As of December 31, 2018, the Company was licensed in the following states: Alaska, Arizona, California, Colorado, Hawaii, Idaho, Michigan, Montana, Nevada, Oregon, Utah, and Washington. Direct premiums written in 2018 were \$152,304,630 and 91.5% was concentrated in California. The Company targets small to medium-sized companies in the following industries: health care, hospitality, manufacturing, professional services, and retail and wholesale services. Business is generated through a network of independent brokers.

REINSURANCE

Intercompany Pooling Agreement

Effective January 1, 2017, the Company entered into an Intercompany Pooling Agreement with its parent and affiliates. Accident Fund Insurance Company of America

is the lead company in the pool. The following table illustrates each participant's pooled share as of December 31, 2018:

<u>Company</u>	<u>State of Domicile</u>	<u>Pooling Share</u>
Accident Fund Insurance Company of America (AFICA)	MI	98.97%
Accident Fund General Insurance Company (AFG)	MI	0%
Accident Fund National Insurance Company (AFN)	MI	0%
United Wisconsin Insurance Company (UWIC)	WI	0%
Third Coast Insurance Company	WI	0%
CompWest Insurance Company	CA	1.03%
Pool Total		<u>100.00%</u>

The agreement authorizes and empowers the Company to (1) collect and receive all premiums, (2) adjust and pay all losses, (3) reinsure or cancel any and all policies and contracts of insurance, and (4) act as though the policies and contracts of insurance and reinsurance were issued by the Company. It further provides for the complete sharing of all income and expenses of the pooled business with the exception of the investment operations, liabilities for federal income tax, or other items not relating to the underwriting operations of the parties. Accounts are required to be settled quarterly.

Assumed

Aside from amounts assumed under the Intercompany Pooling Agreement, the Company participates in the National Workers Compensation Reinsurance Pool (NWCRP). Amounts assumed from the NWCRP were immaterial during the examination period.

Ceded

The Company participated in the following ceded reinsurance agreements under the Intercompany Pooling Agreement as of December 31, 2018:

Type of Contract	Line(s) of Business	Reinsurer(s) and Participation	Company's Retention	Reinsurer's Limit
Catastrophe Excess of Loss First Layer	Workers' Compensation	<u>Certified:</u> Lloyd's of London – Various (56.5%) Hannover Rueck SE (5.0%) <u>Unauthorized:</u> Various reinsurers (38.5%)	\$10 million each and every loss occurrence	\$10 million excess of \$10 million each and every loss occurrence, \$10 million in aggregate
Second Layer	Workers' Compensation	<u>Certified:</u> Lloyd's of London – Various (52.0%) Various reinsurers (13.0%) <u>Authorized:</u> Markel Global RE (5.0%) <u>Unauthorized:</u> Various reinsurers (30.0%)	\$20 million each and every loss occurrence	\$20 million excess of \$20 million each and every loss occurrence, \$20 million in aggregate
Third Layer	Workers' Compensation	<u>Certified:</u> Lloyds of London – Various (61.825%) Various reinsurers (5.0%) <u>Authorized:</u> Markel Global RE (2.5%) <u>Unauthorized:</u> Various reinsurers (30.675%)	\$40 million each and every loss occurrence	\$40 million excess of \$40 million each and every loss occurrence, \$160 million in aggregate
Quota Share	Commercial Property	<u>Unauthorized:</u> Allianz Risk Transfer AG	5.0% up to \$8 million each and every Policy, each and every loss	95.0% up to \$152 million each and every Policy, each and every loss

Type of Contract	Line(s) of Business	Reinsurer(s) and Participation	Company's Retention	Reinsurer's Limit
Quota Share	Commercial Automobile Liability	<u>Certified:</u> Lloyds of London – Various <u>Unauthorized:</u> Various reinsurers	13.0% of Company's net loss up to \$1 million, any one loss occurrence, \$85,000 underinsured motorist limit and \$2500 Personal Injury Protection	87.0% up to \$1 million, any one loss occurrence, \$85,000 underinsured motorist limit and \$2500 Personal Injury Protection
Quota Share	General Liability	<u>Unauthorized:</u> Various reinsurers	17.5% up to \$1 million per occurrence, \$2 million in aggregate	17.5% up to \$1 million per occurrence, \$2 million in aggregate

FINANCIAL STATEMENTS

The following financial statements are based on the statutory financial statements filed by the Company with the California Department of Insurance and present the financial condition of the Company for the period ending December 31, 2018. The accompanying comments to the amounts in the financial statements should be considered an integral part of the financial statements. No adjustments were made to the financial statements as a result of the examination.

Statement of Financial Condition as of December 31, 2018

Underwriting and Investment Exhibit for the Year Ended December 31, 2018

Reconciliation of Surplus as Regards Policyholders from December 31, 2015
through December 31, 2018

Statement of Financial Condition

as of December 31, 2018

<u>Assets</u>	<u>Assets</u>	<u>Assets Not Admitted</u>	<u>Net Admitted Assets</u>	<u>Notes</u>
Bonds	\$ 139,658,453	\$	\$ 139,658,453	
Preferred stocks	1,067		1,067	
Common stocks	18,286		18,286	
Cash, cash equivalents, and short-term investments	9,062,342		9,062,342	
Investment income due and accrued	763,579		763,579	
Uncollected premiums and agents' balances in course of collection	42,806,020	1,891,560	40,914,460	
Deferred premiums, agents' balances and installments booked but deferred and not yet due (including \$7,365,438 earned but unbilled premiums)	40,599,742	743,018	39,856,724	
Accrued retrospective premiums	72,037	7,414	64,623	
Amounts recoverable from reinsurers	73,850		73,850	
Other amounts receivable under reinsurance contracts	10,461		10,461	
Net deferred tax asset	2,142,417	283,918	1,858,499	
Guaranty funds receivable or on deposit	18,101		18,101	
Furniture and equipment	244	244		
Receivables from parent, subsidiaries and affiliates	16,990		16,990	
Aggregate write-ins for other than invested assets	<u>240,492</u>	<u>141,805</u>	<u>98,687</u>	
Total assets	<u>\$ 235,484,081</u>	<u>\$ 3,067,959</u>	<u>\$ 232,416,122</u>	

Liabilities, Surplus, and Other Funds

		<u>Current Year</u>	<u>Notes</u>
Losses and loss adjustment expenses	\$	\$ 15,665,390	(1)
Reinsurance payable on paid loss and loss adjustment expenses		412,563	
Loss adjustment expenses		1,932,632	(1)
Commissions payable, contingent commissions and other similar charges		705,512	
Other expenses		498,508	
Taxes, licenses, and fees		469,569	
Current federal and foreign income taxes		1,011,445	
Unearned premiums		6,709,320	
Advance premiums		92,853	
Dividends declared and unpaid: Policyholders		172,937	
Ceded reinsurance premiums payable		60,369,661	
Funds held by company under reinsurance treaties		9,378	
Amounts withheld or retained by company for account of others		151,164	
Provision for reinsurance		270,000	
Payable for parent, subsidiaries and affiliates		1,196,021	
Payable for securities		37,150	
Aggregate write-ins for liabilities		225,237	
Total liabilities		89,929,070	
Common capital stock	\$ 3,000,000		
Gross paid-in and contributed surplus	47,000,000		
Unassigned funds (surplus)	92,487,052		
Surplus as regards policyholders		<u>142,487,052</u>	
Total liabilities, surplus, and other funds		<u>\$ 232,416,122</u>	

Underwriting and Investment Exhibit
for the Year Ended December 31, 2018
Statement of Income

Underwriting Income

Premiums earned		\$ 14,648,894
Deductions:		
Losses incurred	\$ 6,593,408	
Loss adjustment expenses incurred	2,103,103	
Other underwriting expenses incurred	<u>3,386,375</u>	
Total underwriting deductions		<u>12,082,886</u>
Net underwriting gain		2,566,008
<u>Investment Income</u>		
Net investment income earned	\$ 3,878,780	
Net realized capital losses	<u>(777,761)</u>	
Net investment gain		3,101,019
<u>Other income</u>		
Net loss from agents' or premium balances charged off	\$ (143,380)	
Finance and service charges not included in premiums	13,964	
Aggregate write-ins for miscellaneous income	<u>1,117</u>	
Total other income		<u>(128,299)</u>
Net income before dividends to policyholders, after capital gains tax and before federal and foreign income taxes		
Dividends to policyholders		203,181
Net income after dividends to policyholders, after capital gains tax and before federal and foreign income taxes		5,335,547
Federal and foreign income taxes incurred		<u>472,147</u>
Net income		<u>\$ 4,863,400</u>

Capital and Surplus Account

Surplus as regards policyholders, December 31, 2017		\$ 137,695,194
Net income	\$ 4,863,400	
Change in net unrealized capital gains	145,202	
Change in net deferred income tax	(121,214)	
Change in nonadmitted assets	504,860	
Change in provision for reinsurance	<u>(270,000)</u>	
Change in surplus as regards policyholders for the year		<u>4,791,858</u>
Surplus as regards policyholders, December 31, 2018		<u>\$ 142,487,052</u>

Reconciliation of Surplus as Regards to Policyholders
from December 31, 2015 through December 31, 2018

Surplus as regards policyholders, December 31, 2015			\$ 127,716,613
	Gain in Surplus	Loss in Surplus	
	<u> </u>	<u> </u>	
Net income	\$ 17,998,000	\$	
Net unrealized capital gains	148,274		
Change in net deferred income tax		2,127,869	
Change in nonadmitted assets		524,581	
Change in provision for reinsurance		269,600	
Aggregate write-ins for gains and losses in surplus		<u>453,785</u>	
Total gains and losses	<u>\$ 18,146,274</u>	<u>\$ 3,375,835</u>	
Net increase in surplus as regards policyholders			<u>14,770,439</u>
Surplus as regards policyholders, December 31, 2018			<u>\$ 142,487,052</u>

COMMENTS ON FINANCIAL STATEMENT ITEMS

Losses and Loss Adjustment Expenses

The December 31, 2018 losses and loss adjustment expense reserves were evaluated by a consulting actuary from the Michigan Department of Insurance and Financial Services. Based on the analysis performed, the Company's losses and loss adjustment expense reserves were found to be reasonably stated. An actuary from the California Department of Insurance (CDI) reviewed the work performed by the lead state, and concurred with their conclusion that losses and loss adjustment expense reserves were reasonably stated.

SUBSEQUENT EVENTS

A novel strain of coronavirus (COVID-19) was detected and reported to World Health Organization (WHO) in December 2019. Since then, it has spread around the world, resulting in business and social disruption. The outbreak was declared a Public Health Emergency of International Concern by the WHO on January 30, 2020. The pandemic has triggered unprecedented government mandates and health and safety measures which have significantly impacted the U.S. and global financial markets, in particular, U.S. publicly traded equity securities, and impacts on yields and interest rates in the U.S. bond market. As the pandemic still unfolds, it is too early to draw any definite conclusions as to its overall impact to the Company at this time.

SUMMARY OF COMMENTS AND RECOMMENDATIONS

Current Report of Examination

None.

Previous Report of Examination

Subsequent Events – Corporate Governance Annual Disclosure (Page 13): It was recommended that the Company file the full attestation as required by California Insurance Code Section 936.3, subdivision (b), in order for the 2015 and 2016 Corporate Governance Annual Disclosures to be complete. The Company is now in compliance.

ACKNOWLEDGEMENT

Acknowledgement is made of the cooperation and assistance extended by the Company's officers and employees during the course of this examination.

Respectfully submitted,

_____/S/_____

Jennifer Whitehurst, CFE
Examiner-In-Charge
Associate Insurance Examiner
Department of Insurance
State of California

_____/S/_____

Kyo Chu, CFE
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