REPORT OF EXAMINATION

OF THE

EXPLORER INSURANCE COMPANY

AS OF

DECEMBER 31, 2016

Filed On June 28, 2018

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Los Angeles, California
May 31, 2018

Honorable Dave Jones
Insurance Commissioner
California Department of Insurance
Sacramento, California

Dear Commissioner:

Pursuant to your instructions, an examination was made of the

EXPLORER INSURANCE COMPANY

(hereinafter also referred to as the Company) at its home office located at 15025 Innovation Drive, San Diego, CA 92128.

SCOPE OF EXAMINATION

We have performed our multi-state examination of the Company. The previous examination of the Company was made as of December 31, 2012. This examination covers the period from January 1, 2013 through December 31, 2016.

The examination was conducted in accordance with the National Association of Insurance Commissioners Financial Condition Examiners 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. The examination also included identifying and evaluating significant risks that could cause the Company'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 did not attest to the fair presentation of the financial statements included herein. If, during the course of the examination an adjustment was identified, the impact of such adjustment would 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.

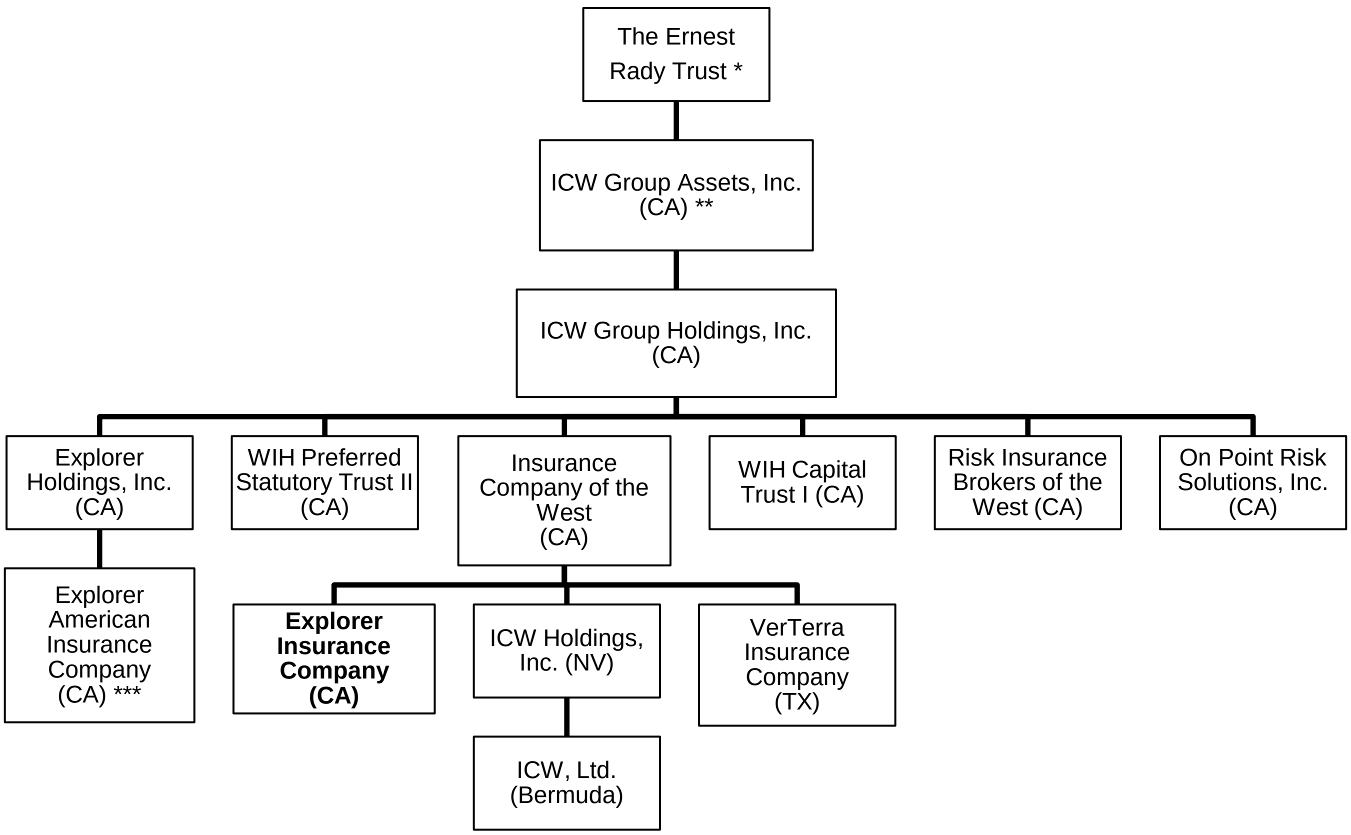
The examination was a coordinated examination and was conducted concurrently with the examinations of other insurance entities in the holding company group, including Insurance Company of the West (California), Explorer American Insurance Company (California), and VerTerra Insurance Company (Texas).

COMPANY HISTORY

All of the Company's outstanding shares are owned by Insurance Company of the West (West). On October 15, 2015, West purchased an additional 19,000 shares of the Company's capital stock for $1,900,000. As of December 31, 2016, West holds 45,000 capital shares of the Company.

MANAGEMENT AND CONTROL

The Company is a member of an insurance holding company system of which ultimate control is held by The Ernest Rady Trust. The Company's ultimate parent is the ICW Group Holdings, Inc., a California holding company which is 82.65% owned by American Assets, Inc. (dba ICW Group Assets, Inc.). The following abridged organizational chart is limited to the entities the Company had interrelationships as of December 31, 2016 (all ownership is 100% unless otherwise indicated):



* The Ernest Rady Trust, owns 75.88% of ICW Group Assets, Inc.; 10.6% is owned by Donald Rady Trust #2; 13.52% owned by other individuals with less than 10% controlled by one individual.

** ICW Group Assets, Inc. owns 82.65% of ICW Group Holdings, Inc.; 14.8% is owned by Ernest Rady Trust; 2.55% owned by other individuals with less than 10% controlled by one individual.

*** Effective January 1, 2017, Explorer American Insurance Company (EAIC) became a wholly-owned subsidiary of the Insurance Company of the West. Effective May 15, 2017, EAIC's name was changed to ICW National Insurance Company.

The five members of the board of directors, who are elected annually, manage the business and affairs of the Company. Following are members of the board and principal officers of the Company serving at December 31, 2016:

Directors

Name and Location	Principal Business Affiliation
Bernard M. Feldman Del Mar, California	Vice Chairman Insurance Company of the West
Teresa R.T. Leon San Diego, California	Vice President, Secretary, and General Counsel Insurance Company of the West
Kevin M. Prior San Diego, California	President and Chief Executive Officer Insurance Company of the West
Ernest S. Rady La Jolla, California	Chairman of Board Insurance Company of the West
Fariborz Rostamian San Diego, California	Senior Vice President, Treasurer, and Chief Financial Officer Insurance Company of the West

Principal Officers

Name	Title
Kevin M. Prior	President and Chief Executive Officer
David G. Hoppen *	Senior Vice President
Fariborz Rostamian	Senior Vice President, Treasurer, and Chief Financial Officer
Paul F. Zamora	Senior Vice President
Susan L. Karlan	Senior Vice President
Richard S. Marshall	Senior Vice President
Teresa R.T. Leon	Vice President, Secretary, and General Counsel
Richard S. Fineman	Vice President
Amanda J. Granger	Vice President

* On October 19, 2017, John Novak replaced David G. Hoppen as the Chief Operating Officer with an official effective date of January 1, 2018.

Intercompany Agreements

Federal Tax Allocation Agreement - Since 1996, the Company and its affiliates have been parties to a Federal Tax Allocation Agreement with its ultimate parent, American Assets, Inc. Pursuant to the terms of the agreement, the consolidated federal tax liability is allocated among the subsidiaries in the ratio that each subsidiary's separate tax return liability bears to the total consolidated federal tax liabilities of all subsidiaries that are members of the consolidated group. This agreement was in place before prior approval was required under California Insurance Code (CIC) Section 1215.5(b)(4). Taxes paid under this agreement for 2013 and 2014 were $6,616,879 and $7,278,651, respectively.

Effective January 1, 2015, this Federal Tax Allocation Agreement was amended to rename some of the participants as follows: American Assets, Inc. and AAI Aviation, Inc. (collectively known as "AAI"), ICW Group Holdings, Inc., Insurance Company of the West (West), the Company, Explorer American Insurance Company (American), VerTerra Insurance Company (VerTerra), Explorer Holdings, Inc., ICW Holdings, Inc., ICW, Ltd., On Point Risk Solutions, Inc., and Risk Insurance Brokers of the West. The California Department of Insurance (CDI) approved this agreement on April 2, 2015. Taxes paid under this agreement for 2015 and 2016 were $8,721,099 and $8,129,757, respectively.

Intercompany Affiliated Management Agreement – Effective January 1, 2015, the Company, its parent, West and its affiliates, American and VerTerra, collectively known as ICW Group, entered into an Intercompany Affiliated Management Agreement (Agreement) with its ultimate parent ICW Group Holdings, Inc. (ICW Holdings). Under the terms of the Agreement, ICW Holdings will provide general administrative services to the ICW Group. The Company will receive insurance-related services from West; and American will provide insurance services to the Company for personal-lines automobile business. Each service recipient agrees to reimburse the performing entity for the actual cost of services provided. The CDI approved the Agreement on

December 19, 2014. The amounts paid by the Company for these services for 2015 and 2016 were $6,606,217 and $16,028,058, respectively.

Amended and Restated Investment Management Agreement – Since July 1, 2012, the Company, its parent, West and its affiliates, American, VerTerra, ICW, Ltd. together with its ultimate parent, ICW Group Holdings, Inc., collectively known as ICW Group Entities, have been parties to an Investment Management Agreement (Agreement) provided by American Assets Investment Management, LLC, (AAIM), a Delaware limited liability company, and an affiliated entity. Under the terms of the Agreement, AAIM has provided investment advisory services to the ICW Group Entities. As compensation, the ICW Group Entities have paid AAIM, a fee based on the actual cost incurred in managing its investment. Effective October 7, 2013 and March 3, 2014, First and Second amendments, respectively, were made to the Agreement. The amounts paid by the Company for these services for the years 2013 and 2014, were $439,430 and $547,371, respectively.

To consolidate the first and second amendments to the Agreement that were not previously approved by the CDI, effective March 20, 2015, the ICW Group Entities and AAIM, entered into the Amended and Restated Investment Management Agreement (Amended Agreement). The CDI approved the Amended Agreement on March 20, 2015. The amounts paid by the Company for these services for the years 2015 and 2016, were $235,000, and $313,000, respectively.

TERRITORY AND PLAN OF OPERATION

As of December 31, 2016, the Company was licensed and authorized to write various property and casualty lines of insurance in the following 28 states:

Arizona	Hawaii	Massachusetts	New Mexico	Vermont
California	Idaho	Michigan	Oregon	Virginia
Colorado	Illinois	Mississippi	Pennsylvania	Washington
Connecticut	Indiana	Montana	Tennessee	West Virginia
Delaware	Iowa	Nevada	Texas	
Florida	Maryland	New Jersey	Utah	

The Company specializes in writing nonstandard private passenger automobile liability and physical damage coverages. The Company generated nationwide direct premiums of $27.4 million, primarily from California, $27.3 million (99.5%); New Jersey, $71,000 (0.3%); and Pennsylvania, $52,000 (0.2%). The direct premiums written consisted of private passenger automobile liability, $15.7 million (57.1%); private passenger automobile physical damage, $11.6 million (42.4%); and workers compensation, $131,000 (0.5%).

REINSURANCE

Intercompany Quota Reinsurance Pooling Agreement

The Company is party to an intercompany reinsurance pooling agreement with its parent, Insurance Company of the West (West), and its affiliate, VerTerra Insurance Company (VerTerra). Under the terms of this agreement dated December 31, 1995, the Company and VerTerra cede 100% of their written premiums to West. West, in turn, retrocedes 15% and 1.5% pro rata portion of premiums, losses and expenses to the Company and VerTerra, respectively. The following table illustrates each Participant’s pooled share as of December 31, 2016.

Company Name	NAIC #	State of Domicile	Pool Participation
Insurance Company of the West	27847	CA	83.5%
Explorer Insurance Company	40029	CA	15.0%
VerTerra Insurance Company	10029	TX	1.5%
Pool Total			100.0%

The agreement provides that receivable and payable balances are to be settled within 30 days of the receipt of the monthly report.

Assumed

Assumed business is limited to the Company's participation in the intercompany quota share reinsurance pooling agreement.

Ceded

Ceded business is limited to the Company's participation in the intercompany quota share reinsurance pooling agreement.

ACCOUNTS AND RECORDS

The Company did not disclose all material related party transactions, including a description of all material management or service contracts and cost-sharing agreements in Note 10 to the Financial Statements. It is recommended that the Company disclose all material related party transactions in its Notes to the Financial Statements in accordance with Statement of Statutory Accounting Principles No. 25, Paragraph 19.

<u>FINANCIAL STATEMENTS</u>

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, 2016. The accompanying comments on financial statements should be considered an integral part of the financial statements. There is no examination adjustments to the amounts reported in the annual statements.

Statement of Financial Condition as of December 31, 2016

Underwriting and Investment Exhibit for the Year Ended December 31, 2016

Reconciliation of Surplus as Regards Policyholders from December 31, 2012 through December 31, 2016

Statement of Financial Condition
as of December 31, 2016

Assets	Ledger and Nonledger Assets	Assets Not Admitted	Net Admitted Assets	Notes
Bonds	$ 215,200,180	$ 464,220	$ 214,735,960	
Preferred stocks	16,870,253	362,100	16,508,153	
Common stocks	52,411,705		52,411,705	
Cash and short-term investments	40,425,876		40,425,876	
Receivable for securities	10,000		10,000	
Investment income due and accrued	2,221,045		2,221,045	
Premiums and agents' balances in course of collection	13,005,867	6,858	12,999,009	
Deferred premiums, agents' balances and Installments booked but deferred and not yet due	11,046,923		11,046,923	
Net deferred tax asset	5,008,715		5,008,715	
Guaranty funds receivable or on deposit	208,813		208,813	
Aggregate write-ins for other than invested assets	508,621	5,338	503,283	
Total assets	$ 356,917,998	$ 838,516	$ 356,079,482	

Liabilities, Surplus and Other Funds			
Losses		$ 157,051,904	(1)
Reinsurance payable on paid loss and loss adjustment expenses		2,770,117	
Loss adjustment expenses		45,331,302	(1)
Commissions payable, contingent commissions and other similar charges		1,142,098	
Other expenses		(574,279)	
Current federal and foreign income taxes		130,006	
Unearned premiums		11,626,078	
Dividends declared and unpaid, policyholders		520,697	
Ceded reinsurance premiums payable		9,790,662	
Drafts outstanding		256,333	
Payable to parent, subsidiaries and affiliates		2,927,011	
Derivatives		43,400	
Aggregate write-ins for liabilities		3,344	
Total liabilities		231,018,673	
Common capital stock	$ 4,500,000		
Gross paid-in and contributed surplus	8,070,835		
Unassigned funds (surplus)	112,489,974		
Surplus as regards policyholders		125,060,809	
Total liabilities, surplus and other funds		$ 356,079,482	

Underwriting and Investment Exhibit
for the Year Ended December 31, 2016

Statement of Income

Underwriting Income		
Premiums earned		$ 147,017,459
Deductions:		
Losses incurred	$ 80,995,951	
Loss adjustment expenses incurred	14,380,467	
Other underwriting expenses incurred	32,822,469	
Total underwriting deductions		128,198,886
Net underwriting gain		18,818,573
Investment Income		
Net investment income earned	$ 9,535,355	
Net realized capital loss	(352,900)	
Net investment gain		9,182,455
Other Income		
Net loss from agents' or premium balances charged off (amount recovered $0, amount charged off $ 188,430)	$ (188,430)	
Finance and service charges not included in premiums	467,249	
Aggregate write-ins for miscellaneous income	(265,982)	
Total other income		12,837
Net income before dividends to policyholders, after capital gains tax and before all other federal and foreign income taxes		28,013,865
Dividends to policyholders		889,131
Net income, after dividends' to policyholders, after capital gains tax and before all other federal and foreign income taxes		27,124,734
Federal and foreign income taxes incurred		8,129,757
Net income		$ 18,994,977

Capital and Surplus Account

Surplus as regards policyholders, December 31, 2015		$ 101,466,811
Net income	$ 18,994,977	
Change in net unrealized capital losses	3,376,340	
Change in net deferred income tax	1,016,801	
Change in nonadmitted assets	205,880	
Change in surplus as regards policyholders for the year		23,593,998
Surplus as regards policyholders, December 31, 2016		$ 125,060,809

Reconciliation of Surplus as Regards Policyholders
from December 31, 2012 through December 31, 2016

Surplus as regards policyholders, December 31, 2012		$ 47,278,242
	Gain in Surplus	
Net income	$ 64,418,960	
Net unrealized capital gains	6,881,281	
Change in net deferred income tax	3,945,512	
Change in nonadmitted assets	636,814	
Capital changes, paid in	1,900,000	
Net increase in surplus as regards policyholders		77,782,567
Surplus as regards policyholders, December 31, 2016		$ 125,060,809

COMMENTS ON FINANCIAL STATEMENT ITEMS

(1) Losses and Loss Adjustment Expenses

Based on an analysis by a Casualty Actuary from the California Department of Insurance, the Company's loss and loss adjustment expense reserves as of December 31, 2016 were found to be reasonably stated, and have been accepted for the purposes of this examination.

SUBSEQUENT EVENTS

On December 7, 2017 the CDI approved the Second Amended and Restated Federal Tax Allocation Agreement to be effective January 1, 2018. The Second Amended Agreement reflects an update in the name of ICW National Insurance Company (formerly Explorer American Insurance Company), plus the addition of the two new affiliated companies, ICW Casualty Insurance Company, and ICW Premier Insurance Company, and the removal of Pacific Encino Assets, Inc., an entity that was dissolved on December 8, 2014.

SUMMARY OF COMMENTS AND RECOMMENDATIONS

Current Report of Examination

Accounts and Records (Page 8): It is recommended that the Company disclose all material related party transactions in its Notes to the Financial Statements in accordance with Statement of Statutory Accounting Principles No. 25, Paragraph 19.

Previous Report of Examination

Management Agreements – Investment Management Agreement (Page 5): It was recommended that the Company report said agreement in its Annual Holding Company Registration Statement Form B in accordance with California Insurance Code Section (CICS) 1215.4(b), and submit the agreement to the California Department of Insurance (CDI) for approval in accordance with CICS1215.5(b)(4). The Company complied with this recommendation.

Management Agreements – Management Services Agreement (Page 5): It was recommended the Company ensure that agreements to provide services between related parties are formalized by a written agreement. It is also recommended that the Company prepare a written management services agreement that provides or clearly identifies the entity providing services, the nature of the services provided and a listing of the entities that party to the agreement. Furthermore, the agreement should set forth appropriate methods to allocate costs between parties for services rendered and provide for timely settlements of amounts owed. Lastly, the agreement should be written in accordance with CICS 1215.5 and submitted to the CDI for approval in accordance with CICS 1215.5(b)(4). The Company complied with this recommendation.

Accounts and Records – Derivatives (Page 8): It was recommended that the Company report balances (i.e. either asset or liability) pertinent to the Company's written call options on the line caption "Derivatives" in accordance with the National Association of Insurance Commissioners Property & Casualty Annual Statement Instructions. The Company complied with this recommendation.

Accounts and Records – Premium Receivable/Commission Payable Balances (Page 8): It was recommended that the Company not offset receivables and payables or report balances net of each other, unless a valid right to offset exists in accordance with Statement of Statutory Accounting Principles Number 64. The Company complied with this recommendation.

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/________________________

Ferdinand Ison
Examiner-In-Charge
Senior Insurance Examiner
Department of Insurance
State of California

____/S/________________________

Edward Aros, CFE
Examiner-In-Charge
Senior Insurance Examiner (Supervisor)
Department of Insurance
State of California