

REPORT OF EXAMINATION
OF THE
PREFERRED EMPLOYERS INSURANCE COMPANY
AS OF
DECEMBER 31, 2022

Commissioners Signature

A handwritten signature in blue ink, appearing to be 'D. DeLoe', written over a horizontal line.

Filed on June 3, 2024

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Los Angeles, California
May 13, 2024

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

Dear Commissioner:

Pursuant to your instructions, an examination was made of the

PREFERRED EMPLOYERS INSURANCE COMPANY

(hereinafter also referred to as the Company) its statutory home office is located at 9797 Aero Drive, Suite 200, San Diego, California 92123.

SCOPE OF EXAMINATION

We have performed our multi-state examination of the Company. The previous examination of the Company was as of December 31, 2018. This examination covered the period from January 1, 2019 through December 31, 2022.

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 Delaware as the lead state of the Berkley Insurance Company subgroup of W. R. Berkley Corporation. It was conducted concurrently with the examinations of the following insurance entities in the holding company group:

Company	NAIC CoCode	Domiciled State
Acadia Insurance Company	31325	Iowa
Admiral Indemnity Company	44318	Delaware
Admiral Insurance Company	24856	Delaware
Berkley Assurance Company	39462	Iowa
Berkley Casualty Company	39462	Iowa
Berkley Insurance Company	32603	Delaware
Berkley Life and Health Insurance Company	64890	Iowa
Berkley National Insurance Company	38911	Iowa
Berkley Prestige Insurance Company	17412	Iowa
Berkley Regional Insurance Company	29580	Iowa
Berkley Specialty Insurance Company	31295	Delaware
Carolina Casualty Insurance Company	10510	Iowa
Clermont Insurance Company	33480	Iowa
Continental Western Insurance Company	10804	Iowa
Firemen's Insurance Company of Washington, D.C.	21784	Delaware
Gemini Insurance Company	10833	Delaware
Great Divide Insurance Company	25224	North Dakota
Intrepid Casualty Company	17182	Iowa
Intrepid Insurance Company	10749	Iowa
Intrepid Specialty Insurance Company	17181	Iowa
Key Risk Insurance Company	10885	Iowa
Midwest Employers Casualty Company	23612	Delaware
Nautilus Insurance Company	17370	Arizona
Preferred Employers Insurance Company	10900	California
Riverport Insurance Company	36684	Iowa
StarNet Insurance Company	40045	Iowa
Tri-State Insurance Company of Minnesota	31003	Iowa
Union Insurance Company	25844	Iowa
Union Standard Lloyds	43435	Texas

COMPANY HISTORY

The Company was incorporated under the laws of California on December 11, 1997, and commenced business on June 1, 1998. The Company writes workers' compensation business for small employers in California. The Company is 100% owned by Berkley Insurance Company, a Delaware domiciled insurer, who writes commercial lines insurance.

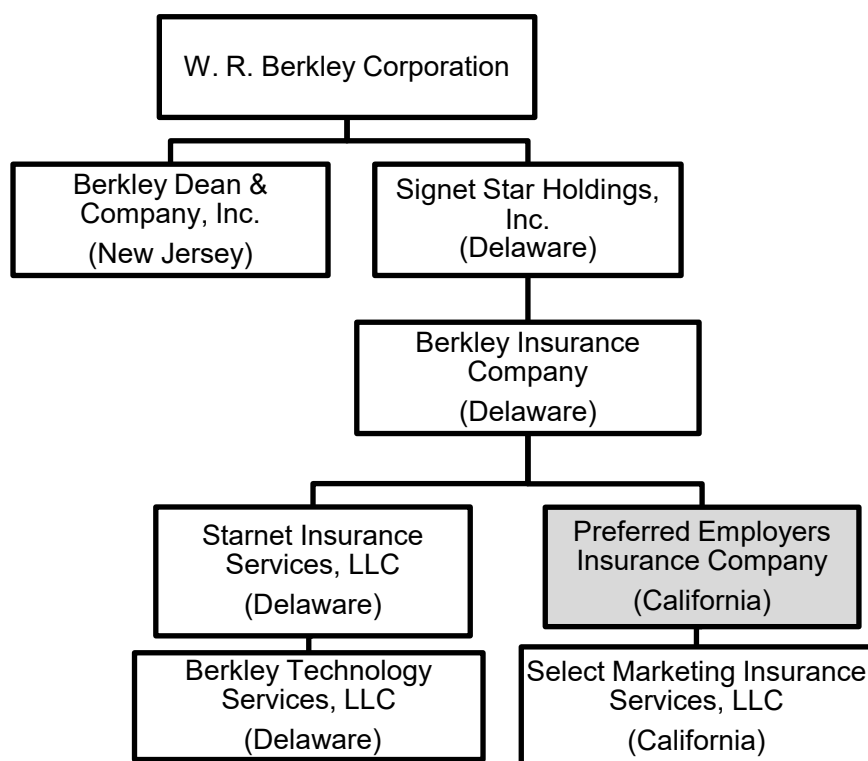
The ultimate parent is W. R. Berkley Corporation, a publicly-traded entity on the New York Stock Exchange founded in 1967 and based in Greenwich, Connecticut, specializing in commercial lines insurance and reinsurance coverage throughout the United States and abroad.

Capitalization

The Company is authorized to issue 10,000 shares of common stock with a par value of \$1,000 per share. As of December 31, 2022, there were 3,500 shares issued and outstanding and held by Berkley Insurance Company.

MANAGEMENT AND CONTROL

The Company is a member of an insurance holding company system of which W. R. Berkley Corporation is the ultimate controlling entity. The following is an abridged organizational chart reflecting the ownership structure at December 31, 2022 (All ownership is 100%).



The six 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, 2022:

Directors

<u>Name and Location</u>	<u>Principal Business Affiliation</u>
Richard M. Baio West Harrison, New York	Executive Vice President, Chief Financial Officer, and Treasurer W. R. Berkley Corporation
William R. Berkley, Jr. Greenwich, Connecticut	President and Chief Executive Officer W. R. Berkley Corporation
Paul J. Hancock ⁽¹⁾ Brookfield, Connecticut	Senior Vice President and Chief Actuary W. R. Berkley Corporation
Carol J. LaPunzina ⁽¹⁾ Demarest, New Jersey	Senior Vice President - Human Resources W. R. Berkley Corporation
James G. Shiel ⁽¹⁾ Pound Ridge, New York	Executive Vice President and Chief Investments Officer W. R. Berkley Corporation
Philip S. Welt Stamford, Connecticut	Executive Vice President, General Counsel, and Secretary W. R. Berkley Corporation

Principal Officers

<u>Name</u>	<u>Title</u>
William R. Berkley, Jr.	President and Chief Executive Officer
Richard M. Baio	Executive Vice President, Chief Financial Officer, and Treasurer
Philip S. Welt	Secretary

⁽¹⁾ Effective March 21, 2024, the following individuals resigned from the Board of Directors: Paul Hancock, Carol LaPunzina, and James Shiel. As of the same date, the following individuals were elected to the Board of Directors: Lee Iannarone, Scott Mansolillo, and Justin R. Woytowich.

Management Agreements

Administrative Service Agreement: Effective February 1, 2006, the Company entered into an Administrative Service Agreement with its wholly-owned subsidiary, Select Marketing Insurance Services, LLC (SMI). Under the terms of this agreement, SMI markets and solicits workers' compensation insurance business on behalf of the Company. Similarly, the Company provides administrative services, offices, equipment, and staff for SMI to perform its business. Compensation for shared services and the use of facilities for both parties are based on the actual costs in accordance with California Insurance Code (CIC) Section 1215.5(a) and are settled on a monthly basis. This agreement was approved by the California Department of Insurance (CDI) on December 27, 2005, as required under CIC Section 1215.5(b)(4). Pursuant to the agreement, the Company paid SMI \$462,995, \$468,140, \$399,859, and \$359,980 in 2019, 2020, 2021, and 2022, respectively.

Computer Services Agreement: Effective January 1, 2002, the Company entered into a Computer Services Agreement with Berkley Technology Services, LLC (BTS), an affiliate. Under the terms of this agreement, BTS provides computer and data processing services, including programming, operations, network management, and consulting services. The actual cost for these services is charged to the Company on a quarterly basis. This agreement was approved by the CDI on February 15, 2002, as required under CIC Section 1215.5(b)(4). Pursuant to the agreement, the Company paid BTS \$2,611,587, \$2,456,508, \$2,489,371, and \$2,726,584 in 2019, 2020, 2021, and 2022, respectively.

Investment Advisory Agreement: The Company entered into an Investment Advisory Agreement dated April 23, 1998, and amended April 24, 1998, with Berkley Dean & Company, Inc. (BDC), an affiliate, to provide investment advisory and management services. BDC is compensated based on an annual fee equal to 0.25% of the first \$10 million and 0.20% thereafter of the net asset value of the portfolio at the end of each quarter. This agreement was approved by the CDI on April 27, 1998. Pursuant to the agreement, the following fees were paid: \$105,155, \$107,221, \$81,136, and \$80,436 in 2019, 2020, 2021, and 2022, respectively.

Management Agreement: On January 1, 2013, the Company entered into a Management Agreement with its parent, Berkley Insurance Company (BIC). Services provided by BIC to the Company include: underwriting, collection and settlement of premiums, claims adjustment and payment, appointment and termination of producers, advertising sales promotion and production, compute reinsurance ceded and assumed adjustments, preparing general ledger accounting and financial statements, and other administrative functions. The management fees for these services are calculated by the actual cost of services and settled with BIC on a daily basis. In order to determine actual costs in relation to indirect and shared expenses, the Company utilizes a cost method allocation in conformity with the statement of Statutory Accounting Principles No. 70. This agreement was approved by the CDI on May 21, 2013, as required under CIC Section 1215.5(b)(4). Pursuant to the agreement, BIC allocated expenses to the Company of \$11,746,383, \$11,316,565, \$10,632,806, and \$9,895,975 in 2019, 2020, 2021, and 2022, respectively.

Tax Allocation Agreement: Effective April 23, 1998, the Company entered into a Tax Allocation Agreement with its ultimate parent, W. R. Berkley Corporation (WRB), and its affiliates. Under the terms of this agreement, participants in the group file a consolidated federal income tax return. WRB is responsible for filing and making federal income tax estimates and final payments on behalf of the participants. Allocation of taxes is based upon separate return calculations with intercompany tax balance payable or receivable being settled in amounts as if separate returns were filed. Intercompany balances are settled quarterly within 45 days after the end of each quarter. This agreement was approved by the CDI on April 27, 1998 as required under CIC Section 1215.5(b)(4). The Company paid or (recovered) the following federal income taxes under this agreement were \$64,624, \$(52,371), \$32,870, and \$136,258, for 2019, 2020, 2021, and 2022, respectively.

TERRITORY AND PLAN OF OPERATION

The Company is licensed to transact property and casualty insurance business in all states and the District of Columbia, except Minnesota and New York. The Company solely writes workers' compensation insurance business.

For the year ending December 31, 2022, the Company wrote \$134,255,684 of direct premiums, with more than ten thousand policyholders. Of the total direct premiums written, 97.9% were written in California. The business approach is to offer products tailored to the specific needs of small businesses that employ fewer than fifty employees. The business is marketed and produced through a network of independent brokers throughout California.

REINSURANCE

Assumed

The Company does not assume reinsurance.

Ceded

The Company was a party to the Multiple Line Quota Share Reinsurance Contract (the Reinsurance Agreement) dated April 1, 2000, with an affiliate, Signet Star Reinsurance Company (SSRC), a Delaware corporation, whereby the Company ceded 90% of the net liability to the reinsurer. Effective January 1, 2013, the Reinsurance Agreement was amended to increase the cession rate from 90% to 100%, and it reflected that SSRC was renamed Berkley Insurance Company. This agreement was approved by the California Department of Insurance on March 8, 2013, as required under California Insurance Code Section 1215(b)(4).

ACCOUNTS AND RECORDS

Bylaws – Number of Directors

According to the January 1, 2017 Amended Bylaws - Article III. Directors, Section 2. Number of Directors, states the exact number of directors shall be seven until changed as provided in this Section. However, based on the review of the Board of Directors' (BOD) meeting minutes for the period under examination, the BOD consisted of only six directors.

It is recommended that the Company implement procedures to ensure future compliance with the required number of directors in accordance with its Bylaws. Based on this

recommendation, the Company amended its Bylaws, effective December 20, 2023, to change the number of authorized directors from seven to no less than three nor more than nine. The Company is now in compliance with the Bylaws.

Insurance Holding Company System Annual Registration Statement (Form B) Filing

California Insurance Code (CIC) Section 1215.4(b) requires, in part, that every insurer subject to registration shall file an annual registration statement with the commissioner on a form and in a format prescribed by the National Association of Insurance Commissioners (NAIC). The annual registration statement (Form B), Item 5 – Transactions and Agreements, provides that the description of the agreements in force shall include, among other things, the nature and amounts of payments between related parties. Based on a review of the Company's Form B filed with the California Department of Insurance, the Company did not report the amount of payments between related parties as required by CIC Section 1215.4(b).

It is recommended that the Company comply with CIC Section 1215.4(b) in future Insurance Holding Company System Annual Registration Statement filings and report the amount of payments between related parties.

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, 2022. The accompanying comments on financial statements should be considered an integral part of the financial statements. There were no adjustments to the financial statements as a result of the examination.

Statement of Financial Condition as of December 31, 2022

Underwriting and Investment Exhibit for the Year Ended December 31, 2022

Reconciliation of Surplus as Regards Policyholders from December 31, 2018 through December 31, 2022

Statement of Financial Condition
as of December 31, 2022

<u>Assets</u>	<u>Ledger and Nonledger Assets</u>	<u>Assets Not Admitted</u>	<u>Net Admitted Assets</u>	<u>Notes</u>
Bonds	\$ 38,908,338	\$	\$ 38,908,338	
Cash, cash equivalents, and short-term investments	13,163,494		13,163,494	
Other Invested Assets	1,000	1,000	0	
Receivables for securities	11,126		11,126	
Investment income due and accrued	164,194		164,194	
Uncollected premiums and agents' balances in the course of collection	5,388,835	789,977	4,598,858	
Deferred premiums, agents' balances and installments booked but deferred and not yet due	38,444,376	72,759	38,371,617	
Net deferred tax asset	247,283		247,283	
Guaranty funds receivable or on deposit	226,235		226,235	
Aggregate write-ins for other than invested assets	<u>6,917,938</u>	<u>297,106</u>	<u>6,620,922</u>	
Total assets	<u>\$ 103,472,819</u>	<u>\$ 1,160,752</u>	<u>\$ 102,312,067</u>	
 <u>Liabilities, Surplus and Other Funds</u>				<u>Notes</u>
Losses and loss adjustment expenses				0 (1)
Commissions payable, contingent commissions and other similar charges			6,594,267	
Current federal and foreign income taxes			34,258	
Ceded reinsurance premiums payable			44,783,943	
Aggregate write-ins for liabilities			<u>39,039</u>	
Total liabilities			51,451,506	
Common capital stock		\$ 3,500,000		
Gross paid-in and contributed surplus		7,500,000		
Unassigned funds (surplus)		<u>39,860,561</u>		
Surplus as regards policyholders			<u>50,860,561</u>	
Total liabilities, surplus, and other funds			<u>\$ 102,312,067</u>	

Underwriting and Investment Exhibit
for the Year Ended December 31, 2022

Statement of Income

Underwriting Income

Premium earned	\$	0
Deduction:		
Losses and Loss expense incurred	\$	0
Other underwriting expenses incurred	0	
	<u>0</u>	
Total underwriting deductions		<u>0</u>
Net underwriting loss		0

Investment Income

Net investment income earned	\$	830,817
Net realized capital losses	<u>(8,634)</u>	
Net investment gain		822,183
Net income after dividends to policyholders, after capital gains tax, and before all other federal and foreign income taxes		822,183
Federal and foreign income taxes incurred		<u>138,944</u>
Net income	<u>\$</u>	<u>683,239</u>

Capital and Surplus Account

Surplus as regards policyholders, December 31, 2021	\$	50,415,456
Net income	\$	683,239
Change in net unrealized capital gains	7,259	
Change in net deferred income tax	138,737	
Change in nonadmitted assets	(665,853)	
Aggregate write-ins for gains and losses in surplus	<u>281,722</u>	
Change in surplus as regards policyholders for the year		<u>445,104</u>
Surplus as regards policyholders, December 31, 2022	<u>\$</u>	<u>50,860,561</u>

Reconciliation of Surplus as Regards Policyholders
from December 31, 2018 through December 31, 2022

Surplus as regards policyholders, December 31, 2018			\$ 47,967,865
	<u>Gain in Surplus</u>	<u>Loss in Surplus</u>	
Net income	\$ 3,214,888	\$	
Change in net unrealized capital gains	8,323		
Change in net deferred income tax	155,606		
Change in nonadmitted assets		720,584	
Aggregate write-ins for gains and losses in surplus	<u>234,463</u>		
Total gains and losses	<u>\$ 3,613,280</u>	<u>\$ 720,584</u>	
Net increase in surplus as regards policyholders			<u>2,892,696</u>
Surplus as regards policyholders, December 31, 2022			<u>\$ 50,860,561</u>

COMMENTS ON FINANCIAL STATEMENT ITEMS

(1) Losses and Loss Adjustment Expenses

As of December 31, 2022, the Company reported zero net losses and loss adjustment expenses reserves (LAE) since one hundred percent of its losses and LAE expenses were ceded to its parent, Berkley Insurance Company. A Casualty Actuary from the California Department of Insurance reviewed the actuarial work prepared by the lead state's consulting actuary, INS Consulting, Inc., and concurred that the group's losses and LAE reserve as of December 31, 2022 were reasonable and have been accepted for purposes of this examination.

SUMMARY OF COMMENTS AND RECOMMENDATIONS

Current Report of Examination.

Accounts and Records – Insurance Holding Company System Annual Registration Statement (Form B) Filing (Page 9): It is recommended that the Company comply with the California Insurance Code (CIC) Section 1215.4(b) in future Insurance Holding Company System Annual Registration Statement filings and report the amount of payments between related parties.

Previous Report of Examination.

Management and Control – Corporate Records (Page 8): It was recommended that the Company implement procedures in its board meeting to ensure adherence to the CIC Section 735. The Company is now in compliance.

Comments on Financial Statement Items – Cash and Short-term Investments (Page 13): It was recommended that the Company includes the Company's name in the Company's operating cash account to ensure adherence to the CIC 1100. The Company is now in compliance.

ACKNOWLEDGMENT

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

Respectfully submitted,

Cuauhtemoc Beltran, CFE
Examiner-In-Charge
Senior Insurance Examiner, Supervisor
Department of Insurance
State of California

Sayaka Dillon, CFE
Bureau Chief
Department of Insurance
State of California