

REPORT OF EXAMINATION  
OF THE  
HOME WARRANTY OF AMERICA, INC.  
AS OF  
DECEMBER 31, 2012

Filed May 20, 2014

## TABLE OF CONTENTS

	<u>PAGE</u>
SCOPE OF EXAMINATION .....	1
SUBSEQUENT EVENTS .....	2
COMPANY HISTORY: .....	2
Capitalization .....	3
MANAGEMENT AND CONTROL:.....	3
Management Agreements.....	5
CORPORATE RECORDS.....	6
TERRITORY AND PLAN OF OPERATION.....	7
REINSURANCE .....	8
FINANCIAL STATEMENTS: .....	8
Statement of Financial Condition as of December 31, 2012 .....	9
Underwriting and Investment Exhibit for the Year Ended December 31, 2012 .....	10
Reconciliation of Surplus as Regards Contract Holders from December 31, 2009 through December 31, 2012.....	11
COMMENTS ON FINANCIAL STATEMENT ITEMS:.....	12
Claims Adjusted and Unpaid or in Process of Adjustment .....	12
SUMMARY OF COMMENTS AND RECOMMENDATIONS: .....	12
Current Report of Examination .....	12
Previous Report of Examination .....	12
ACKNOWLEDGMENT .....	13

Los Angeles, California  
March 3, 2014

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

Dear Commissioner:

Pursuant to your instructions, an examination was made of the

HOME WARRANTY OF AMERICA, INC.

(hereinafter also referred to as the Company). The Company's domiciliary address is located at 2030 Main Street, Suite 1300, Irvine, California 92614, and its administrative office and primary location of books and records are located at 1371 Abbott Court, Suite A, Buffalo Grove, Illinois 60089.

SCOPE OF EXAMINATION

We have performed our single-state examination of the Company. The previous examination of the Company was made as of December 31, 2009. This examination covers the period from January 1, 2010 through December 31, 2012. 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, to identify prospective risks, and to obtain information about the Company, including corporate governance, identification and assessment of inherent risks, and the evaluation of the system controls and procedures used to mitigate those risks. The examination also included an assessment of the principles used and the significant estimates made by management, as well as an evaluation of the overall financial statement presentation, and management's compliance with Statutory Accounting

Principles and Annual Statement instructions. All accounts and activities of the Company were considered in accordance with the risk-focused examination process.

In addition to those items specifically commented upon in this report, other phases of the Company's operations were reviewed including the following areas that require no further comment: fidelity bonds and other insurance; pensions, stock ownership and insurance plans; growth of company; loss experience; accounts and records; and statutory deposits.

### SUBSEQUENT EVENTS

Effective September 26, 2013, Mr. Eric Palm was appointed and named Director, President, Treasurer, and Secretary of the Company. Under these titles and positions, he oversees the over-all operations of the Company.

The Company's former Treasurer, Ms. Sandra Pappas, resigned on August 9, 2013; and the former Secretary, Mr. Robert Sobel, resigned on September 26, 2013.

### COMPANY HISTORY

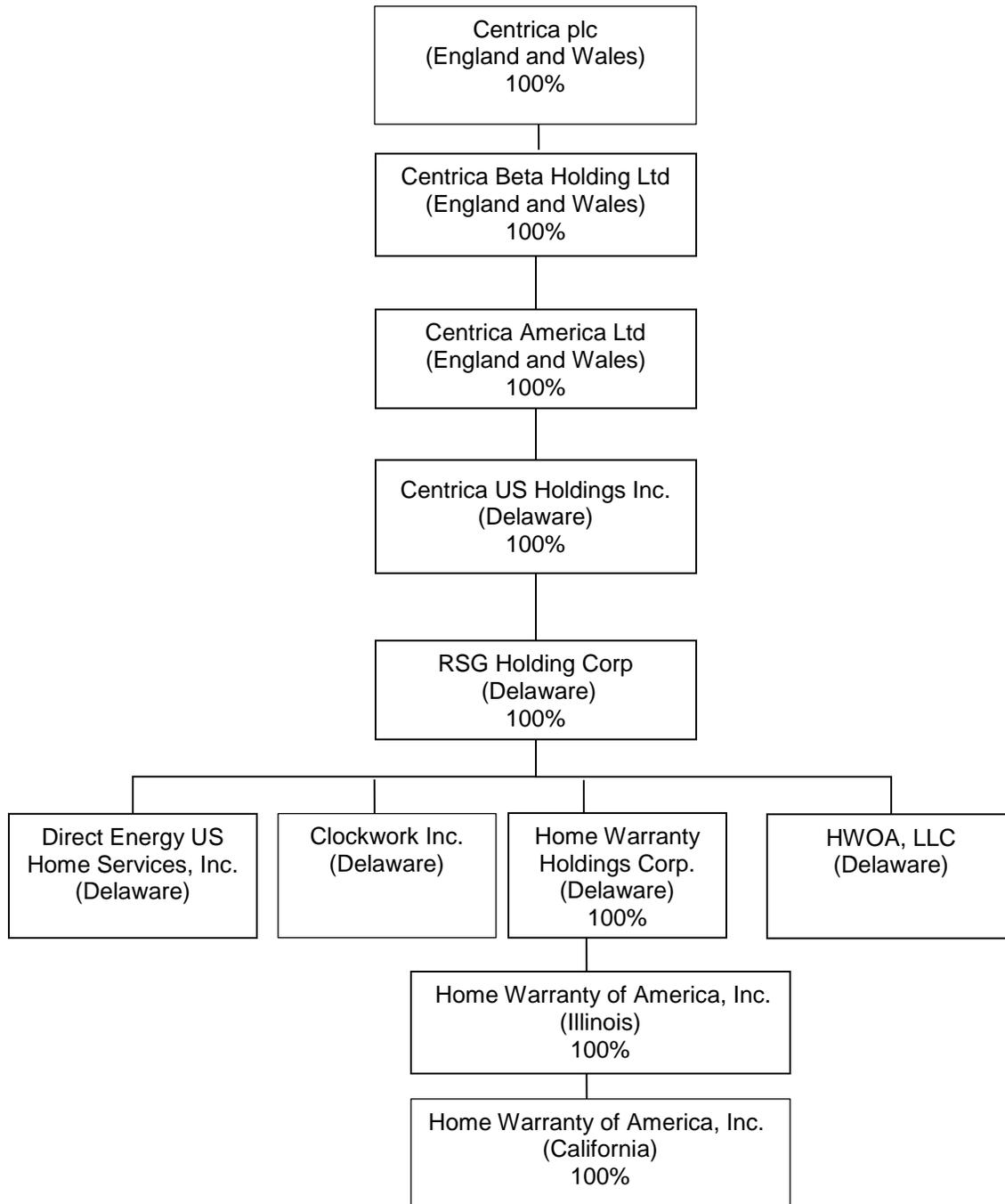
The Company was incorporated in California on November 6, 2000 and began transacting business on May 3, 2005. Effective March 1, 2012, the Company's parent, Home Warranty of America, Inc., (HWA) an Illinois corporation was purchased by RSG Holding Corp, an indirect subsidiary of Centrica, plc (a public limited company), which is a multi-national integrated energy company based in the United Kingdom, for a total cash purchase of \$48.0 million.

## Capitalization

The Company is authorized to issue 10,000 shares of common stock with a par value of \$10 per share. The common stock of the Company is 100% owned by HWA, an Illinois corporation. As of December 31, 2012, there were 8,000 shares outstanding.

## MANAGEMENT AND CONTROL

The Company is a wholly-owned subsidiary of Home Warranty of America, Inc., an Illinois Corporation (HWA), which in turn is wholly-owned by Home Warranty Holding Corp., a Delaware Corporation. The Company's ultimate parent, Centrica plc, is a multi-national company traded on the London Stock Exchange. The following organization chart depicts the Company's position within the holding company system as of December 31, 2012 (all ownership is 100%):



Management of the Company is under the control of a single-member board elected annually. A listing of the member of the board and principal officers serving on December 31, 2012 follows:

Director

Name and Location

Principal Business Affiliation

Julie Ainsworth<sup>(a)</sup>  
Winnetka, Illinois

President  
Home Warranty of America, Inc.  
(California)

Principal Officers

Name

Title

Julie Ainsworth<sup>(a)</sup>  
Sandra Pappas<sup>(b)</sup>  
Robert Sobel<sup>(c)</sup>

President  
Treasurer  
Secretary

(a) Julie Ainsworth resigned as President on February 19, 2013 and was replaced by Mr. Eric Palm on February 19, 2013.

(b) Sandra Pappas resigned as Treasurer, effective August 9, 2013.

(c) Robert Sobel resigned as Secretary, effective September 26, 2013

Management Agreements

Services Agreement: On December 16, 2004, the Company entered into a service agreement with its parent, HWA. Under the terms of the agreement, HWA provides the Company with certain administrative support services, including but not limited to the following: computer services and equipment; human resources; payroll; supplies; facility space; and back office support services. This agreement was approved by the California Department of Insurance (CDI) on July 25, 2005. For 2010 and 2011 the Company paid HWA \$491,691 and \$728,259, respectively, under the terms of this agreement. This agreement was terminated by the issuance of the new service agreement due to the acquisition of the Company by RSG Holding Corp on March 1, 2012.

On March 1, 2012, the Company entered into a new service agreement with an affiliate, HWOA, LLC, a Delaware limited liability company (HWOA). Under the terms of the agreement, HWOA provides the Company with certain administrative support services, including but not limited to the following: claims payment and adjusting; underwriting; facility sharing; preparation of financial reports; advertising; sales promotion and agency development and reserving for claims and expenses. Compensation is based on actual cost and an allocation method based on other factors/ratios under the terms of this agreement. This agreement was approved by the CDI on August 1, 2012. For 2012, HWOA LLC received compensation of \$826,607 from the Company for services it provided under the terms of this agreement.

Tax Allocation Agreement: Since January 1, 2005, the Company and its affiliates had been parties to a consolidated federal income tax agreement with the ultimate parent, Home Warranty Holdings Corp., a Delaware corporation. This agreement was approved by the CDI on October 23, 2007. Under the terms of the agreement for 2010 and 2011 the Company paid \$0. This agreement was terminated by the issuance of the new tax agreement during the acquisition of the Company by RSG Holding Corp on March 1, 2012.

Effective March 1, 2012, the Company and its affiliates entered into a consolidated federal income tax agreement with Centrica US Holdings, Inc., a Delaware corporation. The Company's tax liability or refund, under the terms of this agreement, is the same as it would have been had it filed on a separate stand-alone basis. In 2012 the Company paid \$0 under the terms of the agreement. This agreement was approved by the CDI on August 1, 2012.

### CORPORATE RECORDS

Pursuant to California Insurance Code Section (CICS) 735, the Company is required to inform the board members of the receipt of the examination report; both in the form first formally prepared by the examiners, and in the form officially filed by the Commissioner,

and enter these facts within the board minutes. A review of the board minutes disclosed that the Company did not make the required reference. It is recommended that the Company implement procedures to ensure future compliance with CICS 735.

Pursuant to CICS 1200, the Company is required to disclose the authorization and approval of its investments within its minutes. In addition, CICS 1201 requires that the entry of approval be documented within the minutes and include specific references to amounts, facts, names of approving directors, and the value of the securities. A review of the Company's minute disclosed that the Company failed to adhere to the reporting requirements of CICS 1200 and 1201. It is recommended that the Company implement procedure to ensure compliance with the provisions of CICS 1200 and 1201.

#### TERRITORY AND PLAN OF OPERATION

As of December 31, 2012, the Company is licensed to sell home protection contracts in California, Florida, and Virginia. The contracts (named Whole Home Contracts) provide coverage for major mechanical systems and appliances to residential homeowners. This includes repair and/or replacement of the covered items as long as they are located within the confines of the foundation of the home, are in place and in good working order on the effective date of the contract, and become inoperative due to normal wear and tear. The Company offers 13-month and 12-month Whole Home Contracts. The 13-month Whole Home Contract is offered to consumers who are involved with real estate transactions, and the 12-month Whole Home Contract is offered directly to consumers who are not involved in real estate transactions.

The Company's sale focus with respect to the Whole Home Contract is primarily in Southern California. Marketing of its Whole Home Contracts is performed by the Company utilizing one sales manager, five sales representatives, and third party real estate professionals.

The Company also offers Direct Energy Protection Plans (Protection Plans) in

California; however, the Company has not yet started actively marketing its Protection Plans in California, but has planned to do so in 2014. The Protection Plans are individual repair and maintenance plans covering major mechanical systems and appliances in residential homes.

During 2012, the Company wrote \$2.54 million of total direct premiums, with \$1.64 million (64.7%) written in California, \$0.48 million (18.9%) written in Florida, and \$0.42 million (16.4%) written in Virginia.

### REINSURANCE

The Company did not assume or cede any reinsurance during the examination period.

### FINANCIAL STATEMENTS

The financial statements prepared for this examination report include:

Statement of Financial Condition as of December 31, 2012

Underwriting and Investment Exhibit for the Year Ended December 31, 2012

Reconciliation of Surplus as Regards Contract Holders from December 31, 2009 through December 31, 2012

Statement of Financial Condition  
as of December 31, 2012

<u>Assets</u>	<u>Ledger and Nonledger Assets</u>	<u>Assets Not Admitted</u>	<u>Net Admitted Assets</u>	<u>Notes</u>
Cash and short-term investments	\$ 2,894,506	\$	\$ 2,894,506	
Home protection contract fees receivable	278,712	40,000	238,712	
Other assets	<u>83,000</u>	<u>          </u>	<u>83,000</u>	
 Total assets	 <u>\$ 3,256,218</u>	 <u>\$ 40,000</u>	 <u>\$ 3,216,218</u>	
 <u>Liabilities, Surplus and Other Funds</u>				
Claims adjusted and unpaid or in process of adjustment			\$ 100,000	(1)
Other expenses			24,585	
Taxes, licenses and fees			16,843	
Federal income taxes			73,000	
Unearned home protection contract fees			1,049,877	
Payable to parent, subsidiaries and affiliates			72,431	
Escheat payable			<u>864</u>	
 Total liabilities			 1,337,600	
 Common capital stock		 \$ 80,000		
Gross paid-in and contributed surplus		1,620,000		
Unassigned funds (surplus)		<u>178,618</u>		
Surplus as regards contract holders			<u>1,878,618</u>	
 Total liabilities, surplus and other funds			 <u>\$ 3,216,218</u>	

Underwriting and Investment Exhibit  
for the Year Ended December 31, 2012

Statement of Income

Underwriting Income

Home protection contract fees earned \$ 2,375,523

Deductions:

Claims incurred	\$	877,306
Claims service expenses incurred		472,910
Other underwriting expenses incurred		<u>700,725</u>

Total underwriting deductions 2,050,941

Net underwriting gain 324,582

Investment Income

Net investment loss	\$	(19,494)
Net realized capital gain		<u>63,165</u>

Net investment gain 43,671

Other Income

Receivables balance written off	\$	<u>(6,069)</u>
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Total other loss (6,069)

Net income before federal income taxes 362,184

Federal income taxes incurred 50,250

Net income \$ 311,934

Capital and Surplus Account

Surplus as regards contract holders, December 31, 2011	\$	1,576,879
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Net income	\$	311,934
Change in nonadmitted assets		(20,000)
Change in Unrealized gain on investments		<u>9,805</u>

Change in surplus as regards contract holders for the year 301,739

Surplus as regards contract holders, December 31, 2012	\$	<u>1,878,618</u>
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Reconciliation of Surplus as Regards Contract Holders  
from December 31, 2009 through December 31, 2012

Surplus as regards contract holders, December 31, 2009 per Examination				\$ 1,087,985
	<u>Gain in Surplus</u>	<u>Loss in Surplus</u>		
Net income	\$ 783,023	\$	20,000	
Change in nonadmitted assets			20,000	
Change in unrealized gain on investment	<u>27,610</u>			
Total gains and losses	<u>\$ 810,633</u>	<u>\$</u>	<u>20,000</u>	
Net increase in surplus as regards contract holders				<u>790,633</u>
Surplus as regards contract holders, December 31, 2012, per Examination				<u>\$ 1,878,618</u>

## COMMENTS ON FINANCIAL STATEMENT ITEMS

### (1) Claims Adjusted and Unpaid or in Process of Adjustment

Based on a review of claim payments and reserves subsequent to the examination date, the reserve for the above captioned account appears to be reasonable and has been accepted for purposes of this examination.

## SUMMARY OF COMMENTS AND RECOMMENDATIONS

### Current Report of Examination

Corporate Records- (Page 6): It is recommended that the Company implement procedures to ensure compliance with the provision of California Insurance Code Sections (CICS) 735. It is also recommended that the Company implement procedure to ensure compliance with the provisions of CICS 1200 and 1201.

### Previous Report of Examination

Corporate Records-(Page 5): It was recommended that the Company correctly identify the directors in future reporting periods. The Company complied with this recommendation.

Accounts and Records-(Page 7): It was recommended that the Company implement procedures to ensure the accuracy of its reported financial statements and to comply with the National Association of Insurance Commissioners Annual Statement Instructions in reporting deferred tax credits. The Company complied with this recommendation.

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,

\_\_\_\_\_/S/\_\_\_\_\_  
Bridget Lopez, CFE  
Examiner-In-Charge  
Associate Insurance Examiner  
Department of Insurance  
State of California