

REPORT OF EXAMINATION  
OF THE  
HOMESITE INSURANCE COMPANY  
OF CALIFORNIA  
AS OF  
DECEMBER 31, 2016

FILED ON JUNE 28, 2018

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Los Angeles, California  
May 24, 2018

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

Dear Commissioner:

Pursuant to your instructions, an examination was made of the

### HOMESITE INSURANCE COMPANY OF CALIFORNIA

(hereinafter also referred to as the Company) at its main administrative office located at 1 Federal Street, Suite 400, Boston, Massachusetts 02110. The Company's statutory address is 2710 Gateway Oaks Drive, Suite 150N, Sacramento, California 95833.

### SCOPE OF EXAMINATION

We have performed our multi-state examination of the Company. The previous examination of the Company was as of December 31, 2011. This examination covered the period from January 1, 2012 through December 31, 2016.

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 Wisconsin as the lead state of the Homesite Group Incorporated subgroup of the American Family Mutual Insurance Company. It was conducted concurrently with the examinations of other insurance entities in the holding company group and included participation from the following states: Georgia, Illinois, New York, and Texas.

### COMPANY HISTORY

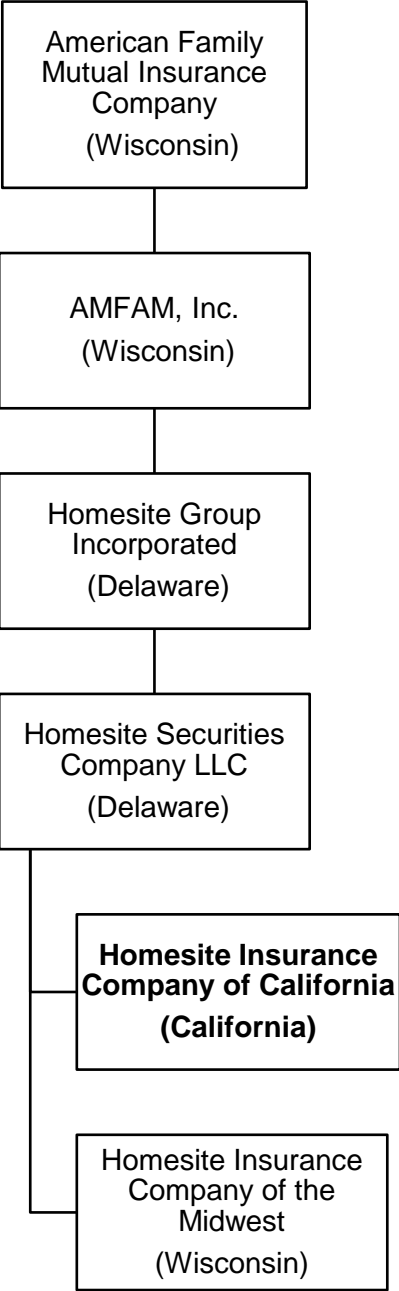
The Company is a wholly-owned subsidiary of Homesite Securities Company LLC (HSC), which in turn, is wholly-owned by Homesite Group Incorporated (HGI), both are Delaware entities.

HGI had been privately owned by multiple entities and individuals. Owners included Alleghany Corporation, Metalmark Capital, through its management of the Morgan Stanley Capital Partners funds, and The Plymouth Rock Company Inc.

Effective December 31, 2013, HGI and all of its operating insurance subsidiaries were acquired and became 100% owned by AMFAM, Inc., a Wisconsin corporation.

### MANAGEMENT AND CONTROL

The Company is a member of an insurance holding company system of which American Family Mutual Insurance Company is the ultimate controlling entity. Following is an abridged organizational chart. All ownership is 100%.



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

<u>Name and Location</u>	<u>Principal Business Affiliation</u>
Fabian J. Fondriest Concord, Massachusetts	President and Chief Executive Officer Homesite Group Incorporated
Michael D. Lorion Millbury, Massachusetts	Chief Financial Officer, Treasurer, and Senior Vice President Homesite Group Incorporated
Andrew A. McElwee, Jr. New London, New Hampshire	Executive Vice President and Chief Operating Officer Homesite Group Incorporated
James T. Morahan, Jr. Foxboro, Massachusetts	Vice President Homesite Group Incorporated
Anthony M. Scavongelli Duxbury, Massachusetts	Executive Vice President and General Counsel Homesite Group Incorporated

Principal Officers

<u>Name</u>	<u>Title</u>
Fabian J. Fondriest	Chief Executive Officer
Andrew A. McElwee, Jr.	President
Michael D. Lorion	Chief Financial Officer, Treasurer, and Senior Vice President
Anthony M. Scavongelli	General Counsel, Secretary, and Executive Vice President
Christopher L. Conti	Executive Vice President
Peter B. Settel	Executive Vice President
Mishthi G. Hanson <sup>(a)</sup>	Senior Vice President
David M. Pfahler, Jr.	Senior Vice President
James T. Morahan, Jr.	Vice President
Maureen Fidler <sup>(b,c)</sup>	Assistant Secretary
Troy P. Van Beek	Assistant Treasurer

The following changes in management occurred subsequent to the examination date:

- (a) Mishthi G. Hanson, Senior Vice President, has resigned, effective January 2, 2018.
- (b) Maureen Fidler, Assistant Secretary resigned, effective June 29, 2017.
- (c) Effective June 30, 2017, Susan G. Anderson was appointed to the offices of Vice President, Assistant General Counsel, and Assistant Secretary.

### Management Agreements

Intercompany Service Agreement: On November 3, 1999, the Company entered into an Intercompany Service Agreement with Homesite Group, Inc. (HGI) for the leasing of employees and facilities to the Company. Under the terms of the agreement, the Company reimburses HGI for salaries, administrative services, and facilities based on the actual cost of these services. The agreement was amended, effective April 1, 2014, to add American Family Mutual insurance Company (AFMIC) to provide investment services. On April 10, 2014, the Amendment was approved by the California Department of Insurance (CDI). The total payment made by the Company for the services for the years 2014, 2015, and 2016 are \$8,561,470, \$11,448,009, and \$14,396,854, respectively.

Tax Allocation Agreement: The Company and its affiliates are parties to a consolidated federal income tax liability allocation agreement with HGI. The tax allocation is based on separate return calculations. Intercompany tax balances are settled within thirty days after the filing of the consolidated income tax return by HGI. On February 3, 2015, the CDI approved an amendment to add Homesite General Agent, LLC to the agreement, effective December 31, 2014. Taxes paid and recovered by the Company for the years 2012, 2013, 2014, 2015, and 2016 are \$1,191,008, (\$2,160,615), \$128,420, \$275,616, and \$139,654, respectively.

The Company's 2016 consolidated federal income tax return was filed on October 13, 2017 and the tax settlement was completed on January 26, 2018. The Company was not in compliance with the thirty day settlement provisions of its tax



agreement. It is recommended the Company implement procedures to ensure compliance with the settlement provisions of its tax agreement. This is a repeat recommendation

### TERRITORY AND PLAN OF OPERATION

The Company has authority to write fire, marine, plate glass, liability, boiler, burglary, sprinkler, team and vehicle, and miscellaneous lines in the state of California only. At December 31, 2016, the Company had direct written premiums of \$87,219,824, of which 98% is homeowners multiple peril and 2%, allied lines. The Company's products are largely distributed by affinity partners who include homeowners in the marketing of other financial products. The Company's largest affinity partners are direct writing auto insurers, who market the Homesite Homeowners Product for the convenience of their customers.

### REINSURANCE

#### Assumed

The Company has no assumed reinsurance.

#### Ceded

Loss Portfolio Transfer and 100% Quota Share Reinsurance Agreement: Prior to January 1, 2014, the Company and its affiliates were parties to an Intercompany Reinsurance Pooling Agreement (Pooling Agreement). This Pooling Agreement was terminated upon the Company and Homesite Insurance Company of the Midwest (HMW) entered into a Loss Portfolio Transfer and 100% Quota Share Reinsurance Agreement, effective January 1, 2014, whereby the Company is the ceding company and HMW is the reinsurer. Concurrently, HMW entered into a similar Loss Portfolio Transfer and 100% Quota Share Reinsurance Agreement with the ultimate controlling

parent, American Family Mutual Insurance Company (AFMIC), whereby HMW is the ceding company and AFMIC is the reinsurer. These agreements were approved by the California Department of Insurance on September 5, 2014. AFMIC is licensed in California.

#### National Flood Insurance Program

The Company writes flood business through the National Flood Insurance Program (NFIP) as part of the Write Your Own (WYO) flood insurance program. The NFIP was established pursuant to the National Flood Insurance Act of 1968 and is administered by the Federal Insurance Administration of the Federal Emergency Management Agency (FEMA). The NFIP is designed to involve private insurers in a WYO flood insurance program financially backed by FEMA at no risk to the insurer.

#### ACCOUNTS AND RECORDS

During the course of the examination, a review was made of the Company's unclaimed property filings with the California State Controller's Office (SCO). California Code of Civil Procedure (CCP) Part 3, Title 10, Chapter 7, Article 3, Sections 1530 and 1532 - Unclaimed Property Law requires that all tangible personal property located in the state of California, that is held or owing in the ordinary course of business and has remained unclaimed by the owner for more than three years after it became payable or distributable, is escheated to the SCO.

During our review of the Company's outstanding check list as of December 31, 2016, it was noted that several checks were more than three years old and should have been escheated to the SCO. It is recommended that the Company escheat unclaimed property to the SCO and implement procedures to ensure future compliance with CCP Sections 1530 and 1532.

## 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, 2016. The accompanying comments to the amounts reported in the annual statements should be considered an integral part of the financial statements. There were no examination adjustments made to surplus as a result of the examination.

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, 2011  
through December 31, 2016

Statement of Financial Condition  
as of December 31, 2016

<u>Assets</u>	<u>Ledger and Nonledger Assets</u>	<u>Assets Not Admitted</u>	<u>Net Admitted Assets</u>	<u>Notes</u>
Bonds	\$ 29,019,449	\$	\$ 29,019,449	
Cash and short-term investments	2,710,209		2,710,209	
Investment income due and accrued	158,958		158,958	
Premiums and agents' balances in course of collection	9,212,236		9,212,236	
Premiums, agents' balances and installments booked but deferred and not yet due (including \$0 earned but unbilled premiums)	7,437,502		7,437,502	
Amounts recoverable from reinsurers	<u>5,223,315</u>		<u>5,223,315</u>	
 Total assets	 <u>\$ 53,761,669</u>		 <u>\$ 53,761,669</u>	
 <u>Liabilities, Surplus and Other Funds</u>				
Losses and Loss adjustment expenses			\$ 0	(1)
Commissions payable, contingent commissions and other similar charges			1,116,112	
Other expenses			388,232	
Taxes, licenses and fees			674,913	
Current federal and foreign income taxes			50,822	
Net deferred tax liability			18,202	
Advance premiums			1,941,398	
Ceded reinsurance premiums payable			5,346,622	
Amounts withheld or retained by company for account of others			176,361	
Payable to parent, subsidiaries and affiliates			<u>7,001,275</u>	
 Total liabilities			 16,713,937	
 Common capital stock		\$ 2,600,000		
Gross paid-in and contributed surplus		26,850,001		
Amounts recoverable from reinsurers		<u>7,597,731</u>		
Surplus as regards policyholders			<u>37,047,732</u>	
 Total liabilities, surplus and other funds			 <u>\$ 53,761,669</u>	

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

Statement of Income

Underwriting Income

Premiums earned		\$ 0
Deductions:		
Losses and loss expenses incurred	\$ 0	
Other underwriting expenses incurred	<u>(109,002)</u>	
Total underwriting deductions		<u>(109,002)</u>
Net underwriting loss		(109,002)

Investment Income

Net investment income earned	\$ 352,818	
Net realized capital loss	<u>(14,958)</u>	
Net investment gain		337,860
Net income after dividends to policyholders, after capital gains tax and before federal and foreign income taxes		446,862
Federal and foreign income taxes incurred		<u>108,059</u>
Net income		<u>\$ 338,803</u>

Capital and Surplus Account

Surplus as regards policyholders, December 31, 2015		\$ 36,716,447
Net income	\$ 338,803	
Change in net unrealized capital losses	(1,068)	
Change in net deferred income tax	<u>(6,450)</u>	
Change in surplus as regards policyholders for the year		<u>331,285</u>
Surplus as regards policyholders, December 31, 2016		<u>\$ 37,047,732</u>

Reconciliation of Surplus as Regards Policyholders  
from December 31, 2011 through December 31, 2016

Surplus as regards policyholders, December 31, 2011			\$ 24,206,200
	<u>Gain in Surplus</u>	<u>Loss in Surplus</u>	
Net income	\$ 16,047,334	\$	
Change in net unrealized capital losses		498,892	
Change in net deferred income tax		5,216,169	
Change in nonadmitted assets	<u>2,509,259</u>	<u></u>	
Total gains and losses	<u>\$ 18,556,593</u>	<u>\$ 5,715,061</u>	
Net increase in surplus as regards policyholders			<u>12,841,532</u>
Surplus as regards policyholders, December 31, 2016			<u>\$ 37,047,732</u>

## COMMENTS ON FINANCIAL STATEMENT ITEMS

### (1) Losses and Loss Adjustment Expenses

The Lead State, Wisconsin, retained the American Actuarial Consulting Group, LLC (AACG) for the purpose of assisting this examination in determining the reasonableness of the Group's loss and loss adjustment expense reserves. Since the business of the Company was pooled, it was necessary to evaluate the losses on a group-wide basis. Based on the analysis by AACG and the review of their work by a Casualty Actuary from the California Department of Insurance, the Company's December 31, 2016 reserves for losses and loss adjustment expenses were determined to be reasonably stated and have been accepted for purposes of this examination.

## SUBSEQUENT EVENTS

Effective January 1, 2017, American Family Mutual Insurance Company (AFMIC), a Wisconsin mutual insurer, converted to a stock insurer and changed its name to American Family Mutual Insurance Company, S.I. (AFMIC SI). AFMIC SI is 100% owned by a newly formed Wisconsin stock holding company, AmFam Holdings, Inc., which in turn, is 100% owned by American Family Insurance Mutual Holding Company (AFI MHC), a newly formed Wisconsin mutual holding company. As a result, AFI MHC is the new ultimate controlling parent of the Company.

## SUMMARY OF COMMENTS AND RECOMMENDATIONS

### Current Report of Examination

Management and Controls: Management Agreements – Tax Allocation Agreement (Page 6): The Company was not in compliance with the thirty day settlement provisions of its tax agreement. It is recommended the Company implement procedures to ensure compliance with the settlement provisions of its tax agreement.

Accounts and Records – Unclaimed Property (Page 8): The Company’s outstanding check list as of December 31, 2016 noted several checks were more than three years old and should had been escheated to the State Controller’s Office (SCO). It is recommended that the Company escheat unclaimed property to the SCO and implement procedures to ensure future compliance with California Code of Civil Procedure Sections 1530 and 1532.

#### Previous Report of Examination

Management and Control – Management Agreements – Consolidated Federal Income Tax Liability Allocation Agreement (Page 6): It was recommended the Company implement procedures to ensure compliance with the settlement provisions of the tax agreement. The Company has not complied with the recommendation.

Accounts and Records: Information System Controls (Page 9): It was recommended that the Company establish and implement appropriate control policies and procedures to strengthen its information system controls. The Company has complied.



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/\_\_\_\_\_

Thomas Podsiadlo, CFE  
Examiner-In-Charge  
Senior Insurance Examiner  
Department of Insurance  
State of California

\_\_\_\_\_/s/\_\_\_\_\_

Grace Asuncion, CFE  
Senior Insurance Examiner, Supervisor  
Department of Insurance  
State of California