# BEST'S COMPANY REPORT

## WESTERN PACIFIC MUTUAL INSURANCE COMPANY, A RISK RETENTION GROUP

**Domiciliary Address:** 9265 Madras Court, Littleton, Colorado 80130 United States

**AMB #:** 011238 **NAIC #:** 40940 **FEIN #:** 84-1144314

**Phone:** +1-303-263-0311 **Fax:** +1-303-470-9119 **Website:** N/A

AM BEST
A-
EXCELLENT
Financial Strength Rating

**Best's Credit Rating Effective Date**
November 18, 2022

**Analytical Contacts**

Robert Gabriel
Financial Analyst
Robert.Gabriel@ambest.com
+1(908) 439-2200 Ext. 5725

Farhad Eslami
Associate Director
Fred.Eslami@ambest.com
+1(908) 439-2200 Ext. 5406

**Information**

Best's Credit Rating Methodology

Guide to Best's Credit Ratings

Market Segment Outlooks

**Financial Data Presented**

The financial data in this report reflects the most current data available to the Analytical Team at the time of the rating. Updates to the financial exhibits in this report are available here: Best's Financial Report.

# Western Pacific Mutual Insurance Company, A Risk Retention Group

**AMB #:** 011238 | **NAIC #:** 40940 | **FEIN #:** 84-1144314

## Best's Credit Ratings

| Financial Strength Rating (FSR) | Issuer Credit Rating (ICR) |
|---|---|
| **A-** | **a-** |
| **Excellent** | **Excellent** |
| Outlook: **Stable** | Outlook: **Stable** |
| Action: **Affirmed** | Action: **Affirmed** |

## Assessment Descriptors

| | |
|---|---|
| Balance Sheet Strength | **Strongest** |
| Operating Performance | **Adequate** |
| Business Profile | **Limited** |
| Enterprise Risk Management | **Appropriate** |

## Rating Rationale

**Balance Sheet Strength: Strongest**

- Western Pacific Mutual Insurance Company, A Risk Retention Group (WPMIC) maintains the strongest level of risk-adjusted capitalization, as measured by Best's Capital Adequacy Ratio (BCAR) across all VaR levels.
- Liquidity measures are favorable and well supported by an investment base that consists primarily of fixed-income and equity securities.
- The company maintains a conservative approach to reserving that has produced consistently favorable loss reserve development on both calendar and accident year bases.
- Low reinsurance dependence relative to its peers, which is indicative of the company retaining the bulk of its underwriting risk.

**Operating Performance: Adequate**

- Variable net underwriting income is offset by stable and strong investment returns, resulting in positive net income in eight of the last ten years.
- Five- and ten-year average operating ratios significantly outperform its peers in the commercial casualty composite.
- The company reported an uptick in its loss and LAE ratio in 2019 and 2020, largely due to the timing issues of recoveries related to the company's warranty deductible program. Normalized loss results, which are net of loss recoveries, are supportive of the company's adequate operating performance.

**Business Profile: Limited**

- Formed in 1990 in the state of Colorado, the company is the risk-bearing entity that supports its affiliated company, Residential Warranty Company, LLC.
- The company is a risk retention group with members that are homebuilder contractors and re-modelers, providing home warranty and general liability lines of coverage.
- Stable and high membership retention despite the industry's cyclical nature, which has caused a number of exits as well as consolidations.
- Although diversified geographically, the company's predominant lines of business are home warranties and general liability.

**Enterprise Risk Management: Appropriate**

- Appropriate enterprise risk management with board and management involvement with regularly scheduled meetings.
- Well-defined underwriting, pricing and reserving standards and strategies with a continuous focus on improving risk management and risk mitigation practices.
- Tail risk is monitored, as reflected by the company's strongest category of BCAR score at the 99.8% VaR level.
- The company has a quota share reinsurance program with an affiliated company, Eastern Atlantic Insurance Company (EAIC), on its general liability coverage. EAIC accepts 30% of all risks.

**Outlook**

- The stable outlooks reflect AM Best’s expectations that the company's operating performance has stabilized and will generate adequate results that will support the company's strongest level of balance sheet strength.

**Rating Drivers**

- Negative rating pressure could occur following a material decline in the company's risk-adjusted capitalization.
- The company's ratings could be negatively impacted by a sustained and material deterioration in underwriting and operating performance, stemming from an inability to collect on loss recoveries related to its large deductible homebuilders.

## Credit Analysis

### Balance Sheet Strength

The ratings reflect Western Pacific Mutual Insurance Company, A Risk Retention Group's (WPMIC) excellent capitalization, historically conservative investment strategy, prudent and conservative reserving. Historically, WPMIC has maintained sufficient capital to support its ongoing obligations and has effectively managed its long-term exposure to loss from its ten-year homeowner warranty policies.

## Balance Sheet Strength (Continued...)

### Capitalization

Risk-adjusted capitalization remains at the strongest levels and supportive of written premiums, investments and loss reserves. As of year-end 2021, WPMIC's surplus was $132 million, which is over 22 times gross written premium.

The company has a quota share reinsurance program with an affiliated company, Eastern Atlantic (EAIC), on its GL coverage. EAIC is rated "a-" by AM Best and accepts 30% of all risks. Warranty losses are limited to the value of any insured home, and (to date) losses have not reached levels where surplus has been impacted.

### Asset Liability Management - Investments

WPMIC's investment philosophy is to purchase stocks and bonds for long-term investment, rather than active trading. WPMIC's investment income has remained relatively consistent in recent years and remains the main contributor to net income. In 2021, total invested assets were $165 million, which was an increase of 9.4% from the prior year. The investment portfolio makeup is 57% in bonds, 35% in common stocks and 6% in cash and cash equivalents.

### Reserve Adequacy

In general, reserves are set conservatively for both warranty and general liability lines. Typically for the warranty business, claims are handled as outlined in the specific warranty policy and procedure booklet issued to the homeowner on occupancy. Claims specialists are allocated by state as booklets vary. In-house technical staff provides engineering and construction overviews. There have been no changes to the claims handling approach used in managing WPMIC's warranty loss portfolio.

There have been no notable frequency and severity trends in the warranty claims experience. The warranty loss ratio from inception, including IBNR and the portion of loss reserves for future claims that is maintained in the unearned premium reserve is 51%. Western's warranty loss experience is primarily timing driven by the larger builders in the company's deductible program. The Company sees reimbursement for losses on claims related to the deductible program, however the timing of these recoveries can vary and take several months.

General liability claims related to construction issues are coordinated through an affiliate, Residential Warranty Company, LLC (RWC). Non-construction claims are handled exclusively through Integrity (which is the same third-party administrator which handles EAIC claims) and there have been no changes to the claims handling approach used in managing WPMIC's general liability loss portfolio, nor have there been any frequency or severity issues to date. The GL loss ratio from inception, including IBNR is 50% (similar to the warranty ratio). The GL large loss experience has been low and largely driven by slip and fall bodily injury claims.

## Operating Performance

WPMIC has seen some volatility in its pre-tax operating income and net income over the previous five-year period, which has put pressure on the company's adequate operating performance assessment. Underwriting results have been enhanced by consistent levels of net investment income in each of the last five years. The five and ten-year operating ratios of 52.0% and 58.9% are significantly lower that the industry composite of 88.7% and 87.7%, respectively, due to its strong investment returns.

WPMIC has recorded underwriting losses during the last 5 years mainly due to the difficult housing market and the economic downturn that began in 2008. Net premiums written have a 5 year cagr of 9.6%, but are still significantly lower than pre-crisis levels due to the prolonged downturn in the housing market. WPMIC's combined ratios have been above 100% and significantly exceed the industry average partially due to the RRG's decision to retain all key personnel through the down cycle so expense levels have not decreased and remains elevated.

While the five-year average loss and LAE ratio does compare favorably to the industry composite, 58.2% versus 28.1%, the five-year average underwriting expense ratio is elevated at 99%, which is due to the RRG's relatively high fixed expenses. The loss and LAE ratio has seen spikes in 2019 and 2020, largely due to the timing issues of recoveries related to the Company's warranty deductible program.

Net investment income has remained relatively flat as equity markets have been volatile and interest rates remain low. However, WPMIC has shown that it is capable of offsetting reduced underwriting income or underwriting losses with investment income as the housing market recovers.

WPMIC's long term growth will remain dependent on the business success of its members, which is tied to the long term trends of the overall home building economy. The U.S. homebuilding industry has slow growth since the economic crisis in 2007, however there have

## Operating Performance (Continued...)

been signs of improvement in recent years, which ultimately could be of great benefit to WPMIC. The company has specialized knowledge in their chosen lines of insurance, and its management is committed to mitigating risk. As a result, its membership remains strong and consistent.

## Business Profile

WPMIC specializes in marketing homeowner warranties, providing coverage for damage caused by design and construction defects. Underwriting operations of the company mainly focus on product liability coverages in all fifty states as specified under the 1986 Federal Liability Risk Retention Act.

Home warranty provides ten full years of coverage. The builder retains the liability for meeting the requirements of the warranty in the first two years, while WPMIC is responsible for major structural defects occurring in years 3 through 10. If the builder is unable fulfill its obligations in the first two years of the warranty, WPMIC would assume the builder's responsibilities. This guarantee of the builder's obligations, combined with the automatic transfer of the warranty to any subsequent buyers provides added protection to the homeowner.

The company offers two types of warranty policies, one for their large deductible builders and one for their nondeductible builders. There has been a significant change in the company's business mix over the past ten years, where a larger percentage of its warranty business is now being written under the large deductible policies.

Prior to 2004, the company exclusively wrote home owners warranty on newly constructed residential housing. In 2004, it introduced general liability coverage to its members. The GL coverages emanated from the needs of its members. The introduction of general liability was largely due to the fact that the coverage distinction between G/L coverages and warranty was difficult to determine in some instances.

Builders who participate in the program are members of the RWC. In order to be accepted as a participant of WPMIC, a builder must meet certain stringent screening requirements, as evaluated by RWC. These include proof of financial strength to support its participation in the warranty program, technical competence as a builder proven through inspection of homes under construction, and positive indications of business integrity through references from homeowners, suppliers and banks.

WPMIC, working in conjunction with RWC, has in place an active and successful subrogation program to recover claim payments in those circumstances where the builder or subcontractor ultimately is responsible. If a builder does not meet certain asset requirements, they are required to post an alternate security (a letter of credit, a bond or cash) which can be used in the event of a claim where the builder is held liable.

## Enterprise Risk Management

WPMIC's operation is ERM driven, as every decision made has a direct impact on its ERM. Thus, every manager is directly involved in risk management.

ERM practices include the following:

Being a Risk Retention Group in the home building arena means WPMIC's entire focus is on home construction issues. Some issues are: The economy, foreclosures, the existing inventory, ever changing building codes/regulations and the costs of new construction. Each of these issues potentially impacts all of insureds and, therefore, the hazards the company insures against. Risks are concentrated in the homebuilding industry, however WPMIC is permitted to write business in all 50 states, thus, it is not overly reliant on one jurisdiction. Pricing is monitored in a variety of ways including: monitoring ISO changes, monitoring hit ratios, reviewing renewal retention rates and most importantly, the day to day dialogue with builder members.

WPMIC monitors the frequency and severity of losses. It actively tracks both the general liability line and the warranty line for any adverse trends. Its claims committee, consisting of claims department personnel, underwriting manager, operations manager/treasurer, and corporate counsel meets monthly. The committee discusses all claims open greater than 90 days and any serious new claims.

Management reviews the regulatory/legal/claims environment through various means including ISO, membership in the National Association of Homebuilders, various state/regional homebuilder associations, its defense counsel, internal counsel and its members/insureds.

WPMIC has contracted with an external party for a disaster recovery plan. An IT steering committee discusses computer programming languages (to have a plan should a language become obsolete) and relationships with computer consulting firms should a need for IT assistance (expansion or turnover) arise.

**Enterprise Risk Management (Continued...)**

WPMIC has established a comprehensive succession plan that involves the continuation of the Parmer group of companies, including WPMIC.

### Reinsurance Summary

The company has a quota share reinsurance program with an affiliated company, Eastern Atlantic Insurance Company (EAIC), on its GL coverage. EAIC is rated "a-" by AM Best and accepts 30% of all risks.

### Environmental, Social & Governance

AM Best considers WPMIC's exposure to material environmental, social and corporate governance (ESG) risks to be low. As an organization that is involved in insuring the risks of its members that operate in the construction industry, the company feels its underwriting activities have low exposure to climate risk, and its profile on underwriting and investment are not exposed to so-called toxic assets and industries. The company operates in line with market peers, and at present ESG factors are unlikely to impact the credit quality of the company over the short-term. Currently, there are no regulatory requirements for the company relating to ESG.

## Financial Statements

| | 9-Months | | Year End - December 31 | | | |
|---|---|---|---|---|---|---|
| | 2022 | | 2021 | | 2020 | |
| **Balance Sheet** | **USD (000)** | **%** | **USD (000)** | **%** | **USD (000)** | **%** |
| Cash and Short Term Investments | 6,759 | 4.2 | 10,169 | 6.1 | 24,228 | 15.9 |
| Bonds | 99,213 | 62.2 | 95,566 | 57.4 | 81,080 | 53.2 |
| Preferred and Common Stock | 50,440 | 31.6 | 58,245 | 35.0 | 44,398 | 29.1 |
| Other Invested Assets | 569 | 0.4 | 527 | 0.3 | 531 | 0.3 |
| **Total Cash and Invested Assets** | 156,981 | 98.4 | 164,507 | 98.8 | 150,237 | 98.6 |
| Premium Balances | 1,432 | 0.9 | 1,231 | 0.7 | 1,113 | 0.7 |
| Other Assets | 1,145 | 0.7 | 762 | 0.5 | 1,024 | 0.7 |
| **Total Assets** | 159,558 | 100.0 | 166,499 | 100.0 | 152,374 | 100.0 |
| Loss and Loss Adjustment Expense Reserves: | | | | | | |
| Net Reported Loss Reserves* | 7,315 | 4.6 | 6,780 | 4.1 | 4,547 | 3.0 |
| Net IBNR Loss Reserves* | 2,815 | 1.8 | 1,090 | 0.7 | 3,771 | 2.5 |
| Net LAE Reserves | ... | ... | 1,110 | 0.7 | 1,397 | 0.9 |
| Total Net Loss and LAE Reserves | 10,130 | 6.3 | 8,979 | 5.4 | 9,716 | 6.4 |
| Net Unearned Premiums | 18,328 | 11.5 | 17,857 | 10.7 | 16,521 | 10.8 |
| Other Liabilities | 6,951 | 4.4 | 7,676 | 4.6 | 4,066 | 2.7 |
| **Total Liabilities** | 35,409 | 22.2 | 34,512 | 20.7 | 30,303 | 19.9 |
| Paid-In and Contributed Surplus | 16,192 | 10.1 | 16,192 | 9.7 | 16,192 | 10.6 |
| Unassigned Surplus | 107,956 | 67.7 | 115,795 | 69.5 | 105,879 | 69.5 |
| **Total Policyholders' Surplus** | 124,148 | 77.8 | 131,987 | 79.3 | 122,071 | 80.1 |
| **Total Liabilities and Surplus** | 159,558 | 100.0 | 166,499 | 100.0 | 152,374 | 100.0 |

Source: BestLink® - Best's Financial Suite
* Interim reserves balances include LAE.

**Last Update**
April 03, 2023

**Identifiers**
**AMB #:** 011238
**NAIC #:** 40940
**FEIN #:** 84-1144314

**Contact Information**

Domiciliary Address:
9265 Madras Court, Littleton,
Colorado 80130
United States

**Phone:** +1-303-263-0311
**Fax:** +1-303-470-9119

**Financial Data Presented**

The financial data in this report reflects the most current data available at the time the report was printed.

# Western Pacific Mutual Insurance Company, A Risk Retention Group

## Operations

**Date Incorporated:** June 28, 1990 **|** **Date Commenced:** July 23, 1990

**Domiciled:** Colorado, United States

**Licensed:** (Current since 11/27/2018). It is authorized in all other states under the Federal Liability Risk Retention Act and operates in the District of Columbia, American Samoa, AL, AK, AZ, AR, CA, CT, DE, FL, GA, HI, ID, IL, IN, IA, KS, KY, LA, ME, MD, MA, MI, MN, MS, MO, MT, NE, NV, NH, NJ, NM, NY, NC, ND, OH, OK, OR, PA, RI, SC, SD, TN, TX, UT, VT, VA, WA, WV, WI and WY. The company is licensed in Colorado.

**Business Type:** Property/Casualty
**Organization Type:** Mutual - RRG (Risk Retention Group)
**Marketing Type:** Other Direct
**Financial Size:** VIII ($100 Million to $250 Million)

## Best's Credit Ratings

### Rating Relationship

**AM Best Rating Unit: 011238 - Western Pacific Mutual Ins Co, A RRG**

Refer to the Best's Credit Report for AMB# 011238 - Western Pacific Mutual Insurance Company, A Risk Retention Group for details regarding the rating rationale, credit analysis, and financial exhibits available at the time the credit analysis was performed.

### Best's Credit Rating History

AM Best has assigned ratings on this company since 2001. In our opinion, the company has an Excellent ability to meet their ongoing insurance obligations and an Excellent ability to meet their ongoing senior financial obligations.

The following are the most recent rating events, for longer history refer to Rating History in BestLink:

| | Best's Financial Strength Ratings | | | Best's Long-Term Issuer Credit Ratings | | |
|---|---|---|---|---|---|---|
| **Effective Date** | **Rating** | **Outlook** | **Action** | **Rating** | **Outlook** | **Action** |
| **Current - Nov 18, 2022** | **A-** | **Stable** | **Affirmed** | **a-** | **Stable** | **Affirmed** |
| Oct 28, 2021 | A- | Negative | Affirmed | a- | Negative | Affirmed |
| Oct 20, 2020 | A- | Stable | Affirmed | a- | Stable | Affirmed |
| Sep 26, 2019 | A- | Stable | Affirmed | a- | Stable | Affirmed |
| Aug 23, 2018 | A- | Stable | Affirmed | a- | Stable | Affirmed |

## Management

Administration of WPMIC's affairs is guided by George A. Parmer, Chairman and President, who since 1981, also has been the President of Residential Warranty Company, LLC, the sponsor of this risk retention group. He also serves as President of Eastern Atlantic Insurance Company, an affiliated company with whom WPMIC shares some common management and contractual relationships. The two companies, however, have no ownership interests in each other.

Residential Warranty Company, LLC (RWC) performs warranty administration duties which include marketing, screening and processing applicants, underwriting risks, premium collection, arranging inspections of buildings under construction, and setting applicable building standards. It also provides an informal complaint and dispute service, administers claims on behalf of WPMIC, and conducts subrogation efforts for claims that have been paid by the carrier. RWC is reimbursed for the services provided at rates designed to be sufficient for its actual costs, which may be redetermined from time to time. RWC assisted with the formation of this risk retention group on behalf of its participating builders.

WPMIC has a management agreement, on a flat fee basis with, Seven Kites Strategic Consulting Inc. of Littleton, Colorado. The firm provides WPMIC with day-to-day operational support. The contract is on a yearly basis with an automatic renewal provision.

### Officers

**President:** George A. Parmer
**Vice President:** Sherlyn W. Farrell
**Secretary:** G. Adam Parmer
**Treasurer:** Robert Yeselavage

### Directors

George A. Parmer
John L. Schilling
Leonard Tintner

## History

WPMIC was incorporated on June 28, 1990, as a mutual insurance company under the laws of Colorado. It was formed with $750,000 of guaranty fund capital and surplus. These amounts were provided in cash using a surplus note of $350,000 and a letter of credit for $400,000. With the approval of the Colorado Division of Insurance, WPMIC repaid the surplus note and its accumulated interest, and released the $400,000 letter of credit which had been issued at the group's licensure. Simultaneously, the company issued a subordinated debenture for $1.1 million of which approximately half was paid in 1997. The remaining balance of the debenture was paid in full as of the end of June 2000.

Prior to August 1998, a contribution to surplus was made by insureds for each new structure for which a home warranty was provided. The contribution per structure was $15 through June 30, 1994, and $25 per structure thereafter, except for national builder members for which the contribution per structure remained at $15. These fees were recorded as capital contributions. The contribution requirement was discontinued as of the end of July 1998.