

Report
of the
Examination of
Middleton Insurance Company
Middleton, Wisconsin
As of December 31, 2016

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State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

Scott Walker, Governor
Theodore K. Nickel, Commissioner

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August 15, 2017

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Honorable Theodore K. Nickel
Commissioner of Insurance
State of Wisconsin
125 South Webster Street
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Commissioner:

In accordance with your instructions, an examination has been performed as of
December 31, 2016, of the affairs and financial condition of:

MIDDLETON INSURANCE COMPANY
Middleton, Wisconsin

and the following report thereon is respectfully submitted:

I. INTRODUCTION

The previous examination of Middleton Insurance Company (the company) was made in 2012 as of December 31, 2011. The current examination covered the intervening time period ending December 31, 2016, and included a review of such subsequent transactions deemed essential to complete this examination.

The "Summary of Examination Results" contains elaboration on all areas of the company's operations. Special attention was given to the action taken by the company to satisfy the recommendations and comments made in the previous examination report.

The company is annually audited by an independent public accounting firm as prescribed by s. Ins 50.05, Wis. Adm. Code. An integral part of this compliance examination was the review of the independent accountant's work papers. Based on the results of the review of these work papers, alternative or additional examination steps deemed necessary for the completion of this examination were performed. The examination work papers contain

documentation with respect to the alternative or additional examination steps performed during the course of the examination.

In addition to auditing, the public accounting firm performs non-auditing services for the company, including assistance with complex transactions such as accounting for income taxes and compilation of the annual statement. On December 13, 2010, an exemption was granted by the Commissioner, pursuant to s. Ins 50.08 (5), Wis. Adm. Code, permitting the independent auditor to perform this non-audit work for the company.

The company was organized as a town mutual insurance company on January 4, 1876, under the provisions of the then existing Wisconsin Statutes. The original name of the company was the Middleton Fire Insurance Company. Subsequent amendments to the company's articles and bylaws changed the company's name to that presently used.

During the period under examination, there was one amendment to the articles of incorporation and there were no amendments to the bylaws. This change was to Article III, Section 1 of the Articles of Incorporation, which states that anyone over the age of 75 years cannot "stand for election" to the board of directors. This change was approved on October 12, 2012.

The company is currently licensed to write property, including windstorm and hail, and nonproperty insurance. The company is currently licensed to write business in the following counties:

Columbia	Dane
Dodge	Grant
Green	Iowa
Jefferson	Lafayette
Rock	Sauk

A review was made of the policy and application forms currently used by the company. The company issues approved policies with or without endorsements for terms of one year with premiums payable on the advance premium basis. The company charges a \$30.00 annual policy fee for new and renewal policies and a \$3.00 fee for the choice of an installment method of payment.

Business of the company is acquired through 131 agents, one of whom is a director of the company. Agents are presently compensated for their services as follows:

Type of Policy	Compensation
All types of policies	15%

Agents have no authority to adjust losses. Most losses are adjusted by outside adjusters. Inspections are performed by Steve Leadholm, Manager, who receives \$30.00 - \$40.00 for inspections, \$30.00 per hour in-office, plus \$.50/mile for travel allowance.

Policyholders may participate in the management and control of the company by attending and voting at all annual or special meetings of the members. No member may vote by proxy. The annual meeting of the company for the election of directors and special meetings of the company are held in accordance with its articles of incorporation.

Board of Directors

The board of directors consists of six members divided into three classes. One class is elected at each annual meeting for a term of three years. Vacancies on the board may be filled by the directors for the interim to the next annual meeting when a director shall be chosen for the unexpired term.

The current board of directors consists of the following policyholders of the company:

Name	Principal Occupation	Residence	Term Expires
David Goplin	Builder/Contractor	Oregon, WI	2018
Eric Straehl *	Insurance Agent	Blanchardville, WI	2018
Thomas Stuessy	Farmer/operates Agri-business	Brooklyn, WI	2018
Timothy Amend	Engineering/Sales	Oregon, WI	2019
Gerald Jensen	Farmer/operates Agri-business	Nekoosa, WI	2019
Samuel Stuessy	Farmer/operates Agri-business	Brooklyn, WI	2020

* Directors who are also agents are identified with an asterisk.

Members of the board currently receive \$100.00 for each meeting attended and \$75.00 for each staff meeting attended. Travel expense of \$.50/mile is paid for any meeting.

Section 612.13 (1m), Wis. Stat., requires:

- (1) If a town mutual has fewer than nine directors, no more than one director may be an employee or representative of the town mutual; and
- (2) Employees and representatives of a town mutual may not constitute a majority of its board.

The company is in compliance with these requirements.

Officers

Officers are elected by the board of directors from among its members and hold office for one year or until their successors are duly elected and qualified. The officers and manager serving at the present time are as follows:

Name	Office	2016 Compensation
Gerald Jensen	President	\$ 2,675
Eric Straehl	Vice-President	1,100
Dave Goplin	Secretary/Treasurer	1,625
Steve Leadholm	Manager	36,530*

* Represents consulting and inspection fees paid to Schiffler and Company.

Reported compensation is the total compensation paid by the insurer for the year and includes salary, commissions, director fees and rental income as applicable.

Committees of the Board

The company's bylaws allow for the formation of certain committees by the board of directors. The committees at the time of the examination are listed below:

Audit & Salary Committee

Thomas Stuessy, Chair
Samuel Stuessy

Adjusting – Loss Committee

Samuel Stuessy, Chair
Gerald Jensen
Eric Straehl

Executive Committee

Gerald Jensen, Chair
Eric Straehl
David Goplin

Investment – Budget Committee

David Goplin, Chair
Timothy Amend
Eric Straehl

The President is an *ex-officio* member of all committees.

Growth of Company

The growth of the company since the previous examination as compiled from its filed annual statements was as follows:

Year	Net Premiums Earned	Policyholders	Net Income	Admitted Assets	Policyholders' Surplus
2016	\$746,591	1,809	\$ (81,454)	\$2,849,314	\$2,067,966
2015	833,021	1,862	72,020	2,613,884	1,918,187
2014	818,340	1,909	(300,901)	2,523,120	1,753,343
2013	787,593	1,831	120,772	2,644,501	1,801,500
2012	700,910	1,581	(26,367)	2,370,198	1,680,713
2011	678,589	1,416	(102,464)	2,411,608	1,881,043

The ratios of gross and net premiums written to surplus as regards policyholders

since the previous examination were as follows:

Year	Gross Premiums Written	Net Premiums Written	Policyholders' Surplus	Writings Net	Ratios Gross
2016	\$1,399,089	\$733,538	\$2,067,966	36%	68%
2015	1,452,280	822,045	1,918,187	43	76
2014	1,471,554	858,182	1,753,343	49	84
2013	1,334,015	852,929	1,801,500	47	74
2012	1,140,986	766,352	1,680,713	46	68
2011	998,245	684,880	1,881,043	36	53

For the same period, the company's operating ratios were as follows:

Year	Net Losses and LAE Incurred	Other Underwriting Expenses Incurred	Net Premiums Earned	Loss Ratio	Expense Ratio	Composite Ratio
2016	\$496,432	\$404,361	\$746,591	66%	55%	122%
2015	406,536	400,372	833,021	49	49	98
2014	813,059	414,352	818,340	99	48	148
2013	257,907	396,186	787,593	33	46	79
2012	408,080	355,207	700,910	58	46	105
2011	497,284	322,890	678,589	73	47	120

The company reported a cumulative increase in surplus of 10% over the last five years. During 2014, the decrease in surplus was due to net losses incurred of \$779,035. The company experienced an increase in losses in 2014 due to three regional wind and hailstorms on April 3rd, June 8th, and July 11th. Unrealized gains on Wisconsin Reinsurance Corporation stock over the last five years were \$396,195, a 57% increase in value. The number of policyholders has increased by 27.8% over the last five years and gross premiums written have increased 40.2% while net premiums written have increased 7.1% for the same period.

II. REINSURANCE

The examiners' review of the company's reinsurance portfolio revealed there is currently one ceding treaty. The treaty contained proper insolvency clauses. The treaty complied with s. Ins 13.09 (3), Wis. Adm. Code, concerning maximum wind loss. Company retentions of risk complied with s. Ins 13.06, Wis. Adm. Code.

1. Type of contract: Casualty Excess of Loss (AX1)
Reinsurer: Wisconsin Reinsurance Corporation
Effective date: January 1, 2017, continuous
Lines reinsured: Liability
Company's retention: \$10,000
Coverage: 100% of each and every loss, including loss adjustment expense, subject to the maximum policy limits of:
 - a. \$1,000,000 per occurrence, single limit or combined for bodily injury and property damage liability
 - b. \$1,000,000 split limits, in any combination of bodily injury and property damage liability
 - c. \$25,000 for medical payments, per person; \$25,000 per accident
Reinsurance premium: 50% of net premium written
Annual deposit premium: \$105,000
Termination provisions: 60-day advance notice requirement in the event that either party wishes to terminate the contract
2. Type of contract: First Surplus (B1)
Lines reinsured: All property business
Company's retention: \$350,000
Coverage: Over \$350,000 in respect to a risk; on a pro rata basis up to \$2,000,000

Pro rata portion of each and every loss, including loss adjustment expense, corresponding to the amount of the risk ceded

Premium: Pro rata portion of all premiums corresponding to the amount of each risk ceded
Annual deposit premium: \$223,202

Ceding commission: Commission allowance: 15% of the premium paid
Profit commission: 15% of the net profit

3. Type of contract: First Per Risk Excess of Loss (C1)
 - Lines reinsured: All property business
 - Company retention: \$75,000
 - Coverage: 100% of each and every loss in excess of \$75,000 up to \$100,000, including loss adjustment expense
 - Reinsurance premium: The company's net premium for the year multiplied by 17.5%
Annual deposit premium: \$186,690

4. Type of contract: Second Per Risk Excess of Loss (C2)
 - Lines reinsured: All property business
 - Company retention: \$175,000
 - Coverage: 100% of any loss, including loss adjustment expense, in excess of the company's retention up to \$175,000
 - Reinsurance premium: The company's net premium for the year multiplied by 6.00%
Annual deposit premium: \$64,008

5. Type of contract: First Aggregate Excess of Loss (D1)
 - Lines reinsured: All property business
 - Company retention: Losses equal to 70.00% of net premium written
 - Coverage: 100% of the amount by which the aggregate net losses, including loss adjustment expenses, exceed the retention up to 60.00% of net premium written
 - Premium: The company's net premium for the year multiplied by 6.00%
Annual deposit premium: \$70,308

6. Type of contract: Second Aggregate Excess of Loss (D2)
 - Lines reinsured: All property business
 - Company retention: Losses equal to 130% of net premium written
 - Coverage: 100% of annual aggregate losses, including loss adjustment expenses, in excess of the retention
 - Premium: 2.5% of net premiums written, subject to a minimum annual premium of \$29,295

III. FINANCIAL DATA

The following financial statements reflect the financial condition of the company as reported to the Commissioner of Insurance in the December 31, 2016, annual statement. No adjustments were made as a result of the examination.

Middleton Insurance Company
Statement of Assets and Liabilities
As of December 31, 2016

Assets	Ledger	Nonledger	Not Admitted	Net Admitted
Cash on hand	\$ 100	\$	\$	\$ 100
Cash deposited at interest	1,298,627			1,298,627
Stocks and mutual fund investments	1,133,953			1,133,953
Premiums, agents' balances and installments:				
In course of collection	47,870			47,870
Deferred and not yet due	127,291			127,291
Investment income accrued		685		685
Reinsurance recoverable on paid losses and LAE	15,522			15,522
Electronic data processing equipment	5,037			5,037
Fire dues recoverable	293			293
Other expense-related assets:				
Reinsurance commission receivable	16,061			16,061
Other nonexpense-related assets:				
Miscellaneous receivable	159			159
Securities receivable	203,716			203,716
Other nonadmitted assets:				
Prepaid expenses	<u>200</u>	<u> </u>	<u>200</u>	<u> </u>
Totals	<u>\$2,848,829</u>	<u>\$685</u>	<u>\$200</u>	<u>\$2,849,314</u>

Liabilities and Surplus

Net unpaid losses	\$ 124,187
Unpaid loss adjustment expenses	2,488
Commissions payable	39,480
Unearned premiums	573,908
Reinsurance payable	18,004
Amounts withheld for the account of others	129
Other liabilities:	
Expense-related:	
Accounts payable	2,347
Accrued salaries and wages	1,608
Nonexpense-related:	
Premiums received in advance	<u>19,197</u>
Total liabilities	781,348
Policyholders' surplus	<u>2,067,966</u>
Total Liabilities and Surplus	<u>\$2,849,314</u>

Middleton Insurance Company
Statement of Operations
For the Year 2016

Net premiums and assessments earned		\$ 746,591
Deduct:		
Net losses incurred	\$451,563	
Net loss adjustment expenses incurred	44,869	
Net other underwriting expenses incurred	<u>404,361</u>	
Total losses and expenses incurred		<u>900,793</u>
Net underwriting gain (loss)		(154,202)
Net investment income:		
Net investment income earned		13,883
Other income (expense):		
Miscellaneous income (expense)		<u>58,865</u>
Net income (loss) before federal income taxes		(81,454)
Federal income taxes incurred		<u> </u>
Net Income (Loss)		<u>\$ (81,454)</u>

Middleton Insurance Company
Reconciliation and Analysis of Surplus as Regards Policyholders
For the Five-Year Period Ending December 31, 2016

The following schedule is a reconciliation of surplus as regards policyholders during the period under examination as reported by the company in its filed annual statements:

	2016	2015	2014	2013	2012
Surplus, beginning of year	\$1,918,187	\$1,753,343	\$1,801,500	\$1,680,713	\$1,881,043
Net income (loss)	(81,454)	72,020	(300,901)	120,772	(26,367)
Net unrealized capital gain or (loss)	230,856	92,679	250,865	2,092	(173,963)
Change in nonadmitted assets	<u>377</u>	<u>145</u>	<u>1,879</u>	<u>(2,077)</u>	<u> </u>
Surplus, End of Year	<u>\$2,067,966</u>	<u>\$1,918,187</u>	<u>\$1,753,343</u>	<u>\$1,801,500</u>	<u>\$1,680,713</u>

Reconciliation of Policyholders' Surplus

The examination resulted in no adjustments to policyholders' surplus. The amount reported by the company as of December 31, 2016, is accepted.

IV. SUMMARY OF EXAMINATION RESULTS

Compliance with Prior Examination Report Recommendations

Comments and recommendations contained in the last examination report and the action taken on them by the company are as follows:

1. Corporate Records—It is recommended that the company establish that a quorum of ten members exists at annual meetings, or defer the annual meeting, as stated in its articles of incorporation.

Action—Compliance

Current Examination Results

Corporate Records

The minutes of the annual meetings of policyholders and meetings of the board of directors and committees thereof were reviewed for the period under examination and also for the subsequent period.

Biographical data relating to company officers and directors have been reported in accordance with the provisions of s. Ins 6.52, Wis. Adm. Code.

The company has executed formal written agreements with its agents. The contracts include language indicating the agent will represent the company's interests "in good faith."

Conflict of Interest

In accordance with a directive of the Commissioner of Insurance, each company is required to establish a procedure for the disclosure to its board of directors of any material interest or affiliation on the part of its officers, directors, or key employees which conflicts or is likely to conflict with the official duties of such person. A part of this procedure is the annual completion of a conflict of interest questionnaire by the appropriate persons. The company has adopted such a procedure for disclosing potential conflicts of interest. Conflict of interest questionnaires were reviewed for the period under examination with no apparent conflicts being noted.

Fidelity Bond and Other Insurance

The company is afforded coverage under the terms of the following bonds or contracts and has complied with s. Ins 13.05 (6), Wis. Adm. Code, which sets forth the minimum requirements for fidelity bond coverage:

Type of Coverage	Coverage Limits
Fidelity bond	\$ 140,000
Worker's compensation:	
Employee injury	statutory
Liability:	
Liability and medical expenses	1,000,000
Other than products/completed operations aggregate	2,000,000
Products/completed operations aggregate	2,000,000
Property	
Damage to premises	100,000
Business personal property	80,250
Commercial umbrella	1,000,000
Insurance company professional liability	1,000,000
Directors and officers professional liability	1,000,000

Service Contract

The Manager, Steve Leadholm, is a consultant provided by Schiffler and Company. Steve Leadholm is the owner of Schiffler and Company. The company does not have a written third-party agreement with Schiffler and Company. This could lead to misunderstandings about the nature and scope of work related to the manager position and how its consultant is to be paid. It is recommended that the company enter into a written agreement, approved by the board, with Schiffler and Company stating how Schiffler and Company's staff should be compensated.

Underwriting

The company has a written underwriting guide. The guide covers all the lines of business that the company is presently writing. The company has regular inspection procedures for both new and renewal business. Steve Leadholm, Manager, or a third-party contractor, inspects new business and, on a periodic basis, existing business. However, there is no written inspection guide. It is recommended that the company establish a formal inspection procedure for new and renewal business, whereby a sampling of new applications and of renewal business is inspected by staff or a contractor independent of the risk under consideration. The guide should also delineate the documentation standard for the inspection.

Claims Adjusting

The company has an adjusting committee consisting of at least three directors as required by s. 612.13 (4), Wis. Stat. The function of this committee is to adjust or supervise the adjustment of losses.

Accounts and Records

The examiners' review of the company's records indicated that the company is in compliance with s. Ins 13.05, Wis. Adm. Code, which sets forth the minimum standards for the handling of cash and recording of cash transactions by town mutual insurance companies. The examiners noted the following:

1. A proper policy register is maintained.
2. A proper cash receipts journal is maintained.
3. A proper cash disbursements journal is maintained.
4. A proper general journal is maintained.
5. A proper general ledger is maintained.

An extensive review was made of income and disbursement items. Cash receipts were traced from source records and the proper recording and eventual deposit thereof ascertained. Negotiated checks issued during the period under examination were reviewed, test checked for proper endorsement, and traced to cash records. The verification of assets and determination of liabilities were made as of December 31, 2016.

The company is audited annually by an outside public accounting firm.

EDP Environment

Company personnel were interviewed with respect to the company's electronic data processing environment. Access to the computers is limited to people authorized to use those computers. However, the examination revealed that the company's personnel did not use recommended security best practices in its daily operations. It is recommended that the company strengthen its information technology control environment to improve security.

Company personnel back up the computers daily and the backed-up data is kept off-site. Additional file backup is performed daily by an outside vendor. The company has manuals documenting the use of its software and outlining the steps to complete specific tasks. The

manuals assist in the continuity of operations by providing instructions for seldom-used applications or when staff turnover occurs.

Business Continuity Plan

A business continuity plan identifies steps to be performed by a company in the event of business interruptions including, but not limited to, the inability to access its computer, the loss of information on its computer, the loss of a key employee, or the destruction of its office building. The company has developed a business continuity plan. The company's business continuity plan appears to be adequate. However, it has never been tested. It is recommended that the company, with the assistance of the company's EDP vendors, test its business continuity plan.

Invested Assets

Section 610.23, Wis. Stat., requires insurers to hold all investments and deposits of its funds in its own name except that:

- (1) Securities kept under a custodial agreement or trust arrangement with a bank or banking and trust company may be issued in the name of a nominee of the bank or banking and trust company; and
- (2) Any insurer may acquire and hold securities in bearer form.

For securities not held under a custodial agreement or trust arrangement with a bank or banking and trust company, s. Ins 13.05 (4), Wis. Adm. Code, requires that:

Non-negotiable evidences of company investments such as registered bonds, certificates of deposits, notes, etc., shall be maintained in a safe or vault with adequate safety controls or in a safe deposit box in a bank. Negotiable evidences of company investments shall be maintained in a safety deposit box in a bank. Access to a company safe deposit box containing negotiable securities shall require the presence and signature of at least 2 officers, directors or employees of the company.

The company is in compliance with these requirements.

Effective January 1, 2017, the company entered into a safekeeping agreement with a custodial bank with regard to investments. The agreement was in compliance with ch. 610.23, Wis. Stat., and our departmental guidelines.

Investment Rule Compliance

The investment rule for town mutual insurers allows a company to invest in common stocks, common stock mutual funds, and other higher risk investments (referred to as "Type 2")

provided that the town mutual has a sufficient amount of lower risk investments (referred to as "Type 1"). A town mutual may invest in Type 2 securities only if it already has sufficient Type 1 investments. Type 1 investments must equal or exceed the greater of items 1, 2, or 3.

1. Liabilities plus \$300,000	\$1,081,348
2. Liabilities plus 33% of gross premiums written	1,243,047
3. Liabilities plus 50% of net premiums written	1,148,117
4. Amount required (greater of 1, 2, or 3)	1,243,047
5. Amount of Type 1 investments as of 12/31/2016	1,298,627
6. Excess or (deficiency)	\$ 55,580

The company has sufficient Type 1 investments.

ASSETS

Cash and Invested Cash **\$1,298,727**

The above asset is comprised of the following types of cash items:

Cash in company's office	\$ 100
Cash deposited in banks—checking accounts	143,839
Cash deposited in banks at interest	<u>1,154,788</u>
Total	<u>\$1,298,727</u>

Cash in company's office at year-end represents the company's petty cash fund. A physical count of petty cash was made by the examiners during the course of the examination and the balance reconciled to year-end.

Cash deposited in banks subject to the company's check and withdrawal consists of one account. Verification of the checking account balance was made by obtaining confirmations directly from the depository and reconciling the amounts shown thereon to company records.

Cash deposited in banks at interest represents the aggregate of seven deposits in four depositories. Deposits were verified by direct correspondence with the respective depositories and by inspection of the certificates in the company's safe deposit box. Interest received during the year 2016 totaled \$14,631.20 and was verified to company cash records. Rates of return earned on cash deposits ranged from 0.41% to 1.25%. Accrued interest on cash deposits totaled \$685 at year-end.

Stock Investments **\$1,133,953**

The above asset consists of the aggregate fair value of stocks held by the company as of December 31, 2016. Stocks owned by the company are located in the company's safe deposit box.

Stock certificates were physically examined by the examiners. The company's investment in stocks was in conformance with Wisconsin Statutes and the rules of the Commissioner of Insurance as regards investments made by town mutual insurers.

Dividends received during 2016 on stocks amounted to \$8,472 and were traced to cash receipts records. There were no accrued dividends at year-end.

Premiums, Agents' Balances in Course of Collection **\$47,870**

This asset represents the amounts due from agents or policyholders which are not in excess of 90 days past due at year-end. A review of accounts receivable – direct billing verified the accuracy of this asset.

Premiums Deferred and Not Yet Due **\$127,291**

This asset represents modal premium installments (such as monthly, quarterly, etc.) that are not yet due. A review of a sample from the company's detailed list of deferred premiums verified the accuracy of this asset.

Investment Income Accrued **\$685**

Interest due and accrued on the various assets of the company at December 31, 2016, consists of the following:

Certificates of Deposit	\$685
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Reinsurance Recoverable on Paid Losses and LAE **\$15,522**

The above asset represents recoveries due to the company from reinsurance on losses and loss adjusting expenses which were paid on or prior to December 31, 2016. A review of year-end accountings with the reinsurer verified the above asset.

Electronic Data Processing Equipment **\$5,037**

The above balance consists of computer hardware and operating system software, net of depreciation as of December 31, 2016. A review of receipts and other documentation verified the balance. Non-operating system software was properly nonadmitted.

Fire Dues Recoverable **\$293**

This asset represents the amount overpaid to the State of Wisconsin for 2016 fire dues. The examiners reviewed the company's fire department dues calculation and found this asset to be correctly calculated. The actual amount paid was verified to the cash disbursement records.

Reinsurance Commission Receivable**\$16,061**

The above asset represents the amount of reinsurance commissions that the company expected to receive as of December 31, 2016. A review of the terms of the reinsurance agreement and year-end accounting with the reinsurer verified the above asset.

Securities Receivable**\$203,716**

The above asset represents the amount due resulting from the maturing of a certificate of deposit. The check for the proceeds was deposited in the company's checking account on January 5, 2017. A review of the advice of deposit issued by the bank verified the above asset.

LIABILITIES AND SURPLUS

Unearned Premiums **\$573,908**

This liability represents the reserve established for unearned premiums in compliance with s. Ins 13.08 (3), Wis. Adm. Code. This reserve was established using a daily pro rata methodology and by adjusting for unearned premium held by the reinsurer.

Net Unpaid Losses **\$124,187**

This liability represents losses incurred on or prior to December 31, 2016, that remained unpaid as of that date. The examiners reviewed the reasonableness of this liability by totaling actual loss payments made subsequent to December 31, 2016, with incurred dates in 2016 and prior years. The examiners' development of unpaid losses is compared with the amount estimated by the company in the following schedule.

	Company Estimate	Examiners' Development	Difference
Incurred but unpaid losses	\$ 383,091	\$ 327,551	\$(55,540)
Less: Reinsurance recoverable on unpaid losses	<u>(258,904)</u>	<u>(206,373)</u>	<u>52,531</u>
Net Unpaid Losses	<u>\$ 124,187</u>	<u>\$ 121,178</u>	<u>\$ (3,009)</u>

The examiners' review of claim files included open claims, paid claims, claims closed without payment, and claims that were denied during the examination period. The review indicated that claims are investigated and evaluated properly and that payments are made promptly and in accordance with policy provisions upon the submission of a proper proof of loss.

In addition, the review of claims handling procedures and files revealed the following:

1. A proper loss register is maintained.
2. Claim files contained sufficient investigatory data and documentation to verify settlement payments or reserve estimates.
3. Proofs of loss were properly signed.

Unpaid Loss Adjustment Expenses **\$2,488**

This liability represents the company's estimate of amounts necessary to settle losses which were incurred prior to December 31, 2016, but which remained unpaid as of year-end. The methodology used by the company in establishing this liability is a combination of case

file loss adjustment expense reserves and an estimate developed by the company's public accounting firm.

The examiners' analysis of expenses incurred in the current year related to the settlement of prior year losses, as well as estimates of amounts necessary to settle any prior losses remaining unpaid at the examination date, determined this liability to be adequately stated.

Commissions Payable **\$39,480**

This liability represents the commissions payable to agents as of December 31, 2016. The examiners reviewed the company's commissions-payable calculation and found the liability to be reasonably stated.

Reinsurance Premium Payable **\$18,004**

This liability consists of amounts due to the company's reinsurer at December 31, 2016, relating to transactions which occurred on or prior to that date.

Liability	\$ (3,853)
Class C1	(8,065)
Class C2	(2,418)
Class DE1	(2,649)
Class DE2	<u>(1,103)</u>
	(18,088)
Deferred Premium	<u>36,092</u>
Total	<u><u>\$ 18,004</u></u>

Premiums Received in Advance **\$19,197**

This liability represents the total premiums received prior to year-end for policies with effective dates after December 31, 2016. The examiners reviewed 2016 premium and cash receipt records to verify the accuracy of this liability.

Other Liabilities **\$4,084**

This liability consists of accrued salaries and wages, payroll withholding, and accounts payable. Supporting records and subsequent cash disbursements verified these items.

V. CONCLUSION

Middleton Insurance Company is a town mutual insurer with an authorized territory of ten counties. The company has been in business for over 140 years providing property and liability insurance to its policyholders.

The company reported assets of \$2,849,314, liabilities of \$781,348 and policyholders' surplus of \$2,067,966 at year-end 2016. Surplus increased 12% over the previous five-year period. The company reported net income in two of the five years under examination, with net losses in 2012, 2014, and 2016. The year 2014 was a particularly difficult year due to three regional wind and hailstorms. Unrealized gains on Wisconsin Reinsurance Corporation stock over the last five years were \$396,195, a 57% increase in value. The number of policyholders has increased by 27.8% over the last five years, and gross premiums written have increased 40.2% while net premiums written have increased 7.1% for the same period.

The current examination of the company resulted in four recommendations listed in the following section.

VI. SUMMARY OF COMMENTS AND RECOMMENDATIONS

1. Page 14 - Service Contract—It is recommended that the company enter into a written agreement, approved by the board, with Schiffler and Company stating how Schiffler and Company's staff should be compensated.
2. Page 14 - Underwriting—It is recommended that the company establish a formal inspection procedure for new and renewal business, whereby a sampling of new applications and of renewal business is inspected by staff or a contractor independent of the risk under consideration. The guide should also delineate the documentation standard for the inspection.
3. Page 15 - EDP Environment—It is recommended that the company strengthen its information technology control environment to improve security.
4. Page 16 - Business Continuity Plan—It is recommended that the company, with the assistance of the company's EDP vendors, test its business continuity plan.

VII. ACKNOWLEDGMENT

The courteous cooperation extended to the examiners by the company's personnel is hereby acknowledged.

In addition to the undersigned, James Krueger of the Office of the Commissioner of Insurance, State of Wisconsin, participated in the examination.

Respectfully submitted,

John Ebsen
Examiner-in-Charge