Report of the Examination of

Sugar Creek Mutual Insurance Company

Elkhorn, Wisconsin

As of December 31, 2018

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State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

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December 9, 2019

Honorable Mark V. Afable
Commissioner of Insurance
State of Wisconsin
125 South Webster Street
Madison, Wisconsin 53703

Commissioner:

In accordance with your instructions, an examination has been performed as of December 31, 2018, of the affairs and financial condition of:

SUGAR CREEK MUTUAL INSURANCE COMPANY
Elkhorn, Wisconsin

and the following report thereon is respectfully submitted:

I. INTRODUCTION

The previous examination of Sugar Creek Mutual Insurance Company (Sugar Creek or the company) was made in 2014 as of December 31, 2013. The current examination covered the intervening time period ending December 31, 2018, 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 recommendation 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 preparation of financial statements and adjusting journal entries, preparation of tax returns, and preparation of depreciation schedules. 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 February 1, 1873, under the provisions of the then existing Wisconsin Statutes. The original name of the company was The Farmers Mutual Fire Insurance Company of the Town of Sugar Creek. Subsequent amendments to the company's articles and bylaws changed the company's name to that presently used. On January 1, 2005, Union Mutual Fire Insurance Company merged with and into the company, with the company remaining the surviving entity. During the period under examination, there was one amendment to the articles of incorporation and no amendments to the bylaws. The articles of incorporation were amended to provide that the Board of Directors be made up of no less than five members and up to nine members.

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:

Dane	Racine
Green	Rock
Jefferson	Walworth
Kenosha	Waukesha

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 policy fee equal to $25 on all policies except for the Tenant broad form policy. The company also charges installment fees of $5.00/billing for quarterly and semi-annual billings, and $2.50/billing for monthly ACH billings. Additionally, for dwelling policies, the company imposes surcharges for poor premium payment history, beginning with a $25 late fee, and for customers with a history of late payments, incremental surcharges as follows: In addition to the $25 late charge, $20 for the first cancellation billing (for a total of $45), $40 for the second cancellation billing (for a total of $65), and $60 for the third cancellation billing (for a total of $85).

Business of the company is acquired through thirteen agents, none of whom are directors of the company. Agents are presently compensated for their services as follows:

Type of Policy	Compensation	
	New	Renewal
Commercial Liability	19%	14%
Homeowner's/Farmowner's	19	14
Mobile Homeowner's	19	14
Fire & Extended Coverate	19	14

Agents can also receive additional contingent bonus commission ranging from 1% to 3%, contingent on attainment of certain premium volume, timeliness of renewals, and loss ratio requirements.

Agents do not have authority to adjust losses. Losses are primarily adjusted by an external company that receives an hourly fee as compensation for each loss adjusted. The company's President and Chief Executive Officer is authorized to adjust minor losses and also reviews and approves all claims adjusted by the external loss adjustment company. All loss payments are reviewed by the claims committee of the Board of Directors.

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 nine 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	Expiry
Robert Johnson	Auctioneer	Milton, WI	2022
Robert Agnew	Farmer/Semen Sales	Whitewater, WI	2022

Name	Principal Occupation	Residence	Expiry
Melinda Haak	IMT Account Manager	Lake Geneva, WI	2022
Bruce Vander Veen	Farmer	Sharon, WI	2021
Robert Janes	Banker	Evansville, WI	2021
David Kyle	Farmer	Elkhorn, WI	2021
Gene Lauderdale	Farmer	Elkhorn, WI	2020
Donald Schmaling	Farmer	Delevan, WI	2020
Alex McQuillen	Farmer	Whitewater, WI	2020

Members of the board currently receive the following compensation: The chairman receives $350 per board meeting, $200 per committee meeting, $300 per diem for other meetings, plus travel expenses in accordance with IRS limits; other board members receive $250 per board meeting, $200 per committee meeting, $300 per diem for other meetings, plus travel expenses in accordance with IRS limits.

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. Officers serving at the present time are as follows:

Name	Office	2018 Compensation
Robert Agnew	Chairman	$ 3,600
Robert Janes	Vice-Chairman	2,485
Bruce Vander Veen	Secretary	1,943
David Kyle	Treasurer	2,002
Adam Reed	President and Chief Executive Officer	98,633

Reported compensation is the total compensation paid by the insurer for the year and includes salary, commissions, and director fees as applicable. The president of the company is compensated by a salary and does not receive director fees for board or committee compensation.

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:

Adjusting/Inspection Committee
Robert Agnew
Robert Janes
Gene Lauderdale

Claims Committee
Whole board

Finance Committee
David Kyle
Robert Janes

Personnel Committee
Bruce Vander Veen
Robert Janes
David Kyle

Business Planning Committee
Alex McQuillen
Robert Janes
Robert Johnson

Underwriting Committee
Bruce Vander Veen
Don Schmaling
Melinda Haak

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	Policies In Force	Net Income	Admitted Assets	Policyholders' Surplus
2018	$1,189,336	1,553	$(137,935)	$9,606,235	$8,526,273
2017	1,162,377	1,539	112,464	9,867,616	8,865,396
2016	1,191,142	1,573	92,839	9,193,815	8,279,032
2015	1,179,520	1,621	101,642	8,467,999	7,472,243
2014	1,076,032	1,665	167,724	8,261,807	7,327,746
2013	1,139,806	1,724	66,342	7,723,312	6,822,795

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 Ratios Net	Writings Ratios Gross
2018	$1,648,522	$1,218,335	$8,526,273	14%	19%
2017	1,610,029	1,195,491	8,865,396	13	18
2016	1,624,251	1,158,165	8,279,032	14	20
2015	1,705,262	1,237,764	7,472,243	17	23
2014	1,653,361	1,080,393	7,327,746	15	23
2013	1,675,546	1,121,162	6,822,795	16	25

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	Com-posite Ratio
2018	$968,139	$703,840	$1,189,336	81%	58%	139%
2017	636,436	662,265	1,162,377	55	55	110
2016	656,298	623,905	1,191,142	55	54	109
2015	553,582	626,564	1,179,520	47	51	98
2014	489,089	597,682	1,076,032	45	55	101
2013	732,298	608,096	1,139,806	64	54	118

During the period under examination, the company assets increased $1,882,923, or 24.4%, and policyholders' surplus increased $1,703,478, or 25% over their 2013 balances.

Policies in force decreased from 1,724 to 1,553 for the period under examination; however, there was an increase in net premiums written from $1,121,162 to $1,218,335, or 8.7%. The company's net investment income increased over the last five years from $48,836 in 2013 to $148,106 in 2018.

The company reported net income in four of the five years under examination. The net loss and loss adjustment expense ratios were between 45% and 81%, with an average of 57%, and the underwriting expense ratios were between 51% and 58% for the period. The company's composite ratio was between 98% and 139% but averaged 111% for the period under examination.

II. REINSURANCE

The examiners' review of the company's reinsurance portfolio revealed there are currently two ceding treaties, one with Wisconsin Reinsurance Corporation, providing property and casualty coverages, and one with Factory Mutual Insurance Company, providing equipment breakdown coverages. The Wisconsin Reinsurance Corporation treaty contained a proper insolvency clause and complied with s. Ins 13.09 (3), Wis. Adm. Code, concerning maximum wind loss. The Factory Mutual Insurance Company treaty contained a proper insolvency clause. Company retentions of risk complied with s. Ins 13.06, Wis. Adm. Code.

Reinsurer:	Wisconsin Reinsurance Corporation
Effective date:	January 1, 2019
Termination provisions:	Either party may terminate as of January 1, by giving at least 90 days' written notice to the other party

The coverages provided under this treaty are summarized as follows:

1.	Type of contract:	Class AX1 – Casualty Excess of Loss
	Lines reinsured:	All casualty or liability business
	Company's retention:	$10,000 each and every loss occurrence including loss adjustment expenses
	Coverage:	100% of each and every loss occurrence, including loss adjustment expenses, in excess of the company retention subject to the maximum policy limits of: a. $1,000,000 per occurrence, single limit, 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. d. $25,000 for medical payments, per accident for Personal Lines.
	Reinsurance premium:	The rate for each annual period shall be determined by multiplying the rate by the company's net premium. Current rate is 50%. Annual deposit premium: $116,707
2.	Type of contract:	Class C1 – First Per Risk Excess of Loss
	Lines reinsured:	All property business
	Company's retention:	$125,000 per risk per loss occurrence

	Coverage:	$125,000 excess of retention including loss adjusting expenses each and every loss.
	Reinsurance premium:	The rate for each annual period shall be determined by multiplying the rate by the company's net premium. Current rate is 6.04%. Annual deposit premium: $85,008
3.	Type of contract:	Class C2 – Second Per Risk Excess of Loss
	Lines reinsured:	All property business
	Company's retention:	$250,000 per risk per loss occurrence
	Coverage:	$750,000 excess of retention including loss adjusting expenses each and every loss.
	Reinsurance premium:	The rate for each annual period shall be determined by multiplying the rate by the company's net premium. Current rate is 5.25%. Annual deposit premium: $73,890
4.	Type of contract:	Class C3 – Third Per Risk Excess of Loss
	Lines reinsured:	All property business
	Company's retention:	$1,000,000 per risk per loss occurrence
	Coverage:	$1,000,000 excess of retention including loss adjusting expenses each and every loss.
	Reinsurance premium:	The rate for each annual period shall be determined by multiplying the rate by the company's net premium. Current rate is 2.00%. Annual deposit premium: $28,148
5.	Type of contract:	Class D1 – First Aggregate Excess of Loss
	Lines reinsured:	All business written by the company
	Company's retention:	75% of net premium written
	Coverage:	65% of the amount by which the aggregate of the company's losses, including loss adjustment expenses, exceeding 75% of net premium written (losses from 75% to 140% of net premium written).
	Reinsurance premium:	The rate for each annual period shall be determined by multiplying the rate by the company's net premium Current rate is 5.90%. Annual deposit premium: $78,143

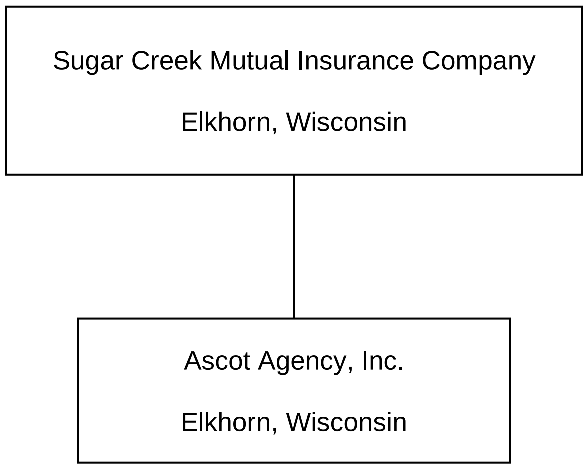
6.	Type of contract:	Class D2 – Second Aggregate Excess of Loss
	Lines reinsured:	All business written by the company
	Company's retention:	140% of net premium written
	Coverage:	100% of annual aggregate losses, including loss adjustment expenses, exceeding 140% of net premium written and in excess of the company's retention.
	Reinsurance premium:	The rate for each annual period shall be determined by multiplying the rate by the company's net premium. Current rate is 2.00%. Annual deposit premium: $26,489

<u>Equipment Breakdown Coverage</u>

Reinsurer:	Factory Mutual Insurance Company
Effective date:	January 1, 2017, and is continuous until terminated according to termination provisions described below.
Lines reinsured:	All equipment breakdown liability associated with Farmowners and Homeowners business, with stated exclusions
Company's retention:	None
Coverage:	100% of losses ceded under this treaty
Reinsurance premium:	With respect to Homeowners policies, there is a $25 flat charge per policy with a maximum limit of liability of $100,000 per risk without prior written agreement of the reinsurer. For Farmowners policies there is a sliding scale depending of the type of farm: Hobby Farms range from $25 to $380 flat charge per policy depending on the total insured value, up to a maximum of $10,000,000; and Industrial Agriculture range from $35 to $823 flat charge per policy depending on total insured values up to $10,000,000. Farm liability is subject to a maximum limit of liability of $10,000,000 per risk without prior written agreement of the reinsurer.
Ceding commission:	The current commission rate is 35% of the premiums ceded. Return commission shall be allowed at the same rate on all return premiums paid to the company.
Termination provisions:	By either party, on any April 1, July 1, October 1, or January 1, with 90 days' advance written notice by certified mail.
Additional comments:	The treaty contains a profit sharing clause where the reinsurer will share in its profits with the company if losses incurred are less than 30% of Premiums Earned. The profit sharing amount is calculated as an amount equal to one-half of the difference between Losses Incurred and 30% of Premiums Earned during the profit sharing period, which is an annual twelve month period commencing on January 1 and ending on December 31.

III. AFFILIATED COMPANIES

The company is the ultimate controlling person of a holding company system. The organizational chart below depicts the company's relationship with its wholly owned subsidiary insurance agency. A brief description of this affiliate follows the organizational chart.



Ascot Agency, Inc. (the agency) was created by four directors of the company in 1989 for the purpose of providing complementary coverages not available through the company. In 1999, the agency was purchased by the company for a total of $1,800 ($300 per share), with the company holding 100% of the outstanding shares.

The agency writes noncompeting business to policyholders. Major lines of business written include auto, life, and health insurance. As of December 31, 2018, the agency's unaudited financial statement reported assets of $5,398, liabilities of $0, and equity of $5,398. Operations for 2018 produced a net income of $1,039. The agency's equity balance is reported on the company's financial statements as a nonadmitted asset. Sugar Creek provides all of the administrative and management services necessary for the agency through a service agreement. In 2018, the agency paid the company $300 per month for services provided under this agreement.

IV. FINANCIAL DATA

The following financial statements reflect the financial condition of the company as reported to the Commissioner of Insurance in the December 31, 2018, annual statement. Adjustments made as a result of the examination are noted at the end of this section in the area captioned "Reconciliation of Policyholders' Surplus."

Sugar Creek Mutual Insurance Company
Statement of Assets and Liabilities
As of December 31, 2018

Assets	Ledger	Nonledger	Not Admitted	Net Admitted
Cash in company's office	$ 150	$	$	$ 150
Cash deposited in checking	155,921			155,921
Cash deposited at interest	552,865			552,865
Bonds	3,979,656			3,979,656
Stocks and mutual fund investments	4,485,479			4,485,479
Real estate	93,536			93,536
Premiums, agents' balances and installments:				
In course of collection	52,204			52,204
Deferred and not yet due	177,570			177,570
Investment income accrued		34,979		34,979
Fire dues recoverable	461			461
Reinsurance premium recoverable	2,146			2,146
Other nonexpense related assets:				
Federal income tax recoverable	71,268			71,268
Other nonadmitted assets:				
Investment in Ascot Agency		5,398	5,398	
Totals	$ 9,571,256	$ 40,377	$ 5,398	$ 9,606,235

Liabilities and Surplus

Net unpaid losses	$ 145,000
Loss adjustment expenses unpaid	8,525
Commissions payable	43,831
Unearned premiums	792,872
Other liabilities:	
Expense related:	
Accounts payable	44,730
Director and agent fees and expenses payable	5,363
Accrued wages	5,125
Nonexpense related:	
Premiums received in advance	34,516
Total Liabilities	1,079,962
Policyholders' Surplus	8,526,273
Total Liabilities and Surplus	$ 9,606,235

Sugar Creek Mutual Insurance Company
Statement of Operations
For the Year 2018

Net premiums and assessments earned		$1,189,336
Deduct:		
Net losses incurred	$877,026	
Net loss adjustment expenses incurred	91,113	
Net other underwriting expenses incurred	703,840	
Total losses and expenses incurred		1,671,979
Net underwriting gain (loss)		(482,643)
Net investment income:		
Net investment income earned	148,106	
Net realized capital gains (losses)	99,913	
Total investment gain (loss)		248,019
Other income (expense):		
Policy and installment fees	41,320	
Billing and late fees	9,169	
Total other income (expense)		50,489
Net income (loss) before federal income taxes		(184,135)
Federal income taxes incurred		(46,200)
Net Income (Loss)		$ (137,935)

Reconciliation and Analysis of Surplus as Regards Policyholders
For the Five-Year Period Ending December 31, 2018

The following schedule is a reconciliation of surplus as regards policyholders during the last five years as reported by the company in its filed annual statements.

	2018	2017	2016	2015	2014
Surplus, beginning of year	$8,865,396	$8,279,032	$7,472,243	$7,327,746	$6,822,795
Net income (loss)	(137,935)	112,464	92,839	101,642	167,724
Net unrealized capital gain or (loss)	(200,149)	473,950	710,153	38,854	335,361
Change in non-admitted assets	(1,039)	(50)	3,797	4,001	1,866
Surplus, End of Year	$8,526,273	$8,865,396	$8,279,032	$7,472,243	$7,327,746

Reconciliation of Policyholders' Surplus

The examination resulted in no adjustments to policyholders' surplus. The amount reported by the company as of December 31, 2018, is accepted. The examination resulted in the following reclassification:

Examination Reclassifications

	Debit	**Credit**
Bonds		$ 981,620
Stocks and mutual fund investments	$981,620	
Total Reclassifications	$981,620	$981,620

V. 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. Cash and Invested Cash—It is recommended that the company file abandoned property reports with the State Treasurer's Office as required by s. 177, Wis. Stat., and maintain copies of these filings.

   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.

In accordance with the provisions of s. Ins 6.52, Wis. Adm. Code, a report shall be provided to the Commissioner by a company with respect to the appointment or election of any new director, trustee, or officer elected or appointed within 15 days after such appointment or election. While reviewing the reporting of biographical data of the current directors of the company, it was discovered that the company did not file such a report for one of its directors. It is recommended that the company report biographical data relating to officers and directors in accordance with the provisions of s. Ins 6.52, Wis. Adm. Code.

The examination team reviewed all active agent agreements for content and execution and found that the company has appropriately 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, and the review revealed one disclosed conflict. One board member’s spouse is also an agent of the company. During board meetings, however, that board member recuses himself whenever matters involving his spouse’s agency are voted on.

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	$ 500,000
Worker's compensation:	
Employee injury	Statutory
Employee liability:	
Each accident	100,000
Each employee	100,000
Policy limit	500,000
Property:	
Buildings	415,700
Business personal property	28,605
Rental value	1,500
Commercial general liability:	
General aggregate limit	1,000,000
Each occurrence limit	1,000,000
Medical expense limit, one person	5,000
Professional liability and D&O coverage:	
Each claim	7,000,000
Aggregate	7,000,000
Employment practices liability	1,000,000

Underwriting

The company has written underwriting guidelines. The guidelines cover all the lines of business that the company is presently writing.

The company has a formal inspection procedure for both new and renewal business. All new applications are reviewed by the office manager or the president and chief executive officer. All new policies are inspected by an outside inspection firm within 60 days. Sugar Creek reserves the right to cancel the policy, within the first 60 days of the policy's effective date, by written notice to the insured per s. 631.36 (2), Wis. Stat. Renewal inspections occur every three years, with inspection reports being reviewed by the office manager and/or the president and chief executive officer.

As required by s. Ins 13.04, Wis. Adm. Code, each policyholder must sign a statement that he/she understands that the company is an assessable mutual and that the policyholder might be required to pay a share of legal assessments. During a review of a sample of 20 policies, the examination team discovered that one policy file did not include a signed undertaking. It is recommended that the company take action to ensure that all policy files contain a signed undertaking from the policyholder.

Agency Operations

The company has established Ascot Agency, Inc., which was described in the section of this report entitled “Affiliated Companies.” In accordance with s. 617.11, Wis. Stat., and s. Ins 40.03, Wis. Adm. Code, all insurers that are members of an insurance holding company system are required to report to the Commissioner the information concerning the insurer and its affiliates, including the annual registration statement (Form B), the summary registration statement (Form C), and any other filings which may be required as the agency increases operations. The company has not properly filed all required holding company filings for the agency for 2015, 2016, and 2018. Forms B and C were filed for the years ending December 31, 2014 and 2017. It is recommended that the company make all required holding company filings for its wholly owned insurance agency for all future years in accordance with s. Ins 40.03, Wis. Adm. Code.

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, 2018.

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 the computers. An automated process backs up the computers nightly and the backed-up data is kept in a cloud-based data vault which is managed by a third-party vendor.

The company has manuals documenting the use of its software and outlining the steps to complete specific tasks. Such manuals assist in the continuity of operations by providing instructions for seldom-used applications or when staff turnover occurs. The examination determined that the level of documentation contained in the manuals was reasonable.

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.

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 safety 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 safety deposit box containing negotiable securities shall require the presence and signature of at least 2 officers, directors or employees of the company.

It appears that the company is in compliance with the above requirements.

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	$1,379,962
2.	Liabilities plus 33% of gross premiums written	1,623,974
3.	Liabilities plus 50% of net premiums written	1,689,130
4.	Amount required (greater of 1, 2, or 3)	1,689,130
5.	Amount of Type 1 investments as of 12/31/2018	5,258,678
6.	Excess or (deficiency)	$3,569,548

The company does have sufficient Type 1 investments.

Investment Advisor Agreements

The examiners reviewed the company’s agreements with their investment advisor. The company is subject to discretionary arrangements, with fees charged based on assets under management, and assessed and calculated separately for the equity securities portfolio and for the fixed income securities portfolio. The investment advisor’s investment policy statement specifically referenced and incorporated the insurance company’s statement of investment policy and guidelines. However, the investment agreements do not specify whether the standard of conduct of the investment advisor is that of a fiduciary or some other standard, nor were the agreements executed by the investment advisor. Best practices prescribe that agreements with investment advisors include provisions describing whether or not the investment advisor is serving as a fiduciary in advising the company, and that they are properly executed by both the company and the investment advisor. It is recommended that the company's agreements with investment advisors include provisions that indicate whether the standard of conduct of the investment advisor is that of a fiduciary or some other standard, and that they are properly executed by both the company and the investment advisor.

ASSETS

Cash and Invested Cash **$708,936**

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

Cash in company's office	$ 150
Cash deposited in banks—checking accounts	155,921
Cash deposited in banks at interest	552,865
Total	$708,936

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

Cash deposited in banks subject to the company's check and withdrawal consists of two accounts maintained in two banks. The primary operating checking account balance was verified by obtaining confirmation directly from the depository and reconciling the amount shown thereon to company records. The company also has an operating account, with a December 31, 2018, balance of $7,382, that is used solely for payroll related payments. The balance in this account was verified by direct observation through the holding institution’s secure customer portal.

Unclaimed Funds

During the prior examination, it was noted that the company did not remit unclaimed funds to the Wisconsin Department of Revenue in compliance with ch. 177, Wis. Stat. (Uniform Unclaimed Property Act), which states that after five years an original payment becomes abandoned property and requires that all unclaimed property be reverted to the state. Checks should be accounted for as outstanding until such time as they are cashed by the payee or are presumed abandoned, at which point they should be reported as a liability until remitted to the state. In accordance with a recommendation from the last examination, the company has implemented a process to account for and remit uncashed checks as unclaimed property to the State of Wisconsin. However, as part of their unclaimed property procedures, the company is using a dormancy period of one year instead of five years for uncashed checks. It is recommended that the company remit property presumed abandoned to the Wisconsin

Department of Revenue in accordance with the requirement of s. 177.17, Wis. Stat., using a dormancy period of five years.

Book Value of Bonds **$2,998,036**

The above asset consists of the aggregate market value of bonds held by the company as of December 31, 2018. The company reported a balance for this line item of $3,979,656, while the examination resulted in a balance of $2,998,036. The difference is summarized as follows:

Bonds as originally reported	$3,979,656
Reclass to stocks and mutual fund investments	(981,620)
Total bonds	$2,998,036

Bonds owned by the company are held in a custodial account. Bonds were verified by review of a confirmed custodian year-end statement of the company’s investments. Bond purchases and sales for the period under examination were checked to brokers' invoices and advices. The company's investment in bonds was in conformance with Wisconsin Statutes and the rules of the Commissioner of Insurance regarding investments made by town mutual insurers.

During the examiner’s review of the company’s bond holdings, it was noted that the company owns preferred stocks, classified as perpetual preferred stocks, but has presented them on the annual statement as bonds. According to the town mutual annual statement instructions, preferred stock should be reported in Schedule D, Section 1 - Part 1, as a component of stocks and mutual fund investments. Moreover, the company reported the preferred stocks at amortized value. According to SSAP No. 32, the statement value reporting for perpetual preferred stocks is generally based on market value, while statement value reporting for bonds is based upon amortized cost. The preferred stocks owned by the company have declined in value; however, they are incorrectly reported as bonds at a cost-based statement value of $981,620 instead of at market value, which is $894,222. Therefore, the total investments of the company are overstated by $87,398, bonds are overstated by $981,620, and preferred stocks are understated by $894,222. The table above shows the reclassification between bonds and stocks and mutual fund investments; however, the company’s surplus was not adjusted for the difference between the reported value and market values of preferred stock because the amount of the adjustment is not material.

It is recommended that the company value its investments in perpetual preferred stocks at market value instead of amortized book value, in accordance with SSAP No. 32, and list them in Schedule D, Section 1 - Part 1, in accordance with the town mutual annual statement instructions.

Interest received during 2018 on bonds amounted to $132,352 and was traced to cash receipts records. Accrued bond interest of 20,533 at December 31, 2018, was checked and allowed as a nonledger asset. Interest received and accrued on bonds, as reported by the company, was $187,017 and $31,590, respectively. The difference of $52,665 in interest received and $11,057 in interest accrued was due to the misclassification of perpetual preferred stocks.

Stocks and Mutual Fund Investments **$5,467,099**

The above asset consists of the aggregate market value of stocks and mutual funds held by the company as of December 31, 2018. The company reported a balance for this line item of $4,485,479, while the examination resulted in a balance of $5,467,099. The difference is due to the reclassification of perpetual preferred stocks from the line item for bonds, which is summarized as follows:

Stock and mutual fund investments	$4,485,479
Reclass from bonds	981,620
Total	$5,467,099

Stocks owned by the company are primarily held in a custodial account, with two issues held in the company's safe. During the examiner's physical review of company held securities, it was noted that the annual statement reported six more shares of Wisconsin Reinsurance Class A Common shares than was actually owned by the company. The company owns 19,001 shares, but the annual statement reported ownership of 19,007 shares. Further, the valuation of the shares was overstated by $848 because the six overstated shares were included in the valuation at $141 per share. It is recommended that the company properly complete

Schedule D, Section 1 - Part 3 for Common Stocks, including the correct number of shares and valuation amounts for common stocks when completing the annual statement.

Stocks and mutual funds held by the custodian were independently confirmed with the custodian. Stock certificates in the company safe were physically inspected by the examiners. Stock and mutual fund purchases and sales for the period under examination were checked to brokers' invoices and advices. The company's investment in stocks and mutual funds 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 2018 on stocks and mutual funds amounted to $150,797 and were traced to cash receipts records. Accrued dividends of $12,937 at December 31, 2018, were checked and allowed as a nonledger asset. Dividends received and accrued on stocks and mutual fund investments, as reported by the company, were $98,132 and $1,880, respectively. The differences of $52,665 in dividends received and $11,057 in accrued dividends were due to the misclassification of perpetual preferred stocks described in the section of this report captioned "Bonds."

Book Value of Real Estate **$93,536**

The above amount represents the company's investment in real estate, net of depreciation, as of December 31, 2018. The company's real estate holdings consisted of its home office building and land.

The required documents supporting the validity of this asset were reviewed and were in order. Adequate hazard insurance was carried on the real estate and contents as noted under the caption "Fidelity Bond and Other Insurance." The company's investment in real estate and related items was in conformance with the Wisconsin Statutes and the rules of the Commissioner of Insurance as regards investments made by town mutual insurers. Real estate depreciation is calculated using the straight-line method.

Premiums, Agents' Balances in Course of Collection **$52,204**

This asset represents the amounts due from agents or policyholders which are not in excess of 90 days past due at year's end. A review of detailed premium records verified the accuracy of this asset.

Premiums Deferred and Not Yet Due **$177,570**

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 **$34,979**

Investment income due and accrued on the various assets of the company at December 31, 2018, consists of the following:

Cash deposited at interest	$ 1,509
Bonds	20,533
Stocks and mutual fund investments	12,937
Total	$34,979

In contrast to the foregoing schedule, the company reported accrued interest on bonds of $31,590 and accrued dividends on stocks and mutual fund investments of $1,880. The difference of $11,057 in each instance was due to the company's misclassification of perpetual preferred stocks as bonds, rather than stocks and mutual fund investments, as described in the section of this report captioned "Bonds."

Fire Dues Recoverable **$461**

This asset represents the amount overpaid to the State of Wisconsin for 2018 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 Premium Recoverable **$2,146**

The asset represents the amount of reinsurance premium that the company had overpaid as of December 31, 2018. The examiners verified the balance directly with the reinsurer.

Federal Income Taxes Recoverable **$71,268**

This asset represents the amount of federal income tax recoverable the company expected to receive as of December 31, 2018. A review of the company's federal income tax filing verified the above asset.

Investment in Ascot Agency, Inc. **$0**

Investment in Ascot Agency, Inc., of $5,398 represents the unaudited value of the company's subsidiary agency as of December 31, 2018. The company has properly nonadmitted this asset, thus the balance shown is $0.

LIABILITIES AND SURPLUS

Net Unpaid Losses **$145,000**

This liability represents losses incurred on or prior to December 31, 2018, 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, 2018, with incurred dates in 2018 and prior years. The examiners' development of unpaid losses is compared with the amount estimated by the company in the following schedule. The examination team concluded that, although net unpaid losses determined by the examination team were less than net unpaid losses reported by the company as of December 31, 2018, the difference was not material for the purpose of this examination, and presented a more conservative view of potential loss payments.

	Company Estimate	Examiners' Development	Difference
Incurred but unpaid losses	$145,000	$104,387	$40,613
Less: Reinsurance recoverable on unpaid losses	0	0	0
Net Unpaid Losses	$145,000	$104,387	$40,613

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 **$8,525**

This liability represents the company's estimate of amounts necessary to settle losses which were incurred prior to December 31, 2018, but which remained unpaid as of year’s end. The methodology used by the company in establishing this liability is through an estimation of unpaid loss adjustment expenses relative to net unpaid losses at year’s end.

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 **$43,831**

This liability represents the commissions payable to agents as of December 31, 2018. The examiners reviewed the company's commission calculation and found the liability to be reasonably stated.

Unearned Premiums **$792,872**

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. A recalculation of a sample from the company's detailed list of unearned premiums verified the accuracy of this asset.

Accounts Payable **$44,730**

This liability represents miscellaneous company liabilities that were incurred prior to December 31, 2018, which had not been paid. Supporting records and subsequent cash disbursements verified these items.

General payables	$ 5,139
Accrued deferred compensation - accrual for deferred compensation expense for paid time off and vacation time earned, but not used	38,327
Amounts withheld for the account of others - employee payroll deductions	1,264
Total	$44,730

Director and Agent Fees and Expenses Payable **$5,363**

This liability represents accrued expenses and reimbursements to company personnel and the board of directors as of year's end. Supporting records and subsequent cash disbursements verified this liability.

Accrued Wages **$5,125**

This liability represents the accrued wages and salaries payable that were earned prior to year's end. Supporting records and subsequent cash disbursements verified this liability.

Premiums Received in Advance **$34,516**

This liability represents the total premiums received prior to year's end for policies with effective dates after December 31, 2018. The examiners reviewed 2018 premium and cash receipt records to verify the accuracy of this liability.

VI. CONCLUSION

Sugar Creek Mutual Insurance Company is a town mutual insurer with an authorized territory of eight counties. The company has been in business for more than 146 years providing property and liability insurance to its policyholders.

The company reported assets of $9,606,235, liabilities of $1,079,962, and policyholders' surplus of $8,526,273 at year-end 2018. The number of policyholders has decreased from 1,724 in 2013 to 1,553 in 2018, and the company reported a net income in four of the five years under examination. Surplus increased 25% over the five-year period.

The company has complied with the one recommendation from the previous examination. The current examination resulted in seven recommendations. The recommendations relate to corporate records, underwriting, agency operations, unclaimed funds, stocks and mutual fund investments, book value and classification of bonds and preferred stocks, and investment advisor agreements. The examination resulted in no adjustment to surplus.

VII. SUMMARY OF COMMENTS AND RECOMMENDATIONS

1. Page 16 - Corporate Records—It is recommended that the company report biographical data relating to officers and directors in accordance with the provisions of s. Ins 6.52, Wis. Adm. Code.

2. Page 18 - Underwriting—It is recommended that the company take action to ensure that all policy files contain a signed undertaking from the policyholder.

3. Page 18 - Agency Operations—It is recommended that the company make all required holding company filings for its wholly owned insurance agency for all future years in accordance with s. Ins 40.03, Wis. Adm. Code.

4. Page 21 - Investment Advisor Agreements—It is recommended that the company's agreements with investment advisors include provisions that indicate whether the standard of conduct of the investment advisor is that of a fiduciary or some other standard, and that they are properly executed by both the company and the investment advisor.

5. Page 22 - Unclaimed Funds—It is recommended that the company remit property presumed abandoned to the Wisconsin Department of Revenue in accordance with the requirement of s. 177.17, Wis. Stat., using a dormancy period of five years.

6. Page 24 - Book Value of Bonds—It is recommended that the company value its investments in perpetual preferred stocks at market value instead of amortized book value, in accordance with SSAP No. 32, and list them in Schedule D, Section 1 - Part 1, in accordance with the town mutual annual statement instructions.

7. Page 24 - Stocks and Mutual Fund Investments—It is recommended that the company properly complete Schedule D, Section 1 - Part 3 for Common Stocks, including the correct number of shares and valuation amounts for common stocks when completing the annual statement.

VIII. ACKNOWLEDGMENT

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

In addition to the undersigned, Mark T. McNabb of the Office of the Commissioner of Insurance, State of Wisconsin, participated in the examination.

Respectfully submitted,

James Vanden Branden
Examiner-in-Charge