

Report  
of the  
Examination of  
Calumet Equity Mutual Insurance Company  
New Holstein, Wisconsin  
As of December 31, 2010

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# State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

*Scott Walker, Governor*  
*Theodore K. Nickel, Commissioner*

*Wisconsin.gov*

June 15, 2011

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Honorable Theodore K. Nickel  
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, 2010, of the affairs and financial condition of:

CALUMET EQUITY MUTUAL INSURANCE COMPANY  
New Holstein, Wisconsin

and the following report thereon is respectfully submitted:

## I. INTRODUCTION

The previous examination of Calumet Equity Mutual Insurance Company (the company) was made in 2007 as of December 31, 2006. The current examination covered the intervening time period ending December 31, 2010, 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.

The company was organized as a town mutual insurance company on March 10, 1873, under the provisions of the then existing Wisconsin Statutes. The original name of the company was the Mutual Fire Insurance Company of the Town of New Holstein. 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 filed amendment to the articles of incorporation and no amendments to the bylaws. The annual policyholders' meeting date was requested changed from the first Thursday in March of each year to be the second Thursday in March at the annual meeting in 2009. The company filed the correct form with this office but failed to document that they had the ten members attending this annual meeting which constitutes a quorum according to the company's articles of incorporation. Due to the fact that there was no quorum present the meeting and vote was invalid and it should have been brought up and voted on at another meeting which had a quorum present to vote. It is recommended that the company follow its articles of incorporation when making amendments to its articles of incorporation and bylaws.

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:

Brown	Calumet
Dodge	Fond du Lac
Green Lake	Kewaunee
Manitowoc	Oconto
Outagamie	Ozaukee
Shawano	Sheboygan
Washington	Waupaca
Waushara	Winnebago

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 also charges a policy fee based on type of policy and payment frequency. Renter and tenant policy fees range

from \$10-\$12, homeowner policy fees range from \$30-\$32, farmowner policy and dwelling fire policy fees range from \$65-\$76.

Business of the company is acquired through approximately 203 agents representing 39 agencies. Agents are presently compensated for their services as follows:

<b>Type of Policy</b>	<b>Compensation</b>
Homeowner & Mobile Homeowner	17%
Farmowner	15
Town & Country	15
Standard Non-Farm	17
Standard Farm	15
Commercial	15

Agents do not have authority to adjust losses. The larger losses are adjusted by outside professional adjusters and the smaller losses are adjusted by the company's president. The president is a salaried employee who receives an hourly fee for adjusting losses and \$0.51 per mile for travel allowance. Directors may also adjust losses but do so infrequently. They are paid an hourly fee as approved by the board, plus the above travel allowance. All losses are reviewed and approved by the Loss Adjustment Committee.

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 five 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:

<b>Name</b>	<b>Principal Occupation</b>	<b>Residence</b>	<b>Expiry</b>
Jerry Criter	Farmer	Chilton	2013
Gerald Heus	Excavation Contractor	New Holstein	2013
Glen Calnin	Banking	Chilton	2012
Grant Mortimer	Distribution	Chilton	2012
Terry Criter	Farmer	Chilton	2011

The current articles of incorporation require board membership to be composed of six directors. Effective April 30, 2007, the company's former Secretary/Treasurer and member of the board retired. The April 2007 minutes of the board of directors indicated an intention to present an amendment to the articles of incorporation reducing the board from six to five members for approval at the 2008 annual meeting of policyholders. It was noted that this amendment to the articles of incorporation was never completed nor was any such change officially approved by the board of directors, presented to the members at an annual meeting for approval, or sent to this office for approval. It is recommended that the company operate according to its articles and bylaws or amend them to describe the intended number of directors.

External members of the board currently receive \$300 for each board meeting attended. Internal members receive no fee for board meetings attended but do receive meeting pay for attending board-directed seminars or training. All board members receive \$0.51 per mile for travel expenses.

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 not in compliance with these requirements. The company currently has five members on its board and it was discovered during this examination that two of these directors are officers who qualify as an employee or representative of the town mutual. It is recommended that the company become compliant with the number of inside and outside directors in accordance with s. 612.13 (1m), Wis. Stat.

### **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:

<b>Name</b>	<b>Office</b>	<b>2010 Compensation</b>
Jerry Criter	President	\$16,595
Gerald Heus	Vice President	5,800
April Tarras	Secretary/Treasurer	61,000

Reported compensation is the total salary compensation paid by the insurer for the full year and includes adjusting fees and other special meeting fees as applicable. In addition the Secretary/Treasurer works for an agency that writes policies for the company and they received a total of \$5,497 in commissions during the year.

### **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 Committee**

Gerald Heus, Chair  
Glen Calnin  
Jerry Criter  
April Tarras

#### **Executive Committee**

Jerry Criter, Chair  
Gerald Heus  
April Tarras

#### **Rate Committee**

Gerald Heus, Chair  
Jerry Criter  
April Tarras  
Other board members called to assist

#### **Nominating Committee**

Jerry Criter, Chair  
Gerald Heus  
April Tarras

### **Growth of Company**

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

<b>Year</b>	<b>Net Premiums Earned</b>	<b>Policies In Force</b>	<b>Net Income</b>	<b>Admitted Assets</b>	<b>Policyholders' Surplus</b>
2010	\$796,781	1,917	\$(343,486)	\$1,815,008	\$ 816,260
2009	700,144	1,751	(226,970)	1,992,088	1,098,617
2008	711,003	1,634	84,735	2,175,046	1,437,123
2007	713,603	1,625	(59,673)	2,081,287	1,315,856
2006	742,344	1,653	(60,535)	2,143,731	1,326,320

The ratios of gross and net premiums written to surplus as regards policyholders since the previous examination were as follows:

<b>Year</b>	<b>Gross Premiums Written</b>	<b>Net Premiums Written</b>	<b>Policyholders' Surplus</b>	<b>Writings Net</b>	<b>Ratios Gross</b>
2010	\$1,306,497	\$844,794	\$ 816,260	103%	160%
2009	1,214,765	763,791	1,098,617	70	111
2008	1,115,360	704,696	1,437,123	49	78
2007	1,079,538	705,963	1,315,856	54	82
2006	1,095,363	713,000	1,326,320	60	83

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

<b>Year</b>	<b>Net Losses and LAE Incurred</b>	<b>Other Underwriting Expenses Incurred</b>	<b>Net Premiums Earned</b>	<b>Loss Ratio</b>	<b>Expense Ratio</b>	<b>Composite Ratio</b>
2010	\$786,227	\$428,086	\$796,781	99%	51%	150%
2009	616,455	391,713	700,144	88	51	139
2008	336,765	369,566	711,003	47	53	99
2007	510,624	354,892	713,603	72	50	122
2006	547,650	358,558	742,344	74	50	124

The company experienced underwriting losses in each year under examination except 2008. The above financial loss results are primarily attributed to the company's hailstorm- and fire-related claims experience.

Gross and net premiums written and policies in force have steadily increased during the period under examination. The company continues to emphasize marketing efforts going forward through agency visitations to renew interest in Calumet Equity Mutual with the objective of generating new business to improve overall profitability. At the same time the company has increased its underwriting inspections on all new policies and continues to re-inspect its upcoming renewals depending on the size of the risk involved.

Admitted assets and surplus steadily declined since the prior examination associated with the above sustained losses. Unrealized capital gains on Wisconsin Reinsurance Corporation common stock partially offset the company's underwriting losses during the period under examination.



## II. REINSURANCE

The examiners' review of the company's reinsurance portfolio revealed there is currently one ceding treaty. The treaty contained a proper insolvency clause and 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.

Reinsurer:	Wisconsin Reinsurance Corporation
Effective date:	January 1, 2011
Termination provisions:	The company or reinsurer may terminate this contract of reinsurance as of 12:01 a.m. Central Standard Time on any January 1, by giving the other party at least 90 days' prior written notice

The coverages provided under this treaty are summarized as follows:

1. Type of contract: Class A Casualty Excess of Loss
- Lines reinsured: All business classified as casualty or liability written by the company
- Company's retention: \$5,000 in respect to each and every loss
- Coverage: 100% of any loss, including loss adjustment expense, in excess of the company's retention subject to maximum policy limits as follows:
  - (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; \$25,000 per accident

Company agrees to retain sole responsibility for milk contamination if it does not impose the deductible on its insured policies; however, the reinsurer agrees to waive the deductible if the insured provides the company evidence of completion of the Dairy Quality Assurance Program within 12 months prior to the date of the claim
- Reinsurance premium: 52.5% of net premium written subject to:
  - (a) Minimum Annual Premium of 75% of Annual Deposit Premium
  - (b) Annual Deposit Premium = \$105,000

2. Type of contract: Class B First Surplus
- Lines reinsured: All property business written by the company
- Company's retention: \$400,000 plus at least 50% on a pro rata basis per ceded risk when the company's net retention is \$400,000 or less
- Company shall retain on each loss a per loss retention in an amount equal to 10% of the loss and loss adjusting expenses otherwise recoverable
- Coverage: Company may cede on a pro rata basis and the reinsurer shall be obligated to accept up to \$800,000, when the company's net retention is \$400,000 or more in respect to a risk
- Company may cede on a pro rata basis and the reinsurer shall be obligated to accept up to 50% of such risk, when the company's net retention is \$400,000 or less in respect to a risk
- Reinsurance premium: Pro rata portion of all premiums, fees and assessments charged by the company, corresponding to the amount of each risk ceded hereunder
- Ceding commission: Reinsurer shall allow the company a commission allowance equal to 15% of premiums ceded to reinsurer
- Return commission shall be allowed at the same rate on all return premiums paid to the company
- Reinsurer shall pay the company a profit commission of 15% of net profit accruing to the reinsurer during each accounting period in accordance with profit commission formulas outlined in the contract
3. Type of contract: Class C-1 First Layer Excess of Loss
- Lines reinsured: All property business written by the company
- Company's retention: \$55,000
- Coverage: 100% of any loss, including loss adjustment expense, in excess of the company's retention subject to a \$85,000 limit of liability in respect to each and every loss occurrence
- Reinsurance premium: 15.0% of net premiums written (NPW) based on the loss experience for the prior four years, subject to the following minimum and maximum rates:
- Minimum Rate: 6.5% NPW  
Maximum Rate: 15.0% NPW  
Annual Deposit Premium: \$147,520  
Minimum Premium: 75% Annual Deposit Premium

4. Type of contract: Class C-2 Second Layer Excess of Loss
- Lines reinsured: All property business written by the company
- Company's retention: \$140,000
- Coverage: 100% of any loss, including loss adjustment expense, in excess of the company's retention, subject to a \$260,000 limit of liability in respect to each and every loss occurrence
- Reinsurance premium: 4.25% of net premium written subject to the following:
- Annual Deposit Premium: \$41,797  
 Minimum Premium: 75% Annual Deposit Premium
5. Type of contract: Class D/E1 First Aggregate Excess of Loss
- Lines reinsured: All lines of business written by the company
- Company's retention: Losses, including loss adjustment expenses, in an amount equal to not less than 55% of net premiums written
- Coverage: 100% of aggregate net losses, including loss adjustment expense, in excess of the company's Attachment Point equal to 60% of net premium written
- Reinsurance premium: 7.5% of net premium written (NPW) based on the company's loss experience for the prior eight years subject to the following minimum and maximum rates:
- Minimum Rate: 7.5% NPW  
 Maximum Rate: 10.0% NPW  
 Annual Deposit Premium: \$80,885  
 Minimum Premium: 75% Annual Deposit Premium
6. Type of contract: Class D/E2 Second Aggregate Excess of Loss
- Lines reinsured: All business written by the company
- Company's retention: Losses, including loss adjustment expenses, in an amount equal to not less than 115% of NPW
- Coverage: 100% of aggregate net losses, including loss adjustment expense, in excess of the Attachment Point equal to 115% of net premium written, subject to a limit of 100% of all loss
- Reinsurance premium: 3% of net premium written subject to:
- Annual Deposit Premium: \$32,354  
 Minimum Premium: 75% Annual Deposit Premium

### **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, 2010, 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."

**Calumet Equity Mutual Insurance Company**  
**Statement of Assets and Liabilities**  
**As of December 31, 2010**

<b>Assets</b>	<b>Ledger</b>	<b>Nonledger</b>	<b>Not Admitted</b>	<b>Net Admitted</b>
Cash on hand	\$ 50	\$	\$	\$ 50
Cash in checking	68,618			68,618
Cash deposited at interest	485,016			485,016
Bonds	20,000			20,000
Stocks and mutual fund investments	983,728			983,728
Real estate	49,593			49,593
Premiums, agents' balances and installments:				
In course of collection	6,352			6,352
Deferred and not yet due	193,434			193,434
Investment income accrued		2,240		2,240
Reinsurance recoverable on paid losses and LAE	5,128			5,128
Electronic data processing equipment	848			848
Furniture and fixtures				
Other nonadmitted assets:				
Computer software	5,708		5,708	
Automobile	<u>5,536</u>	<u>          </u>	<u>5,536</u>	<u>          </u>
<b>Totals</b>	<b><u>\$1,824,011</u></b>	<b><u>\$2,240</u></b>	<b><u>\$11,244</u></b>	<b><u>\$1,815,007</u></b>

**Liabilities and Surplus**  
**As of December 31, 2010**

Net unpaid losses	\$ 226,309
Unpaid loss adjustment expenses	24,000
Commissions payable	41,533
Fire department dues payable	318
Unearned premiums	605,326
Reinsurance payable	61,358
Other liabilities:	
Expense-related:	
Accounts payable	10,388
Nonexpense-related:	
Premiums received in advance	28,785
Rent security deposits	<u>730</u>
Total liabilities	998,747
Policyholders' surplus	<u>816,260</u>
<b>Total Liabilities and Surplus</b>	<b><u>\$1,815,007</u></b>

**Calumet Equity Mutual Insurance Company**  
**Statement of Operations**  
**For the Year 2010**

Net premiums and assessments earned		\$ 796,781
Deduct:		
Net losses incurred	\$656,599	
Net loss adjustment expenses incurred	129,628	
Net other underwriting expenses incurred	<u>428,086</u>	
Total losses and expenses incurred		<u>1,214,313</u>
Net underwriting gain (loss)		(417,532)
Net investment income:		
Net investment income earned	<u>(2,436)</u>	
Total investment gain (loss)		(2,436)
Other income (expense):		
Miscellaneous	182	
Installment and policy fees	<u>76,300</u>	
Total other income		<u>76,482</u>
Net income (loss) before federal income taxes		(343,486)
Federal income taxes incurred		<u>0</u>
Net Income (Loss)		<u>\$ (343,486)</u>

**Calumet Equity Mutual Insurance Company**  
**Reconciliation and Analysis of Surplus as Regards Policyholders**  
**For the Four-Year Period Ending December 31, 2010**

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:

	<b>2010</b>	<b>2009</b>	<b>2008</b>	<b>2007</b>
Surplus, beginning of year	\$1,098,617	\$1,437,123	\$1,315,856	\$1,326,320
Net income	(343,486)	(226,970)	84,735	(59,673)
Net unrealized capital gain or (loss)	62,962	(115,593)	19,433	77,216
Change in nonadmitted assets	<u>(1,833)</u>	<u>4,057</u>	<u>17,099</u>	<u>(28,007)</u>
Surplus, End of Year	<u>\$ 816,260</u>	<u>\$1,098,617</u>	<u>\$1,437,123</u>	<u>\$1,315,856</u>

### Reconciliation of Policyholders' Surplus

A reconciliation of the policyholders' surplus as reported by the company in its filed annual statement and as determined by the examination is detailed in the following schedule:

Policyholders' surplus per December 31, 2010, annual statement		\$816,260
<b>Item</b>	<b>Increase</b>	
Adjustment to net unpaid losses	<u>\$12,900</u>	
Increase to surplus per examination		<u>12,900</u>
Policyholders' Surplus per Examination		<u>\$829,160</u>

## 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 board of director minutes demonstrate active oversight of operations through the inclusion of more specific comments or reference to attachments, as it relates to investment decisions, financial results and claim approval status.

Action—Compliance.

2. Corporate Records—It is recommended that the board appointed committees meet on a regularly scheduled basis to demonstrate more active involvement of the board's committees and prepare minutes demonstrating oversight or otherwise demonstrate that similar oversight is conducted at the full board level.

Action—Partial compliance; see comments in the "Summary of Current Examination Results."

3. Business Plans—It is recommended that the company update its business plan on an annual basis to provide more meaningful goals and objectives against which to measure operating performance.

Action—Compliance.

4. Business Plans—It is recommended that the company also complete formal budgetary expense projections to provide a measure for monitoring expense performance in relation to business plan goals and objectives.

Action—Compliance.

5. Underwriting—It is recommended that the company review and implement a periodic, ongoing inspection program on a reasonable cyclical basis, whereby a sampling of new applications and renewal business is inspected, including maintenance of reasonably current property value information.

Action—Compliance.

6. Claims Adjusting—It is recommended that the company comply with s. 612.13 (4), Wis. Stat., by appointing at least three directors to its loss adjustment committee.

Action—Compliance.

7. Business Continuity Plan—It is recommended that the company update its disaster recovery plan to reflect necessary changes associated with the identification of the primary coordinator replacement, control center replacement and manager responsibility changes for backup storage, in conjunction with the recent retirement of its former Secretary/Treasurer.

Action—Compliance.



8. Business Continuity Plan—It is recommended that the company's disaster recovery plan incorporate the specific data file backup measures as it relates to daily, weekly, monthly and annual file generation and rotation between the home office and its backup storage site.

Action—Compliance.

9. Investment Rule Compliance—It is recommended that the company establish a formal investment policy, which includes directions for addressing long-range objectives for meeting compliance with the Town Mutual Investment Rule, as well as reviewing other potential investment options.

Action—Noncompliance; see comments in the "Summary of Current Examination Results."

10. Investment Rule Compliance—It is also recommended that the company divest itself of any common or preferred stock that is publicly traded to address compliance with Type 2 investment rule guidelines.

Action—Noncompliance; see comments in the "Summary of Current Examination Results."

11. Cash and Invested Cash—It is recommended that procedures also be established for manager review and initialing of bank reconciliations to provide additional management oversight.

Action—Compliance.

12. Cash and Invested Assets—It is recommended that certificate of deposit records be maintained to reflect current bank issuer and issue dates in accordance with renewals and redemptions.

Action—Compliance.

13. Net Unpaid Losses—It is recommended that proof of loss form signoffs by the policyholder should be obtained based on a reasonable dollar threshold.

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.

The prior year's board of director minutes contained general statements indicating that financial statement transactions were presented and reviewed but included no supporting detail as to financial results noted. Similarly, the board of director minutes typically contain a general statement referencing a report on claims or inspections, but with limited supporting detail related to specific claim status or payment approvals. Current year 2011 board of director minutes were generally prepared in the format of an agenda outline with more comments as to issues discussed or results. It is suggested that the board of director minutes continue to concentrate on these areas to demonstrate active oversight of the company's operations through the inclusion of more specific comments or reference to attachments, as it relates to investment decisions, financial results, nominations, claim approval status, and rate adjustments. According to the company's Articles of Incorporation, the board of directors is to appoint officers immediately after the annual meeting. During the review of the board of director meeting minutes it was noted that this was not documented in the minutes for the board of directors meeting after each annual meeting. It is recommended that the board of directors appoint officers in accordance with the company's articles of incorporation during the next scheduled board of director meeting after each annual meeting and document it in their meeting minutes.

The board has established the following committees and related responsibilities:

- Executive Committee - authority to invest, redeem, or surrender bonds, stocks, mutual funds or cash and appoint new agents or terminate existing agents.
- Loss Adjustment Committee - authority to oversee claims settlement.
- Nominating Committee - authority to present to the policyholders at the annual meeting the names of the eligible policyholders selected to fill an expired term or vacated unexpired term of a director.
- Rate Committee - responsible for reviewing and recommending policy rates.

No formal committee meeting minutes were kept to document the executive, loss adjustment or nominating committee meetings during the period since the prior examination from 2006 to 2011. It was determined that these committees were present and acted on items at each board meeting but it was not noted in the meeting minutes. The Rate Committee had minutes on a few meetings held since 2007. It is recommended that the board-appointed committees meet on a regularly scheduled basis to demonstrate more active involvement of the board's committees and prepare minutes demonstrating oversight or otherwise demonstrate that similar oversight is conducted at the full-board level.

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 agencies. Some of these agreements were quite old and did not include each individual agent's signature. The agency contracts include language indicating the agent will represent the company's interests "in good faith." It is suggested that the company execute formal written agreements with each of its agents that include language indicating that the agent will represent the company's interests "in good faith" or some type of acknowledgement of the agency contract provisions.

The company has procedures in place to keep the appointment of agents with the Office of the Commissioner of Insurance (OCI) current. The company was unaware that if an agent does not pay their agent license fee on time they were automatically removed from the company's appointed agent list. The company needs to reappoint those agents as soon as the agent reinstates their license. It is suggested that the company reappoint the agents who let their licenses lapse with OCI once the agents reinstate their licenses.

### **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 the exception of the year 2009 which the company forgot to complete, with one apparent conflict being noted. The Secretary/Treasurer also works for an outside insurance agency and receives a minimal commission. It is suggested that the company make sure that the conflict of interest questionnaires be completed and retained for each and every year.

### **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:

<b>Type of Coverage</b>	<b>Coverage Limits</b>
Fidelity bond	\$ 500,000
Worker's compensation:	
Employee injury	Statutory
Employee liability:	
Each accident	1,000,000
Each employee	1,000,000
Policy limit	1,000,000
Combined professional and D&O liability:	
Company professional liability	2,000,000
Directors & officers liability	2,000,000
Deductible each claim	10,000
Employment practices liability:	
Each claim and aggregate	1,000,000
Deductible each claim	5,000
Commercial umbrella:	
Aggregate limits	3,000,000
Products/completed operations	3,000,000
Limit per occurrence	3,000,000
Retained limit	10,000
Building – home office:	
Building	249,400
Aggregate limit	2,000,000
Limit per occurrence	1,000,000
Fire legal limit	100,000
Medical limit	5,000
Deductible	250
Commercial liability – rental property	
Aggregate limit	3,000,000
Personal and advertising injury limit	1,000,000
Limit per occurrence	1,000,000
Fire damage limit	100,000
Medical expense limit	5,000

Type of Coverage	Coverage Limits
Business auto:	
Bodily injury – each person/accident	\$1,000,000
Property damage – each accident	500,000
Medical payments – each person	10,000
Uninsured motorist – each person/accident	1,000,000
Underinsured motorist – each person/accident	1,000,000
Deductible	1,000

### **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 a formal inspection procedure for both new and renewal business. A sampling of new applications and renewal business is inspected by committee members who are independent of the risk under consideration and review.

### **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. The verification of assets and determination of liabilities were made as of December 31, 2010. Negotiated checks issued during the period under examination were reviewed, test checked for proper endorsement, and traced to cash records. The company

requires two manual signatures on disbursement checks over \$3,000. During the examination it was noted that several checks over this amount were prepared and issued without the second signature. It is recommended that the company adhere to its policy regarding check signatures in compliance with s. 13.05 (4) (b), Wis. Adm. Code. Outstanding uncashed checks over five years are to be filed under an Unclaimed Property Report and be turned over to the State of Wisconsin as required by ch. 177, Wis. Stat., and the company is to maintain copies of these filings. The company has not made these filings in a few years as there are outstanding checks dating back to 2004. It is recommended that the company file Unclaimed Property Reports as required by ch. 177, Wis. Stat., and maintain copies of these filings.

The company is audited annually by an outside public accounting firm. During the examination it was discovered that there were numerous errors and omissions in the 2010 annual statement. This was brought to the company's attention for discussion with their public accounting firm. It is recommended that the company's annual statement be completed in accordance with the town mutual annual statement instructions.

### **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. Company personnel back up the computers on a daily, weekly, monthly and annual basis. The backed-up data is kept off-site, although the backup site is located in close proximity to the company's home office location. Backup files were compared to the company's backup log for reasonable consistency with retention requirements.

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 but it has not been updated to reflect the new off-site computer backup procedures. It is suggested that the company continually update their business continuity plan as events change in their business environment.

### **Business Strategic Plan**

The company has developed a business strategic plan which outlines its company's vision and mission along with identifying its strengths, weaknesses, opportunities and threats. It addresses its competition and defines its customers and marketplace. It states its goals and plans by business segment by year. The company developed this business strategic plan and reviews and updates it annually. The company's business strategic plan appears to be adequate and the company is using it to measure its ongoing performance at its board of director meeting financial results presentations.

### **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.

The company is in compliance with these 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	\$1,298,747
2. Liabilities plus 33% of gross premiums written	1,429,891
3. Liabilities plus 50% of net premiums written	1,421,144
4. Amount required (greater of 1, 2, or 3)	1,429,891
5. Amount of Type 1 investments as of 12/31/2010	<u>573,634</u>
6. Excess or (deficiency)	<u>\$ (856,256)</u>

The company does not have sufficient Type 1 investments.

The company’s investment portfolio consists primarily of certificates of deposit and the common stock of Wisconsin Reinsurance Corporation. The company has continued to report a deficiency in Type 1 investments, in accordance with the Town Mutual Investment Rule, during the period since the prior examination with a deficiency of \$(856,256) reported as of the current examination date.

Type 2 investments were approximately 54% of admitted assets, which exceeds the 30% limit approved by this office. The investment rule prescribes that a town mutual shall divest any investment which does not comply with the rule within three years of its noncompliance, unless the Commissioner permits a longer period or requires a shorter period. The Type 2 investments consist primarily of the common stock holdings of Wisconsin Reinsurance Corporation, which approximates 87% of the investments in common stocks, preferred stocks and stock mutual funds, limiting the ability to achieve compliance by divestment in the short term. No new Type 2 investments have been made given the Type 1 deficiency. It is again recommended that the company divest itself of any common or preferred stock that is publicly traded to address compliance with Type 2 investment rule guidelines or request a waiver from this office.

Long-range compliance would appear to depend primarily on growth in the volume of quality business. It is again recommended that the company establish a formal investment policy, which includes directions for addressing long-range objectives for meeting compliance with the



Town Mutual Investment Rule, as well as reviewing other potential investment options and submit it to this office for approval.

## ASSETS

**Cash and Invested Cash** **\$553,684**

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

Cash in company's office	\$ 50
Cash deposited in banks—checking accounts	68,618
Cash deposited in banks at interest	<u>485,016</u>
Total	<u>\$553,684</u>

Cash in the company's office at year-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-end.

Cash deposited in banks subject to the company's check and withdrawal consists of three accounts maintained in two banks. Verification of checking account balances was made by obtaining confirmations directly from the depositories and reconciling the amounts shown thereon to company records.

Cash deposited in banks represents the aggregate of ten deposits in six depositories. Deposits were verified by direct correspondence with the respective depositories and by an actual count and inspection of certificates and/or passbooks. Interest received during the year 2010 totaled \$11,673 and was verified to company cash records. Rates of interest earned on cash deposits ranged from 0.20% to 4.45%. Accrued interest on cash deposits totaled \$1,993 at year-end.

**Book Value of Bonds** **\$20,000**

The above asset consists of the aggregate book value of bonds held by the company as of December 31, 2010. Bonds owned by the company are located in a safe deposit box in a local bank.

Bonds were physically inspected by the examiners. There were no bond purchases or sales during the period under examination. The company's investment in bonds was in conformance with Wisconsin Statutes and the rules of the Commissioner of Insurance as regards investments made by town mutual insurers.

Interest received during 2010 on bonds amounted to \$1,300 and was traced to cash receipts records. Accrued interest of \$225 at December 31, 2010, was checked and allowed as a non-ledger asset.

**Stocks and Mutual Fund Investments** **\$983,728**

The above asset consists of the aggregate market value of stocks and mutual funds held by the company as of December 31, 2010. Stocks owned by the company are located in a safe deposit box in a local bank or held under a custodial agreement.

Stock certificates were physically examined 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 individual 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. However, the aggregate investment in common stocks, preferred stocks and mutual funds exceeded the 30% of admitted asset limit approved by this office largely due to the appreciation of its stock in Wisconsin Reinsurance Corporation.

Dividends received during 2010 on stocks and mutual funds amounted to \$8,688 and were traced to cash receipts records. Accrued dividends of \$22 at December 31, 2010, were checked and allowed as a non-ledger asset.

**Book Value of Real Estate** **\$49,593**

The above amount represents the company's investment in real estate, net of depreciation, as of December 31, 2010. The company's real estate holdings consisted of the company's home office building valued at \$9,408 and an adjacent rental property valued at \$40,185.

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** **\$6,352**

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 policy balance due premium records verified the accuracy of this asset.

**Premiums Deferred and Not Yet Due** **\$193,434**

This asset represents modal premium installments (such as monthly, quarterly, etc.) that are not yet due. This balance was reconciled to the company's Unearned Premium Report based on the "Billing Basis," which includes future unbilled installments. Verification of this asset relied on the recalculation of a sample of unearned premiums reported on the "Annual Basis," as discussed further under the section captioned "Unearned Premium."

**Investment Income Accrued** **\$2,240**

Interest due and accrued on the various assets of the company at December 31, 2010, consists of the following:

Cash deposited as interest	\$1,993
Bond	225
Stocks and mutual funds	<u>22</u>
Total	<u>\$2,240</u>

**Reinsurance Recoverable on Paid Losses and LAE** **\$5,128**

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, 2010. A review of year-end accountings with the reinsurer verified the above asset.

**Electronic Data Processing Equipment** **\$848**

The above balance consists of computer hardware and operating system software, net of depreciation as of December 31, 2010. A review of receipts and other documentation verified the balance. Non-operating system software was properly nonadmitted. Depreciation is calculated on the straight-line method. Current depreciation expense and accumulated depreciation were verified on a sample basis. Given the immaterial balance, the examination primarily relied on fixed asset records maintained by the company's public accounting firm.

**Automobile****\$0**

This asset consists of \$5,536 for an automobile owned by the company at December 31, 2010. In accordance with annual statement requirements, this amount has been reported as a nonadmitted asset, thus the balance shown above is \$0.

## LIABILITIES AND SURPLUS

### Net Unpaid Losses

**\$128,409**

This liability represents losses incurred on or prior to December 31, 2010, 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, 2010, with incurred dates in 2010 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	\$1,181,658	\$1,160,158	\$21,500
Less: Reinsurance recoverable on unpaid losses	<u>(955,349)</u>	<u>(946,749)</u>	<u>(8,600)</u>
Net Unpaid Losses	<u>\$ 226,309</u>	<u>\$ 213,409</u>	<u>\$12,900</u>

The net difference is reflected in Section III of this report under the heading "Reconciliation of Policyholders' Surplus."

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.

The examination also noted that the company routinely allows claims to remain open for a number of years without settlement while the company waits for information from the claimant or for the insured to repair covered damages. This practice may be interpreted to be an unfair settlement policy by failure to initiate and conclude claim investigations in a reasonable period of time. It also increases the company's exposure to additional loss sustained on damaged and unrepaired property. It is recommended that the company adopt procedures for timely settlement of claims in compliance with s. Ins 6.11 (3) (a) 2, Wis. Adm. Code.

**Unpaid Loss Adjustment Expenses** **\$24,000**

This liability represents the company's estimate of amounts necessary to settle losses which were incurred prior to December 31, 2010, but which remained unpaid as of year-end. The methodology used by the company in establishing this liability is based on the number of open claims at year-end and an average adjusting expense amount per claim.

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** **\$41,533**

This liability represents the commissions payable to agents as of December 31, 2010. The examiners reviewed the company's subsequent commission payments and found the liability to be reasonably stated.

**Fire Department Dues Payable** **\$318**

This liability represents the fire department dues payable to the State of Wisconsin as of December 31, 2010.

The examiners reviewed the company's fire department dues calculation and found this liability to be correctly calculated. The actual amount paid was verified to the cash disbursement records.

**Unearned Premiums** **\$605,326**

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, which was previously approved by this office. This liability was verified by tracing the premium cash receipts sample selected under the cash transaction cycle to inclusion on the company's Unearned Report.

**Reinsurance Payable** **\$61,358**

This liability consists of amounts due to the company's reinsurer at December 31, 2010, relating to transactions which occurred on or prior to that date. A review of year-end accountings with the reinsurer and subsequent payment verified the above amount.

**Accounts Payable****\$10,388**

This account represents various expenses the company incurred prior to December 31, 2010, which had not yet been paid. The balance primarily includes accrued miscellaneous office billings. Review of supporting records and the search for unrecorded liabilities verified the reasonableness of this balance.

**Premiums Received in Advance****\$28,785**

This liability represents the total premiums received prior to year-end for policies with effective dates after December 31, 2010. The examiners reviewed 2010 premium and cash receipt records to verify the accuracy of this liability and found that it included payments received for multiple payment policies. The company's computer system classifies the multiple payment policies which were paid before their due date as advance premium. The examiners reviewed the detail listing of advance premiums and noted many early multiple payments included in advance premium which should have been included in earned premium but since the amount was immaterial it was decided to pass on any adjustments. It is recommended that the company report only premiums received before year-end in advance of the policies' effective dates as advance premium on their annual statement.

**Rent Security Deposits****\$730**

This liability represents security deposits received for the company's rental property. Review of tenant deposits verified the accuracy of this liability.



## V. CONCLUSION

This examination found Calumet Equity Mutual Insurance Company to have admitted assets of \$1,815,007, liabilities of \$900,847 and surplus of \$914,960 as of December 31, 2010. The company has provided property and liability insurance for over 137 years and currently has an authorized territory consisting of 16 counties.

The company experienced underwriting losses in each year under examination except 2008. The above financial loss results are primarily attributed to the company's hailstorm- and fire-related claims experience.

Gross and net premiums written, as well as policies in force, have steadily increased during the period since the prior examination, associated primarily with increased number of policies and higher premium rates. The company continues to emphasize marketing efforts going forward through agency visitations to renew interest in Calumet Equity Mutual with the objective of generating new business to improve overall profitability. At the same time the company has increased its underwriting inspection on all new policies and continues to re-inspect its upcoming renewals depending on the size of the risk involved.

Admitted assets and surplus steadily declined since the prior examination associated with the above sustained losses. Unrealized capital gains on Wisconsin Reinsurance Corporation common stock partially offset the company's underwriting losses during the period under examination.

The current examination has 12 recommendations, 2 of which are repeat recommendations and 1 partial compliance of a prior examination recommendation, along with 5 suggestions. Of the 12 recommendations, 3 were for violations of the company's articles of incorporation and bylaws, 3 were for violations of the Wisconsin Administrative Codes or Statutes. The remaining recommendations were to complete the annual statement correctly, adhere to its check signing policy, establish a formal investment policy, address compliance with the Town Mutual Investment Rule, and adopt procedures for the timely settlement of older claims. The 5 suggestions included strengthening the board of directors meeting minutes, updating its formal written agreements with its individual agents and agencies, reappointing agents who fail to timely

pay their license fees, completing conflict of interest statements annually, and updating its business continuity plan.

## VI. SUMMARY OF COMMENTS AND RECOMMENDATIONS

1. Page 2 - Articles and Bylaws—It is recommended that the company follow its articles of incorporation when making amendments to its articles of incorporation and bylaws.
2. Page 4 - Articles and Bylaws—It is recommended that the company operate according to its articles and bylaws or amend them to describe the intended number of directors.
3. Page 4 - Directors and Officers—It is recommended that the company become compliant with the number of inside and outside directors in accordance with s. 612.13 (1m), Wis. Stat.
4. Page 16 - Corporate Records—It is suggested that the board of director minutes continue to concentrate on these areas to demonstrate active oversight of the company's operations through the inclusion of more specific comments or reference to attachments, as it relates to investment decisions, financial results, nominations, claim approval status, and rate adjustments.
5. Page 16 - Corporate Records—It is recommended that the board of directors appoint officers in accordance with the company's articles of incorporation during the next scheduled board of director meeting after each annual meeting and document it in their meeting minutes.
6. Page 17 - Corporate Records—It is recommended that the board-appointed committees meet on a regularly scheduled basis to demonstrate more active involvement of the board's committees and prepare minutes demonstrating oversight or otherwise demonstrate that similar oversight is conducted at the full-board level.
7. Page 17 - Corporate Records—It is suggested that the company execute formal written agreements with each of its agents that include language indicating that the agent will represent the company's interests "in good faith" or some type of acknowledgement of the agency contract provisions.
8. Page 17 - Corporate Records—It is suggested that the company reappoint the agents who let their licenses lapse with OCI once the agents reinstate their licenses.
9. Page 18 - Conflict of Interest—It is suggested that the company make sure that the conflict of interest questionnaires be completed and retained for each and every year.
10. Page 20 - Accounts and Records—It is recommended that the company adhere to its policy regarding check signatures in compliance with s. 13.05 (4) (b), Wis. Adm. Code.
11. Page 20 - Accounts and Records—It is recommended that the company file Unclaimed Property Reports as required by ch. 177, Wis. Stat., and maintain copies of these filings.
12. Page 20 - Accounts and Records—It is recommended that the company's annual statement be completed in accordance with the town mutual annual statement instructions.

13. Page 21 - Business Continuity Plan—It is suggested that the company continually update their business continuity plan as events change in their business environment.
14. Page 22 - Investment Rule Compliance—It is again recommended that the company divest itself of any common or preferred stock that is publicly traded to address compliance with Type 2 investment rule guidelines or request a waiver from this office.
15. Page 22 - Investment Rule Compliance—It is again recommended that the company establish a formal investment policy, which includes directions for addressing long-range objectives for meeting compliance with the Town Mutual Investment Rule, as well as reviewing other potential investment options and submit it to this office for approval.
16. Page 28 - Net Unpaid Losses—It is recommended that the company adopt procedures for timely settlement of claims in compliance with s. Ins 6.11 (3) (a) 2, Wis. Adm. Code.
17. Page 30 - Premiums Received in Advance—It is recommended that the company report only premiums received before year-end in advance of the policies' effective dates as advance premium on their annual statement.

## **VII. ACKNOWLEDGMENT**

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

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

Respectfully submitted,

Russell Lamb  
Examiner-in-Charge