

Report
of the
Examination of
Equitable Reserve Association
Neenah, Wisconsin
As of December 31, 2010

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State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

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August 22, 2011

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Commissioners:

In accordance with the instructions of the Wisconsin Commissioner of Insurance, a compliance examination has been made of the affairs and financial condition of:

EQUITABLE RESERVE ASSOCIATION
Neenah, Wisconsin

and this report is respectfully submitted.

I. INTRODUCTION

The previous examination of Equitable Reserve Association (the society, ERA, or the association) was conducted in 2006 as of December 31, 2005. The current examination covered the intervening period ending December 31, 2010, and included a review of such 2011 transactions as deemed necessary to complete the examination.

The examination was conducted using a risk-focused approach in accordance with the NAIC Financial Condition Examiners Handbook, which sets forth guidance for planning and performing an examination to evaluate the financial condition and identify prospective risks of an insurer. This approach includes the obtaining of information about the insurer including corporate governance, the identification and assessment of inherent risks within the insurer, and the evaluation of system controls and procedures used by the insurer to mitigate those risks. The examination also included an assessment of the principles used and significant estimates made by management, as well as an evaluation of the overall financial statement presentation and management's compliance with statutory accounting principles, annual statement instructions, and Wisconsin laws and regulations.

The examination consisted of a review of all major phases of the society's operations and included the following areas:

- History
- Management and Control
- Corporate Records
- Conflict of Interest
- Fidelity Bonds and Other Insurance
- Employees' Welfare and Pension Plans
- Territory and Plan of Operations
- Affiliated Companies
- Growth of Society
- Reinsurance
- Financial Statements
- Accounts and Records
- Data Processing

Emphasis was placed on the audit of those areas of the society's operations accorded a high priority by the examiner-in-charge when planning the examination. Special

attention was given to the action taken by the society to satisfy the recommendations and comments made in the previous examination report.

The society 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.

Independent Actuary's Review

An independent actuarial firm was engaged under a contract with the Office of the Commissioner of Insurance. The actuary reviewed the adequacy of aggregate life and annuity reserves, aggregate accident and health reserves, refunds to members, asset adequacy analysis, and deferred life insurance premiums. The actuary's results were reported to the examiner-in-charge. As deemed appropriate, reference is made in this report to the actuary's conclusion.

II. HISTORY AND PLAN OF OPERATION

The society was organized in 1897 as the Supreme Assembly of the Equitable Fraternal Union under the Wisconsin laws applicable to fraternal benefit societies. The present name was adopted on April 15, 1930, following a merger with the Fraternal Reserve Association in 1929. On December 19, 1949, Germania Mutual Life Insurance of Wisconsin merged into the society. On August 1, 1970, the society acquired The Royal League, a fraternal benefit society located in Berwyn, Illinois, through merger and reinsurance.

Equitable Reserve Association is licensed as a fraternal benefit society under ch. 614, Wis. Stat. As a fraternal benefit society, ERA has no capital stock and exists solely for the benefit of its members and their beneficiaries.

According to the articles of incorporation, the purpose of the association, which exists solely for the benefit of its members and their beneficiaries, is to unite fraternally persons who have an interest consistent with the following:

- Improving the financial well being of all its members through insurance products and fraternal benefits;
- Strengthening the family through the promotion of educational opportunities and interaction with other families through fraternal events and chapter meetings;
- Encouraging altruistic behavior through the raising of funds and volunteer activities which may include working with any not-for-profit and other fraternal benefit societies on volunteer activities;
- Improving the communities in which we live through these volunteer activities and by sponsoring programs that benefit these communities; and
- Upholding democratic ideals that promote patriotism, good citizenship and good governance as exemplified by the democratic process for governing the association in which all members can take part.

In 2010, the society collected direct premium in the following states:

Wisconsin	\$6,392,868	84.6%
Illinois	233,202	3.0
Minnesota	171,042	2.3
All others	<u>763,655</u>	<u>10.1</u>
Total	<u>\$7,560,767</u>	<u>100.0%</u>

The society is licensed in the above states as well as Colorado, District of Columbia, Indiana, Iowa, Kentucky, Michigan, Missouri, Nebraska, Ohio, and North Dakota.

The major products marketed by the society include interest-sensitive whole life and term products, adjustable whole life, flexible premium deferred annuities, immediate annuities, traditional life, and disability income. The major products are marketed through 51 fieldworkers. Business is written primarily through a captive agency force, which currently consists of 6 agency managers and 18 full-time and part-time agents. ERA has also been using the independent agency system in markets not currently served by its captive sales force. Currently, ERA has contracts with 7 personal producing general agents and 20 brokers.

The following chart is a summary of the premium income reported by the society in 2010. The growth of the society is discussed in the "Financial Data" section of this report.

Premium Income

Line of Business	Direct Premium	Reinsurance Assumed	Reinsurance Ceded	Net Premium
Interest sensitive life	\$2,878,652	\$ 0	\$170,105	\$2,708,547
Other life	538,338	0	87,630	450,708
Annuities	4,176,324	0		4,176,324
Disability	<u>112,529</u>	<u>0</u>	<u>41,865</u>	<u>70,664</u>
Total All Lines	<u>\$7,705,843</u>	<u>\$ 0</u>	<u>\$299,600</u>	<u>\$7,406,243</u>

III. MANAGEMENT AND CONTROL

Governance

Effective November 2009, significant changes to the association's bylaws were made to strengthen the association and to allow the association to adapt more rapidly to corporate governance and other regulatory changes. Sections that were no longer required were removed and many were reworded. One significant change was to give the board of directors authority to acquire any other fraternal benefit society or authorize the association to merge with any other fraternal benefit society.

Effective July 1, 2010, the association's articles of incorporation and bylaws were amended by a majority vote at the quadrennial meeting of the association's general assembly.

Amendments to the articles of incorporation included:

- Changing the supreme governing body to be the board of directors, to be made up of benefit members of the society and providing that directors are to be elected by the membership in a manner prescribed in the bylaws. Previously, the supreme governing body was the general assembly, which met every four years and elected the members of the board of directors.
- Granting the board of directors powers that were previously given to the general assembly. These powers include: the right to charter chapters and grant chapters such powers as the board may determine; the power to enact bylaws and to repeal or amend them; and the power to amend or repeal the articles of incorporation in whole or in part by a two-thirds vote of the full board.

Other changes to the bylaws that were amended at that time included:

- Providing for the election of the board directors by a direct vote of the membership. Each member is granted one vote and no proxies are acceptable. Director nominations can be made by any ten or more members or be made by the governance committee of the board of directors.
- Providing for the terms of the directors to be staggered with no less than two and no more than six being elected in any given year. Previously, all directors were elected at the same time by the general assembly.
- Providing that the board of directors will appoint the president and that the president will appoint all other executive officers, subject to ratification by the board. Previously, the president was elected by the general assembly and served a four-year term. The bylaw changes also provided that the board of directors could remove any director or executive officer for cause.
- Providing that the board of directors will appoint a governance committee and an audit committee.

Membership

The society has three classes of membership: benefit membership, junior membership, and social membership. A benefit member is a person age 16 or older who is granted a certificate of membership and insurance benefits or who receives a settlement agreement benefit by virtue of such insurance. Benefit members are the only membership class that has the right to vote in the affairs of the society. A junior member is a person under age 16 eligible in all respects but age for benefit membership. A social member is a person age 16 or more who is granted a certificate of membership without insurance benefits. All three classes of membership may participate in the affairs and activities of the chapter in which they are members, and may hold office in the chapter.

Growth of Life Certificates

Year	Number
2010	19,114
2009	19,696
2008	20,460
2007	21,176
2006	21,869
2005	22,611

Board of Directors

The board of directors consists of nine members. The board consists of employee directors who are the executive officers of the society and non-employee directors who are elected by the society's members. The elected directors must always be a majority of the total number of directors and may not be less than the number of directors required to amend the articles of incorporation or the bylaws (currently a two-thirds majority). The president is appointed by the board of directors and the president appoints the other executive officers, subject to ratification by the board. The non-employee board members currently receive a monthly fee of \$1,485 for their service on the board. There is no additional compensation for their duties as board members. Executive officers do not receive additional compensation for their duties as board members.

Currently the board of directors consists of the following persons:

Name and Residence	Principal Occupation	Term Expires
Ernie G. Bellin Oshkosh, WI	Retired, formerly Fraternal Director ERA	2012
Steven N. Hooyman Appleton, WI	Principal Baker Tilly Investment Advisors	2012
Daniel C. Huber Combined Locks, WI	Attorney	2014
Peter C. Kelly Neenah, WI	CEO—United Way of the Fox Cities	2014
Mary Beth Leib Oshkosh, WI	Sr. Vice President and Chief Strategy Officer Red Magasin	2012
Steven A. White Sherwood, WI	Controller Valley Insurance Associates	2014
Melvin L. Rambo Appleton, WI	President, ERA	2012
George E. Reckin Neenah, WI	Sr. Vice President, Treasurer, and Actuary—ERA	2012
Jane E. Tennant Neenah, WI	Vice President and Corporate Secretary—ERA	2012

Officers of the Society

The officers serving at the time of this examination are as follows:

Name	Office	2010 Compensation
Melvin L. Rambo	President and CEO	\$170,261
George E. Reckin	Sr. Vice President, Treasurer, and Chief Actuary	134,147
Jane R. Tennant	Vice President & Corporate Secretary	94,123

Committees of the Board

The society'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:

Governance Committee

Daniel C. Huber, Chair
Jane E. Tennant, Secretary
Peter C. Kelly
Mary Beth Leib
George E. Reckin

Audit Committee

Steven A. White, Chair
George E. Reckin, Secretary (non-voting)
Steven N. Hooyman
Daniel C. Huber

Investment Committee

Steven N. Hooyman, Chair
Melvin L. Rambo, Secretary
George E. Reckin
Jane E. Tennant
Steven A. White

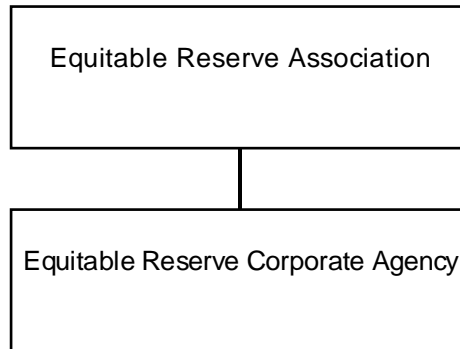
Fraternal Committee

Mary Beth Leib, Chair
Ernie G. Bellin
Peter C. Kelly
Jane E. Tennant
Mary Wolf, Secretary (non-voting employee)

IV. AFFILIATED COMPANIES

Equitable Reserve Association is a member of a holding company system. The organizational chart below depicts the relationships among the affiliates in the group. A brief description of the significant affiliates of Equitable Reserve Association follows the organizational chart.

Organizational Chart As of December 31, 2010



Equitable Reserve Corporate Agency, Inc.

The society owns 100% of the common stock of Equitable Reserve Corporate Agency, Inc. The corporate agency operates similarly to a managing general agent and is used to offer products to ERA's members, which the society currently does not offer. These products include long-term care, Medicare supplement, major medical, and mutual funds. As of December 31, 2010, the agency's unaudited financial statement reported assets of \$19,659, liabilities of \$7,964, and unassigned funds of \$11,695. Operations for 2010 produced a net loss of \$9,244.

V. REINSURANCE

The society's reinsurance portfolio and strategy are described below. The society cedes excess life coverage to a small number of reinsurance companies on either a yearly renewable term (YRT) or coinsurance (CO) basis. The society retains \$100,000 of YRT and \$50,000 of coinsurance for individual lives in a standard classification, with less retained for substandard risks. Retentions for substandard classifications vary by risk levels based on age. Beginning September 1, 2010, the society's retention limit on new business was lowered to \$50,000 per life. Each case is coinsured on a 50/50% quota share basis.

The society's net retention for accidental death on any one risk is \$50,000. The largest of these policies placed with reinsurance has total reinsurance policy coverage of \$150,000, for a total largest accidental death benefit of \$200,000.

The society's net retention for waiver of premium is the same as the underlying life certificate (therefore, up to \$100,000 for YRT and \$50,000 for CO).

For disability income certificates underwritten June 1, 1988, to June 30, 2003, the society retained 50% of the risk, not to exceed a maximum retention per occupational class. For certificates underwritten during that time, the highest retained disability coverage is \$1,250 of monthly income. Disability reinsurance coverage is placed with Generali USA Life Reassurance Company. There is currently no reinsurance placement for disability certificates underwritten.

For other than disability, the society's current reinsurance company is Optimum Re Insurance Company. A facultative contract with Swiss Re Life Company, effective August 1, 1989, is in run-off status with only a few remaining policies. All contracts reviewed contained the required insolvency provision.

VI. FINANCIAL DATA

The following financial statements reflect the financial condition of the society as reported to the Commissioner of Insurance in the December 31, 2010, annual statement. Also included in this section are schedules which reflect the growth of the society, NAIC Insurance Regulatory Information System (IRIS) ratio results during the period under examination, and the compulsory and security surplus calculation. Adjustments made as a result of the examination are noted at the end of this section in the area captioned "Reconciliation of Members' Surplus per Examination."

Equitable Reserve Association
Assets
As of December 31, 2010

	Assets	Nonadmitted Assets	Net Admitted Assets
Bonds	\$111,911,152		\$111,911,152
Stocks:			
Common stocks	3,247,673	\$ 1,000	3,246,673
Real estate:			
Occupied by the society	97,233		97,233
Cash, cash equivalents, and short-term investments	5,549,941		5,549,941
Contract loans	5,857,902		5,857,902
Investment income due and accrued	1,279,537		1,279,537
Premiums and considerations:			
Uncollected premiums and agents' balances in course of collection	5,123		5,123
Reinsurance:			
Amounts recoverable from reinsurers	19,177		19,177
Electronic data processing equipment and software	27,287	3,666	23,621
Furniture and equipment, including health care delivery assets	20,525	20,525	
Receivable from parent, subsidiaries and affiliates	7,904	7,904	
Health care and other amounts receivable	134,742	134,742	
Write-ins for other than invested assets:			
Prepaid expenses	141,250	141,250	
Company owned automobiles	16,695	16,695	
Inventory	19,559	19,559	
Miscellaneous	6,249	6,249	
	<u> </u>	<u> </u>	<u> </u>
Total Assets	<u>\$128,341,949</u>	<u>\$351,590</u>	<u>\$127,990,359</u>

Equitable Reserve Association
Liabilities, Surplus, and Other Funds
As of December 31, 2010

Aggregate reserve for life contracts		\$116,564,068
Aggregate reserve for accident and health contracts		303,432
Liability for deposit-type contracts		2,505,735
Contract claims:		
Life		418,330
Accident and health		2,475
Provision for refunds payable in following calendar year:		
Apportioned for payment		50,000
Premiums and annuity considerations received in advance		2,165
Contract liabilities not included elsewhere:		
Interest maintenance reserve		1,319,292
Commissions to fieldworkers due or accrued		35,611
General expenses due or accrued		346,819
Taxes, licenses, and fees due or accrued		10,889
Amounts withheld or retained by society as agent or trustee		67,472
Amounts held for fieldworkers' account, including fieldworkers' credit balances		6,806
Remittances and items not allocated		8,561
Miscellaneous liabilities:		
Asset valuation reserve		525,371
Write-ins for liabilities:		
Postretirement benefit liability		<u>1,363,266</u>
Total liabilities		123,530,292
Unassigned funds (surplus)	<u>\$4,460,067</u>	
Total surplus and other funds		<u>4,460,067</u>
Total Liabilities, Surplus, and Other Funds		<u>\$127,990,359</u>

**Equitable Reserve Association
Summary of Operations
For the Year 2010**

Premiums and annuity considerations for life and accident and health contracts	\$ 7,406,243
Considerations for supplementary contracts with life contingencies	214,426
Net investment income	5,622,472
Amortization of interest maintenance reserve	316,439
Commissions and expense allowances on reinsurance ceded	12,936
Reserve adjustments on reinsurance ceded	
Miscellaneous income	<u>22,458</u>
Total income items	13,594,974
Death benefits	\$ 2,002,987
Matured endowments	73,166
Annuity and old age benefits	3,525,023
Disability, accident and health benefits including premiums waived	59,138
Surrender benefits and withdrawals for life contracts	1,446,954
Interest and adjustments on contract or deposit-type contract funds	149,104
Payments on supplementary contracts with life contingencies	282,918
Increase in aggregate reserve for life and accident and health contracts	<u>3,323,018</u>
Subtotal	10,862,308
Commissions on premiums, annuity considerations, and deposit-type contract funds	349,896
General insurance expenses and fraternal expenses	3,356,296
Insurance taxes, licenses, and fees	173,339
Increase in loading on deferred and uncollected premiums	<u>1,612</u>
Total deductions	<u>14,743,451</u>
Net gain from operations before refunds to members	(1,148,477)
Refunds to members	<u>20,111</u>
Net gain from operations after refunds to members and before realized capital gains or losses	(1,168,589)
Net realized capital gains or (losses)	<u>227,559</u>
Net Loss	<u>\$ (941,030)</u>

**Equitable Reserve Association
Cash Flow
For the Year 2010**

Premiums collected net of reinsurance		\$ 7,386,238
Net investment income		5,887,517
Miscellaneous income		<u>249,820</u>
Total		13,523,575
Benefit and loss payments	\$ 7,177,702	
Commissions, expenses paid, and aggregate write-ins for deductions	3,874,759	
Refunds paid to members	<u>90,111</u>	
Total deductions		<u>11,142,572</u>
Net cash from operations		2,381,003
Proceeds from investments sold, matured, or repaid:		
Bonds	\$25,915,314	
Stocks	<u>3,712,403</u>	
Total investment proceeds		29,627,717
Cost of investments acquired (long-term only):		
Bonds	26,106,579	
Stocks	<u>3,348,819</u>	
Total investments acquired		29,455,398
Net increase (decrease) in contract loans and premium notes	<u>426,689</u>	
Net cash from investments		(254,370)
Cash provided from (applied for) financing and miscellaneous sources:		
Net deposits on deposit-type contract funds and other insurance liabilities	(194,457)	
Other cash provided (applied)	<u>(23,272)</u>	
Net cash from financing and miscellaneous sources		<u>(217,729)</u>
Reconciliation:		
Net change in cash, cash equivalents, and short- term investments		1,908,904
Cash, cash equivalents, and short-term investments:		
Beginning of year		<u>3,641,037</u>
End of Year		<u>\$ 5,549,941</u>

**Equitable Reserve Association
Compulsory and Security Surplus Calculation
December 31, 2010**

Assets		\$127,990,359
Less liabilities		<u>123,530,292</u>
Adjusted surplus		4,460,067
Annual premium:		
Individual life and health	\$3,138,361	
Factor	<u>15%</u>	
Total	470,754	
Greater of 7.5% of considerations or 2% of reserves for annuities and deposit administration funds	<u>911,590</u>	
Compulsory surplus		<u>1,382,344</u>
Compulsory Surplus Excess or (Deficit)		<u>\$ 3,077,723</u>
Adjusted surplus (from above)		\$ 4,460,067
Security surplus: (140% of compulsory surplus, factor reduced 1% for each \$33 million in premium written in excess of \$10 million with a minimum of 110%)		<u>1,935,281</u>
Security Surplus Excess or (Deficit)		<u>\$ 2,524,786</u>

**Equitable Reserve Association
Reconciliation and Analysis of Surplus
For the Five-Year Period Ending December 31, 2010**

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

	2010	2009	2008	2007	2006
Surplus, beginning of year	\$5,142,917	\$ 6,666,754	\$ 8,596,361	\$9,238,931	\$10,486,880
Net income	(941,030)	(1,721,239)	(2,315,916)	(788,080)	(748,854)
Change in net unrealized capital gains/losses	206,067	762,617	(1,071,662)	81,026	78,648
Change in nonadmitted assets and related items	(10,457)	6,419	893,766	38,101	(28,403)
Change in reserve on account of change in valuation basis					(300,000)
Change in asset valuation reserve	62,570	(221,782)	564,204	(15,970)	(249,340)
Postretirement benefit prior period adjustment	_____	(349,853)	_____	42,354	_____
Surplus, End of Year	<u>\$4,460,067</u>	<u>\$ 5,142,917</u>	<u>\$ 6,666,754</u>	<u>\$8,596,361</u>	<u>\$ 9,238,931</u>

**Equitable Reserve Association
Insurance Regulatory Information System
For the Five-Year Period Ending December 31, 2010**

The society's NAIC Insurance Regulatory Information System (IRIS) results for the period under examination are summarized below. Unusual IRIS results are denoted with asterisks and discussed below the table.

Ratio	2010	2009	2008	2007	2006
#1 Change in surplus	-13% *	-23% *	-22% *	-7%	12% *
#2 Net income to total income	-7 *	-11 *	-18 *	-6 *	-6 *
#3 Adequacy of investment income	118 *	120 *	125 *	130	132
#4 Nonadmitted to admitted assets	0	0	0	1	1
#5 Total real estate and mortgage loans to cash and invested assets	0	0	0	0	0
#6 Total affil. investments to surplus	0	0	0	0	0
#7 Surplus relief	0	0	0	0	0
#8 Change in premium	-25 *	56 *	-7	7	-29 *
#9 Change in product mix	5.0 *	15.7 *	1.6	1.9	9.7 *
#10 Change in asset mix	0.2	0.4	0.1	0.1	0.1
#11 Change in reserving	9	-8	-9	9	-1

The exceptional results for Ratios No. 1 and No. 2 are primarily due to the society's net losses for each of the years under examination. The society's net income has been negatively affected by its expense levels compared to the size of the society, a decreasing amount of insurance in force, and decreasing investment income.

The unusual result for Ratio No. 3 for 2008, 2009, and 2010 is primarily due to the decreasing spread between the interest rate that the society is earning on its investments and the interest credited to policyholders.

The unusual results for Ratios No. 8 and No. 9 for 2006, 2009, and 2010 are primarily due to the changes in the society's annuity premium volume in those years. Annuity premiums decreased in 2006, increased significantly in 2009, and decreased again for 2010. When general interest rates declined, additions to ERA's annuities, such as ERA's Fixed Payment Deferred Annuity (FPDA), became more attractive than other "new money" interest rate alternatives. Note that the society placed a limit on the amount of annuity premium that it would accept for 2010 and continued the limit for 2011.

Growth of Equitable Reserve Association

Year	Admitted Assets	Liabilities	Members' Surplus
2010	\$127,990,359	\$123,530,292	\$ 4,460,067
2009	124,622,344	119,479,427	5,142,917
2008	120,017,439	113,350,685	6,666,754
2007	120,854,494	112,258,133	8,596,361
2006	119,277,466	110,038,535	9,238,931
2005	117,385,510	106,898,630	10,486,880

Net Life Premiums, Annuity Considerations, and Deposits

Year	Life Insurance Premiums	Annuity Considerations	Deposit-type Contract Funds
2010	\$3,140,710	\$4,176,325	\$104,761
2009	3,440,890	6,203,517	263,868
2008	3,564,901	2,503,561	165,128
2007	3,760,371	2,344,677	697,233
2006	4,015,564	2,213,965	117,452
2005	4,384,614	4,438,811	195,869

Life Insurance In Force (in thousands)

Year	Gross Risk In Force	Ceded	Net
2010	\$513,969	\$89,409	\$424,560
2009	516,646	84,910	431,736
2008	531,288	79,936	451,352
2007	543,369	79,747	463,622
2006	547,366	81,063	466,303
2005	559,121	76,784	482,337

Accident and Health

Year	Net Premiums Earned	Incurred Claims and Cost Containment Expenses*	Commissions Incurred	Other Expenses Incurred**	Combined Loss and Expense Ratio
2010	\$73,011	\$(90,458)	\$ (939)	\$45,067	(63.5)%
2009	72,557	20,850	(321)	41,027	84.8
2008	74,867	(6,833)	3,956	51,582	65.1
2007	83,160	185,963	6,241	37,271	275.9
2006	72,579	114,363	1,078	41,464	216.2
2005	80,624	(43,647)	(263)	47,271	4.2

* Includes increase in contract reserves

** Includes taxes, licenses, and fees

Surplus has decreased \$6.0 million or 57.5% from the prior examination. This decrease continues a steady decline that has occurred over the last ten years. The prior examination report noted a surplus decrease of \$8.0 million between 2000 and 2005. The society has taken steps to reduce expenses; redesign agent recruitment, distribution, and financing; and focus its marketing efforts. However, the society continues to experience decreasing membership and insurance in force.

The negative incurred health claims and cost containment expenses in 2005 was due to a number of individuals going off disability status.

Reconciliation of Members' Surplus per Examination

The following schedule is a reconciliation of members' surplus between that reported by the society and as determined by this examination:

Members' surplus December 31, 2010, per annual statement			\$4,460,067
	Increase	Decrease	
Aggregate reserve for life contracts	\$	\$89,523	
Aggregate reserve for accident and health contracts		60,000	
Postretirement benefit liability	_____	<u>65,000</u>	
Net increase or (decrease)			<u>(214,523)</u>
Members' Surplus December 31, 2010, per Examination			<u>\$4,245,544</u>

VII. SUMMARY OF EXAMINATION RESULTS

Compliance with Prior Examination Report Recommendations

There were 11 specific comments and recommendations in the previous examination report. Comments and recommendations contained in the last examination report and actions taken by the society are as follows:

1. Custodial Agreement—It is recommended that the society's custodial agreements be updated to include language consistent with the NAIC Financial Condition Examiners Handbook.
Action—Compliance
2. Schedule D—It is recommended the society complete its Schedule D correctly in future annual statements in accordance with the NAIC Annual Statement Instructions-Fraternal and the Purposes and Procedures Manual of the NAIC Securities Valuation Office.
Action—Compliance
3. Premium Loans—It is recommended that the society exclude premium loans from the parenthetical inset under the Contract Loans line on future statements.
Action—Compliance
4. Premium Loans—It is recommended that the society make corrections to its administrative system to properly record the policy loan interest rate change after the loan's initial five years.
Action—Compliance
5. Asset Valuation Reserve—It is recommended the society complete its Asset Valuation Reserve Schedule correctly in future annual statements in accordance with the NAIC Annual Statement Instructions-Fraternal and the Purposes and Procedures Manual of the NAIC Securities Valuation Office.
Action—Compliance
6. Loss Reserves—It is again recommended that the society continue to review its valuation procedures to ensure correct factors are being used and properly applied for the various life plans.
Action—Noncompliance; see comments in the "Summary of Current Examination Results."
7. Information Technology—It is recommended that the society conduct an annual testing of the business continuity plan, and the test results should be reviewed and approved by the senior management.
Action—Compliance

8. Information Technology—It is recommended that the society have an alternate site ready for back-up tapes, computer operations, and critical business functions when the current office location is inaccessible to employees.

Action—Compliance

9. Information Technology—It is recommended that the society create separate User IDs for each programmer analyst to perform security-related functions.

Action—Compliance

10. Information Technology—It is recommend that controls over user-developed applications and spreadsheets used in preparation of the financial statements should be implemented to ensure data integrity and data security.

Action—Compliance

11. Management Discussion and Analysis—It is recommended that the society include a discussion of all material changes from year to year for significant financial statement items and a discussion of material events in future Management Discussion and Analysis filings.

Action—Compliance

Summary of Current Examination Results

This section contains comments and elaboration on those areas where adverse findings were noted or where unusual situations existed. Comment on the remaining areas of the society's operations is contained in the examination work papers.

Loss Reserves

Based on the independent actuary's analysis, there were many errors noted in the reserve calculations resulting in adjustments to reserves. A similar recommendation regarding reserve calculations was contained in the prior examination report. The following recommendations were noted by the actuary:

- It is recommended that the society's valuation system be updated to add IPC reserves on plans where currate factors are employed and remove the additional IPC reserve on plans where continuous factors are already used.
- It is again recommended that the society audit the in-force data, at least annually, to ensure that deceased joint annuitants are removed when appropriate. It is also recommended that the society establish procedures to ensure that the coding for single or joint and last survivor mortality is correct.
- It is again recommended that at least annually the society perform a comparison between the life valuation data files and waiver of premium reserves to ensure the accuracy and completeness of both.
- It is recommended that the society either update their valuation system to compute disability income claim reserves in accordance with their stated methodology or update the methodology document so that the reported reserves can be reproduced.
- It is again recommended that the society replace the reserve factors for the 2001 CSO term plans with factors that correspond to the reserve demonstration shown in the actuarial memorandum.

Due to the items noted, the aggregate reserve for life contracts was increased by the examination by \$89,523 and the aggregate reserve for accident and health contracts was increased by \$60,000.

Actuarial Opinion Memorandum

Based on the independent actuary's review of the actuarial opinion memorandum, the memorandum was lacking the following information that is specified in s. Ins 50.79 (2) (a), Wis.

Adm. Code:

- Source of liability in-force data
- Pertinent risks associated with each major line of business and how they were analyzed
- Source of asset data
- Quality distribution for existing assets
- Description of any bond call function modeled
- Sources for asset spreads and defaults assumptions

It is recommended that the society comply with s. Ins 50.79 (2) (a), Wis. Adm. Code, when preparing the annual actuarial opinion memorandum.

The independent actuary's review also noted that the actuarial opinion memorandum did not include a disclosure and justification of any material changes in assumptions from prior testing in compliance with Actuarial Standard of Practice 22. It is recommended that a disclosure and justification of any material changes in assumptions from prior testing be included in future actuarial opinion memorandums in compliance with ASOP 22 Section 3.3.1.

Postretirement Benefit Liability

The examiner's review of the society's postretirement liability of \$1,363,266 noted that the only changes recorded to the liability from the prior year were actual cash activity (benefit payments and reimbursements by participants). The society did not properly record net periodic postretirement benefits cost. As a result, the postretirement benefits liability was increased by \$65,000. As the society had already corrected its postretirement benefit liability on its second quarter 2011 statutory statement, no recommendation is made.

VIII. CONCLUSION

Surplus has decreased \$6.0 million or 57.5% from the prior examination. This decrease continues a steady decline that has occurred over the last ten years. The prior examination report noted a surplus decrease of \$8.0 million between 2000 and 2005. The society has taken steps to reduce expenses; redesign agent recruitment, distribution, and financing; and focus its marketing efforts. However, the society continues to experience decreasing membership and insurance in force. As of December 31, 2010, the company reported annual premiums and annuity considerations of \$7,406,243 and net loss of \$941,030.

The examination made seven recommendations pertaining to proper loss reserves, proper completion of the actuarial opinion memorandum, and the postretirement benefits liability. The examination made three adjustments of account balances that reduced surplus reported by the society in its year-end 2010 statutory financial statement by the net amount of \$214,523. The examination determined that as of December 31, 2010, the society had total admitted assets of \$127,990,359, total liabilities of \$123,744,815, and total capital and surplus of \$4,245,544.

IX. SUMMARY OF COMMENTS AND RECOMMENDATIONS

1. Page 24 - Loss Reserves—It is recommended that the society's valuation system be updated to add IPC reserves on plans where curtate factors are employed and remove the additional IPC reserve on plans where continuous factors are already used.
2. Page 24 - Loss Reserves—It is again recommended that the society audit the in-force data, at least annually, to ensure that deceased joint annuitants are removed when appropriate. It is also recommended that the society establish procedures to ensure that the coding for single or joint and last survivor mortality is correct.
3. Page 24 - Loss Reserves—It is again recommended that at least annually the society perform a comparison between the life valuation data files and waiver of premium reserves to ensure the accuracy and completeness of both.
4. Page 24 - Loss Reserves—It is recommended that the society either update their valuation system to compute disability income claim reserves in accordance with their stated methodology or update the methodology document so that the reported reserves can be reproduced.
5. Page 24 - Loss Reserves—It is again recommended that the society replace the reserve factors for the 2001 CSO term plans with factors that correspond to the reserve demonstration shown in the actuarial memorandum.
6. Page 25 - Actuarial Opinion Memorandum—It is recommended that the society comply with s. Ins 50.79 (2) (a), Wis. Adm. Code, when preparing the annual actuarial opinion memorandum.
7. Page 25 - Actuarial Opinion Memorandum—It is recommended that a disclosure and justification of any material changes in assumptions from prior testing be included in future actuarial opinion memorandums in compliance with ASOP 22 Section 3.3.1.

X. ACKNOWLEDGMENT

The courtesy and cooperation extended during the course of the examination by the officers and employees of the society is acknowledged.

In addition to the undersigned, the following representatives of the Office of the Commissioner of Insurance, State of Wisconsin, participated in the examination:

Name	Title
Rauf A. Mirza	Insurance Financial Examiner
Eleanor Y. Oppriecht	Insurance Financial Examiner
Carmenza L. Rincon	Insurance Financial Examiner
Victoria Y. Chi	IT Specialist
Jerry C. DeArmond	Reserve Specialist

Respectfully submitted,

Thomas R. Houston
Examiner-in-Charge