

Report  
of the  
Examination of  
MIC Reinsurance Corporation  
Milwaukee, Wisconsin  
As of December 31, 2011

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# State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

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

**Wisconsin.gov**

April 19, 2013

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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, a compliance examination has been made of the affairs and financial condition of:

MIC REINSURANCE CORPORATION  
Milwaukee, Wisconsin

and this report is respectfully submitted.

## I. INTRODUCTION

This is the first examination of MIC Reinsurance Corporation (hereinafter also the company or MICRC) since it was organized on December 3, 2009. The current examination covered the intervening period ending December 31, 2011, and included a review of such 2012 and 2013 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 company including corporate governance, the identification and assessment of inherent risks within the company, and the evaluation of system controls and procedures used by the company 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 company'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 Company
- Reinsurance
- Financial Statements
- Accounts and Records
- Data Processing

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

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.

## **II. HISTORY AND PLAN OF OPERATION**

MIC Reinsurance Corporation was incorporated under the laws of Wisconsin on December 3, 2009, and is a wholly owned subsidiary of Mortgage Guaranty Insurance Corporation (hereinafter also MGIC). On February 22, 2010, the company was issued a certificate of authority and was licensed to write mortgage guaranty insurance business in the state of Wisconsin. The company was capitalized by MGIC for \$3,000,000, which includes \$1,000,000 in the form of 100,000 authorized and issued common shares with a par value of \$10.00 per share and \$2,000,000 of paid-in and contributed surplus.

MICRC was organized in preparation for an affiliate, MGIC Indemnity Corporation (hereinafter also MIC), writing new business under a reactivation plan that was not disapproved by this office in conjunction with a Stipulation and Order (No. 09-C32277) dated July 15, 2009, placed on MIC. This is described further in MIC's examination report, which was examined concurrently with the company by this office. The company is to provide MIC with excess of loss reinsurance coverage on primary residential mortgage guaranty insurance risks in five states that do not permit a direct writing insurer to recognize balance sheet credit for reinsurance that is ceded to a subsidiary insurer, namely, California, Illinois, New York, Ohio, and Texas. MICRC is to assume MIC's liability for mortgage losses in excess of 25% or 30% of the indebtedness of the mortgage borrower dependent on the jurisdiction the insured loan was originated in pursuant to two treaties. As of December 31, 2011, the company had not assumed any business from MIC.

MICRC does not have any employees, and all of its day-to-day business operations are performed by MGIC pursuant to an intercompany services agreement. Further discussion of the MGIC Investment Corporation holding company system, description of MICRC's significant affiliates, and description of the company's intercompany agreements are included in the section of this report captioned "Affiliated Companies."

As December 31, 2011, the company was only licensed in the state of Wisconsin.

### III. MANAGEMENT AND CONTROL

#### Board of Directors

The board of directors consists of seven members, each of whom, with one exception, is an officer of the company. The directors are elected at the annual shareholder's meeting to serve a one-year term. Officers are elected at board meetings and are to hold those positions until the earlier of their resignation or removal by the board of directors. Each member of the MICRC board of directors also serves as a member of other boards of directors in the holding company group and receives no specific compensation for services performed as a director of MICRC.

Currently the board of directors consists of the following persons:

Name and Residence	Principal Occupation	Term Expires
Curt S. Culver Nashotah, Wisconsin	MGIC Chairman of the Board and Chief Executive Officer	2013
Heidi A. Heyrman Pewaukee, Wisconsin	MGIC Vice President of Regulatory Relations, Assistant General Counsel and Assistant Secretary	2013
Jeffrey H. Lane Mequon, Wisconsin	MGIC Executive Vice President, General Counsel and Secretary	2013
J. Michael Lauer Elm Grove, Wisconsin	MGIC Executive Vice President and Chief Financial Officer	2013
Timothy J. Mattke Whitefish Bay, Wisconsin	MGIC Vice President, Controller and Chief Accounting Officer	2013
Lawrence J. Pierzchalski Oconomowoc, Wisconsin	MGIC Executive Vice President, Risk Management	2013
Patrick Sinks Mequon, Wisconsin	MGIC President and Chief Operating Officer	2013

## Officers of the Company

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

<b>Name</b>	<b>Office</b>	<b>2011 Compensation</b>
Curt S. Culver	Chairman of the Board and Chief Executive Officer	\$4,564,274
Heidi A. Heyrman	Vice President of Regulatory Relations, Assistant General Counsel and Secretary	437,383
Jeffrey H. Lane	Executive Vice President, General Counsel and Assistant Secretary	2,558,003
J. Michael Lauer	Executive Vice President and Chief Financial Officer	1,821,760
Timothy J. Mattke	Vice President and Controller	471,402
Patrick Sinks	President and Chief Operating Officer	2,593,458

## 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:

### **Securities Investment Committee**

J. Michael Lauer, Chair  
Heidi A. Heyrman  
Timothy J. Mattke

#### **IV. AFFILIATED COMPANIES**

MIC Reinsurance Corporation is a member of a holding company system whose ultimate controlling parent is MGIC Investment Corporation (hereinafter also MGIC Investment). The organizational chart below depicts the relationships among the affiliates in the group. A brief description of the significant affiliates follows the organizational chart.

##### **Organizational Chart As of December 31, 2011**

- MGIC Investment Corporation
  - Mortgage Guaranty Insurance Corporation
    - MGICA PTY Limited
      - MGIC Australia PTY Limited
  - MIC Reinsurance Corporation
  - MGIC Indemnity Corporation
    - MIC Reinsurance Corporation of Wisconsin
  - MGIC Credit Assurance Corporation
  - MGIC Reinsurance Corporation of Wisconsin
    - MGIC Mortgage and Consumer Asset II, LLC (Note #1)
  - MGIC Assurance Corporation
  - MGIC Reinsurance Corporation of Vermont
  - eMagic.com, LLC
  - MGIC Mortgage and Consumer Asset I, LLC (Note #1)
    - CMI Investors LP 2 (99% ownership interest)
    - CMI Investors LP 5 (99% ownership interest)
    - CMI Investors LP 8 (99% ownership interest)
    - CMI Investors LP 9 (99% ownership interest)
- MGIC Reinsurance Corporation
- MGIC Mortgage Reinsurance Corporation
- MGIC Residential Reinsurance Corporation
- MGIC Insurance Services Corporation
- MGIC Investor Services Corporation
- MGIC Mortgage Services, LLC

Note # 1: MGIC Mortgage and Consumer Asset II, LLC, holds a 1% ownership interest in CMI Investors LPs; the remaining 99% interest is held in MGIC Mortgage and Consumer Asset I, LLC.

#### **MGIC Investment Corporation**

MGIC Investment was incorporated in Wisconsin on June 22, 1984, under the name Management Financing Corporation. MGIC Investment was established as a holding company to consolidate the ownership and capitalization of the legal entities within the MGIC enterprise. The initial capital funding of Management Financing Corporation was provided by The Northwestern Mutual Life Insurance Company and by senior executive officers of MGIC. The holding company name was changed to MGIC Investment Corporation effective March 1, 1985. An initial public



offering of MGIC Investment common capital stock was completed in August of 1991, and a second public offering was completed in June 1992. The issued and outstanding shares of MGIC Investment's common capital stock are traded on the New York Stock Exchange under the ticker symbol MTG.

As of January 17, 2012, Old Republic International Corporation owned 6.75% of the outstanding stock of MGIC Investment. As of September 30, 2012, the officers and directors of MGIC Investment, comprised of 17 individual shareholders, had ownership interest in MGIC Investment of approximately 1.7%. Interests held by directors included 451,001 share units held under MGIC Investment's directors' deferred compensation plan for which the holders currently do not have rights to exercise investment or voting power.

The MGIC enterprise is principally engaged in writing mortgage guaranty insurance on residential mortgage loans. MGIC Investment Corporation's insurance subsidiaries provide mortgage guaranty insurance to mortgage lenders, and its non-insurance operating subsidiaries provide products and services to the mortgage finance industry, including contract underwriting, real estate valuations, loan servicing, administering special insurance bonds and policies, brokerage for errors and omissions policies, and internet-based technology services.

As of December 31, 2011, MGIC Investment's consolidated GAAP basis audited financial statements reported total assets of \$7,216,230,000, total liabilities of \$6,019,415,000, and total shareholders' equity of \$1,196,815,000. Operations for 2011 produced a net loss of \$485,892,000.

### **Mortgage Guaranty Insurance Corporation**

MGIC was incorporated under the laws of Wisconsin on February 20, 1979, as Liberty Mortgage Insurance Corporation (LMIC). LMIC was originally owned by Verex Corporation and was acquired by MGIC Investment Corporation in November 1984. The name Liberty Mortgage Insurance Corporation was changed to Mortgage Guaranty Insurance Corporation on March 1, 1985, when MGIC began writing new business.

MGIC formerly had two classes of issued and outstanding common capital stock, Class A common stock and Class B common stock. MGIC Investment Corporation retained

ownership of the MGIC Class B common stock and effective September 30, 1985, contributed 100% of the MGIC Class A common stock to the former MGIC Investment subsidiary Mortgage Guaranty Reinsurance Corporation (MGRC). Effective May 25, 1999, MGRC was dissolved pursuant to a plan of voluntary dissolution and liquidation approved by the Commissioner. Upon the dissolution of MGRC, all 35,000 issued and outstanding shares of MGIC Class B common stock held by MGIC Investment Corporation were redeemed at a price of \$1,000 per share and the remaining assets and liabilities of the liquidated MGRC legal entity including 100% of the MGIC Class A common capital stock transferred to MGIC Investment Corporation. MGIC's capital stock presently is comprised solely of one class of common stock, wholly owned by MGIC Investment Corporation.

MGIC provides residential mortgage guaranty insurance in all 50 U.S. states, the District of Columbia, Guam, and Puerto Rico. MGIC serves as the lead operating company in the MGIC Group and provides administrative and managerial services to its affiliates. MGIC's direct and indirect costs incurred in providing services to its affiliates are allocated to the respective affiliates pursuant to intercompany agreements. Excess of loss insurance coverages on risks written by MGIC are ceded to four MGIC affiliate insurers to enable MGIC to comply with statutory restrictions in some states that limit an insurer's net retention of mortgage guaranty insurance for any one risk to not more than either 25% or 30% of the total indebtedness to the insured, depending on the jurisdiction.

As of December 31, 2011, MGIC's statutory financial statements reported total admitted assets of \$5,528,912,276, total liabilities of \$3,960,130,146, and policyholders' surplus of \$1,568,782,130. Operations for 2011 produced a net loss of \$397,086,634.

### **MGIC Indemnity Corporation**

MGIC Indemnity Corporation is a Wisconsin-domiciled mortgage guaranty insurer originally incorporated in Wisconsin in 1956 under the name Mortgage Guaranty Insurance Corporation (Old MGIC). In 1984 the Commissioner approved a plan (the Plan) whereby the ongoing successful business enterprise of Old MGIC could be protected from the bankruptcy of Baldwin-United Corporation and be continued in a successor legal entity. Pursuant to the Plan,

effective February 28, 1985, the business operations of Old MGIC were transferred to a successor insurer named Mortgage Guaranty Insurance Corporation (the present-day MGIC), Old MGIC changed its name to Wisconsin Mortgage Assurance Corporation (WMAC), and WMAC entered into court-ordered liquidation proceedings under the supervision of the Commissioner.

Under the 1985 liquidation proceedings, WMAC discontinued issuance of new insurance business, its existing book of business entered run-off status managed by the present-day MGIC, and 100% of WMAC's existing net retained liability for insurance risks was ceded to a group of international reinsurers under quota share reinsurance treaties. In December 1998, the WMAC liquidation proceedings were terminated and WMAC entered rehabilitation proceedings. Mortgage Guaranty Insurance Corporation (the present-day MGIC) purchased WMAC as of December 31, 1998, under a plan of rehabilitation approved by the Commissioner. WMAC changed its name to the current MGIC Indemnity Corporation effective June 1, 2000. MIC has not written any new business since 1985, and its entire portfolio of business is comprised of renewal policies in run-off. All claims have been paid by WMAC or its reinsurers, and only a small amount of insurance in-force remains in run-off.

In 2009 MIC's reactivation plan was approved by this office, the Federal Home Loan Mortgage Corporation and certain named federal government-sponsored enterprises subject to certain conditions. In preparation of writing new mortgage risks MIC received a \$200 million capital contribution from MGIC Investment in 2009. MIC has also been actively trying to obtain licenses to write business in all U.S. states and as of year-end 2011 has been successful in obtaining licensure in 52 jurisdictions (includes the District of Columbia and Puerto Rico), but has not begun writing any new business under the reactivation plan.

As of December 31, 2011, MIC's statutory financial statements reported total admitted assets of \$234,900,424, total liabilities of \$401,903, and policyholders' surplus of \$234,498,521. Operations for 2011 produced net income of \$4,777,300.

### **MGIC Reinsurance Corporation**

MGIC Reinsurance Corporation (hereinafter also MRC) was incorporated under the laws of Wisconsin on February 21, 1985, and commenced business on March 1, 1985. MRC was

organized to provide MGIC with excess of loss reinsurance coverage and as of year-end 2011 assumes all of its business from MGIC. MRC provides reinsurance to MGIC on primary and pool mortgage guaranty coverage in excess of 25% of the total indebtedness to the insured, principally on business written in six states.

As of December 31, 2011, MRC's statutory financial statements reported total admitted assets of \$285,643,251, total liabilities of \$217,523,585, and policyholders' surplus of \$68,119,666. Operations for 2011 produced a net loss of \$7,936,675.

### **MGIC Assurance Corporation**

MGIC Assurance Corporation (hereinafter also MAC) was organized under the laws of Oklahoma in 1937 under the name Insurers Indemnity and Insurance Company and was subsequently renamed Financial Security Assurance, Inc. of Oklahoma (FSAOK). FSAOK was acquired by MGIC in 1995 and effective November 18, 1996, redomesticated to Wisconsin and adopted the name MGIC Assurance Corporation.

All of the issued and outstanding capital stock of MAC was contributed to the MGIC subsidiary insurer, MGIC Surety Corporation (Surety), in 1997. MGIC Surety Corporation was merged with and into MGIC effective November 30, 2002. Upon the merger of Surety, the assets and liabilities of MGIC Surety Corporation, including 100% of the issued and outstanding capital stock of MAC, transferred to MGIC.

MAC established a segregated account in 1997 pursuant to the requirements of s. 611.24 (1), Wis. Stat., and s. Ins 3.09 (12) (g), Wis. Adm. Code, through which MAC was authorized to conduct junior lien guaranty insurance business. MAC commenced writing insurance on second mortgages and home equity lines of credit in 1997. MAC terminated writing new business in the segregated account effective January 1, 2002. Its portfolio of junior lien insurance risks consisting solely of renewal business on existing policies written through the segregated account was assumed by its affiliate, MGIC Credit Assurance Corporation, in December 2004. In 2007, MAC began writing credit default coverage on loans secured by unimproved residential properties in its general account, but in 2008 discontinued offering such coverage and is currently running off its business.

As of December 31, 2011, MAC's statutory financial statements reported total admitted assets of \$10,389,198, total liabilities of \$446,664, and policyholders' surplus of \$9,942,534. Operations for 2011 produced net income of \$141,238.

#### **MGIC Reinsurance Corporation of Wisconsin**

MGIC Reinsurance Corporation of Wisconsin (hereinafter also MRCW) was incorporated under the laws of Wisconsin on February 15, 1996, and commenced operations on April 1, 1996. MRCW was established to provide reinsurance to MGIC for primary and pool mortgage guaranty policy liabilities in excess of 25% of the total indebtedness to the insured, for mortgage guaranty policies written in all jurisdictions except six states. MRCW assumes all of its business from MGIC and does not cede any reinsurance.

As of December 31, 2011, MRCW's statutory financial statements reported total admitted assets of \$846,437,582, total liabilities of \$745,199,995, and policyholders' surplus of \$101,237,587. Operations for 2011 produced a net loss of \$37,719,335.

#### **MGIC Mortgage Reinsurance Corporation**

MGIC Mortgage Reinsurance Corporation (hereinafter also MMRC) was organized under the laws of Wisconsin on July 1, 1996, and commenced business on the same date. MMRC provides reinsurance to MGIC on mortgage guaranty primary and pool coverage in excess of 25% of the total indebtedness to the insured on business written in six states. MMRC's reinsurance on any loan is limited to a maximum of 25% of the total indebtedness to the insured. MMRC assumes all of its business from MGIC and does not cede any reinsurance.

As of December 31, 2011, MMRC's statutory financial statements reported total admitted assets of \$27,694,271, total liabilities of \$17,495,652, and policyholders' surplus of \$10,198,619. Operations for 2011 produced a net loss of \$75,992.

#### **MGIC Residential Reinsurance Corporation**

MGIC Residential Reinsurance Corporation (hereinafter also MRRC) was organized under the laws of Wisconsin on July 1, 1996, and commenced business on that date. MRRC provides reinsurance to MGIC on mortgage guaranty primary and pool coverage in excess of 25% of the total indebtedness to the insured on business written in six states. MRRC reinsurance

on any loan is limited to a maximum of 25% of the total indebtedness to the insured. MRRC assumes all of its business from MGIC and does not cede any reinsurance.

As of December 31, 2011, MRRC's statutory financial statements reported total admitted assets of \$26,903,063, total liabilities of \$17,495,634, and policyholders' surplus of \$9,407,429. Operations for 2011 produced a net loss of \$183,273.

#### **MGIC Credit Assurance Corporation**

MGIC Credit Assurance Corporation (hereinafter also MCAC) was organized under the laws of Wisconsin on April 30, 1997, and commenced business on May 21, 1997. MCAC is a wholly owned subsidiary of MGIC and was established to write mortgage guaranty insurance for lenders in certain states on second mortgages and home equity lines of credit. MCAC commenced writing direct business in 1998 and terminated writing new business effective January 1, 2002. MCAC's current portfolio of insurance risks consists solely of renewal business on existing policies, and its entire book of business is in run-off.

As of December 31, 2011, MCAC's statutory financial statements reported total admitted assets of \$43,367,930, total liabilities of \$1,244,961, and policyholders' surplus of \$42,122,969. Operations for 2011 produced a net loss of \$62,097.

#### **MGIC Reinsurance Corporation of Vermont**

MGIC Reinsurance Corporation of Vermont (hereinafter also MRCV) was incorporated under the laws of Vermont on September 28, 1999, to operate as a sponsored captive insurance company pursuant to Title 8, Chapter 141 of the Vermont Statutes. The Vermont Statutes permit a licensed insurer and participating sponsors to establish a sponsored captive reinsurance company to reinsure business written by a licensed insurer. MRCV reinsures MGIC mortgage guaranty risks on loans that were originated, purchased, or serviced by mortgage lenders which participate in MRCV captive reinsurance. For the business assumed by MRCV on behalf of a participating sponsor, MRCV establishes a protected cell account in which assets of each such participant are separately maintained and accounted for with respect to the participant's liabilities for mortgage guaranty risks assumed by the participant. A separate participation agreement is established between MRCV and each respective participant. By

establishing a participation agreement with MRCV, a lender which desires to engage in captive reinsurance is able to participate as a sponsored captive and is not required to establish a separate insurance or reinsurance legal entity.

As of December 31, 2011, MRCV's statutory financial statements reported total admitted assets of \$14,827,442, including \$11,089,334 of trust assets, total liabilities of \$7,652,600 and policyholders' surplus of \$7,174,842. Operations for 2011 produced a net loss of \$1,067,730.

### **MIC Reinsurance Corporation of Wisconsin**

MIC Reinsurance Corporation of Wisconsin (hereinafter also MICRCW) was organized and incorporated under the laws of the state of Wisconsin on December 3, 2009. MICRCW was established to provide reinsurance to MIC for primary mortgage guaranty policy liabilities in excess of 25% of the total indebtedness to the insured, for mortgage guaranty policies written in all jurisdictions except five states as part of MIC's reactivation plan, which was discussed earlier. As of year-end 2011, MICRCW has not commenced writing business.

As of December 31, 2011, MICRCW's statutory financial statements reported total admitted assets of \$5,538,959, total liabilities of \$501,017, and policyholders' surplus of \$5,037,942. Operations for 2011 produced net income of \$15,523.

### **Written Agreements with Affiliates**

In addition to common staffing and management control, MIC Reinsurance Corporation's relationship to its affiliates is affected by various written agreements and undertakings. Reinsurance agreements are described in Section V of this report entitled "Reinsurance." A brief summary of the other agreements and undertakings follows, arranged by effective date.

#### **Tax Sharing Agreement**

Effective January 22, 1986, MGIC Investment Corporation entered into a tax-sharing agreement with MGIC and specified affiliates of the MGIC Group that qualify for inclusion in such an agreement under the Internal Revenue Code. The agreement has been amended nine times to add or delete the participation of applicable affiliated entities, and currently provides that each

of the Wisconsin-domiciled MGIC insurers is a participant in the agreement, which includes MICRC in an amendment effective December 14, 2009. Under this agreement, MGIC Investment Corporation files a consolidated U.S. Federal Income Tax Return that includes MGIC and other affiliates of the holding company group.

The agreement sets forth the rights and obligations of the parties to the agreement with respect to the determination and settlement of federal income tax liabilities as well as the allocation of the MGIC Group's consolidated U.S. federal income tax liability in accordance with a rational, systematic formula. The agreement provides for computation of tax, settlement of balances between affiliates, tax-sharing, filing the return, audits and other adjustments, dispute resolution and other administrative requirements. The agreement calls for the prompt settlement of estimated federal tax payments and final year-end calculated adjusted payments on the notified due dates.

#### Servicing Agreement

MGIC entered into a Servicing Agreement effective January 1, 1996, with MGIC Investment Corporation and certain named affiliates of the MGIC Group. The agreement has been amended nine times and ratified once to add or delete the participation of applicable affiliated entities, and currently provides that each of the Wisconsin-domiciled MGIC insurers is a participant in the agreement, which includes MICRC in an amendment effective December 14, 2009. Under this agreement MGIC performs management and administrative services essential to the day-to-day operation of various affiliates within the MGIC holding company. Services provided by MGIC to its affiliates include provision of office space and employees; administration of underwriting, risk management and claims; performance as agent for funds collection and disbursement; maintenance of investment portfolios and execution of investment transactions; maintenance of depository accounts; maintenance of books and records including financial records; and the preparation and delivery of reports, tax returns, and documents and filings, as required. MGIC's direct costs and indirect expenses incurred in providing services to the individual affiliates are allocated to the respective affiliates each quarter, which is to be



determined in accordance with generally accepted accounting principles and in a manner consistent with regulatory authorities having jurisdiction over members to the agreement.

#### Indemnity Agreement

Effective September 1, 2000, an Indemnity Agreement was established between MGIC and MIC to facilitate the withdrawal of MIC from the state of New York. The agreement pertains solely to MIC's liabilities in the state of New York for WMAC run-off mortgage guaranty insurance policies written prior to February 28, 1985, including primary insurance issued under master policies on individual mortgage loans and pool insurance issued under mortgage trust supplemental or pool policies. Pursuant to the agreement, MGIC agrees to pay any WMAC insured located in New York all of WMAC's obligations at any time in the event that WMAC has failed to pay any amount due to the insured under WMAC's outstanding policies. Each WMAC insured shall have privity with, direct right of action against, and the right to file claims directly with MGIC to pay WMAC's obligations after WMAC has failed to pay. Under the agreement, MGIC issued an endorsement as required by applicable law to advise insureds of MGIC's indemnity agreement for WMAC business, and MGIC issued an undertaking to governmental agencies in New York for payment of taxes and other liabilities of WMAC to such agencies. Under the agreement, MGIC is entitled to recover from WMAC the amount paid by MGIC in payment of WMAC obligations as a result of this agreement. The agreement will remain in effect for so long as any of WMAC's policies remain outstanding and in force.

#### Shared Resources Agreement

In preparation for the reactivation business plan for MGIC Indemnity Corporation, discussed earlier in this report, Mortgage Guaranty Insurance Corporation and MIC entered into a shared resources agreement on March 11, 2010. In the event that MIC begins writing direct mortgage guaranty insurance business, the date on which MIC issues its first policy will be the effective date of this agreement. On the aforementioned date the servicing agreement with MGIC, discussed earlier in this section of the report, will be terminated with respect to MIC and be replaced by this shared resources agreement. The purpose of this agreement is for MGIC to continue to provide MIC with management and administrative services in connection with MIC

writing new mortgage guaranty insurance business. Management and administrative services to be provided by MGIC to MIC are essentially the same ones outlined in the servicing agreement. In consideration of the services provided to MIC under this agreement, MIC shall pay to MGIC, on a monthly basis, 20% of the premiums written by MIC during the calendar month, which is subject to an adjustment for estimated actual cost performed at the end of each calendar year.

## **V. REINSURANCE**

The reinsurance portfolio and strategy of MIC Reinsurance Corporation is described below. The company's reinsurance contracts contain proper insolvency provisions.

MIC has implemented a reactivation plan to write new mortgage risks in those jurisdictions where MGIC does not comply with applicable capital requirements in order to write mortgage insurance, diligently pursued waivers of applicable capital requirements, and weren't granted such waivers. In preparation of writing new mortgage insurance risks MIC has executed two reinsurance agreements with affiliates to facilitate compliance with statutory requirements that a mortgage guaranty insurer must limit its retention under a single policy of insurance to not more than 25% of the debt of the mortgage borrower.

One of the reinsurance agreements was entered into with MICRC on August 1, 2012, whereby MIC would cede to the company mortgage guaranty risks in excess of 25% or 30% of the indebtedness of the mortgage borrower depending on the jurisdiction in which the insured loan was originated.

MIC has also executed an agreement with MICRC effective August 1, 2012, whereby the company would assume primary business risks relating to the Group's captive reinsurance program on a variable quota share basis, which ranges from 3.85% to 50% coverage and only applies to deep coverage certificates.

The reinsurance agreements described above that MIC has executed with MICRC applies to business written in the following U.S. jurisdictions:

- Illinois, New York, Ohio and Texas for coverage of over 25% of the indebtedness to the insured; and
- California for coverage of over 30% of the indebtedness to the insured.

The specified territories covered under the agreements are a result of the foregoing states not permitting an insurer to recognize balance sheet credit for reinsurance that is ceded to a subsidiary insurer or to a subsidiary insurer with the coverage mentioned.

## **VI. FINANCIAL DATA**

The following financial statements reflect the financial condition of the company as reported to the Commissioner of Insurance in the December 31, 2011, annual statement. Also included in this section are schedules that reflect the growth of the company, NAIC Insurance Regulatory Information System (IRIS) ratio results for the period under examination, and the minimum policyholders position calculation. Adjustments made as a result of the examination are noted at the end of this section in the area captioned "Reconciliation of Surplus per Examination."

**MIC Reinsurance Corporation**  
**Assets**  
**As of December 31, 2011**

	<b>Assets</b>	<b>Nonadmitted Assets</b>	<b>Net Admitted Assets</b>
Bonds	\$2,720,863	\$0	\$2,720,863
Cash, cash equivalents, and short-term investments	272,634	0	272,634
Investment income due and accrued	19,634	0	19,634
Current federal and foreign income tax recoverable and interest thereon	<u>1,499</u>	<u>0</u>	<u>1,499</u>
Total Assets	<u>\$3,014,630</u>	<u>\$0</u>	<u>\$3,014,630</u>

**MIC Reinsurance Corporation**  
**Liabilities, Surplus, and Other Funds**  
**As of December 31, 2011**

Net deferred tax liability	\$ 447
Payable to parent, subsidiaries, and affiliates	<u>4,060</u>
Total liabilities	4,507
Common capital stock	\$1,000,000
Gross paid in and contributed surplus	2,000,000
Unassigned funds (surplus)	<u>10,123</u>
Surplus as regards policyholders	<u>3,010,123</u>
Total Liabilities and Surplus	<u>\$3,014,630</u>

**MIC Reinsurance Corporation  
Summary of Operations  
For the Year 2011**

**Underwriting Income**

Premiums earned		\$ 0
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Deductions:

Other underwriting expenses incurred	<u>\$40,374</u>	
Total underwriting deductions		<u>40,374</u>
Net underwriting gain (loss)		(40,374)

**Investment Income**

Net investment income earned	37,534	
Net realized capital gains (losses)	<u>28</u>	
Net investment gain (loss)		<u>37,562</u>

Net income (loss) after dividends to policyholders but before federal and foreign income taxes		(2,812)
Federal and foreign income taxes incurred		<u>(1,515)</u>

Net Loss		<u>\$ (1,297)</u>
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**MIC Reinsurance Corporation**  
**Cash Flow**  
**For the Year 2011**

Net investment income			<u>\$ 64,238</u>
Total			64,238
Commissions, expenses paid, and aggregate write-ins for deductions	\$ 40,374		
Federal and foreign income taxes paid (recovered)	<u>(850)</u>		
Total deductions			<u>39,524</u>
Net cash from operations			24,714
Proceeds from investments sold, matured, or repaid:			
Bonds	<u>\$1,850,850</u>		
Total investment proceeds		1,850,850	
Cost of investments acquired (long-term only):			
Bonds	<u>2,052,255</u>		
Total investments acquired		<u>2,052,255</u>	
Net cash from investments			(201,405)
Cash from financing and miscellaneous sources:			
Other cash provided (applied)	<u>(6,940)</u>		
Net cash from financing and miscellaneous sources			<u>(6,940)</u>
<b>Reconciliation:</b>			
Net change in cash, cash equivalents, and short-term investments			(183,631)
Cash, cash equivalents, and short-term investments:			
Beginning of year			<u>456,265</u>
End of Year			<u>\$ 272,634</u>

**MIC Reinsurance Corporation  
Policyholders Position Calculation  
December 31, 2011**

Surplus as regards policyholders	\$3,010,123	
Less:		
Investments in excess of maximum allowable by ch. 620, Wis. Stat.	<u>163,278</u>	
Total policyholders position		<u>\$2,846,845</u>
Net minimum policyholders position:		
Total individual loans	0	
Total group loans	<u>0</u>	
Total minimum policyholders position		<u>0</u>
Excess of total policyholders position over minimum policyholders position		<u>\$2,846,845</u>



**MIC Reinsurance Corporation  
Analysis of Surplus  
For the Two-Year Period Ending December 31, 2011**

The following schedule details items affecting surplus during the period under examination as reported by the company in its filed annual statements:

	2011	2010
Surplus, beginning of year	\$3,011,711	\$ 0
Net income	(1,297)	11,867
Change in net deferred income tax	(291)	(156)
Capital changes:		
Paid in	0	1,000,000
Surplus adjustments:		
Paid in	<u>0</u>	<u>2,000,000</u>
Surplus, End of Year	<u>\$3,010,123</u>	<u>\$3,011,711</u>

**MIC Reinsurance Corporation  
Insurance Regulatory Information System  
For the Two-Year Period Ending December 31, 2011**

The NAIC Insurance Regulatory Information System (IRIS) does not report any results for this company for the period under examination. This is because the system needs two prior years of operational data to calculate the IRIS results. The company was incorporated on December 3, 2009, and began filing statements as of March 31, 2010.

**Growth of MIC Reinsurance Corporation**

Year	Admitted Assets	Liabilities	Surplus as Regards Policyholders	Net Income
2011	\$3,014,630	\$ 4,507	\$3,010,123	\$(1,297)
2010	3,022,867	11,156	3,011,711	11,867

  

Year	Gross Premium Written	Net Premium Written	Premium Earned	Loss and LAE Ratio	Expense Ratio	Combined Ratio
2011	\$0	\$0	\$0	0.0%	0.0%	0.0%
2010	0	0	0	0.0	0.0	0.0

As described earlier in the report the company was organized on December 3, 2009, in preparation for MIC's commencement of writing new business again under a reactivation plan.

The company is to assume business from MIC under two executed reinsurance agreements as described in Section V of this report captioned "Reinsurance." The company was initially capitalized through issuance of 100,000 shares of common stock with a par value of \$10.00 per share and \$2,000,000 in paid-in capital contributions from its direct upstream affiliate, MGIC, which was also explained earlier in this report. The increase in surplus from the original capitalization of the company is primarily a result of investment income earned exceeding operational expenses allocated from MGIC over the two-year period of its existence. As of December 31, 2011, MIC had not begun to write new business and this is the reason why MICRC does not report any premium writings or operational ratios in 2010 or 2011.

#### **Reconciliation of Surplus per Examination**

No adjustments were made to surplus as a result of the examination. The amount of surplus of \$3,010,123 reported by the company as of December 31, 2011, is accepted.

## **VII. SUMMARY OF EXAMINATION RESULTS**

### **Compliance with Prior Examination Report Recommendations**

The current examination is the first examination of the company performed by the Wisconsin Office of the Commissioner of Insurance since it was incorporated in the state of Wisconsin effective December 3, 2009. Review and evaluation of compliance with prior examination findings is not applicable.

## **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 company's operations is contained in the examination work papers.

### **Investment Limitations**

The examination completed a review of the company's investment holdings as of year-end 2011 to verify that it was in compliance with applicable investment limitations under Wisconsin law. Chapter 620.22, Wis. Stat., establishes the limitations for investments that can be counted toward satisfaction of a mortgage insurance company's minimum policyholders position requirement. Investments that exceed limitations set forth in that statute cannot be counted towards satisfaction of the minimum policyholders position requirement. Section 620.23, Wis. Stat., further defines limitations on authorized investments that can count towards the minimum policyholders position requirement. Section 620.23 (2) (b), Wis. Stat., describes a limitation on total investments in any one issuer, which is 10% of assets for all securities of a single issuer and its affiliates, other than the government of the United States and subsidiaries of the types authorized under s. 611.26 (1) to (3), Wis. Stat. Based on MICRC's \$3,014,630 in admitted assets as of December 31, 2011, the single issuer investment limitation applicable to the company's minimum policyholders position requirement was \$301,463. The company had four investments with adjusted carrying book values that exceeded the aforementioned limitation as reported in its Schedule D - Part 1, Column 11. Therefore, the company should not have included \$314,009 towards its December 31, 2011, minimum policyholders position calculation that was filed with this office in accordance with s. Ins 3.09 (5), Wis. Adm. Code. At year-end 2011, the company reported excess policyholders position over minimum policyholders position of \$3,010,123. The reported excess would have to be reduced by the amount exceeding the limitation; however, there is a "basket" clause, s. 620.22 (9), Wis. Stat., that allows insurers to invest 5% of their first \$500 million of assets in investments not otherwise permitted by statute. The adjustment, after the application of the basket clause, is reflected in Section VI of this report, under the subsection entitled "Policyholders Position Calculation." It is recommended that the

company adjust its assets as part of the calculation of its minimum policyholders position requirement to reflect investment holdings that exceed limitations governed by s. 620.22, Wis. Stat.

## **VIII. CONCLUSION**

The current examination of MIC Reinsurance Corporation is the first examination of the company performed by the Wisconsin Office of the Commissioner of Insurance since it was incorporated on December 3, 2009. As of December 31, 2011, the company reported assets of \$3,014,630, liabilities of \$4,507, and policyholders' surplus of \$3,010,123. The company was initially capitalized through issuance of 100,000 shares of common stock with a par value of \$10.00 per share and \$2,000,000 in paid-in capital contributions from its direct upstream affiliate, MGIC.

The company was formed to provide MIC with excess of loss reinsurance coverage on primary residential mortgage guaranty insurance risks in five states that do not permit a direct writing insurer to recognize balance sheet credit for reinsurance that is ceded to a subsidiary insurer, once MIC started writing new business under a reactivation plan not disapproved by this office in 2009. As of year-end 2011 the company did not report any assumed business as MIC had not written any new primary mortgage insurance business under the reactivation plan.

The examination verified the financial condition of the company as reported in its annual statement as of December 31, 2011. The examination of MICRC resulted in one recommendation, no adjustments to surplus and no reclassifications. The recommendation relates to the company not adjusting its minimum policyholders position calculation to reflect holdings in excess of Wisconsin's investment limitations.

## **IX. SUMMARY OF COMMENTS AND RECOMMENDATIONS**

1. Page 26 - Investment Limitations—It is recommended that the company adjust its assets as part of the calculation of its minimum policyholders position requirement to reflect investment holdings that exceed limitations governed by s. 620.22, Wis. Stat.

## **X. ACKNOWLEDGMENT**

The courtesy and cooperation extended during the course of the examination by the officers and employees of the company are acknowledged.

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

<b>Name</b>	<b>Title</b>
Ana J. Careaga	Insurance Financial Examiner – Journey
Victoria Y. Chi, CISA, CISM, CRISC	Insurance Financial Examiner – Advanced, Information Systems Audit Specialist
Jerry C. DeArmond, CFE, FLMI, AIRC	Insurance Financial Examiner – Advanced, Loss Reserve Specialist
Tom M. Janke, CFSA, CISA, CRP	Insurance Financial Examiner – Journey
Mike E. Miller	Insurance Financial Examiner
Frederick H. Thornton, CFE, CPCU	Insurance Financial Examiner – Advanced, Exam Planning & Quality Control Specialist

Respectfully submitted,

John E. Litweiler  
Examiner-in-Charge



## **XI. APPENDIX—SUBSEQUENT EVENTS**

There were a number of events that transpired subsequent to December 31, 2011, which significantly impacted members of the company's holding company structure. A brief summary of those events follows.

### MGIC Indemnity Corporation

In August of 2012, MIC began writing new business in those jurisdictions for which MGIC did not have active waivers of capital requirements and through September 30, 2012, MIC's new insurance written was \$587 million. Jurisdictions for which MIC was writing new mortgage insurance in included Florida, Idaho, New Jersey, New York, Ohio, Puerto Rico and Texas.

### Permitted Practice

On September 28, 2012, this office granted MGIC a permitted practice to report its net deferred tax asset as an admitted asset in an amount not to exceed 10% of policyholders' surplus without regard to the limitations and requirements in Statement of Statutory Accounting Principles (SSAP) No. 101, paragraph 11. The application of SSAP No. 101 is otherwise unchanged by this decision. This permitted practice is defined as a percentage of policyholders' surplus, so the dollar amount associated with the permitted practice would vary as policyholders' surplus varies over time. The financial impact of the permitted practice for MGIC as of September 30, 2012, was approximately a \$90 million increase to policyholders' surplus.

### Actions by the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac)

In a letter dated July 24, 2012, MGIC requested that Freddie Mac authorize its use of MIC to write new business in seven states in addition to those already permitted by Freddie Mac in a letter dated January 23, 2012, as part of MGIC management's reactivation plan mentioned earlier in this report. Freddie Mac responded to this request on August 1, 2012, by temporarily allowing MIC, as a limited insurer, to write new business in the requested jurisdictions as long as certain named conditions were agreed to and followed by MGIC. The aforementioned temporary approval was amended in a letter from Freddie Mac dated September 28, 2012, which expanded

the number of territories MIC could write new business in to 16 without obtaining Freddie Mac's prior approval through December 31, 2013, and included the following conditions be met that replaced certain ones named in the January and August 2012 letters from Freddie Mac in addition to other conditions named in them:

- MGIC Investment must contribute \$100 million to MGIC by December 1, 2012;
- MGIC and Freddie Mac must reach an agreement as to substantially all terms by October 31, 2012, to resolve their pool policy insurance dispute then in litigation; and
- This office must provide written confirmation to Freddie Mac that MIC's capital will be unconditionally available to MGIC to support MGIC's policyholder obligations without segregation of those obligations.

Negotiations between MGIC and Freddie Mac, which included the direct involvement of this office and Federal Housing Finance Agency (FHFA), Freddie Mac's conservator, took place to resolve any disagreements regarding the conditions in Freddie Mac's September 28, 2012, letter.

As part of the negotiations MGIC, Freddie Mac, and FHFA came to a tentative agreement prior to October 31, 2012, to resolve the litigated pool policy insurance dispute, which was later approved by each party's respective board of directors in November of 2012. Under the terms of the settlement MGIC agrees to pay Freddie Mac \$267.5 million in claims, with \$100 million payable by December 11, 2012, and \$167.5 million payable in 48 monthly installments beginning on January 2, 2013.

Additionally, as result of negotiations, this office issued a Stipulation and Order on MGIC and MIC dated November 29, 2012, that in the event (A) OCI determines a reasonable probability that MGIC will be unable to make policy payments in full at any time within five years of a financial exam, or (B) MGIC fails to pay valid policy claims when due, OCI will conduct a review within 60 days to quantify the maximum single dividend MIC could prudently pay to MGIC, taking account of MIC's policyholders' interests, applicable law and MIC's financial circumstances at that time, after which OCI will authorize MIC to pay such dividend within 30 days.

As a result of the actions taken by parties involved in the negotiations, some of which were described in the previous two paragraphs, on November 30, 2012, Freddie Mac continued to approve MGIC's use of MIC as a limited mortgage insurer through December 31, 2013; however, this approval may still be withdrawn by Freddie Mac at any time. On December 3,

2012, MGIC Investment transferred \$100 million to MGIC to meet one of the remaining outstanding conditions required by Freddie Mac to continue its approval of MIC as a limited mortgage insurer.

On the same day Freddie Mac issued its letter regarding MIC's eligibility as a limited mortgage insurer, Fannie Mae sent a letter dated November 30, 2012, conditionally approving MIC to write new insurance business in any jurisdictions, in addition to the 16 specified jurisdictions approved in the January 19, 2012, Fannie Mae letter, in which MGIC is not able to write business. The approval is for 60 days from the date MGIC is prohibited from writing new business in a jurisdiction while Fannie Mae evaluates approving MIC in such jurisdiction for a longer period. As with Freddie Mac's approval, Fannie Mae's agreement terminates December 31, 2013. However, in the event MGIC is not allowed to write new business in the state of Wisconsin, the approvals granted MIC by Fannie Mae shall be revoked.

Public Offering by MGIC Investment Corporation and Capital Contribution to Mortgage Guaranty Insurance Corporation

On March 12, 2013, MGIC Investment Corporation received aggregate net proceeds, after underwriting discounts, commissions, and estimated offering expenses, of approximately \$1.15 billion from the sale of 135 million shares of common stock and \$500 million of 2% convertible senior notes due 2020. MGIC Investment Corporation transferred \$800 million to Mortgage Guaranty Insurance Corporation to increase its capital. This transfer restored MGIC's risk to capital to approximately 20 to 1 and, as a result, MGIC met the capital requirements of all jurisdictions having specific capital requirements for mortgage guaranty insurers without the need for any waiver.