Report

of the

Examination of

Millers Classified Insurance Company

Alton, Illinois

As of December 31, 2012

TABLE OF CONTENTS

Page

State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

Scott Walker, *Governor*
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March 9, 2014

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:

MILLERS CLASSIFIED INSURANCE COMPANY
Alton, Illinois

and this report is respectfully submitted.

I. INTRODUCTION

The previous examination of Millers Classified Insurance Company (the company or MCIC) was conducted in 2008 as of December 31, 2007. The current examination covered the intervening period ending December 31, 2013, and included a review of such 2014 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. 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.

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 the company’s loss and loss adjustment expense reserves. 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 company was organized in 1985 as Classified Insurance Company of Wisconsin, as part of the Classified Financial Corporation holding company system. The company was licensed and commenced business on January 1, 1986, when it assumed the direct personal lines of business of American Star Insurance Company, which was at that time an affiliate. In February 1988, the company changed its name to Classified Insurance Company, Inc.

The company was purchased from Classified Financial Corporation by Millers Mutual Insurance Association of Illinois (MMIA), a mutual property and casualty insurer domiciled in the state of Illinois, in 1990. MMIA was also the ultimate parent of Millers General Insurance Company.

On January 1, 1995, the company merged with Millers General Insurance Company, with Millers General Insurance Company being the surviving entity. Prior to the merger, on November 1, 1994, Millers General Insurance Company redomesticated from Illinois to Wisconsin. After the merger, Millers General Insurance Company changed its name to that currently used.

Effective April 1, 2003, MMIA formed Affiliated Mutual Holding Company (AMHC) and converted to a stock subsidiary of AMHC, the mutual holding company, while at the same time changing its name to Millers First Insurance Company (MFIC).

The Illinois Director of Insurance (IL DOI) filed a petition to the Circuit Court of Cook County, Illinois, County Department, Chancery Division (Court), on June 8, 2012, for an order of conservation against MFIC, which was granted by the Court on June 11, 2012. This was due to financial difficulties MFIC suffered after significant storm losses sustained in 2011 through mid-2012. On July 24, 2012, the Court entered into a decision for an order of rehabilitation against MFIC as requested by the IL DOI. This action granted the IL DOI as MFIC's rehabilitator and placed the company under the control of the Illinois Office of the Special Deputy (IL OSD).

Shortly after the order of conservation on the company's direct parent, MFIC, a stipulation and order was issued by the Wisconsin Office of the Commissioner of Insurance (OCI) and agreed to by MCIC effective July 1, 2012, which limited the company's operations. The order prevented the company from writing new business, but allowed it to service existing business among other actions stipulated in the order.

The company voluntarily began running off its existing business by sending nonrenewal notifications beginning on July 2, 2012, for those policies that have policy anniversary dates on or after August 31, 2012. Effective October 17, 2012, the company sold its renewal rights to Electric Insurance Company, domiciled in Massachusetts, for the preferred direct response business (non-auto with policyholders that had a credit score of 700 or higher) written in the states of Illinois, Missouri and Wisconsin. The runoff of the company's existing auto policies was completed by March 31, 2013, and the runoff of the remaining homeowner's policies was completed by September 30, 2013.

MCIC does not have any employees and all of its day-to-day business operations are performed by employees of MFIC pursuant to an intercompany services agreement. A description of the company's intercompany agreements are included in the section of this report captioned "Affiliated Companies."

In 2012, the company wrote direct premium in the following states:

Wisconsin	$2,855,030	43.2%
Missouri	1,858,301	28.1
Illinois	1,732,841	26.2
Iowa	162,184	2.5
Total	$6,608,356	100.0%

Prior to going into runoff, the company concentrated on writing personal lines coverage in four Midwestern States as listed above. In addition to these states the company was also licensed in Colorado, Kansas, North Dakota and South Dakota. The state of South Dakota accepted the company's request to withdraw its license and return its statutory deposit, with the termination of its license effective September 30, 2013.

The major products were marketed through direct response methods and the company's affiliated agency, D.R. Sparks Insurance Services, Inc. (DRS). DRS operated using a general market agency format under the assumed name of Affiliated Insurance Specialists as well as a supplemental marketing plan format using the assumed names Egisure, Egiserve or Millers

First Insurance Agency. Personal service representatives employed by the company serviced all new and existing business. As described earlier, the renewal rights to most of the direct response business have been sold to Electric Insurance Company.

In May 2013, MFIC entered into an Asset Purchase Agreement effective June 1, 2013, with a closing date of June 6, 2013, with RCI Holdings II, LLC (RCI), a Missouri limited liability company. This agreement, approved by the IL DOI through an order issued by the Court, describes the sale of the expiration rights arising from and related to all in-force policies of insurance produced by DRS as of the closing date of the agreement. Since the agency could no longer produce business under the name DRS after the execution of the Asset Purchase Agreement, MFIC changed the name of the agency to Alton Millers Agency, Inc.

The following table is a summary of the net insurance premiums written by the company in 2012. The growth of the company is discussed in the "Financial Data" section of this report.

Line of Business	**Direct Premium**	**Reinsurance Assumed**	**Reinsurance Ceded**	**Net Premium**
Fire	$ 18,636	$1,475	$ 10,490	$ 9,621
Allied lines	7,231	606	4,065	3,772
Homeowner's multiple peril	1,842,461	0	675,084	1,167,377
Inland marine	54,514	0	9,907	44,607
Earthquake	32,571	0	19,952	12,619
Other liability – occurrence	21,975	0	15,770	6,205
Private passenger auto liability	2,441,779	0	112,803	2,328,976
Auto physical damage	2,189,189	0	93,265	2,095,924
Total All Lines	$6,608,356	$2,081	$941,336	$5,669,101

III. MANAGEMENT AND CONTROL

Board of Directors

The board of directors consists of five members. All directors are elected annually to serve a one-year term. Officers are elected at the board's annual meeting. Board members, with the exception of the President & Chairman of the Board, currently each receive $500 per month plus an additional $150 per hour for each meeting exceeding three hours and reimbursement for travel expenses.

Currently the board of directors consists of the following persons:

Name and Residence	Principal Occupation	Term Expires
William C. Bouchein St. Louis, MO	President of BMC, Inc.	2014
Thomas W. Hurd Carmel, IN	Chief Operating Officer of the Grain Division for JBS United, Inc.	2014
James T. Little Blaine, WA	Professor of Finance and Economics at Washington University	2014
George S. Milnor Alton, IL	Chairman of the Board, President and CEO of the Millers First Insurance Companies	2014
R. William Schrimpf, Jr. Edwardsville, IL	Retired	2014

Officers of the Company

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

Name	Office	2012 Compensation*
George S. Milnor	President and CEO	$183,645
Cynthia L. Ellis	Secretary	52,620
Dina M. Sackman	Treasurer	75,477
Francis B. Luitjohan	Sr. Vice President of Claims and Underwriting	110,250
Brian R. Schuelke	Assistant Vice President of Information Systems	109,740
Cynthia A. Simms	Assistant Secretary	51,960

* 2012 compensation represents the gross compensation paid to each officer reported above on behalf of all companies that are a part of the Millers First Insurance Companies.

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:

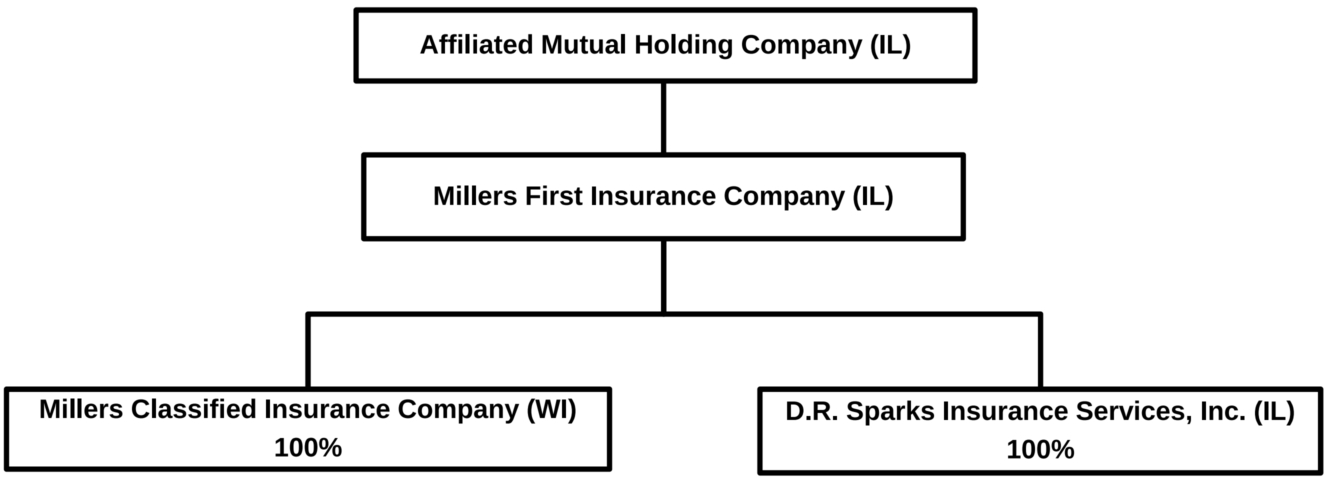
Executive Committee	Audit Committee
Thomas W. Hurd, Chair	James T. Little, Chair
William C. Bouchein	William C. Bouchein
James T. Little	R. William Schrimpf, Jr.
George S. Milnor	

Compensation Committee	Investment Committee
William C. Bouchein, Chair	George S. Milnor, Investment Officer
James T. Little	William C. Bouchein
Thomas W. Hurd	Thomas W. Hurd
	James T. Little

IV. AFFILIATED COMPANIES

Millers Classified Insurance Company 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 follows the organizational chart.

Organizational Chart
As of December 31, 2012



Affiliated Mutual Holding Company

AMHC is a mutual insurance holding company organized on April 1, 2003, to reorganize MMIA into an Illinois stock insurance company with the name Millers First Insurance Company. 100% of the outstanding shares of voting stock of MFIC was issued to and is owned by AMHC. Millers Classified Insurance Company remained a wholly owned subsidiary of MFIC and was not directly affected by the reorganization. Wisconsin approved the change of control of MCIC to AMHC on April 2, 2003.

As of December 31, 2012, the company's audited financial statement reported assets of $1,648,591, liabilities of $14,084, and surplus of $1,634,507. Operations for 2012 produced a net loss of $5,903.

Millers First Insurance Company

MFIC is a stock property and casualty insurer operating under the laws of the state of Illinois. Prior to being placed into rehabilitation, as described earlier the report, the company wrote primarily private passenger auto liability, auto physical damage, and homeowner’s multiple peril, in the same states as MCIC with the exception of Wisconsin. Prior to 2000, MFIC wrote commercial agribusiness; the company exited this market in the fourth quarter of 2000 due to changed market conditions and continued unprofitable results. MFIC continues to pay agribusiness claims as this business is in runoff.

As of December 31, 2012, the company's audited financial statement reported assets of $15,101.199, liabilities of $17,265,332, and policyholders’ surplus of $(2,164,133). Operations for 2012 produced a net loss of $2,739,832.

D.R. Sparks Insurance Services, Inc.

Prior to the Asset Purchase Agreement entered into between MFIC and RCI, described earlier in this report, DRS served as an insurance agency for business placed in Missouri and Illinois, including business placed with MFIC and MCIC. As of December 31, 2012, the company's audited financial statement reported assets of $364,999, liabilities of $668,742, and net retained earnings of $(303,743). Operations for 2012 produced a net loss of $631,780 including elimination of the net deferred tax asset of $358,520.

Agreements with Affiliates

In addition to common staffing and management control, Millers Classified Insurance Company’s relationship to its affiliates is affected by various written agreements and undertakings. A brief summary of the other agreements and undertakings follows.

Affiliated Service Agreement

MFIC, as parent, provides various management, administrative, and operational services to Millers Classified Insurance Company’s business, in accordance with an agreement effective August 1, 2009, which replaced one that was in effect since January 1, 2004.

Management services include, but are not limited to, production of financial statements and reports, appointment of agents, establishment of underwriting guidelines, reinsurance placement, securing of professional liability and other corporate insurance protection, state filing compliance, monitoring of legislative and judicial developments, internal auditing, corporate planning, administration of payroll and employees' benefits, and other general executive management responsibilities.

Administrative and operational services are provided as needed in connection with human resources, pricing and product development, marketing, sales, underwriting, claims examining and adjustment, claims litigation, management and financial accounting, data processing, and investment activities. MFIC completely directs and controls all employees performing services for the benefit of the company. All employees performing services under the agreement are employees of MFIC.

Fees under the agreement consist of both a corporate and service fee. The corporate fee is computed at $2,500 per million of net premium earned. The service fee is computed based upon direct allocation of expenses directly attributable to the company or upon allocation factors proportional to the company's operational activities, which are developed during the financial planning process each year. One-twelfth of the annual corporate fee is to be paid to MFIC each month. At least monthly the company's parent calculates the service fee and bills the company appropriately. Remuneration of the billed service fees is transacted within the month following the billing. Termination of the agreement may be initiated with 30 days' prior written notice by either party on any December 31.

Tax Allocation Agreement

Effective January 1, 2009, Millers Classified Insurance Company entered into a tax allocation agreement with AMHC, MFIC and DRS. This replaced a tax allocation agreement that was in effect since January 1, 2004. Under this agreement, AMHC files a consolidated U.S. federal income tax return that includes MCIC 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 Affiliated Group's consolidated U.S federal income tax liability. The consolidated tax liability is apportioned among the members of the Affiliated Group by the ratio of that portion of the consolidated taxable income attributable to each member of the group having taxable income bears to the consolidated taxable income. Each member pays to AMHC, with excess losses or tax credits, its allocable share of the amounts allocated pursuant to the above, no later than 10 days prior to the due date of the tax payment. Any overpayment of tax will be credited against the next installment payment liability of party to this agreement or refunded to them within 30 days. The agreement applies to all taxable years during which the company is a member of the Affiliated Group, unless earlier terminated by signed written agreement.

Reinsurance Allocation Agreement

Millers Classified Insurance Company and MFIC, entered into a reinsurance allocation agreement effective January 1, 2013. This agreement provides the fair and equitable allocation of loss and LAE recoveries, reinsurance premiums and reinsurance commissions between MCIC and MFIC as named multiple cedents under reinsurance contracts with unaffiliated third parties in accordance with SSAP 62R, paragraph 9. The agreement is continuous and may be terminated by mutual agreement between the two parties.

V. REINSURANCE

The company's reinsurance portfolio and strategy is described below. A list of the companies that have a significant amount of reinsurance in force at the time of the examination follows. All contracts include both MCIC and MFIC as reinsured parties. The contracts contained proper insolvency provisions.

Nonaffiliated Ceding Contracts

1.	Type:	Property Per Risk Excess of Loss
	Reinsurer:	As of December 1, 2012, through the runoff of existing policies in force, participation on this contract was as follows:

	Percentage
Employers Mutual Casualty Company	10%
Platinum Underwriters Reinsurance, Inc.	45
Swiss Reinsurance America Corporation	45
Total	100%

Scope:	All business classified by the company as general property, with stated exclusions
Retention:	$300,000 per risk for each loss occurrence
Coverage:	100% of the excess of the company's retention, up to a limit of $1,450,000 in respect to each risk for any loss occurrence and $2,900,000 in aggregate per loss occurrence
Premium:	Annual deposit premium of $176,600 paid in four equal installments; annual minimum premium of $141,280, subject to adjustment at the rate of 2.3% of subject gross net earned premium income In the event that the contract expires on a runoff basis, premium ceded for the runoff period is to be calculated by multiplying the gross net unearned premium of the policies in force as of the effective date the contract expires by 2.3%, to be paid in four equal quarterly installments
Commissions:	None
Effective date:	July 1, 2011
Termination:	July 1, 2012, or coverage expires on a runoff basis, solely elected by the company, coverage shall remain for those policies in force prior to the effective date of the expiration of the contract until natural expiry or first anniversary of such policies, whichever occurs first not to exceed 18 months from the expiration of the contract

2.	Type:	Property Catastrophe Excess of Loss
	Reinsured:	As of January 1, 2013, through the runoff of existing policies in force, participation on this contract was as follows:

	Percentage
Employers Mutual Casualty Company	1%
XL Re Ltd.	9
Lloyd's Underwriter Syndicate No. 2001 AML	40
Platinum Underwriters Reinsurance, Inc.	50
Total	100%

	Scope:	All business classified by the company as general property, with stated exclusions
	Retention:	The first $500,000 in respect to each loss occurrence and 5% of ultimate net losses in excess of $500,000 not to exceed 5% of $2,000,000
	Coverage:	95% of the excess of the company's retention, up to a limit of 95% of $2,000,000 in respect to each loss occurrence and 95% of $4,000,000 in aggregate. The company may reinstate coverage in the event that coverage under this agreement is exhausted limited to the original retention and limits. The company shall pay an additional premium based upon the pro rata amount of the reinstatement.
	Premium:	$437,000 paid in three equal installments on January 1, April 1 and July 1, 2013
	Commissions:	None
	Effective date:	January 1, 2013
	Termination:	October 1, 2013
3.	Type:	Casualty Excess of Loss
	Reinsured:	As of December 1, 2012, through the runoff of existing policies in force, participation on this contract was as follows:

	Percentage	
	First Layer	Second Layer
Employers Mutual Casualty Company	10%	10%
Platinum Underwriters Reinsurance, Inc.	45	45
Swiss Reinsurance America Corporation	45	45
Total	100%	100%

Scope:	All business classified by the company as casualty, with stated exclusions
Retention:	
First layer	$225,000 in respect to each loss occurrence
Second layer	$1,000,000 in respect to each loss occurrence
Coverage:	
First layer	$775,000 excess of $225,000 in respect to each loss occurrence
Second layer	$2,000,000 excess of $1,000,000 in respect to each loss occurrence
Premium:	
First layer	Annual deposit premium of $233,750 paid in quarterly installments; minimum premium of $187,000, subject to adjustment at the rate of 2.90% of subject gross net earned premium income
Second layer	Annual deposit premium of $125,000 paid in quarterly installments; minimum premium of $100,000, subject to adjustment at the rate of 1.55% of subject gross net earned premium income
Runoff	In the event that the contract expires on a runoff basis, premium ceded for the runoff period is to be calculated by multiplying the gross net unearned premium of the policies in force as of the effective date the contract expires by 2.90% and 1.55% for first and second layers of coverage, respectively, to be paid in four equal quarterly installments
Commissions:	None
Effective date:	July 1, 2011
Termination:	July 1, 2012, or coverage expires on a runoff basis, solely elected by the company, coverage shall remain for those policies in force prior to the effective date of the expiration of the contract until natural expiry or first anniversary of such policies, whichever occurs first not to exceed 18 months from the expiration of the contract

4. Type: Personal Umbrella Quota Share

Reinsured: As of December 1, 2012, through the runoff of existing policies in force, participation on this contract was as follows:

	Percentage
Employers Mutual Casualty Company	10%
Platinum Underwriters Reinsurance, Inc.	45
Swiss Reinsurance America Corporation	45
Total	100%

Scope: All business classified by the company as personal umbrella, with stated exclusions

Retention: 5% of losses each and every claim, occurrence or accident not to exceed $100,000. Additionally 5% of allocated loss adjustment expense each and every claim, occurrence or accident not to exceed 5% of $2,000,000.

Coverage: 95% of the company's liability each and every loss, each and every policy not to exceed $1,900,000. Additionally 95% of allocated loss adjustment expense each and every claim, occurrence or accident not to exceed $1,900,000.

Premium: 95% of the company's subject gross net written premium income

Commissions: A ceding commission of 25% of the company's subject premium ceded to reinsurers

Effective date: July 1, 2011

Termination: July 1, 2012, or coverage expires on a runoff basis, solely elected by the company, coverage shall remain for those policies in force prior to the effective date of the expiration of the contract until natural expiry or first anniversary of such policies, whichever occurs first not to exceed 18 months from the expiration of the contract

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, 2012, 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 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 Surplus per Examination."

Millers Classified Insurance Company
Assets
As of December 31, 2012

	Assets	Nonadmitted Assets	Net Admitted Assets
Bonds	$ 9,020,833	$ 0	$ 9,020,833
Cash, cash equivalents, and short-term investments	1,072,227	0	1,072,227
Investment income due and accrued	75,907	0	75,907
Premiums and considerations:			
Uncollected premiums and agents' balances in course of collection	15,360	8,853	6,507
Deferred premiums, agents' balances, and installments booked but deferred and not yet due	45,660	0	45,660
Accrued retrospective premiums			
Reinsurance:			
Amounts recoverable from reinsurers	84,396	0	84,396
Net deferred tax asset	1,618,368	1,618,368	0
Receivable from parent, subsidiaries, and affiliates	66,994	0	66,994
Write-ins for other than invested assets:			
Salvage/subrogation	872	0	872
Total Assets	$12,000,617	$1,627,221	$10,373,396

Millers Classified Insurance Company
Liabilities, Surplus, and Other Funds
As of December 31, 2012

Losses		$ 5,156,409
Reinsurance payable on paid loss and loss adjustment expenses		4,675
Loss adjustment expenses		1,254,276
Other expenses (excluding taxes, licenses, and fees)		93,410
Taxes, licenses, and fees (excluding federal and foreign income taxes)		(5,280)
Unearned premiums		795,055
Ceded reinsurance premiums payable (net of ceding commissions)		(129,881)
Amounts withheld or retained by company for account of others		64,900
Drafts outstanding		380,595
Payable to parent, subsidiaries, and affiliates		186,534
Total liabilities		7,800,693
Common capital stock	$ 4,000,000	
Gross paid in and contributed surplus	14,176,598	
Unassigned funds (surplus)	(15,603,895)	
Surplus as regards policyholders		2,572,703
Total Liabilities and Surplus		$10,373,396

Millers Classified Insurance Company
Summary of Operations
For the Year 2012

Underwriting Income		
Premiums earned		$ 8,820,707
Deductions:		
Losses incurred	$7,157,598	
Loss adjustment expenses incurred	1,039,205	
Other underwriting expenses incurred	3,016,178	
Total underwriting deductions		11,212,981
Net underwriting gain (loss)		(2,392,274)
Investment Income		
Net investment income earned	374,244	
Net realized capital gains (losses)	180,592	
Net investment gain (loss)		554,836
Other Income		
Net gain (loss) from agents' or premium balances charged off	(14,810)	
Finance and service charges not included in premiums	71,545	
Write-ins for miscellaneous income:		
Reinsurance charge off	2,556	
Total other income		59,291
Net income (loss) after dividends to policyholders but before federal and foreign income taxes		(1,778,147)
Federal and foreign income taxes incurred		0
Net Loss		$(1,778,147)

Millers Classified Insurance Company
Cash Flow
For the Year 2012

Premiums collected net of reinsurance			$ 6,051,959
Net investment income			532,069
Miscellaneous income			59,629
Total			6,643,657
Benefit- and loss-related payments		$8,490,351	
Commissions, expenses paid, and aggregate write-ins for deductions		4,548,391	
Federal and foreign income taxes paid (recovered)		338	
Total deductions			13,039,080
Net cash from operations			(6,395,423)
Proceeds from investments sold, matured, or repaid:			
Bonds	$8,077,004		
Total investment proceeds		8,077,004	
Cost of investments acquired (long-term only):			
Bonds	1,557,250		
Total investments acquired		1,557,250	
Net cash from investments			6,519,754
Cash from financing and miscellaneous sources:			
Other cash provided (applied)		(419,068)	
Net cash from financing and miscellaneous sources			(419,068)
Reconciliation:			
Net change in cash, cash equivalents, and short-term investments			(294,737)
Cash, cash equivalents, and short-term investments:			
Beginning of year			1,366,964
End of Year			$ 1,072,227

Millers Classified Insurance Company
Compulsory and Security Surplus Calculation
December 31, 2012

Assets		$9,020,833
Less security surplus of insurance subsidiaries		0
Less liabilities		7,800,693
Adjusted surplus		2,572,703
Annual premium:		
Lines other than accident and health	$5,669,101	
Factor	20%	
Compulsory surplus (subject to a minimum of $2 million)		$2,000,000
Compulsory Surplus Excess (or Deficit)		$ 572,703
Adjusted surplus (from above)		$2,572,703
Security surplus: (140% of compulsory surplus, factor reduced 1% for each $33 million in premium written in excess of $10 million, with a minimum factor of 110%)		2,800,000
Security Surplus Excess (or Deficit)		$ (227,297)

Millers Classified Insurance Company
Analysis of Surplus
For the Five-Year Period Ending December 31, 2012

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

	2012	2011	2010	2009	2008
Surplus, beginning of year	$ 4,713,472	$ 8,649,930	$10,581,636	$11,391,614	$10,953,142
Net income	(1,778,147)	(3,841,798)	(2,063,495)	(675,215)	501,395
Change in net unrealized capital gains/losses	2,777	(35,009)	14,232	(34,997)	
Change in net deferred income tax	(448,865)	488,485	206,574	(1,288,076)	(336,446)
Change in nonadmitted assets	78,709	(546,380)	(87,017)	1,189,310	273,523
Change in provision for reinsurance	4,756	(1,756)	(2,000)	(1,000)	
Change in surplus notes					
Surplus, End of Year	$ 2,572,703	$ 4,713,472	$ 8,649,930	$10,581,636	$11,391,614

Millers Classified Insurance Company
Insurance Regulatory Information System
For the Five-Year Period Ending December 31, 2012

The company'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	2012	2011	2010	2009	2008
#1	Gross Premium to Surplus	257%	261%	148%	117%	112%
#2	Net Premium to Surplus	220	243	137	108	103
#3	Change in Net Premiums Written	(50)*	(4)	4	(3)	(8)
#4	Surplus Aid to Surplus	0	0	0	0	0
#5	Two-Year Overall Operating Ratio	136*	126*	113*	101*	96
#6	Investment Yield	2.8*	3.2	3.6	3.9	4.3
#7	Gross Change in Surplus	(45)*	(46)*	(18)*	(7)	4
#8	Change in Adjusted Surplus	(45)*	(46)*	(18)*	(7)	4
#9	Liabilities to Liquid Assets	76	75	62	54	51
#10	Agents' Balances to Surplus	0	2	1	1	0
#11	One-Year Reserve Development to Surplus	(5)	(7)	(2)	8	(5)
#12	Two-Year Reserve Development to Surplus	(11)	(5)	5	(3)	(5)
#13	Estimated Current Reserve Deficiency to Surplus	(27)	(16)	(18)	(10)	(5)

The Change in Net Premiums Written Ratio (IRIS ratio #3) measures the change in net premiums written from the previous year and was exceptional in 2012. This primarily reflects the company running off its business beginning on July 2, 2012, and to a lesser extent competition in the personal lines market place.

The Two-Year Operating Ratio (IRIS ratio #5) measures the company’s profitability over the previous two-year period and was exceptional in 2009, 2010, 2011, and 2012. The exceptional result in 2009 was primarily due to poor underwriting results from its auto insurance business lines, increased general expenses incurred and a decrease in net premiums written and earned. In 2010 the negative underwriting results continued and worsened compared to the previous year as the results from the auto insurance business lines continued to be poor and results from homeowner's business worsened partially due to an increase in catastrophic loss events in Wisconsin that year (includes flooding in Milwaukee, Wisconsin, and a tornado in Waukesha County, Wisconsin). Auto claims in 2010 were historically higher per claim due to the effects of a new Wisconsin auto insurance law that took effect in November of 2009, which mandated auto insurance. The 2011 underwriting results were the worst in the company's recent history, and were mostly attributable to losses related to 18 different reportable catastrophic events that fell below the company's per event retention of $1.5 million under its catastrophic reinsurance coverage in effect during that period. The operational results in 2011 were also impacted by decreased net premiums written and earned compared to the previous year due to price competition in the soft personal lines market environment. The 2012 underwriting results were negative as well and were primarily due to over a dozen wind and/or hail events throughout the company's marketing territories; all but one fell under the group’s reduced 2012 reinsurance retention. As with 2011, the 2012 results were also impacted by decreased net premiums written and earned, which was already discussed in the explanation of IRIS ratio #3 above.

The Investment Yield Ratio (IRIS ratio #6) measures the amount of the company’s net investment income as a percentage of the average amount of cash and invested assets and was considered exceptional in 2012. The exceptional ratio is primarily a result of a significantly reduced investment portfolio from the disposal of investments to fund claim and general expense payments, and to a lesser extent the low bond interest rate environment.

The Gross Change in Surplus Ratio (IRIS ratio #7) was considered exceptional in 2010, 2011, and 2012 primarily due to the poor operational results discussed for ratio #5, which caused surplus to decrease those years. Another factor contributing to the exceptional ratio results in 2012 was the implementation of SSAP 101 that caused the company to nonadmit the entire net deferred tax assets balance at year-end 2012.

The Change in Adjusted Policyholders' Surplus Ratio (IRIS ratio #8) measures the improvement or deterioration in the insurer's financial condition based on operational results by factoring out changes in surplus notes, paid-in or transferred capital and surplus, which was also exceptional in 2010, 2011, and 2012 for the same reasons as ratio #7.

Growth of Millers Classified Insurance Company

Year	Admitted Assets	Liabilities	Surplus as Regards Policyholders	Net Income
2012	$10,373,396	$ 7,800,693	$ 2,572,703	$(1,778,147)
2011	18,231,591	13,518,119	4,713,472	(3,841,798)
2010	22,877,916	14,227,986	8,649,930	(2,063,495)
2009	23,169,733	12,588,097	10,581,636	(675,215)
2008	23,105,326	11,713,712	11,391,614	501,395
2007	24,155,065	13,201,923	10,953,142	461,245

Year	Gross Premium Written	Net Premium Written	Premium Earned	Loss and LAE Ratio	Expense Ratio	Combined Ratio
2012	$ 6,610,437	$ 5,669,101	$ 8,820,707	92.9%	52.2%	145.1%
2011	12,311,032	11,438,805	11,598,650	103.0	37.5	140.5
2010	12,771,211	11,869,882	11,818,822	87.7	36.8	124.5
2009	12,374,613	11,459,732	11,459,258	79.3	35.7	115.0
2008	12,767,109	11,779,134	12,002,975	71.1	31.8	102.9
2007	13,797,171	12,743,548	13,053,070	74.2	29.3	103.5

The company has reported five consecutive years of underwriting losses, with the average net underwriting loss of $2.5 million over the five-year period. Please see the explanation of the exceptional Two-Year Operating IRIS Ratio in the previous section, which describes factors contributing to the negative underwriting results over the past four years. The company has reported a net loss in the last four years. Net investment income and other policy fees completely offset the negative underwriting results in 2008 resulting in the company reporting net income in this year. The poor operational results were the primary reason of a 77% decrease in surplus compared to year-end 2008.

Gross and net premium written have decreased by approximately 52% and 56%, respectively, over the last five years. The decrease in writings prior to 2012 was attributable to competition under soft personal lines property and casualty market conditions during the period. There was a modest increase in writings in 2010 as a result of nominal rate changes applied that year and an increase in the company's policy count mainly from automobile business. The decrease in 2012 reflects the company's ceasing new business effective July 1, 2012, under a stipulation and order placed on the company by this office, and the voluntary decision by the company to begin running off its existing business effective July 2, 2012. For the four years prior to 2011 the company's gross and net writings ratios averaged 126% and 116%, respectively, which reflects a fairly conservatively leveraged company.

The company's combined ratio has been over 100% in each of the last five years and has averaged 125.6% over that period. Not only have underwriting results been negative over that period, but the company's net premium volume has not been sufficient to support its general expense structure prior to runoff in 2012. This resulted in MCIC's expense ratio increasing from 29.3% in 2007 to 38% in 2011, despite cost cutting measures taken by the company. Currently the company's expense ratio is 52.2% as a result of running off its business and high general expense structure.

Reconciliation of Surplus per Examination

The following schedule is a reconciliation of surplus as regards policyholders between that reported by the company and as determined by this examination:

	Increase	Decrease	
Surplus December 31, 2012, per annual statement			$2,572,703
Loss adjustment expenses	$0	$1,372,307	
Net increase or (decrease)	$0	$1,372,307	(1,372,307)
Surplus December 31, 2012, per Examination			$1,200,396

Examination Reclassifications

	Debit	Credit
Amounts withheld or retained by company for account of others	$64,900	$
Aggregate write-ins for liabilities		64,900

VII. SUMMARY OF EXAMINATION RESULTS

Compliance with Prior Examination Report Recommendations

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

1. Disaster Recovery Plan—It is recommended that the company periodically conduct a test of its Disaster Recovery Plan.

   Action—Compliance.

2. Reinsurance Agreements—It is recommended that the company reach a written agreement with MCIC in accordance with the NAIC Accounting Practices and Procedures Manual, SSAP 62, Paragraph 9, and that the agreement be filed with this office for prior approval under ch. Ins 40, Wis. Adm. Code.

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

Unclaimed Funds

The examination completed a review of the company's unclaimed property liability and found the balance of $64,900 to be reasonably stated in the annual statement; however, it was reported on the incorrect line of the balance sheet. The company reported the balance on page 3, line 14, "Amounts withheld or retained by company for account of others." According to the NAIC Annual Statement Instructions-Property and Casualty uncashed drafts and checks that are pending escheatment to a state are to be reported as a write-in liability. This reclassification has been reflected in Section V of this report under the heading "Examination Reclassifications." It is recommended that the company report its liabilities relating to unclaimed property pending escheatment as an aggregate write-in for liabilities in accordance with the NAIC Annual Statement Instructions-Property and Casualty.

Loss Adjustment Expenses $2,626,583

The above balance reflects an increase of $1,372,307 as a result of an examination adjustment. This office utilized a third-party actuarial firm to analyze the company's loss and loss adjustment expense reserves as of December 31, 2012. As a result of this analysis it was determined that the loss and allocated loss adjustment reserves reported by the company were within the actuarial firm's reasonable range of estimates; however, the unallocated loss adjustment expense (ULAE) reserve was not. The ULAE reserve was increased by a portion of the actual and projected expenses estimated by the company in order to complete a runoff of its existing claims. After the company had begun running off its existing claims, loss adjustment became the principal activity and, therefore, a significantly larger portion of total expenses was classified as loss adjustment expenses prompting the increase of the ULAE reserve.

In order to estimate the ULAE reserve as of December 31, 2012, the actuarial firm relied on the projected ULAE payments prepared by MCIC and on the company's actual operational results through December 31, 2013. The actuarial firm calculated the ULAE reserve by adding a portion of the actual expense payments incurred in 2013 and a portion of the expenses estimated for subsequent years. As a result, the actuarial firm calculated a total ULAE reserve of $1,734,726. This amount is significantly larger than the carried ULAE reserve of $362,419 reported as of December 31, 2012. The adjustment to this liability is reflected in Section V of this report under the heading “Reconciliation of Members’ Surplus per Examination.” It is recommended that the company establish its loss adjustment expense reserves to better reflect the change in its operations and related budgeted expense projections.

Prior to the adoption of the examination report the company was able to provide evidence that the ULAE reserve has been strengthened as of year-end 2013 to reflect the estimated ULAE costs of $748,267 for 2014, $428,596 for 2015, and $27,400 for 2016. Company management agreed to increase ULAE reserve by approximately $17,000 in the first quarter of 2014.

VIII. CONCLUSION

Policyholders' surplus as reported in the company's annual statement filings has decreased from $11,391,614 as of year-end 2008 to $2,572,703 as of year-end 2012. This represents a decrease of 77% during the period under examination. The company experienced underwriting losses in each of the five years under examination, which contributed to the decline in the company's surplus. Underwriting losses over that period have averaged $2,458,425 each year with the largest loss occurring in 2011 of $4,728,103.

Due to concerns over the company's surplus position, and the fact that the company's direct parent, MFIC, was placed into rehabilitation and under the control of the IL DOI in July of 2012, this office placed a stipulation and order on the company effective July 1, 2012, which prevented the company from writing new business, among other actions. The company voluntarily began nonrenewing business on July 2, 2012, and placed itself into runoff.

The company's day-to-day operations continue to be performed by a significantly reduced number of MFIC employees under an affiliated service agreement between the two companies. The IL DOI continues to allow employees of MFIC to runoff the operations of that company under the supervision of the IL OSD.

The examination verified the financial condition of the company as reported in its annual statement as of December 31, 2012. The examination of MCIC resulted in two recommendations, an adjustment to surplus of $(1,372,307) and a reclassification. One recommendation relates to the company reporting its unclaimed property liability on the incorrect line of the company's balance sheet, which resulted in the reclassification. The other recommendation is in regards to the company not establishing ULAE reserves as of year-end 2012 to reflect the change in its operations and related expense projections. The aforementioned finding resulted in the adjustment to the company's reported surplus.

IX. SUMMARY OF COMMENTS AND RECOMMENDATIONS

1. Page 28 - Unclaimed Funds—It is recommended that the company report its liabilities relating to unclaimed property pending escheatment as an aggregate write-in for liabilities in accordance with the NAIC Annual Statement Instructions-Property and Casualty.

2. Page 29 - Loss Adjustment Expenses—It is recommended that the company establish its loss adjustment expense reserves to better reflect the change in its operations and related budgeted expense projections.

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:

Name	Title
Jerry C. DeArmond	Insurance Financial Examiner – Advanced, Loss Reserve Specialist
Levi A. Olson	Insurance Financial Examiner
Frederick H. Thornton	Insurance Financial Examiner – Advanced, Exam Planning & Quality Control Specialist

Respectfully submitted,

John E. Litweiler
Examiner-in-Charge

XI. APPENDIX—SUBSEQUENT EVENTS

In September 2013, the company released its bulk portion of its anticipated salvage and subrogation provision, which resulted in an increase in the carried loss reserves of $538,518 and a significant decrease in surplus as reported in the company's September 30, 2013, quarterly statement. The decision made by company management to release these reserves was because no active policies remained in force in September and the emergence of storm losses had diminished.