

Report
of the
Examination of
Wisconsin Auto and Truck Dealers Insurance Corporation
Madison, Wisconsin
As of December 31, 2007

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State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

Jim Doyle, Governor
Sean Dilweg, Commissioner

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December 19, 2008

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Honorable Sean Dilweg
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:

WISCONSIN AUTO AND TRUCK DEALERS INSURANCE CORPORATION
Madison, Wisconsin

and this report is respectfully submitted.

I. INTRODUCTION

The previous examination of Wisconsin Auto and Truck Dealers Insurance Corporation (WATDIC or the company) was conducted in 2003 as of December 31, 2002. The current examination covered the intervening period ending December 31, 2007, and included a review of such 2008 transactions as deemed necessary to complete the examination.

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
- 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.

II. HISTORY AND PLAN OF OPERATION

WATDIC is licensed as a stock life and health insurance company under ch. 611, Wis. Stat. The company was incorporated on April 9, 2001, and commenced business on June 1, 2001. The company is controlled by its sole shareholder, Wisconsin Automobile and Truck Dealers Association, Inc. Insurance Trust (the Trust). The company was formed to provide health insurance to automobile and truck dealers licensed in Wisconsin who are eligible members of the Wisconsin Automobile and Truck Dealers Association, Inc. (the Association).

The majority of the current policyholders were previously covered by the Trust. The Trust, organized by the Association in 1948, was initially qualified as a Multiple Employer Welfare Association (MEWA) under Section 501(c) (9), of the Internal Revenue Code. The Association was the plan sponsor and the plan administrator for the employee benefit plan established by the Trust.

The Trust originally self-funded the health benefits it offered using a stop-loss policy from a licensed insurer. However, as a result of rulings by the US Department of Labor regarding such trusts, it was determined that as a MEWA it was not exempt from state insurance regulation.

In order to comply with Wisconsin insurance law, the Trust had to take one of the following actions: 1) liquidate, 2) become fully insured by a licensed insurer, or 3) organize as an insurance company. At the end of 1990, the Trust became fully insured through a licensed insurer and continued to provide health coverage for individuals previously covered under the Trust. In 2001, the Trust established WATDIC. The Office of the Commissioner of Insurance issued a certificate of authority to the company on April 27, 2001.

WATDIC currently writes only in the state of Wisconsin. The major products marketed by the company include group accident and health, dental, short-term disability, and short-term life insurance. Currently, seven licensed agents employed by the Association are marketing business for WATDIC.

As of December 31, 2007, there are 1,195 certificate holders and 2,314 total lives in the company's group health plan. There are 499 certificate holders and 1,005 total lives in the company's group dental plan. The average group size of dealers in the health and dental plans are 12 and 9, respectively.

The term life and disability plans are optional coverages. Most employers insured by the group health plan also participate in the term life and disability coverages. WATDIC's life and disability products are term policies that renew on the first day of each month.

The following chart is a summary of the net insurance premiums collected by the company in 2007 as reported in the company's annual statement. The company does not assume any reinsurance. The growth of the company is discussed in the "Financial Data" section of this report.

Line of Business	Premium Collected		Reinsurance Ceded	Net Premium
Medical - PPO Plan	\$10,119,270	95%	\$564,546	\$ 9,554,724
Dental	343,175	3		343,175
Short-term disability	125,413	1		125,413
Short-term life	<u>65,406</u>	<u>1</u>	<u> </u>	<u>65,406</u>
Total	<u>\$10,653,264</u>	<u>100%</u>	<u>\$564,546</u>	<u>\$10,088,718</u>

III. MANAGEMENT AND CONTROL

Board of Directors

The WATDIC board of directors consists of eight members. Members of the company's board of directors are also trustees of the Trust. Directors are elected annually, on a rotating basis, to serve three-year terms. The WATDIC bylaws require that the President of the Association automatically be named the remaining board member. Since the prior examination, two new directors were added in 2006, with one director resigning in 2007.

The board members currently receive no compensation for serving on the board but receive expense reimbursements for mileage and travel expenses to attend meetings.

Currently the board of directors consists of the following persons:

Name and Residence	Principal Occupation	Term Expires
Frank Porth Columbus, WI	Auto Dealer	2010
David R. Brantmeier Chilton, WI	Auto Dealer	2010
Donald L. Larson Baraboo, WI	Auto Dealer	2010
Richard Kornely Manitowoc, WI	Auto Dealer	2009
Ronald J. Boldt Platteville, WI	Auto Dealer	2008
Robert E. Moody River Falls, WI	Auto Dealer	2008
Walter Sommer Mequon, WI	Auto Dealer	2008
Gary D. Williams Madison, WI	President of the Association	N/A*

*See explanation provided above.

Officers of the Company

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

Name	Office	2007 Compensation
Lee A. Bauman	President	\$125,532
Gary D. Williams	Secretary	24,077
Jacquelyn S. Cyrus*	Interim Treasurer	15,748
Robert J. Foulks	Treasurer	41,830

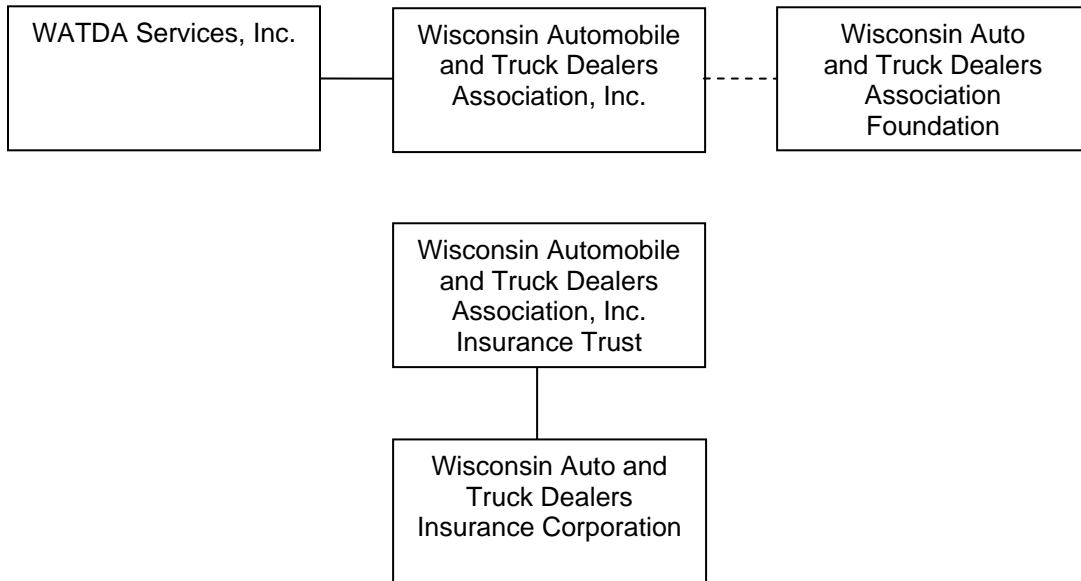
* As of the December 18, 2008, board of directors meeting, Matt LaVold was officially appointed as Treasurer of the company.

Officers are compensated by the Association. The compensation reported above is based on the time allocated to WATDIC through the services agreement with the Association. This agreement is further discussed in the "Affiliated Companies" section of this report. In February of 2008, Robert Foulks resigned as Treasurer of the company. As a result of Foulks' resignation, the board of directors appointed Jacquelyn Cyrus as interim Treasurer for the year ended December 31, 2007.

IV. AFFILIATED COMPANIES

WATDIC 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 affiliates of WATDIC follows the organizational chart.

Organizational Chart As of December 31, 2007



Wisconsin Automobile and Truck Dealers Association, Inc. (the Association)

The Association is a not-for-profit membership organization of automobile and truck dealers in the State of Wisconsin. As such, the Association is directed towards promoting the interests of its automobile and truck dealer members.

The Association provides administration and management services for WATDIC through an administrative service agreement, rather than a direct affiliation between the entities. The expense allocation to WATDIC for services was \$1,416,938 and \$1,441,733 for the periods ended December 31, 2007 and 2006, respectively. As of December 31, 2007, the audited financial statement for the Association reported assets of \$5,461,615, liabilities of \$1,922,804, and net assets of \$3,538,811. Operations for the year ended December 31, 2007, resulted in an increase in unrestricted net assets of \$189,656.

Wisconsin Automobile and Truck Dealers Association, Inc. Insurance Trust (the Trust)

The Trust, formed by the Association, is the sole shareholder of WATDIC. The Trust offers term life coverage for amounts over \$15,000, dependent life coverage and personal accident insurance coverage. These coverages are provided through Prudential Insurance and claims administration is also done by Prudential. The Trust provides coverage through WATDIC for term life up to and equal to \$15,000, short-term disability, health and dental.

These four products are marketed and administered by WATDIC. WATDIC also bills for all of the Trust's products (including Prudential products). The Trust has not actively marketed any of the Prudential products for years and has very few participants under the Prudential coverages. The employer's (dealership) participation in the Trust is contingent upon approval by WATDIC. Upon acceptance for participation, the employer shall recognize the Trust as Group Policyholder and shall agree that the trustees of the Trust have the power to sign as owner of the Master Group Contract(s) and have possession of the Contract(s).

As of December 31, 2007, the audited financial statement for the Trust reported assets of \$8,234,652, liabilities of \$104,056, and net assets of \$8,130,596. Operations for year ended December 31, 2007, resulted in a decrease in net assets of \$(385,245).

WATDA Services, Inc.

WATDA Services, Inc., a wholly owned subsidiary of the Association, is engaged in the sale and distribution of forms to auto and truck dealers in Wisconsin and also administers cafeteria plans for the members of the Association and other employers. As of December 31, 2007, the audited financial statement for WATDA Services, Inc., reported assets of \$1,517,250, liabilities of \$980,386, and stockholder's equity of \$536,864. Operations for the year ended December 31, 2007 resulted in an increase in unrestricted net assets of \$12,214.

Wisconsin Auto & Truck Dealers Association Foundation (the Foundation)

Wisconsin Auto & Truck Dealers Association Foundation is a Section 501(c) (3), Internal Revenue Code organization that is sponsored by the Association. The Foundation was incorporated and commenced business in 1991 to provide scholarships to students in automotive technical programs and other support to youth education. They also provide grants to other non-profit organizations.

Agreements with Affiliates

WATDIC has an agreement with the Association whereby the Association provides administrative services to WATDIC in connection with its group, life, health and group accident insurance to members of the Association. Under the agreement the Association assumes the responsibility for the management and administration of WATDIC's business. On or before November 1 of each year during the term of this agreement the Association presents WATDIC with a proposed budget and management service fee for the coming calendar year subject to the approval of the Association's own budget by the Association Board at its December meeting. The agreement may be terminated by either party with 90 days' written notice to the other party.

The Trust also performs premium collection services for WATDIC. As of December 31, 2007 and 2006, WATDIC reported a receivable of \$75,473 and \$47,178, respectively, from the Trust for premiums collected and not yet remitted. The receivable is further discussed in the "Accident and Health Premiums Due and Unpaid" section of this report.

V. STOP-LOSS INSURANCE

The company did not have a reinsurance agreement for 2007 but had a stop-loss liability policy in force at the time of the examination which is summarized below:

Nonaffiliated Stop-Loss Policy

Type:	Medical, Prescription Drug Plan (PDP) Stop Loss
Insurer:	Sun Life Assurance Company of Canada
Scope:	Fully insured group medical insurance policies and certificates excluding medical conversion policies
Retention:	\$200,000 per covered person per contract year
Coverage:	100% in excess of retention, subject to a maximum lifetime limit of \$2,000,000 per covered person
Premium:	\$37.00 per single employee, employee and family per month
Commission:	None
Effective date:	January 1, 2007
Termination:	December 31, 2007

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, 2007, annual statement. Also included in this section are schedules which 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."

Wisconsin Auto and Truck Dealers Insurance Corporation
Assets
As of December 31, 2007

	Assets	Nonadmitted Assets	Net Admitted Assets
Bonds	\$4,607,992	\$	\$4,607,992
Stocks:			
Preferred stocks	6,997		6,997
Common stocks	1,768,109		1,768,109
Cash, cash equivalents, and short-term investments	1,543,477		1,543,477
Receivables for securities	4,637		4,637
Investment income due and accrued	80,088		80,088
Premiums and considerations:			
Uncollected premiums and agents' balances in course of collection	14,561		14,561
Reinsurance:			
Amounts recoverable from reinsurers	15,024		15,024
Current federal and foreign income tax recoverable and interest thereon	155,000		155,000
Net deferred tax asset	97,309	97,309	0
Electronic data processing equipment and software	461		461
Write-ins for other than invested assets:			
Prepaid expenses	26,704	26,704	0
State tax recoverable	6,390		6,390
Prepaid reinsurance premium	<u>55,084</u>	<u> </u>	<u>55,084</u>
Total Assets	<u>\$8,381,833</u>	<u>\$124,013</u>	<u>\$8,257,820</u>

Wisconsin Auto and Truck Dealers Insurance Corporation
Liabilities, Surplus, and Other Funds
As of December 31, 2007

Aggregate reserve for accident and health contracts	\$ 3,260	
Contract claims:		
Life	11,900	
Accident and health	1,048,440	
Premiums and annuity considerations received in advance	756,909	
Contract liabilities not included elsewhere:		
Interest maintenance reserve	2,423	
General expenses due or accrued	131,237	
Amounts withheld or retained by company as agent or trustee	935	
Remittances and items not allocated	73,465	
Miscellaneous liabilities:		
Asset valuation reserve	351,444	
Payable to parent, subsidiaries and affiliates	<u>9,541</u>	
 Total liabilities		 \$2,389,554
 Common capital stock	 90	
Gross paid in and contributed surplus	5,006,444	
Unassigned funds (surplus)	<u>861,731</u>	
 Total capital and surplus		 <u>5,868,265</u>
 Total Liabilities, Capital and Surplus		 <u>\$8,257,819</u>

Wisconsin Auto and Truck Dealers Insurance Corporation
Summary of Operations
For the Year 2007

Premiums and annuity considerations for life and accident and health contracts	\$10,088,718	
Net investment income	263,071	
Amortization of interest maintenance reserve	<u>(10,286)</u>	
Total income items		\$10,341,503
Death benefits	35,900	
Disability benefits and benefits under accident and health contracts	8,862,023	
Increase in aggregate reserves for life and accident and health contracts	<u>(9,487)</u>	
Subtotal	8,888,436	
Commissions on premiums, annuity considerations, and deposit-type contract funds (direct business only)	60,168	
General insurance expenses	2,043,194	
Insurance taxes, licenses and fees, excluding federal income taxes	<u>57,790</u>	
Total deductions		<u>11,049,588</u>
Net gain (loss) from operations before dividends to policyholders and federal income taxes		(708,085)
Federal and foreign income taxes incurred (excluding tax on capital gains)		<u>(149,468)</u>
Net gain (loss) from operations after dividends to policyholders and federal income taxes and before realized capital gains or losses		(558,617)
Net realized capital gains or (losses)		<u>322,741</u>
Net Loss		<u>\$ (235,876)</u>

Wisconsin Auto and Truck Dealers Insurance Corporation
Cash Flow
For the Year 2007

Premiums collected net of reinsurance	\$10,052,766	
Net investment income	<u>247,304</u>	
Total		\$10,300,070
Benefit- and loss-related payments	9,103,412	
Commissions, expenses paid, and aggregate write-ins for deductions	2,152,912	
Federal and foreign income taxes paid (recovered)	<u>(141,553)</u>	
Total deductions		<u>11,114,771</u>
Net cash from operations		(814,701)
Proceeds from investments sold, matured, or repaid:		
Bonds	\$7,748,054	
Stocks	3,876,711	
Net gains (losses) on cash, cash equivalents, and short-term investments	(58)	
Miscellaneous proceeds	<u>41,066</u>	
Total investment proceeds		11,665,773
Cost of investments acquired (long-term only):		
Bonds	7,270,506	
Stocks	<u>2,840,652</u>	
Total investments acquired		<u>10,111,158</u>
Net cash from investments		1,554,615
Cash from financing and miscellaneous sources:		
Other cash provided (applied)	<u>170,322</u>	
Net cash from financing and miscellaneous sources		<u>170,322</u>
Reconciliation:		
Net change in cash, cash equivalents, and short-term investments		910,236
Cash, cash equivalents, and short-term investments:		
Beginning of year		<u>633,242</u>
End of Year		<u>\$ 1,543,478</u>

**Wisconsin Auto and Truck Dealers Insurance Corporation
Compulsory and Security Surplus Calculation
December 31, 2007**

Assets		\$8,257,819	
Less investments exceeding WI limitations		0	
Less liabilities		<u>2,389,554</u>	
Adjusted surplus			\$5,868,265
Annual premium:			
Individual life and health	\$ 223,881		
Factor	<u>15%</u>		
Total		33,582	
Group life and health	\$9,894,395		
Factor	<u>10%</u>		
Total		989,440	
Compulsory surplus (subject to a \$2,000,000 minimum)			<u>2,000,000</u>
Compulsory Surplus Excess or (Deficit)			<u>\$3,868,265</u>
Adjusted surplus (from above)			\$5,868,265
Security surplus: (140% of compulsory surplus, factor reduced 1% for each \$33 million in premium written in excess of \$10 million, with a minimum of 110%)			<u>2,800,000</u>
Security Surplus Excess or (Deficit)			<u>\$3,068,265</u>

**Wisconsin Auto and Truck Dealers Insurance Corporation
Reconciliation and Analysis of Surplus
For the Five-Year Period Ending December 31, 2007**

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

	2007	2006	2005	2004	2003
Capital and surplus, beginning of year	\$6,183,111	\$6,598,079	\$5,234,319	\$ 6,314,400	\$5,315,280
Net income	(235,876)	(326,395)	1,457,300	(1,056,673)	749,998
Change in net unrealized capital gains/losses	(177,702)	118,525	(41,072)	35,574	176,995
Change in net deferred income tax	(4,573)	(56,928)	(19,822)	(9,218)	118,000
Change in nonadmitted assets and related items	(65,904)	16,229	(52,173)	(5,216)	19,035
Change in asset valuation reserve	(30,791)	(166,399)	19,527	(44,548)	(64,908)
Prior Period Audit Adjustment	<u>200,000</u>	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Capital and Surplus, End of Year	<u>\$5,868,265</u>	<u>\$6,183,111</u>	<u>\$6,598,079</u>	<u>\$ 5,234,319</u>	<u>\$6,314,400</u>

**Wisconsin Auto and Truck Dealers Insurance Corporation
Insurance Regulatory Information System
For the Five-Year Period Ending December 31, 2007**

The company's NAIC Insurance Regulatory Information System (IRIS) results for the period under examination are summarized below.

Ratio	2007	2006	2005	2004	2003
#1 Net change in capital and surplus	-5%	-6%	26%	-17%	19%
#2 Gross change in capital and surplus	-5	-6	26	-17	19
#3 Net income to total income	-2	-3	7	-4	4
#4 Adequacy of investment income	0	0	0	0	0
#5 Nonadmitted to admitted assets	2	1	1	0	0
#6 Total real estate and mortgage loans to cash and invested assets	0	0	0	0	0
#7 Total affiliated investments to capital and surplus	0	2	2	0	1
#8 Surplus relief	0	0	0	0	0
#9 Change in premium	-8	-47	-15	20	28
#10 Change in product mix	0.2	0.1	0	0.1	0
#11 Change in asset mix	1.7	4.2	1.8	4.7	3
#12 Change in reserving ratio	0	0	0	0	0

There were no unusual results.

Growth of Wisconsin Auto and Truck Dealers Insurance Corporation

Year	Admitted Assets	Liabilities	Capital and Surplus
2007	\$ 8,257,819	\$2,389,554	\$5,868,265
2006	9,180,324	2,997,213	6,183,111
2005	11,426,051	4,827,972	6,598,079
2004	11,748,766	6,514,447	5,234,319
2003	11,866,719	5,552,319	6,314,400
2002	8,818,775	3,503,495	5,315,280

Net Life Premiums, Accident and Health Premiums

Year	Life Insurance Premiums	Accident and Health Insurance Premiums	Totals
2007	\$ 66,036	\$10,052,240	\$10,118,276
2006	69,207	10,908,302	10,977,509
2005	106,994	20,708,473	20,815,467
2004	174,155	25,362,570	25,536,725
2003	206,336	20,197,338	20,403,674
2002	175,736	15,757,404	15,933,140

Life Insurance In Force (in thousands)

Year	Gross Risk In Force	Ceded	Net
2007	\$11,607	\$0	\$11,607
2006	12,731	0	12,731
2005	15,794	0	15,794
2004	21,517	0	21,517
2003	25,568	0	25,568
2002	25,979	0	25,979

Accident and Health

Year	Net Premiums Earned	Incurred Claims and Cost Containment Expenses	Commissions Incurred	Other Expenses Incurred	Combined Loss and Expense Ratio
2007	\$10,088,718	\$ 8,776,956	\$60,168	\$1,925,074	106.7%
2006	11,116,914	9,928,787	39,641	2,010,323	107.8
2005	21,464,234	17,070,476	40,607	2,557,216	91.6
2004	24,665,715	24,056,846	68,843	2,357,513	107.4
2003	18,727,519	15,199,364	36,258	2,203,885	93.1
2002	17,307,813	14,040,774	0	1,912,118	92.2

The company's capital and surplus declined in 2006 and 2007 as a result of net losses in both of those years. These losses were the result of many dealerships changing their health benefit offering from lower deductible/higher premium plans to higher deductible/lower premium plans for cost-saving measures. Additionally, two large dealerships left the company.

The company's assets and liabilities declined in 2006 and 2007. Net losses caused the company to draw upon cash reserves and investments to obtain cash for operations. Claim reserves decreased as determined by company actuary.

Life Insurance In Force has steadily declined since 2002 as a result of group terminations and lower participation levels. For Accident and Health, the change in the Combined Loss and Expense Ratio in 2005, was the result of a large, high-loss dealership not being retained. After 2005, the Combined Loss and Expense Ratio increased due to spreading general expenses over fewer premiums.

Reconciliation of Surplus per Examination

The following schedule is a reconciliation of surplus between that reported by the company and as determined by this examination: No adjustments were made as a result of the examination.

VII. SUMMARY OF EXAMINATION RESULTS

Compliance with Prior Examination Report Recommendations

There were 16 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. Corporate Governance—It is recommended that the company file a complete and final version of the bylaws with the commissioner and any amendments thereto within 60 days after adoption of this examination report to comply with s. 611.12 (4), Wis. Stat.

Action—Compliance

2. Affiliated Agreements—It is recommended that the company enter into a formal written agreement with the Trust for services rendered identifying the rights and responsibilities of both parties.

Action—Noncompliance; see “Summary of Current Examination Results.”

3. Conflict of Interest Questionnaire—It is recommended that the company establish a procedure that requires each of its directors, officers, and key employees to annually disclose conflict of interests to the board of directors through a questionnaire, and that the disclosures be retained in compliance with the directive of the Commissioner of Insurance.

Action— Noncompliance; see “Summary of Current Examination Results.”

4. Listing of Agents—It is recommended that the company report to the commissioner all appointments and terminations of insurance agents in compliance with s. 628.11, Wis. Stat.

Action—Compliance

5. Agent Commissions—It is recommended that the company report agent commissions in accordance with the NAIC Annual Statement Instructions.

Action—Compliance

6. Policy Files—It is recommended that the company obtain a signed application with each of its groups.

Action—Compliance

7. Control Environment—It is recommended that the company have proper segregation of duties for the life and disability claims process.

Action—Compliance

8. Investment Restrictions—It is recommended that company compute compulsory and security surplus according to s. 620.03, Wis. Stat., and s. Ins 6.20 (5), Wis. Adm. Code.

Action—Compliance

9. Investment Restrictions—It is further recommended that the company comply with the special investment restrictions for new insurers, pursuant to s. 620.03, Wis. Stat., and s. Ins 6.20 (5), Wis. Adm. Code.

Action—Compliance

10. Bonds—It is recommended that the company maintain purchase invoices and properly report its investments on Schedule D according to the NAIC Annual Statement Instructions.

Action—Compliance

11. Accident and Health Premiums Due and Unpaid—It is recommended that the company exclude premiums paid to the Trust from Accident and Health Premiums Due and Unpaid.

Action—Compliance

12. Premiums and Annuity Considerations for Life and Health Contracts Received in Advance—It is recommended that the company record advance premiums collected from policyholders by the Trust in its financial statements.

Action—Compliance

13. Reinsurance Payable—It is recommended that the company accurately report amounts payable to reinsurers.

Action—Compliance

14. Contract Claim Reserve—It is recommended that the company use its historical experience to apportion its accident and health claim reserves rather than using assumptions.

Action—Compliance

15. Contract Claim Reserve—It is recommended the company report estimates for accident and health claims incurred, but unreported in Exhibit 8.

Action—Compliance

16. IT Environment—It is recommended that the company secure physical access to its computer.

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.

Disaster Recovery Plan

The examination found that the company has a formal disaster recovery plan. However, it was observed that the company has not tested its plan to validate if it is executable. Recovery of the IT infrastructure, the relocation of the offices, and the manual procedures performed by company personnel should be included. Testing of this plan should be performed at least annually. It is recommended that the company test its disaster recovery plan on an annual basis.

Information Technology

The examination review of the company's information technology system noted that weak password controls exist within its network. Weak controls increase the likelihood of passwords being compromised. In addition, passwords are shared with others creating the possibility of unauthorized use of user accounts. Stronger password controls should include a minimum number of six characters and a requirement that passwords be changed at least quarterly but not more often than daily. A password history should be maintained to prevent using the same password. In addition, access should be disabled after a pre-determined number of failed authentications. It is recommended that the company adopt procedures to strengthen its password controls.

Conflict of Interest Questionnaire

Pursuant to a Directive of the Commissioner of Insurance, insurers are required to have officers, directors, and key employees disclose potential conflicts of interest to the board of directors. The previous examination recommended that the company implement procedures to comply with the Directive. During the current examination review, the company was only able to provide conflict of interest statements for each of its officers, directors, and key employees for the year 2008. It is again recommended that the company establish a procedure that requires each

of its directors, officers, and key employees to annually disclose conflict of interests to the board of directors through a questionnaire and that the disclosures are retained in compliance with the Directive of the Commissioner of Insurance.

Health Blank Statement

According to the NAIC Annual Statement Instructions, a reporting entity that is licensed as a Life and Health Insurer which passes the Health Statement Test in the General Interrogatories must complete the Health Statement blank rather than the Life, Accident and Health blank beginning with the first quarter statement for the second year following the reporting year in which the reporting entity passes the Health Statement Test. The examination noted that the company has passed the Health Test for several years and should be filing on the Health quarterly and annual statement blanks. It is recommended that the company file its future quarterly and annual statements using the Health Statement blank when so required by the NAIC Annual Statement Instructions.

Stop-Loss Insurance

The examiners' review of the company's stop-loss policy noted that the insolvency provisions did not explicitly indicate that, pursuant to s. 645.58, Wis. Stat., amounts recoverable by the liquidator shall not be reduced as a result of delinquency proceedings. It is recommended that the company's stop-loss policy be amended to state that the obligations under the stop-loss policy will survive in the event of insolvency of WATDIC without diminution because of the insolvency.

Prior Period Adjustment

The examiners reviewed the 2007 annual statement Notes to Financial Statements number 2 A, which stated "As of June 30, 2007, the balance sheet and surplus were decreased by \$200,000 for a prior period audit adjustment due to a decrease in accident and health aggregate reserves and the related decrease in federal income tax benefit."

The examination review of the 2007 annual statement capital and surplus account found that the company recorded a \$200,000 prior period adjustment to surplus which the examination determined to be a change in estimate. The examiners note that "changes in loss

reserve estimates" is cited as an example of a change in accounting estimate in the NAIC Accounting Practices and Procedures Manual, SSAP No. 3, paragraphs 6 and 7. Changes in estimates are to be recorded through the income statement in the period in which the change becomes known and not as a direct charge to surplus as a prior period adjustment. It is recommended that the company recognize and account for changes in accounting estimates through the income statement in the period in which the change becomes known and not as a direct charge to surplus as a prior period adjustment pursuant to NAIC Accounting Practices and Procedures Manual SSAP No. 3, paragraphs 6 through 8.

Claim Reserves

The examination review of subsequent quarterly annual statements for the periods ending March 31, June 30, and September 30, 2008, revealed that the company's claim reserve liability amount remained unchanged compared to that reported at year-end 2007. The company indicated that while the company may make adjustments to its claims reserves in unusual circumstances, there is not a regular quarterly review of claims activity and assessment of the claim reserves for reasonableness. It is recommended that the company adopt procedures to review the level of claims activity and assess the reasonableness of its reported claim reserve liability on a quarterly basis.

Holding Company

The examination review of the 2007 annual statement Schedule Y, Part 1, identified the Trust as owning WATDIC with only those two entities shown. Schedule Y, Part 1, did not identify the Wisconsin Automobile and Truck Dealers Association, Inc., as being an affiliate of WATDIC, although the company did report transactions between WATDIC and the Association on Schedule Y, Part 2, and in the Notes to Financial Statements.. It is recommended that the company show the Association in the organizational chart in Schedule Y, Part 1, of future annual statements.

Affiliated Agreements

The prior examination recommended that the company enter into a formal written agreement with the Trust for services rendered identifying the rights and responsibilities of both

parties. The examiners inquired with the company to determine if a formal written agreement with the Trust was executed. The company indicated that there still is no agreement between the Trust and the company for these premium collection services.

The examination review of the settlement practices of inter-company transactions revealed that affiliated balances are not being settled on a regular basis. The Trust collects premiums from policyholders and remits the premium received to WATDIC. However, the Trust retains a \$50,000 cash balance and may not remit all cash received. As a result, the company records a receivable from the Trust, which is the balance in this account. The company indicated the balance in the Trust receivable account was allowed to increase due to insufficient cash flow from the Trust's investments. A review of 2008 affiliated transactions indicated the Trust recently made a payment to the company after the Trust liquidated some investments. The company indicated that the Trust's investment advisors are working to make additional cash available so that this receivable does not continue to grow.

The Trust currently collects WATDIC premium from Association members and remits the premium to WATDIC, as noted above. As noted above, the Trust has not fully settled the premium balance due to WATDIC on a regular basis, and the company has not complied with the prior recommendations that the arrangement be supported by a written agreement. The examination finds no reason for WATDIC premiums to be collected by the Trust and remitted to WATDIC. It is recommended that all premium for WATDIC policies be collected directly by WATDIC from policyholders and deposited directly in WATDIC bank accounts rather than be collected through the Trust as required by s. 610.23, Wis. Stat.

The examiners also reviewed the trial balance provided by the company and it revealed that WATDIC netted its inter-company payable to the Association against its inter-company receivable from the Trust on the 2007 annual statement liabilities page, line 24.4. The examiners determined that the two balances did not have the right of offset as defined in the NAIC Accounting Practices and Procedures Manual SSAP No. 64, paragraph 5. Amounts due to or from affiliates shall be offset and reported net only when each of the two parties owes the other determinable amounts and the reporting party has the right to setoff the amount owed with

the amount owed by the other party. It is recommended that the company comply with NAIC Accounting Practices and Procedures Manual SSAP No. 64, paragraph 5.

Pharmacy Rebates

The examination's review of 2008 transactions found that the company received two pharmacy rebate checks related to its prescription drug business from its pharmacy benefit manager (PBM). The first check, received in October 2008, covered the period January 1, 2004, through March 31, 2008. The second check, received in November 2008, covered the period January 1, 2006, through June 30, 2008. The two checks, totaling \$133,820, are deemed immaterial to the company's surplus; therefore, the examination did not make an adjustment to surplus. WATDIC did not accrue a receivable for the pharmacy rebates on its 2007 annual statement. The pharmacy rebates were withheld by the PBM until they received a signed agreement from WATDIC in 2008. It is recommended that WATDIC accrue for its pharmacy rebate receivables on future annual statements in accordance with SSAP No. 84 and disclose the method used to estimate pharmacy rebates in the Notes of future annual statements.

HIRSP Accrual

The examination determined that the company did not accrue for the Health Insurance Risk-Sharing Plan (HIRSP) assessment at year-end 2007. In accordance with NAIC Accounting Practices and Procedures Manual SSAP No. 35, Guaranty Funds and Other Assessments, an accrual for assessments should be established when information is available prior to the issuance of the financial statements when it is probable that an asset has been impaired or a liability has been incurred at the date of the financial statements and the amount can be reasonably estimated.

The company received notice of the first of two assessments in January 2008, prior to the 2007 annual statement being filed, but did not establish a liability for the assessment obligation on the annual statement. The second assessment based on 2007 premium was received after the annual statement was filed. The total HIRSP assessments paid in 2008 based on 2007 premium was \$46,535. The company should have accrued a liability on its 2007 annual statement to estimate the total obligation to HIRSP that was based on 2007 premium. The

omitted \$46,535 accrual is deemed immaterial to the company's surplus; therefore, the examination did not make an adjustment to surplus. However, it is recommended that the company fully accrue for the HIRSP assessments in future annual statements in accordance with NAIC Accounting Practices and Procedures Manual SSAP No. 35.

VIII. CONCLUSION

The examination determined that as of December 31, 2007, the company had total admitted assets of \$8,257,819, total liabilities of \$2,389,554, and policyholder's surplus of \$5,868,175. The examination did not make any adjustments to surplus as reported in the annual statement, as the various differences found by the examination were deemed immaterial relative to the company's reported surplus.

The examination found that the Association failed to fully remit WATDIC premium collected to WATDIC. The examination recommends that WATDIC directly collect its premium from policyholders rather than having the Association collect the premium and remit it to WATDIC. The examination found that WATDIC failed to accrue for its pharmacy benefit rebates receivable, and its HIRSP assessments payable. The examination found that the company improperly offset balance due from the Trust against balances due to the Association on its annual statement when they should have been shown as separate assets and liabilities. The examination found that the company should begin filing on the Health blank instead of the Life, and Accident and Health blank for future filings. The examination found that the company failed to comply with two of the prior examination's recommendations.

Policyholder's surplus has declined 11.1% from \$6,597,989 on December 31, 2005, to \$5,868,175 as of December 31, 2007. This can be attributed to net losses due to dealerships changing their health benefit offering from lower deductible/higher premium plans to higher deductible/lower premium plans for cost-saving measures. In addition, two large dealerships left the company. These losses over the past two years have resulted in the company drawing upon cash reserves and investments to obtain cash for operations.

IX. SUMMARY OF COMMENTS AND RECOMMENDATIONS

1. Page 25 - Disaster Recovery Plan—It is recommended that the company test its disaster recovery plan on an annual basis.
2. Page 25 - Information Technology—It is recommended that the company adopt procedures to strengthen its password controls.
3. Page 26 - Conflict of Interest Questionnaire—It is again recommended that the company establish a procedure that requires each of its directors, officers, and key employees to annually disclose conflict of interests to the board of directors through a questionnaire and that the disclosures are retained in compliance with the Directive of the Commissioner of Insurance.
4. Page 26 - Health Blank Statement—It is recommended that the company file its future quarterly and annual statements using the Health Statement blank when so required by the NAIC Annual Statement Instructions.
5. Page 26 - Stop-Loss Insurance—It is recommended that the company's stop-loss policy be amended to state that the obligations under the stop-loss policy will survive in the event of insolvency of WATDIC without diminution because of the insolvency.
6. Page 27 - Prior Period Adjustments—It is recommended that the company recognize and account for changes in accounting estimates through the income statement in the period in which the change becomes known and not as a direct charge to surplus as a prior period adjustment pursuant to NAIC Practices and Procedures Manual SSAP No. 3, paragraphs 6 through 8.
7. Page 27 - Claim Reserves—It is recommended that the company adopt procedures to review the level of claims activity and assess the reasonableness of its reported claim reserve liability on a quarterly basis.
8. Page 27 - Holding Company—It is recommended that the company show the Association in the organizational chart in Schedule Y, Part 1, of future annual statements.
9. Page 28 - Affiliated Agreements—It is recommended that all premium for WATDIC policies be collected directly by WATDIC from policyholders and deposited directly in WATDIC bank accounts rather than be collected through the Trust as required by s. 610.23, Wis. Stat.
10. Page 29 - Affiliated Agreements—It is recommended that the company comply with NAIC Accounting Practices and Procedures Manual SSAP No. 64, paragraph 5.
11. Page 29 - Pharmacy Rebates—It is recommended that WATDIC accrue for its pharmacy rebate receivables on future annual statements in accordance with SSAP No. 84 and disclose the method used to estimate pharmacy rebates in the Notes of future annual statements.
12. Page 30 - HIRSP Accrual—It is recommended that the company fully accrue for the HIRSP assessments in future annual statements in accordance with NAIC Accounting Practices and Procedures Manual SSAP No. 35.

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
Thomas Houston	Insurance Financial Examiner
Linda Meinholz	Insurance Financial Examiner
Jerry DeArmond	Insurance Financial Examiner--Advanced

Respectfully submitted,

DuWayne Kottwitz
Examiner-in-Charge

Subsequent Events

The company settled out of court with one of its dealerships over a dispute regarding the termination of insurance coverage. The dealership contended that the company's termination was done improperly and that the dealership incurred costs it otherwise would not have. The dealership and the company have agreed to settle and dismiss the dispute without admission of liability by either party for \$312,500.

On December 1, 2008, the company issued a payment in the amount of \$166,250 to the dealership. Beginning in January 2009, nine monthly installments of \$16,250 will be due on or before the fifteenth day of each month.

As of December 31, 2008, the Association's current President will be resigning. A new successor has been named and has been working with the Association since November of 2008. The Association's new President was officially installed in January of 2009.