Report

of the

Examination of

Columbus Mutual Town Insurance Company

Beaver Dam, Wisconsin

As of December 31, 2012

TABLE OF CONTENTS

Page

State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

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August 26, 2013

Honorable Theodore K. Nickel
Commissioner of Insurance
State of Wisconsin
125 South Webster Street
Madison, Wisconsin 53703

Commissioner:

In accordance with your instructions, an examination has been performed as of December 31, 2012, of the affairs and financial condition of:

COLUMBUS MUTUAL TOWN INSURANCE COMPANY
Beaver Dam, Wisconsin

and the following report thereon is respectfully submitted:

I. INTRODUCTION

The previous examination of Columbus Mutual Town Insurance Company (the company) was made in 2011 as of December 31, 2010. The current examination covered the intervening time period ending December 31, 2012, and included a review of such subsequent transactions deemed essential to complete this examination.

The "Summary of Examination Results" contains elaboration on all areas of the company's operations. Special attention was given to the action taken by the company to satisfy the recommendations and comments made in the previous examination report.

The company is annually audited by an independent public accounting firm as prescribed by s. Ins 50.05, Wis. Adm. Code. An integral part of this compliance examination was the review of the independent accountant's work papers. Based on the results of the review of these work papers, alternative or additional examination steps deemed necessary for the completion of this examination were performed. The examination work papers contain documentation with respect to the alternative or additional examination steps performed during the course of the examination.

In addition to auditing, the public accounting firm performs non-auditing services for the company, including bookkeeping services. On December 27, 2010, an exemption was granted by the Commissioner, pursuant to s. Ins 50.08 (5), Wis. Adm. Code, permitting the independent auditor to perform this non-audit work for the company.

The company was organized as a town mutual insurance company on July 5, 1873, under the provisions of the then existing Wisconsin Statutes. The original name of the company was the Columbus, Columbia County Wisconsin Farmers Mutual Insurance Company. Subsequent amendments to the company's articles and bylaws changed the company's name to that presently used.

During the period under examination, there were no amendments to the articles of incorporation. There were no amendments to the bylaws.

The company is currently licensed to write property, including windstorm and hail, and nonproperty insurance. The company is currently licensed to write business in the following counties:

Dane	Jefferson
Dodge	Richland
Columbia	Sauk
Fond du Lac	Washington
Green Lake	Waukesha
Iowa	

A review was made of the policy and application forms currently used by the company. The company issues approved policies with or without endorsements for terms of one year with premiums payable on the advance premium basis. The company did not charge any other fees to policyholders until recent changes as discussed below.

Business of the company is acquired through 16 agents, 1 of whom is a director of the company. Agents are presently compensated for their services as follows:

Type of Policy	Compensation
All policies (new and renewal)	15%

Agents do not have authority to adjust losses. One director, George Decker, has the authority to adjust losses up to $5,000. Outside adjusting firms are used for claims in excess of $5,000. The director-adjuster receives $45.00 for each loss adjusted plus $0.505 per mile for travel allowance. An additional $13.00 per hour is paid to the director-adjuster for claims that take longer than one hour to adjust.

Policyholders may participate in the management and control of the company by attending and voting at all annual or special meetings of the members. No member may vote by proxy. The annual meeting of the company for the election of directors and special meetings of the company are held in accordance with its articles of incorporation.

Board of Directors

The board of directors consists of seven members divided into three classes. One class is elected at each annual meeting for a term of three years. Vacancies on the board may be filled by the directors for the interim to the next annual meeting when a director shall be chosen for the unexpired term.

The current board of directors consists of the following policyholders of the company:

Name	Principal Occupation	Residence	Expiry
Joseph Wedel*	Agent & Company Manager	Beaver Dam, WI	2014
Gordon Neuman	Mechanic	Randolph, WI	2015
Dan Hemling	Retired	Fall River, WI	2013
George Drecker	Retired	Fall River, WI	2015
Jerry Weissmann	Retired	Columbus, WI	2013
Ronald Weiland	Farmer	Columbus, WI	2014
Jeffery Schaefer	Farmer	Watertown, WI	2014

Directors who are also agents are identified with an asterisk.

Members of the board currently receive $60.00 for half-day meetings attended, $125.00 for all-day meetings, and $0.505 per mile for travel expenses.

Section 612.13 (1m), Wis. Stat., requires:

(1) If a town mutual has fewer than nine directors, no more than one director may be an employee or representative of the town mutual; and

(2) Employees and representatives of a town mutual may not constitute a majority of its board.

The company is in compliance with these requirements.

Officers

Officers are elected by the board of directors from among its members and hold office for one year or until their successors are duly elected and qualified. Officers serving at the present time are as follows:

Name	Office	2010 Total Compensation*
Gordon Neuman	President	$ 1,200
Joseph Wedel	Secretary/Treasurer	70,235
Dan Hemling	Vice President	485

* Reported compensation is the total compensation paid by the insurer for the year and includes salary, commissions, director fees and rental income as applicable. Joseph Wedel receives commissions as an agent for the company. In 2012 he received $52,735 in commissions, which is included in the total compensation amount.

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:

Claims Adjusting Committee
All Directors

Inspection Committee
All Directors

Investment Committee
All Directors

Growth of Company

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

Year	Net Premiums Earned	Policies In Force	Net Income	Admitted Assets	Policyholders' Surplus
2012	$270,072	837	$ (24,973)	$1,947,744	$1,404,554
2011	277,889	794	(125,963)	1,799,521	1,447,719
2010	328,658	786	(23,801)	1,914,917	1,548,432

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

Year	Gross Premiums Written	Net Premiums Written	Policyholders' Surplus	Writings Ratios Net	Writings Ratios Gross
2012	$802,228	$297,677	$1,404,554	21%	57%
2011	706,931	283,921	1,447,719	20	49
2010	689,820	266,708	1,548,432	17	45

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

Year	Net Losses and LAE Incurred	Other Underwriting Expenses Incurred	Net Premiums Earned	Loss Ratio	Expense Ratio	Com-posite Ratio
2012	$206,390	$164,224	$270,072	76%	55%	132%
2011	285,375	158,773	277,889	103	56	159
2010	249,943	152,220	328,658	76	57	133

Growth has not been evidenced over the past two years as net premiums earned have steadily declined, net underwriting income and net losses have been severe, and policyholders' surplus is in retreat. During the two-year period under examination, admitted assets increased 1.7% to $1,947,744, surplus decreased 9.3% to $1,404,554, and net premiums earned decreased 17.8% to $270,072.

The company has shown a consistent pattern of underwriting losses in recent years including both years under examination. The loss ratio reached a five-year maximum in 2011 at 103%. This maximum was caused by a large hail storm in that year. In spite of the catastrophe in 2011 the company's loss ratios have been consistently high.

The loss ratio has averaged 82.8% since 2008. The company's high loss ratios are due to the company's poor underwriting practices, as was noted in the previous examination. To remedy this condition the reinsurer required the company to enter into a formal agreement effective in September of 2012. The agreement with Wisconsin Reinsurance Corporation (WRC) combines reasonable rate increases with professional inspection programs and various other best practice measures to get the loss ratios more in line with industry averages. In the view of the management several of these increases, programs, and measures were being implemented during the time of the examination fieldwork. Further discussion of these measures is contained in the section of this report entitled "Underwriting."

The expense ratio has plateaued in recent years at approximately 56%, whereas the ratio has historically been significantly lower. This is mainly due to increased reinsurance costs that have caused a decline in net premiums over the past five years. The professional inspection and loss adjustment programs, discussed in the previous paragraph, are expected to increase the expense ratio in future years.

The composite ratios are significantly above normal in recent years, reporting 132%, 159%, and 133% for the years 2012, 2011, and 2010, respectively.

II. REINSURANCE

The examiners' review of the company's reinsurance portfolio revealed there is currently one ceding treaty. The treaty contained a proper insolvency clause and complied with s. Ins 13.09 (3), Wis. Adm. Code, concerning maximum wind loss. Company retentions of risk complied with s. Ins 13.06, Wis. Adm. Code.

Reinsurer:	Wisconsin Reinsurance Corporation
Effective date:	January 1, 2013, continuous
Termination provisions:	Either party may terminate the contract and/or its exhibits as of any subsequent January 1 by giving to the other party at least 90 days' advance notice in writing

The coverages provided under this treaty are summarized as follows:

1.	Type of contract:	Exhibit AX1 Excess of Loss
	Lines reinsured:	Liability
	Company's retention:	$5,000 each and every loss occurrence
	Coverage:	100% of each and every loss, including loss adjustment expense, subject to the maximum policy limits of: a. $1,000,000 per occurrence, single limit or combined for bodily injury and property damage liability b. $1,000,000 split limits, in any combination of bodily injury and property damage liability c. $5,000 for medical payments, per person; $25,000 per accident
	Reinsurance premium:	60% of the company's gross premium written Annual deposit premium = $79,200
2.	Type of contract:	Exhibit B1 First Surplus
	Lines reinsured:	All property business
	Coverage:	$250,000 or less in respect to a risk; on a pro rata basis up to 50% of such risk Over $250,000 in respect to a risk; on a pro rata basis up to $800,000 Pro rata portion of each and every loss, including loss adjustment expense, corresponding to the amount of the risk ceded
	Reinsurance premium:	Pro rata portion of all premiums corresponding to the amount of each risk ceded

	Ceding commission:	Commission rate = 15% Profit commission = 15%
3.	Type of contract:	Exhibit C1 First Excess of Loss
	Lines reinsured:	All property business
	Company's retention:	$50,000
	Coverage:	100% of each and every loss in excess of $50,000 up to $80,000, including loss adjustment expense
	Reinsurance premium:	Sum of the preceding four years' losses incurred (paid plus outstanding) by the reinsurer, divided by the total of the net premiums written for the same period, multiplied by the factor 125% Current rate is 17.33% Minimum rate = 7.5% Maximum rate = 27.5% Annual deposit premium = $77,012
4.	Type of contract:	Exhibit C2 Second Excess of Loss
	Lines reinsured:	All property business
	Company's retention:	$130,000
	Coverage:	100% of each and every loss in excess of $130,000 up to $250,000, including loss adjustment expense
	Reinsurance premium:	9.00% of net premiums written Annual deposit premium = $39,995
5.	Type of contract:	Exhibit DE1 First Aggregate Excess of Loss
	Lines reinsured:	All business
	Company's retention:	75% of net premium written
	Coverage:	100% of each and every loss in excess of 75% of net premium written up to 145%
	Reinsurance premium:	Sum of the preceding eight years' losses incurred by the reinsurer, of the business year just completed, divided by the total of the net premiums written for the same period multiplied by 125% Current rate is 8.98% Minimum rate = 7.5% Maximum rate = 15.0% Annual deposit premium = $44,647
6.	Type of contract:	Exhibit DE2 Second Aggregate Excess of Loss
	Lines reinsured:	All business

Company’s retention:	145% of net premium written
Coverage:	100% of annual aggregate losses in excess of the retention
Reinsurance premium:	Sum of the preceding eight years’ losses incurred by the reinsurer, of the business year just completed, divided by the total of the net premiums written for the same period multiplied by 125% Current rate is 4.00% Annual deposit premium = $19,887

III. FINANCIAL DATA

The following financial statements reflect the financial condition of the company as reported to the Commissioner of Insurance in the December 31, 2012, annual statement. Adjustments made as a result of the examination are noted at the end of this section in the area captioned "Reconciliation of Policyholders' Surplus."

Columbus Mutual Town Insurance Company
Statement of Assets and Liabilities
As of December 31, 2012

Assets	Ledger	Nonledger	Not Admitted	Net Admitted
Cash in checking	$ 107,373	$	$	$ 107,373
Cash deposited at interest	409,627			409,627
Bonds	633,871			633,871
Stocks and mutual fund investments	691,436			691,436
Premiums, agents' balances and installments:				
In course of collection	37,817		7,188	30,629
Deferred and not yet due	98,806			98,806
Investment income accrued		7,898		7,898
Assessments receivable				
Reinsurance recoverable on paid losses and LAE	(31,896)			(31,896)
Totals	$1,947,034	$7,898	$7,188	$1,947,744

Liabilities and Surplus

Net unpaid losses	$ 132,000
Unpaid loss adjustment expenses	3,500
Commissions payable	14,821
Fire department dues payable	791
Federal income taxes payable	9,068
Unearned premiums	276,366
Reinsurance payable	92,051
Amounts withheld for the account of others	78
Other liabilities:	
Expense-related:	
Accounts payable	3,800
Premium refunds payable	466
Nonexpense-related:	
Premiums received in advance	10,249
Total liabilities	543,190
Policyholders' surplus	1,404,554
Total Liabilities and Surplus	$1,947,744

Columbus Mutual Town Insurance Company
Statement of Operations
For the Year 2012

Net premiums and assessments earned		$270,072
Deduct:		
Net losses incurred	$184,482	
Net loss adjustment expenses incurred	21,908	
Net other underwriting expenses incurred	164,224	
Total losses and expenses incurred		370,614
Net underwriting gain (loss)		(100,542)
Net investment income:		
Net investment income earned	39,523	
Net realized capital gains (losses)	49,046	
Total investment gain (loss)		88,569
Net income (loss) before federal income taxes		(11,973)
Federal income taxes incurred		13,000
Net Income (Loss)		$ (24,973)

Columbus Mutual Town Insurance Company
Reconciliation and Analysis of Surplus as Regards Policyholders
For the Two-Year Period Ending December 31, 2012

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

	2012	2011	2010
Surplus, beginning of year	$1,447,719	$1,548,432	$1,552,726
Net income	(24,973)	(125,963)	(23,801)
Net unrealized capital gain or (loss)	(15,952)	17,720	5,397
Change in nonadmitted assets	(2,240)	7,530	14,110
Surplus, End of Year	$1,404,554	$1,447,719	$1,548,432

Reconciliation of Policyholders' Surplus

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

Policyholders' surplus per December 31, 2012, annual statement			$1,404,554
Item	**Increase**	**Decrease**	
Reinsurance recoverable	$36,300	$	
Total	$36,300	$	
Increase to surplus per examination			36,300
Policyholders' Surplus per Examination			$1,440,854

IV. SUMMARY OF EXAMINATION RESULTS

Compliance with Prior Examination Report Recommendations

Comments and recommendations contained in the last examination report and the action taken on them by the company are as follows:

1. Underwriting—It is recommended that the company adhere to its inspection policy, whereby inspections of insured properties will take place every five years.

   Action—Noncompliance.

2. Underwriting—It is again recommended that the company amend its formal written agency agreements to include provisions concerning its agents' inspection responsibilities and the underwriting standards that agents are expected to follow in determining whether or not to submit an application to the company.

   Action—Compliance.

3. Accounts and Records—It is recommended that the company adopt practices and procedures for maintaining and organizing its accounting records in compliance with ss. Ins 6.80 (4) (b) and 13.05, Wis. Adm. Code.

   Action—Noncompliance.

4. Invested Assets—It is again recommended that the company comply with s. 610.23, Wis. Stat., and s. Ins 13.05, Wis. Adm. Code, as regards custody and control of its invested assets.

   Action—Compliance.

5. Invested Assets—It is again recommended that the company execute a formal written agreement with its investment brokerage firm outlining expectations and duties of both parties. It is again further recommended that the company's board of directors adopt a written investment strategy with guidelines to be followed by the company's investment brokerage firm in making its recommendations and that the written investment strategy with guidelines be referenced in the formal written agreement between the company and its investment brokerage firm.

   Action—Compliance.

6. Net Unpaid Losses—It is recommended that the company develop procedures to more accurately estimate loss reserves when a loss is reported.

   Action—Compliance.

7. Net Unpaid Losses—It is recommended that the company adopt reasonable procedures for timely settlement of claims in compliance with s. Ins 6.11 (3) (a) 2., Wis. Adm. Code.

   Action—Compliance.

Current Examination Results

Corporate Records

The minutes of the annual meetings of policyholders and meetings of the board of directors and committees thereof were reviewed for the period under examination and also for the subsequent period.

The review of the board minutes showed no evidence that the board ever reviewed or approved the investment policy. The current investment policy indicates that it was updated on October 11, 2012. Per s. Ins 6.20 (6) (h) 1., Wis. Adm. Code, the board shall adopt a written plan for acquiring and holding investments. Absent an entry in the board minutes showing that the board did discuss and approve of the revised investment policy, the examiner has no way of verifying that the policy was adopted by the board. It is recommended that the board of directors approve of the investment policy and all amendments to the investment policy and that such approvals are noted in the minutes to the board meetings in accordance with s. Ins 6.20 (6) (h) 1., Wis. Adm. Code.

In the minutes, there is no mention of the board members' discussions, review or approval of investment transactions. The secretary/treasurer noted that the board does discuss and approve investment transactions; but in the absence of such a record in the board minutes, the examiners were unable to verify the board's involvement in investment transactions. It is recommended that the board of directors shall approve of all investment transactions and that such approvals are noted in the minutes to the board meetings in accordance with s. Ins 6.20 (6) (h) 2., Wis. Adm. Code.

The examiners were informed that in late 2012 the company's investment strategy changed. The change was facilitated by the appointment of a new investment broker. The new investment broker promptly sold off the company bond portfolio and replaced the portfolio with short- to medium-term bonds having maturities of 15 years or less. He also introduced Indexed Funds and Exchange Traded Funds to the mutual fund portfolio. Additionally, the footnote disclosure at December 31, 2012, lists the old investment broker in error. The examiners take no exception to this significant change in investment strategy, but could find no evidence of board oversight of the process. For example, there are no discussions of appointing a new investment broker or the portfolio changes in the minutes of the board meetings. It is recommended that the board of directors approve of all significant changes in the investment strategy of the company and that such approvals are noted in the minutes to the board meetings.

Management noted that the company began using professional adjusters in 2013 to better assess the case reserves; however, there is no record in the minutes indicating that the board held discussions concerning this significant change. It is recommended that the board of directors approve of all significant changes in reserving policy and that such approvals are noted in the minutes to the board meetings.

The Articles of Incorporation were amended on June 11, 1997, January 12, 1999, June 4, 2003, and September 27, 2006. However, the Articles of Incorporation have never been restated. It is misleading to the reader to have the Articles of Incorporation dated as of August 1991, when they have been modified with the above amendments. It is recommended that the Articles of Incorporation be restated to include any amendments that the company has made.

Biographical data relating to company officers and directors have been reported in accordance with the provisions of s. Ins 6.52, Wis. Adm. Code.

The company has executed formal written agreements with its agents. The contracts include language indicating the agent will represent the company's interests "in good faith." The agent agreement does not include language specifying which party owns the renewals in the event that the agreement terminates. It is recommended that the company amend its agency agreement to include language which describes the terms and conditions of renewal business when the agreement terminates.

Conflict of Interest

In accordance with a directive of the Commissioner of Insurance, each company is required to establish a procedure for the disclosure to its board of directors of any material interest or affiliation on the part of its officers, directors, or key employees which conflicts or is likely to conflict with the official duties of such person. A part of this procedure is the annual completion of a conflict of interest questionnaire by the appropriate persons. The company has adopted such a procedure for disclosing potential conflicts of interest. Conflict of interest questionnaires were reviewed for the period under examination with no apparent conflicts being noted.

Fidelity Bond and Other Insurance

The company is afforded coverage under the terms of the following bonds or contracts and has complied with s. Ins 13.05 (6), Wis. Adm. Code, which sets forth the minimum requirements for fidelity bond coverage:

Type of Coverage	Coverage Limits
Fidelity bond	$ 110,000
Worker's compensation:	
Employee injury	Statutory
Employee liability:	
Each accident	100,000
Each employee	100,000
Policy limit	500,000
Property coverage:	
Building	7,500
Monies and securities	10,000
Accounts receivable	25,000
Valuable papers	10,000
Sign	10,000
Business income for dependent property	5,000
Forgery and alteration	2,500
Commercial excess liability	1,000,000
Combined professional and D&O liability	1,000,000

Underwriting

The company is normally on a five-year examination cycle. However, due to concerns over the company's continuing underwriting losses, this examination was called after two years. The management appears to have made progress in correcting its underwriting issues since the prior examination. For example the company has signed a formal agreement with its reinsurer, Wisconsin Reinsurance Corporation (WRC), called the "Plan for Improvement." The agreement with WRC contains 15 specific underwriting measures designed to address the company's persistent underwriting losses. The agreement was signed by the company president on September 10, 2012.

The Plan for Improvement combines reasonable rate increases with professional inspection programs and various best practices. For example, the agreement requires a rate increase of 7% for all basic coverage, except farm personal property. This increase was implemented as of January 1, 2012, and was filed with the Commissioner on July 18, 2012. The agreement also requires a policy fee of $10.00, and an installment fee of $5.00 (when applicable), on all new and renewal business. These increases were implemented as of January 1, 2013, and filed with the Commissioner in 2013. Additionally, the company has been implementing a program of independent inspections for all renewal business to be completed by December 31, 2013. The examiners verified through policy sampling that 30% of the renewal policies had been independently inspected in 2013 as a direct result of the agreement with WRC.

Until 2013 the agents of the company performed inspections prior to writing new business and as needed with renewal business. The company has shifted from agent inspections to independent inspections because of the Plan for Improvement between the company and WRC. It is recommended that the underwriting guide specify the company's policy that new and renewal business will be independently inspected.

The company has a written underwriting guide which has been preempted by the Plan for Improvement. The prior examination noted that the underwriting manual required inspections of renewal business every five years. Policy testing performed by the prior examiners showed that these inspections were not being performed. Policy testing performed during the current examination showed that only 30% of the renewal policies tested had inspections. It is again recommended that the company adhere to its inspection policy, whereby inspections of insured properties will take place every five years.

The Plan for Improvement between the company and WRC contains underwriting best practices which are also policies of the company. However, the current underwriting guide does not reflect these best practices. The underwriting manual should be revised to reflect the requirements of the Plan for Improvement to ensure that these practices are made permanent. Of most importance are the following:

- The policy requiring the company to follow up on all of the recommendations of the independent inspectors should be added to the revised underwriting manual.

- The policy requiring the company to nonrenew any policy if a 60-amp service or fuses are present should be added to the revised underwriting manual.

- The policy requiring all solid fuel appliances to be inspected for compliance with NFPA 211 should be added to the revised underwriting manual.

- Review of CCAP and CLUE and/or A+ for all new and renewals and take appropriate actions should be added to the revised underwriting manual.

- The policy requiring all new business to be inspected within 30 days of its effective date to allow action to be taken within the first 60 days of the policy should be added to the revised underwriting manual.

- The policy requiring nonrenewal of policyholders for excessive claims histories defined as three or more claims in three years or four or more claims in five years should be added to the revised underwriting manual.

- The policy requiring any agent with a three-year loss ratio greater than 100% to not be allowed to submit new business should be added to the revised underwriting manual.

The best practices mentioned in the preceding paragraph should become permanent policies of the company. It is recommended that the company revise the underwriting guide to reflect the above best practices contained in the Plan for Improvement between the company and WRC.

The company should require all policyholders who have renters to obtain renters insurance or obtain signed proof of coverage by an alternate insurer. It is recommended that all policyholders who have renters require renters insurance and that a signed proof of coverage be obtained.

The company should require all commercial and farm policies to have liability coverage or obtain signed proof of coverage by an alternate insurer. It is recommended that all commercial and farm policies include liability coverage and that a signed proof of coverage be obtained.

Claims Adjusting

The company has an adjusting committee consisting of at least three directors as required by s. 612.13 (4), Wis. Stat. The function of this committee is to adjust or supervise the adjustment of losses.

Accounts and Records

The examiners' review of the company's records indicated that the company is in compliance with s. Ins 13.05, Wis. Adm. Code, which sets forth the minimum standards for the handling of cash and recording of cash transactions by town mutual insurance companies. The examiners noted the following:

1. A proper policy register is maintained.
2. A proper cash receipts journal is maintained.
3. A proper cash disbursements journal is maintained.
4. A proper general journal is maintained.
5. A proper general ledger is maintained.

An extensive review was made of income and disbursement items. Cash receipts were traced from source records and the proper recording and eventual deposit thereof ascertained. Negotiated checks issued during the period under examination were reviewed, test checked for proper endorsement, and traced to cash records. The verification of assets and determination of liabilities were made as of December 31, 2012.

The company is audited annually by an outside public accounting firm. The accounting firm also performs bookkeeping functions for the company.

The prior examination noted the difficulty the examiners had in obtaining records from the company. This examination noted the following deficiencies in the accounts and records of the company as follows:

- Custodial Agreement—When asked to provide a custodial agreement, the company was not readily able to provide this document. The company treasurer had to request a copy of the custody agreement from their investment advisor.

- Financial Advisors Agreement—The company did not readily have a copy of its investment advisor's agreement at the office. A copy had to be requested from the investment advisor.

- Claims Reports—When asked for an Open Claims Report at 12/31/2012 and a 2013 Claims Paid Report the management produced various reports which lacked credibility.

- Cash Deposit Records—The company does not maintain any form of deposit log and the examiners could not trace individual cash receipts to the deposit logs to indicate that funds were counted and accepted by the bank and that the cash receipt journal is accurate.

It is again recommended that the company adopt practices and procedures for maintaining and organizing its accounting records in compliance with ss. Ins 6.80 (4) (b) and 13.05, Wis. Adm. Code.

EDP Environment

Company personnel were interviewed with respect to the company's electronic data processing environment. Access to the computers is limited to people authorized to use the computers. Company personnel back up the computers weekly and the backed-up data is kept off-site.

The company has manuals documenting the use of its software and outlining the steps to complete specific tasks. The manuals assist the continuity of operations by providing instructions for seldom-used applications or when staff turnover occurs. The examination determined that the level of documentation contained in the manuals was reasonable. In addition, the company's software provider also offers a tech support hotline which the company utilizes for assistance.

Business Continuity Plan

A business continuity plan identifies steps to be performed by a company in the event of business interruptions including, but not limited to, the inability to access its computer, the loss of information on its computer, the loss of a key employee, or the destruction of its office building. The company has developed a business continuity plan which appears to be adequate.

The company's secretary/treasurer and general manager is a key individual and the operations of the company depend on his experience and knowledge. He also serves as a member of the board of directors. He is planning to retire in March of 2014 and the board will take up the issue at an August 12, 2013, board meeting. It is recommended that the company devise a formal succession program as part of its business continuity plan.

Invested Assets

Section 610.23, Wis. Stat., requires insurers to hold all investments and deposits of its funds in its own name except that:

(1) Securities kept under a custodial agreement or trust arrangement with a bank or banking and trust company may be issued in the name of a nominee of the bank or banking and trust company; and

(2) Any insurer may acquire and hold securities in bearer form.

For securities not held under a custodial agreement or trust arrangement with a bank or banking and trust company, s. Ins 13.05 (4), Wis. Adm. Code, requires that:

> Non-negotiable evidences of company investments such as registered bonds, certificates of deposits, notes, etc., shall be maintained in a safe or vault with adequate safety controls or in a safety deposit box in a bank. Negotiable evidences of company investments shall be maintained in a safety deposit box in a bank. Access to a company safety deposit box containing negotiable securities shall require the presence and signature of at least 2 officers, directors or employees of the company.

The company is in compliance with these requirements.

Investment Rule Compliance

The investment rule for town mutual insurers allows a company to invest in common stocks, common stock mutual funds, and other higher risk investments (referred to as “Type 2”) provided that the town mutual has a sufficient amount of lower risk investments (referred to as “Type 1”). A town mutual may invest in Type 2 securities only if it already has sufficient Type 1 investments. Type 1 investments must equal or exceed the greater of items 1, 2, or 3.

1.	Liabilities plus $300,000	$651,802
2.	Liabilities plus 33% of gross premiums written	233,287
3.	Liabilities plus 50% of net premiums written	141,961
4.	Amount required (greater of 1, 2, or 3)	651,802
5.	Amount of Type 1 investments as of 12/31/2012	782,649
6.	Excess or (deficiency)	$130,847

The company does have sufficient Type 1 investments.

ASSETS

Cash and Invested Cash **$517,000**

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

Cash deposited in banks—checking accounts	$107,373
Cash deposited in banks at interest	409,627
Total	$517,000

Cash deposited in banks subject to the company's check and withdrawal consists of one account maintained in a local bank. Verification of checking account balances was made by obtaining the company's CPA confirmation from the depository and reconciling the amount shown thereon to company records.

Cash deposited in banks at interest represents the aggregate of six deposits in six depositories. Deposits were verified by obtaining the company's CPA confirmation with the respective depositories along with the CPA's actual count and inspection of certificates and/or passbooks. Interest received during the year 2012 totaled $8,031 and was verified to company cash records. Rates of interest earned on cash deposits ranged from 0.80% to 5.00%. Accrued interest on cash deposits totaled $2,108 at year-end.

Book Value of Bonds **$633,871**

The above asset consists of the aggregate book value of bonds held by the company as of December 31, 2012. Bonds owned by the company are held in an account with its investment custodian.

Bonds were verified through a review of the December 31, 2012, custodial statement. Bond purchases and sales for the period under examination were checked to brokers' invoices and advices. The company's investment in bonds was in conformance with Wisconsin Statutes and the rules of the Commissioner of Insurance as regards investments made by town mutual insurers.

Interest received during 2012 on bonds amounted to $20,665 and was traced to cash receipts records. Accrued interest of $1,876 at December 31, 2012, was checked and allowed as a nonledger asset.

Stocks and Mutual Fund Investments **$691,436**

The above asset consists of the aggregate market value of stocks and mutual funds held by the company as of December 31, 2012. The company's Wisconsin Reinsurance Corporation and NAMIC Insurance Company, Inc., stock certificates are kept in the company's safety deposit box. All other stocks and all mutual funds owned by the company are held in an account with its investment custodian.

Stock certificates held by the company were verified by obtaining the company's CPA workpapers evidencing physical examination. Stocks and mutual funds held with the company's investment custodian were verified through a review of the December 31, 2012, custodian statement. Stock and mutual fund purchases and sales for the period under examination were checked to brokers' invoices and advices. The company's investment in stocks and mutual funds was in conformance with Wisconsin Statutes and the rules of the Commissioner of Insurance as regards investments made by town mutual insurers.

Dividends received during 2012 on stocks and mutual funds amounted to $11,643 and were traced to cash receipts records.

Premiums, Agents' Balances in Course of Collection **$30,629**

This asset represents the amounts due from agents or policyholders which are not in excess of 90 days past due at year-end. A review of detailed premium records verified the accuracy of this asset.

Premiums Deferred and Not Yet Due **$98,806**

This asset represents modal premium installments (such as monthly, quarterly, etc.) that are not yet due. A review of a sample from the company's detailed list of deferred premiums verified the accuracy of this asset.

Investment Income Accrued **$7,898**

Interest due and accrued on the various assets of the company at December 31, 2012, consists of the following:

Cash deposited at interest	$2,108
Bonds	5,790
Total	$7,898

Reinsurance Recoverable on Paid Losses and LAE **$4,404**

The above asset represents recoveries due to the company from reinsurance on losses and loss adjusting expenses which were paid on or prior to December 31, 2012. The company reported a balance for this line item of $(31,896), while the examination resulted in a balance of $4,404. This adjustment is reflected in the section of this report entitled "Reconciliation of Policyholders' Surplus." A review of year-end accountings with the reinsurer verified the above asset.

There was a large fire loss open at December 31, 2012, which was covered under the company's reinsurance policy for any losses above the attachment point of $45,000. The management paid $81,300 in 2013 for this claim, but did not submit the claim to the reinsurer for a recovery, resulting in a $36,300 monetary loss to the company. Management expressed a concern over rising reinsurance costs had they made the claim to the reinsurer. An alternative approach might be to increase the company's retention on a per risk basis if the company wants to reduce the reinsurance costs. It is recommended that the company promptly submit reinsurance claims on paid losses to their reinsurer. It is further recommended that the company submit the fire loss claim referred to above to the reinsurer for recovery.

LIABILITIES AND SURPLUS

Net Unpaid Losses **$132,000**

This liability represents losses incurred on or prior to December 31, 2012, that remained unpaid as of that date. The examiners reviewed the reasonableness of this liability by totaling actual loss payments made subsequent to December 31, 2012, with incurred dates in 2012 and prior years. The examiners' development of unpaid losses is compared with the amount estimated by the company in the following schedule.

	Company Estimate	Examiners' Development	Difference
Incurred but unpaid losses	$202,373	$172,924	$29,449
Less: Reinsurance recoverable on unpaid losses	70,373	38,899	31,474
Net Unpaid Losses	$132,000	$134,025	$ (2,025)

The above difference of $(2,025) was not considered material for purposes of this examination.

The examiners' review of claim files included open claims, paid claims, claims closed without payment, and claims that were denied during the examination period. The review indicated that claims are investigated and evaluated properly and that payments are made promptly and in accordance with policy provisions upon the submission of a proof of loss in most cases. In addition, the review of claims handling procedures and files revealed the following:

1. A proper loss register is maintained.
2. Claim files contained sufficient investigatory data and documentation to verify settlement payments or reserve estimates.
3. Proofs of loss were not properly signed.

The examination tested all claims payments made in 2012. Of the 49 claims tested the company could not show a proof of loss which was signed by the claimant for 2 of the claims. It is recommended that the company ensure that all proof of loss statements be signed by the claimant prior to the payment of a claim.

Unpaid Loss Adjustment Expenses **$132,000**

This liability represents the company's estimate of amounts necessary to settle losses which were incurred prior to December 31, 2012, but which remained unpaid as of year-end. The methodology used by the company in establishing this liability is to multiply the number of open claims at year-end by the per claim rate paid to its claim adjuster to adjust claims.

The examiners' analysis of expenses incurred in the current year related to the settlement of prior year losses, as well as estimates of amounts necessary to settle any prior losses remaining unpaid at the examination date, determined this liability to be adequately stated.

Commissions Payable **$14,821**

This liability represents the commissions payable on deferred premiums as of December 31, 2012. The examiners’ review of the company’s commission calculation found the liability to be reasonably stated.

Fire Department Dues Payable **$791**

This liability represents the fire department dues payable to the state of Wisconsin as of December 31, 2012. The examiners reviewed the company's fire department dues calculation and found this liability to be correctly calculated. The actual amount paid was verified to the cash disbursement records.

Federal Income Taxes Payable **$9,068**

This liability represents the balance payable at year-end for federal income taxes incurred prior to December 31, 2012. The examiners reviewed the company's 2012 tax return and verified amounts paid to cash disbursement records to verify the accuracy of this liability.

Unearned Premiums **$276,336**

This liability represents the reserve established for unearned premiums in compliance with s. Ins 13.08 (3), Wis. Adm. Code. This reserve was established using a daily pro rata methodology. A recalculation of the company’s detailed list of unearned premiums based on the in-force policy register verified the accuracy of this asset.

Reinsurance Payable **$92,051**

This liability consists of amounts due to the company's reinsurer at December 31, 2012, relating to transactions which occurred on or prior to that date.

This liability consists of amounts due to the company's reinsurer at December 31, 2012, relating to transactions which occurred on or prior to that date. Subsequent payments and confirmations with the reinsurer verified these amounts.

Class AX1 Nonproperty	$21,346
Class B1 First Surplus	39,743
Class C1 Excess of Loss	14,145
Class C2 Excess of Loss	17,978
Class D1 Stop Loss	1,853
Class D2 Stop Loss	6,150
Reinsurance Commissions	(9,164)
Total	$92,051

Amounts Withheld for the Account of Others **$78**

This liability represents employee payroll deductions in the possession of the company at December 31, 2012. Supporting records and subsequent cash disbursements verified this item.

Accounts Payable **$3,800**

This liability represents an estimate of the total miscellaneous accounts payable at December 31, 2012. The examiners reviewed subsequent cash disbursements records to verify the adequacy of this liability.

Premiums Refunds Payable **$466**

This liability represents an estimate of the total policyholder refunds payable at December 31, 2012. The examiners reviewed 2012 premium and cash receipt records to verify the accuracy of this liability.

Premiums Received in Advance **$10,249**

This liability represents the total premiums received prior to year-end for policies with effective dates after December 31, 2012. The examiners reviewed 2012 premium and cash receipt records to verify the accuracy of this liability.

V. CONCLUSION

Columbus Mutual Town Insurance Company is a town mutual insurer with an authorized territory of 11 counties. The company has been in business over 139 years providing property and liability insurance to its policyholders.

The company has not grown over the examination period as evidenced by almost every significant measure. The company has shown a consistent pattern of underwriting losses in recent years including both years under examination. The loss ratio reached a five-year maximum in 2011 at 103%. This maximum was caused in part by a large hail storm in that year. However, there is ample data to suggest that the company’s loss ratios are unusually high. For example, the loss ratio has averaged 82.8% since 2008. Due to this loss experience, the company was required to enter into a formal agreement with its reinsurer effective in September of 2012 as a condition to maintaining its reinsurance contract. The agreement with WRC combined reasonable rate increases with independent inspection programs, and other best practices, in an attempt to improve underwriting results.

The expense ratio has plateaued in recent years at approximately 56%, whereas the ratio has historically been significantly lower. This is mainly due to increased reinsurance costs that have caused a decline in net premiums over the past five years.

The composite ratios are significantly above normal in recent years, coming in at 132%, 159%, and 133% for the years 2012, 2011 and 2010, respectively.

The company was in compliance with 5 out of the 7 prior exam recommendations. As a result of the current exam, there were 15 recommendations, including 2 repeated recommendations and 1 adjustment to surplus. Recommended areas of improvement include submission of reinsurance recoveries, agent contractual language, corporate succession planning, board activity surrounding investments, underwriting best practices, and corporate records.

VI. SUMMARY OF COMMENTS AND RECOMMENDATIONS

1. Page 16 - Corporate Records—It is recommended that the board of directors approve of the investment policy and all amendments to the investment policy and that such approvals are noted in the minutes to the board meetings in accordance with s. Ins 6.20 (6) (h) 1., Wis. Adm. Code.

2. Page 16 - Corporate Records—It is recommended that the board of directors shall approve of all investment transactions and that such approvals are noted in the minutes to the board meetings in accordance with s. Ins 6.20 (6) (h) 2., Wis. Adm. Code.

3. Page 17 - Corporate Records—It is recommended that the board of directors approve of all significant changes in the investment strategy of the company and that such approvals are noted in the minutes to the board meetings.

4. Page 17 - Corporate Records—It is recommended that the board of directors approve of all significant changes in reserving policy and that such approvals are noted in the minutes to the board meetings.

5. Page 17 - Corporate Records—It is recommended that the Articles of Incorporation be restated to include any amendments that the company has made.

6. Page 17 - Corporate Records—It is recommended that the company amend its agency agreement to include language which describes the terms and conditions of renewal business when the agreement terminates.

7. Page 19 - Underwriting—It is recommended that the underwriting guide specify the company's policy that new and renewal business will be independently inspected.

8. Page 19 - Underwriting—It is again recommended that the company adhere to its inspection policy, whereby inspections of insured properties will take place every five years.

9. Page 20 - Underwriting—It is recommended that the company revise the underwriting guide to reflect the above best practices contained in the Plan for Improvement between the company and WRC.

10. Page 20 - Underwriting—It is recommended that all policyholders who have renters require renters insurance and that a signed proof of coverage be obtained.

11. Page 20 - Underwriting—It is recommended that all commercial and farm policies include liability coverage and that a signed proof of coverage be obtained.

12. Page 22 - Accounts and Records—It is again recommended that the company adopt practices and procedures for maintaining and organizing its accounting records in compliance with ss. Ins 6.80 (4) (b) and 13.05, Wis. Adm. Code.

13. Page 22 - Business Continuity Plan—It is recommended that the company devise a formal succession program as part of its business continuity plan.

14. Page 26 - Reinsurance Recoverable on Paid Loss and LAE—It is recommended that the company promptly submit reinsurance claims on paid losses to their reinsurer. It is further recommended that the company submit the fire loss claim referred to above to the reinsurer for recovery.

15. Page 27 - Net Unpaid Losses—It is recommended that the company ensure that all proof of loss statements be signed by the claimant prior to the payment of a claim.

VII. ACKNOWLEDGMENT

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

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

Respectfully submitted,

Gene M. Renard, CFE
Examiner-in-Charge

VIII. SUBSEQUENT EVENT

On September 12, 2013, the company's reinsurer, Wisconsin Reinsurance Corporation, sent a Provisional Notice of Termination (Notice) to Columbus Mutual Town Insurance Company. The Notice acknowledges that WRC has been in the process of working with the company on a Plan for Improvement. WRC stated that the company was not in compliance with the Plan for Improvement at the Notice date, that the reinsurance contract with WRC required a 90-day notice of termination, and that WRC needed adequate time to review these matters with the company. The Notice served to provide the company with provisional notice of termination of the reinsurance contract effective January 1, 2014. Finally, the Notice states that the company will be contacted by a WRC representative.