Report

of the

Examination of

Theresa Mutual Insurance Company

Theresa, Wisconsin

As of December 31, 2013

TABLE OF CONTENTS

Page

State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

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May 22, 2014

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, 2013, of the affairs and financial condition of:

THERESA MUTUAL INSURANCE COMPANY
Theresa, Wisconsin

and the following report thereon is respectfully submitted:

I. INTRODUCTION

The previous examination of Theresa Mutual Insurance Company (the company) was made in 2009 as of December 31, 2008. The current examination covered the intervening time period ending December 31, 2013, 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.

The company was originally organized as a town mutual insurance company on January 7, 1879, under the provisions of the then existing Wisconsin Statutes. The original name of the company was the Theresa Mutual Fire 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 was one amendment to the articles of incorporation and no amendments to the bylaws. The amendment to the articles of incorporation added Ozaukee and Sheboygan counties to the company's territory.

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:

Columbia	Dodge
Fond du Lac	Green Lake
Marquette	Ozaukee
Sheboygan	Washington
Winnebago	

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 three years with premiums payable on the advance premium basis.

Business of the company is acquired through 27 agents, four of whom are directors of the company. Agents are presently compensated for their services as follows:

Type of Policy	**Compensation**
Fire and EC	14%
Liability	14
New business bonus for Fire and EC	12

All losses are adjusted by members of the company's board of directors (private adjusters are used for complex losses). Board members who are also agents do not have authority to adjust losses covering their own policyholders under the company's written loss adjusting guidelines. Adjusters receive $40 for each large loss and $25 for each small loss adjusted plus $.565 per mile for travel allowance.

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 nine 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
Robert Belling*	Dairy Farmer	Lomira, WI	2015
Peter Bonack	Retired Factory Worker	Mayville, WI	2017
Jerome Feucht*	Retired Factory Worker	Mayville, WI	2015
Rodney Justman*	Retired Farmer	Mayville, WI	2016
Tracy Kinyon	Manufacturing & Business Systems Analyst	Lomira, WI	2016
Daniel Kuen	Maintenance,City of Mayville	Lomira, WI	2016
Ralph Pribnow	Farmer	Mayville, WI	2017
Steven Ries	Business Owner	Lomira, WI	2015
Gary Zastrow*	Dairy Farmer	Mayville, WI	2017

Directors who are also agents are identified with an asterisk.

Note: Peter Bonack replaced Roger Fink who retired on March 1, 2014.

Members of the board currently receive $50 for each board meeting attended and $.565 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	2013 Compensation
Roger Fink	President	$ 3,347
Rodney Justman	Vice-President	16,948*
Robert Belling	Secretary and Manager	46,698*
Ralph Pribnow	Treasurer	4,506

* Reported compensation is the total compensation paid by the insurer for the year and includes salary, commissions, director fees and rental income as applicable.

Note: Steven Ries replaced Roger Fink as President on March 1, 2014.

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:

Investment Committee
Steven Ries, Chair
Robert Belling
Peter Bonack
Jerome Feucht
Rodney Justman
Tracy Kinyon
Daniel Kuen
Ralph Pribnow
Gary Zastrow

Inspection Committee
Steven Ries, Chair
Robert Belling
Peter Bonack
Jerome Feucht
Rodney Justman
Tracy Kinyon
Daniel Kuen
Ralph Pribnow
Gary Zastrow

Large Loss Adjusting Committee
Steven Ries, Chair
Robert Belling
Rodney Justman
Ralph Pribnow

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
2013	$562,243	1,199	$ 234,605	$4,190,107	$3,627,019
2012	519,551	1,162	44,561	3,809,468	3,279,824
2011	489,299	1,100	154,424	3,917,371	3,335,366
2010	502,253	1,069	69,700	3,761,436	3,294,545
2009	505,809	1,057	24,746	3,583,460	3,139,900
2008	525,821	1,083	(197,097)	3,490,260	2,964,504

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	Gross
2013	$971,148	$573,673	$3,627,019	16%	27%
2012	928,272	525,560	3,279,824	16	28
2011	922,132	494,379	3,335,366	15	28
2010	906,927	510,774	3,294,545	16	28
2009	875,668	500,867	3,139,900	16	28
2008	922,697	512,121	2,964,504	17	31

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
2013	$160,375	$239,465	$562,243	29%	42%	70%
2012	440,070	223,936	519,551	85	43	127
2011	189,983	230,666	489,299	39	47	85
2010	263,930	238,529	502,253	53	47	99
2009	235,143	252,613	505,809	46	50	97
2008	191,252	231,836	525,821	36	45	82

The company has maintained a strong financial position over the examination period. The company has reported a net income in all five years under examination. The company’s surplus has increased over $650,000 over the five-year examination period. The increase in admitted assets and surplus was due to the combination of positive investment results and the overall underwriting profitability of the company since the previous exam.

Policies in force have increased nearly 11% since the last examination. As a result of the growth, gross premium written has increased 5% and net premium written has increased 12%.

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 (WRC)
Effective date:	January 1, 2014
Termination provisions:	Either party may terminate this contract by giving 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 – Casualty Excess of Loss Reinsurance
	Lines reinsured:	All casualty business written by the company
	Company's retention:	$10,000 in respect to each and every loss occurrence
	Coverage:	100% of each and every loss occurring on the business covered by this contract, including loss adjustment expenses in excess of the retention, subject to maximum policy limits of $1,000,000 per occurrence, $1,000,000 split limits, $25,000 for medical payments, per person; $25,000 per accident
	Reinsurance premium:	50% of casualty premium written for each and every policy issued Annual deposit premium: $81,500
2.	Type of contract:	Exhibit B – First Surplus Reinsurance
	Lines reinsured:	All property business written by the company
	Company's retention:	$600,000 per ceded risk
	Coverage:	Up to $2,000,000 on a pro rata basis
	Reinsurance premium:	Pro rata share of all premiums and fees charged by the company corresponding to the amount of each risk ceded
	Ceding commission:	15%, plus 15% profit commission
3.	Type of contract:	Exhibit C-1 – Excess of Loss - First Layer
	Lines reinsured:	All property business written by the company
	Company's retention:	$70,000 per occurrence

	Coverage:	100% of any loss, including loss adjustment expense, in excess of $70,000, subject to a limit of liability to the reinsurer of $90,000
	Reinsurance premium:	Rate: 15.89% of the company's net premiums in respect to the business covered Annual deposit premium: $110,121
4.	Type of contract:	Exhibit C-2 – Excess of Loss - Second Layer
	Lines reinsured:	All property business written by the company
	Company's retention:	$160,000 per occurrence
	Coverage:	100% of any loss, including loss adjustment expense, in excess of $160,000, subject to a limit of liability to the reinsurer of $140,000
	Reinsurance premium:	Rate: 5.5% of the company's net premiums in respect to the business covered Annual deposit premium: $38,116
5.	Type of contract:	Exhibit C-3 – Excess of Loss - Third Layer
	Lines reinsured:	All property business written by the company
	Company's retention:	$300,000 per occurrence
	Coverage:	100% of any loss, including loss adjustment expense, in excess of $300,000, subject to a limit of liability to the reinsurer of $300,000
	Reinsurance premium:	Rate: 3% of the company's net premiums in respect to the business covered Annual deposit premium: $20,791
6.	Type of contract:	Exhibit D-1 – First Aggregate Excess of Loss Reinsurance
	Lines reinsured:	All business written by the company
	Company's retention:	75% of net written premium (estimated at $580,891)
	Coverage:	65% of the amount by which the aggregate of the company's losses, including loss adjustment expenses, exceed the retention with a limit of 65% of NWP (losses from 75% to 140% of NWP)
	Reinsurance premium:	Rate: 6.25% Annual deposit premium: $48,408 Estimated attachment point: 580,891
7.	Type of contract:	Exhibit D-2 – Second Aggregate Excess of Loss Reinsurance
	Lines reinsured:	All business written by the company

Company’s retention:	140% of net written premium
Coverage:	100% of the amount by which the aggregate of the company’s losses, including loss adjustment expenses, exceed the retention
Reinsurance premium:	Rate: 3.0% Annual deposit premium: $23,236

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, 2013, 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."

Theresa Mutual Insurance Company
Statement of Assets and Liabilities
As of December 31, 2013

Assets	Ledger	Nonledger	Not Admitted	Net Admitted
Cash on hand	$ 50	$	$	$ 50
Cash in checking	(747)			(747)
Cash deposited at interest	282,599			282,599
Bonds	1,884,960			1,884,960
Stocks and mutual fund investments	1,617,343			1,617,343
Real estate	176,630			176,630
Premiums, agents' balances and installments:				
In course of collection	11,661			11,661
Deferred and not yet due	167,000			167,000
Investment income accrued		20,611		20,611
Other expense-related assets:				
Reinsurance commission receivable	11,300			11,300
Deferred commission receivable	6,700			6,700
Other nonexpense-related assets:				
Federal income tax recoverable	12,000			12,000
Furniture and fixtures	2,094		2,904	
Totals	$4,171,590	$20,611	$2,904	$4,190,107

Liabilities and Surplus

Net unpaid losses	$ 91,000
Unpaid loss adjustment expenses	1,000
Commissions payable	35,510
Fire department dues payable	214
Unearned premiums	375,398
Reinsurance payable	54,915
Other liabilities:	
Expense-related:	
Accounts payable	894
Nonexpense-related:	
Premiums received in advance	4,157
Total liabilities	563,088
Policyholders' surplus	3,627,019
Total Liabilities and Surplus	$4,190,107

Theresa Mutual Insurance Company
Statement of Operations
For the Year 2013

Net premiums and assessments earned		$562,243
Deduct:		
Net losses incurred	$132,136	
Net loss adjustment expenses incurred	28,239	
Net other underwriting expenses incurred	239,465	
Total losses and expenses incurred		399,840
Net underwriting gain (loss)		162,403
Net investment income:		
Net investment income earned	39,714	
Net realized capital gains (losses)	40,930	
Total investment gain (loss)		80,644
Other income (expense):		
Miscellaneous income		924
Net income (loss) before federal income taxes		243,971
Federal income taxes incurred		9,366
Net Income (Loss)		$234,605

Theresa Mutual Insurance Company
Reconciliation and Analysis of Surplus as Regards Policyholders
For the Five-Year Period Ending December 31, 2013

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:

	2013	2012	2011	2010	2009
Surplus, beginning of year	$3,279,824	$3,335,366	$3,294,545	$3,139,900	$2,964,504
Net income	234,605	44,561	154,424	69,700	24,746
Net unrealized capital gain or (loss)	111,543	(101,150)	(114,650)	83,898	156,932
Change in nonadmitted assets	1,047	1,047	1,047	1,047	(6,282)
Surplus, End of Year	$3,627,019	$3,279,824	$3,335,366	$3,294,545	$3,139,900

Reconciliation of Policyholders' Surplus

The examination resulted in no adjustments to policyholders' surplus. The amount reported by the company as of December 31, 2013 is accepted.

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. Business Continuity Plan—It is recommended that the company develop an updated business continuity plan which should be filed with this office when completed and should be reviewed and updated on a regular basis.

   Action—Compliance.

2. Cash and Invested Cash—It is suggested that the company ask the custodian to provide detailed custodial reports to the company in a timely manner as agreed in the contract.

   Action—Compliance.

3. Stocks and Mutual Fund Investments—It is recommended that the company file the mutual fund information correctly in the annual statement and track investment ratings of the funds to assure compliance with ss. Ins 6.20 (6) (d) 2. c. and 6.20 (6) (g), Wis. Adm. Code.

   Action—Compliance.

4. Book Value of Real Estate—It is suggested that the company use consistent depreciation schedules for future fixed asset investments.

   Action—Compliance.

5. Electronic Data Processing Equipment—It is recommended that the company depreciate their computer equipment useful life over three years in accordance with the Instructions for Town Mutuals Filing the OCI Town Mutual Annual Statement.

   Action—Compliance.

6. Accounts Payable—It is recommended that the company accrue and report general accounts payable at the end of the year.

   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.

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."

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	$ 170,000
Worker's compensation:	
Employee injury	Statutory
Employee liability:	
Each accident	100,000
Each employee	100,000
Policy limit	500,000
Business owners	
Liability coverages:	
Commercial liability per occurrence	1,000,000
Commercial liability aggregate	2,000,000
Non-owned and hired auto liability	1,000,000
Fire legal liability	100,000
Medical payments per person	10,000
Property coverages:	
Building	130,000
Office equipment and supplies	22,500
Surface water	2,500
Directors and officers liability insurance	
Each claim	2,000,000
Aggregate limit	2,000,000
Agent's errors and omissions	
Each claim	1,000,000
Aggregate limit	1,000,000

Underwriting

The company has a written underwriting guide. The guide covers all the lines of business that the company is presently writing.

The company has a formal inspection procedure for both new and renewal business. A sampling of new applications and renewal business is inspected by committee members who are independent of the risk under consideration and review.

Claims Adjusting

The company has an adjusting committee, consisting of the entire board of directors, as required by s. 612.13 (4), Wis. Stat. In addition, the company has a Large Loss Adjusting Committee, consisting of four board members, that provides additional review on large complex losses. The function of these committees 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, 2013.

The company is audited annually by an outside public accounting firm.

EDP Environment

Company personnel were interviewed with respect to the company's electronic data processing environment. Access to the computers is limited by access codes to people authorized to use the computers.

Company personnel back up the computers daily and the backed-up data is kept in the office safe. Weekly backups are stored at the house of an employee. Annual backups are stored in the safe-deposit box at the bank.

The company has manuals documenting the use of its software and outlining the steps to complete specific tasks. The manuals assist in 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.

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. The company's business continuity plan appears to be adequate.

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	$ 863,088
2.	Liabilities plus 33% of gross premiums written	883,567
3.	Liabilities plus 50% of net premiums written	849,925
4.	Amount required (greater of 1, 2, or 3)	883,567
5.	Amount of Type 1 investments as of 12/31/2013	2,382,938
6.	Excess or (deficiency)	$1,499,371

The company has sufficient Type 1 investments.

ASSETS

Cash and Invested Cash **$281,902**

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

Cash in company's office	$ 50
Cash deposited in banks—checking accounts	(747)
Cash deposited in banks at interest	282,599
Total	$281,902

Cash in company's office at year-end represents the company's petty cash fund. A physical count was made by the examiners during the course of the examination and the balance reconciled to year-end.

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

Cash deposited in banks represents the aggregate of seven deposits in six depositories. Deposits were verified by direct correspondence with the respective depositories and by obtaining direct confirmations from the company’s custodian. Interest received during the year 2013 totaled $3,798 and was verified to company cash records. Rates of interest earned on cash deposits ranged from .750% to 5.150%. The company has purchased several of their CDs from a broker at a premium. As a result, the effective interest rate on these CDs is lower than the stated coupon rate of the CD. Accrued interest on cash deposits totaled $889 at year-end.

Book Value of Bonds **$1,884,960**

The above asset consists of the aggregate book value of bonds held by the company as of December 31, 2013. Bonds owned by the company are located in a custodial account with Comerica Bank.

Bonds were traced to the company’s investment custodial account by the examiners. Bond purchases and sales for the period under examination were checked to brokers' invoices and advices.

Interest received during 2013 on bonds amounted to $64,980 and was traced to cash receipts records. Accrued interest of $19,722 at December 31, 2013, was checked and allowed as a nonledger asset.

On the Annual Statement, Schedule C Section 2 – Bond Investment Income, the interest payments dates in the “How Interest Paid” column were not completed accurately. Additionally, the company incorrectly reported the interest rate on 12 of their bonds. It is recommended that the company accurately complete the Bond Investment Income Schedule in accordance with the Town Mutual Annual Statement Instructions.

During review of the company’s bond holdings it was noted that the company has four bonds from a single issuer with statement value in excess of 3% of admitted assets. The statement value of the four bonds combined is $164,282, which is $38,579 above the limitation for corporate bond issues from a single issuer. Additionally, the company has a common stock with statement value in excess of 3% of admitted assets. The statement value of the common stock is $199,408, which is $73,705 above the limitation for common stock investments in a single issue. It is recommended that the company follow investment limitations pursuant to s. Ins 6.20 (6) (f), Wis. Adm. Code.

The company’s bond portfolio includes a number of securities issued by banks and other financial corporations, which were designed and packaged as debt securities, but with floating rates that appeared to aid the issuer in hedging its own risks or those of clients. In these cases the floating rates cause the cash flows of the securities to be unpredictable because the interest payments are based on specified variables such as market or consumer indexes, rates, or other variables. The floating rates can be subject to wide fluctuation based on changing economic conditions or other circumstances.

The volume of floating rate corporate bonds issued in the United States fluctuates from year to year. From 1996 to 2013, the percentage of corporate bonds that have been issued on a floating rate basis has ranged from 4.8% to 48.9% of corporate bond issuance, with the average for the period amounting to 23.8% of corporate bond issuance. The following table was drawn from data made available to the public from the Web site of the Securities Industry and Financial Markets Association, with the source attributed to Thomson Reuters.

U.S. Corporate Bond Issuance* 1996 – 2013
Callable and Non-Callable by Coupon Type
(Billions in U.S. Dollars)

	Callable		Non-Callable		Total %
	Fixed Rate	**Floating Rate**	**Fixed Rate**	**Floating Rate**	**Floating Rate**
1996	$ 79.1	$ 4.3	$ 200.3	$ 60.0	18.7%
1997	131.4	5.9	232.9	95.9	21.8
1998	240.5	7.8	228.0	134.4	23.3
1999	211.8	5.0	248.8	163.7	26.8
2000	196.6	16.1	166.1	208.6	38.3
2001	400.3	7.5	232.7	135.5	18.4
2002	283.4	2.7	187.8	162.8	26.0
2003	360.4	23.1	177.4	215.0	30.7
2004	238.6	31.7	207.8	302.6	42.8
2005	233.5	59.0	152.3	307.9	48.7
2006	348.3	88.0	192.4	430.2	48.9
2007	420.9	99.0	251.6	356.0	40.4
2008	352.4	57.7	185.7	111.4	23.9
2009	618.3	5.6	236.2	41.1	5.2
2010	575.2	7.8	413.2	66.7	7.0
2011	582.9	8.2	306.4	114.6	12.1
2012	882.8	13.2	415.7	53.3	4.9
2013	800.8	22.3	418.8	131.8	11.2
Totals	$6,9,57.3	$464.9	$4,454.0	$3,091.4	23.8%

* Includes all non-convertible corporate debt, medium-term notes, and Yankee bonds, but excludes all issues with maturities of one year or less and CDs.

Town mutual insurers are considered restricted insurers under s. 620.03 (1), Wis. Stat., and s. Ins 6.20 (6) (a), Wis. Adm. Code, and, as such, are subject to limitation over their investments. This office has imposed and may impose additional special investment restrictions for town mutual insurers if the investment creates additional risk which may compromise their financial position and ability to pay policyholders' claims in full and in a timely manner. Furthermore, pursuant to s. 620.04 (1), Wis. Stat., this office may impose reasonable and temporary restrictions upon the investments of an individual insurer, including prohibition or divestment of a particular asset. This office concludes that the company's investment strategy presents an unreasonable amount of risk to the company and is not appropriate for a town mutual insurance company at this time. The basis for this conclusion and the company's action required by this office is described below.

The examination review of the bonds owned by the company found multiple instances of corporate bonds with variable rates of interest tied to various complex indices.

For instance, for each interest payment on the Protective Life Secd Trs. security, the interest rate is calculated as the change in the average monthly change in the Consumer Price Index plus 185 basis points with the minimum interest rate being 0.0%. This means that the company would not receive interest payments on the security if the average monthly change in the Consumer Price Index is -185 basis points or lower. The absence of interest payments would likely have a negative impact on the security's market value. Furthermore, during prolonged economic conditions that unfavorably affect interest payments of the security, the security may trade, if at all, at a significant discount to its purchase price. Some of the prospectuses disclosed a potential risk that the market for trading these securities may not necessarily exist or be maintained in the future.

The risk that the market for trading these securities may not necessarily exist or be maintained in the future is substantially exacerbated by the very small size of the variable rate corporate debt issues that the company has purchased. Large issues tend to trade more frequently than small issues and investors may have greater awareness about a larger issue because it is widely held and analyzed. An issue size of $250 million represents an approximate lower boundary for a bond issue to attract significant institutional interest when liquidity is a concern. For example, the minimum par amount outstanding for a bond issue's inclusion in the Barclays U.S. Corporate Index is $250 million. The minimum par amount outstanding for a bond issue's inclusion in the Barclays U.S. Floating Rate Note Index is $300 million. A review of the company's variable rate corporate bond portfolio revealed that three of the bonds had the par amounts outstanding ranging from $25,000,000 to $45,000,000.

The objectives of investment regulations as defined in s. 620.01, Wis. Stat., include, in part, to provide for the safety of principal and, to the extent consistent therewith, maximum yield and growth, and to provide sufficient liquidity to avoid the necessity in reasonably expected circumstances for selling assets at undue sacrifice. The interest rate on some of these bonds could drop to 0% for a prolonged period of time, which could significantly impair the value of the bond and prevent the company from earning a reasonable return on their investment. There also may not be a trading market for the security rendering the investment illiquid. In the event that the company may need to dispose of the bond in order to pay claims, there may be no readily available market. It is recommended that, if the company invests in any variable rate corporate debt security, such security must have the following characteristics:

a. the reference for setting the interest rate must be a U.S. Dollar London Interbank Offered Rate of a single specified duration; and
b. the interest rate must have a floor in excess of zero percent; and
c. the total outstanding principal amount of the security at the time of issuance must equal or exceed $250 million.

For the avoidance of any doubt, in investing in any variable rate corporate debt security, the company:

a. may assume that any U.S. Dollar London Interbank Offered Rate will exceed zero percent; and
b. may invest in a security that specifies some increment of interest in excess of a U.S. Dollar London Interbank Offered Rate of a single specified duration; and
c. may invest in a security that is leveraged relative to a U.S. Dollar London Interbank Offered Rate of a single specified duration, provided that there is no basis point reduction in the index provided by the interest rate formula (for example, 125% of the 3-month U.S. Dollar London Interbank Offered Rate is acceptable, while 125% of the 3-month U.S. Dollar London Interbank Offered Rate minus 0.10% is not acceptable); and
d. may not invest in a security that specifies some increment of interest less than a U.S. Dollar London Interbank Offered Rate of a single specified duration, unless such increment is expressed as a percentage of the index (for example, 80% of the 3-month U.S. Dollar London Interbank Offered Rate is acceptable, while the 3-month U.S. Dollar London Interbank Offered Rate minus 0.10% is not acceptable).

It is the responsibility of the board of directors to supervise and direct all investments acquired and held by the company pursuant to s. 6.20 (6) (h), Wis. Adm. Code. This section requires the company's investment strategies and practices are commensurate with its technical and administrative capabilities and expertise with regard to investments. Investments whose interest rate payment is based on complex conditions tied to the results of multiple indices fall outside the area of expertise of town mutual insurers. Further, the board may not delegate its responsibility for overseeing the company's investments to a third-party contractor, pursuant to ss. 612.16 and 611.67, Wis. Stat. The company's board is responsible to oversee the company's investments and the actions of the investment advisor and must understand the details of its investments.

The review of the company's bonds also disclosed the following issues:

1. The company did not have a prospectus for many of its investments in debt securities. It is recommended that the company maintain prospectuses for its current investments.

2. Board minutes did not document how the board of directors approved the investment transactions made by the investment advisor. It is recommended that the minutes clearly indicate board approval of all investment transactions pursuant to s. Ins 6.20 (6) (h), Wis. Adm. Code.

It is recommended that the board of directors modify its written investment policy to specify, in accordance with the instructions included in this report, acceptable characteristics of the investments in variable rate corporate debt securities and provide this office with a copy of the revised investment policy within 60 days of the adoption of this report.

Stocks and Mutual Fund Investments **$1,617,343**

The above asset consists of the aggregate market value of stocks and mutual funds held by the company as of December 31, 2013. Stocks owned by the company are located in a custodial account with Comerica Bank or stored in the safe-deposit box at the company's bank.

Stock certificates that are kept in the safe-deposit box were physically examined by the examiners. 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 2013 on stocks and mutual funds amounted to $1,660 and were traced to cash receipts records. Accrued dividends of $0 at December 31, 2013, were checked and allowed as a nonledger asset.

Book Value of Real Estate **$176,630**

The above amount represents the company's investment in real estate, net of depreciation, as of December 31, 2013. The company's real estate holdings consisted of their home office building.

The required documents supporting the validity of this asset were reviewed and were in order. Adequate hazard insurance was carried on the real estate and contents as noted under the caption "Fidelity Bond and Other Insurance." The company's investment in real estate and related items was in conformance with the Wisconsin Statutes and the rules of the Commissioner of Insurance as regards investments made by town mutual insurers. Real estate depreciation is calculated using the straight-line method.

Premiums, Agents' Balances in Course of Collection **$11,661**

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 **$167,000**

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 **$20,611**

Interest due and accrued on the various assets of the company at December 31, 2013, consists of the following:

Cash deposited at interest	$ 8,410
Bonds	10,025
Total	$20,611

Electronic Data Processing Equipment **$0**

The above balance consists of computer hardware and operating system software, net of depreciation as of December 31, 2013. A review of receipts and other documentation verified the balance. All of the company's electronic data processing equipment has been fully depreciated.

Reinsurance Commission Receivable **$11,300**

The above asset represents the amount of reinsurance commissions that the company expected to receive as of December 31, 2013, under its contract with Wisconsin Reinsurance Corporation. A review of the terms of the reinsurance agreement and year-end accountings with the reinsurer verified the above asset.

Deferred Commission Receivable **$6,700**

The above asset represents the amount of reinsurance commissions that the company expected to receive as of December 31, 2013, under its contract with Wisconsin Reinsurance Corporation. A review of the terms of the reinsurance agreement and year-end accountings with the reinsurer through their unearned premium letter verified the above asset.

Federal Income Tax Recoverable **$12,000**

The above asset represents the amount of federal income tax recoverable the company expected to receive as of December 31, 2013. A review of the company's federal income tax filing verified the above asset.

Furniture and Fixtures **$0**

This asset consists of $2,094 of office furniture owned by the company at December 31, 2013. In accordance with annual statement requirements, this amount has been reported as nonadmitted asset, thus the balance shown above is $0.

LIABILITIES AND SURPLUS

Net Unpaid Losses **$91,000**

This liability represents losses incurred on or prior to December 31, 2013, 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, 2013, with incurred dates in 2013 and prior years. To the actual paid loss figure was added an estimated amount for 2013 and prior losses remaining unpaid at the time of the examination. 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	$599,286	$447,179	$152,107
Less: Reinsurance recoverable on unpaid losses	508,286	357,245	151,041
Net Unpaid Losses	$ 91,000	$ 89,934	$ 1,066

The above difference of $1,066 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 proper proof of loss. 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 properly signed.

Unpaid Loss Adjustment Expenses **$1,000**

This liability represents the company's estimate of amounts necessary to settle losses which were incurred prior to December 31, 2013, but which remained unpaid as of year-end. During review of the company's unpaid loss adjustment expenses balance it was noted the company allocates $1,000 to unpaid loss adjustment expenses at year-end every year. Instead of estimating the amount at $1,000 every year the company should develop a more accurate methodology for estimating their year-end unpaid loss adjusting expenses. It is recommended that the company more accurately estimate the expenses necessary to adjust unpaid losses.

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 inadequately stated. Using the paid-to-paid methodology the examiners came up with an estimate of $14,262. The foregoing amount was not considered material for this examination.

Commissions Payable **$35,510**

This liability represents the commissions payable to agents as of December 31, 2013. The examiners reviewed the company's commission calculation and found the liability to be reasonably stated.

Fire Department Dues Payable **$214**

This liability represents the fire department dues payable to the state of Wisconsin as of December 31, 2013.

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.

Unearned Premiums **$375,398**

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.

Reinsurance Payable **$54,915**

This liability consists of amounts due to the company's reinsurer at December 31, 2013, relating to transactions which occurred on or prior to that date.

December 2013 reinsurer billings	$ 7,413
Deferred reinsurer premiums	47,502
Total	$54,915

Accounts Payable **$894**

This liability consists of amounts due to creditors for office and miscellaneous expenses as of December 31, 2013. Supporting records and subsequent cash disbursements verified this item.

Premiums Received in Advance **$4,157**

This liability represents the total premiums received prior to year-end for policies with effective dates after December 31, 2013. The examiners reviewed 2013 premium and cash receipt records to verify the accuracy of this liability.

V. CONCLUSION

The company was originally organized as a town mutual insurance company on January 7, 1879, under the provisions of the then existing Wisconsin Statutes. The original name of the company was the Theresa Mutual Fire Insurance Company. Subsequent amendments to the company's articles and bylaws changed the company's name to that presently used.

The company has maintained a strong financial position over the examination period. The company has reported a net income in all five years under examination. The company's surplus has increased over $650,000 over the five-year examination period. The increase in admitted assets and surplus was due to the combination of positive investment results and the overall underwriting profitability of the company since the previous exam. Policies in force have increased nearly 11% since the last examination. As a result of the growth, gross premium written has increased 5% and net premium written has increased 12%.

The examination did not result in any changes to surplus. The company complied with all six recommendations from the previous examination report. The current examination resulted in seven recommendations as summarized in the following section.

VI. SUMMARY OF COMMENTS AND RECOMMENDATIONS

1. Page 20 - Book Value of Bonds—It is recommended that the company accurately complete the Bond Investment Income Schedule in accordance with the Town Mutual Annual Statement Instructions.

2. Page 20 - Book Value of Bonds—It is recommended that the company follow investment limitations pursuant to s. Ins 6.20 (6) (f), Wis. Adm. Code.

3. Page 23 - Book Value of Bonds—It is recommended that, if the company invests in any variable rate corporate debt security, such security must have the following characteristics:

   a. the reference for setting the interest rate must be a U.S. Dollar London Interbank Offered Rate of a single specified duration; and
   b. the interest rate must have a floor in excess of zero percent; and
   c. the total outstanding principal amount of the security at the time of issuance must equal or exceed $250 million.

   For the avoidance of any doubt, in investing in any variable rate corporate debt security, the company:

   a. may assume that any U.S. Dollar London Interbank Offered Rate will exceed zero percent; and
   b. may invest in a security that specifies some increment of interest in excess of a U.S. Dollar London Interbank Offered Rate of a single specified duration; and
   c. may invest in a security that is leveraged relative to a U.S. Dollar London Interbank Offered Rate of a single specified duration, provided that there is no basis point reduction in the index provided by the interest rate formula (for example, 125% of the 3-month U.S. Dollar London Interbank Offered Rate is acceptable, while 125% of the 3-month U.S. Dollar London Interbank Offered Rate minus 0.10% is not acceptable); and
   d. may not invest in a security that specifies some increment of interest less than a U.S. Dollar London Interbank Offered Rate of a single specified duration, unless such increment is expressed as a percentage of the index (for example, 80% of the 3-month U.S. Dollar London Interbank Offered Rate is acceptable, while the 3-month U.S. Dollar London Interbank Offered Rate minus 0.10% is not acceptable).

4. Page 24 - Book Value of Bonds—It is recommended that the company maintain prospectuses for its current investments.

5. Page 24 - Book Value of Bonds—It is recommended that the minutes clearly indicate board approval of all investment transactions pursuant to s. Ins 6.20 (6) (h), Wis. Adm. Code.

6. Page 24 - Book Value of Bonds—It is recommended that the board of directors modify its written investment policy to specify, in accordance with the instructions included in this report, acceptable characteristics of the investments in variable rate corporate debt securities and provide this office with a copy of the revised investment policy within 60 days of the adoption of this report.

7. Page 28 - Unpaid Loss Adjustment Expenses—It is recommended that the company more accurately estimate the expenses necessary to adjust unpaid losses.

VII. ACKNOWLEDGMENT

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

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

Respectfully submitted,

Terry Lorenz
Examiner-in-Charge