Report

of the

Examination of

Tri-County Mutual Town Insurance Company

Iron River, Wisconsin

As of December 31, 2010

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State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

Scott Walker, *Governor*
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May 13, 2011

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, 2010, of the affairs and financial condition of:

TRI-COUNTY MUTUAL TOWN INSURANCE COMPANY
Iron River, Wisconsin

and the following report thereon is respectfully submitted:

I. INTRODUCTION

The previous examination of Tri-County Mutual Town Insurance Company (hereinafter Tri-County Mutual or the company) was made in 2006 as of December 31, 2005. The current examination covered the intervening time period ending December 31, 2010, 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 was organized as a town mutual insurance company on January 12, 1909, under the provisions of the then existing Wisconsin Statutes. The original name of the company was the Farmers Mutual Town 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 and 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:

Ashland	Barron
Bayfield	Burnett
Douglas	Iron
Sawyer	Washburn

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 or three years with premiums payable on the advance premium basis. The company also charges an annual policy fee equal to $35.00 and quarterly or semiannual installment fees of $4.00 per installment.

Business of the company is acquired through 24 agents, none of whom are directors of the company. Agents are presently compensated for their services as follows:

Type of Policy	**Compensation**
All lines of business	15%

Agents do not have authority to adjust losses. Members of the adjusting committee of the board have the authority to adjust losses up to $2,000. Losses in excess of this amount are adjusted by one of two independent adjusting services that are used by the company. Board adjusters receive $95 for each loss adjusted plus the IRS allowable mileage for travel allowance. The adjusting services bill the agency based upon a fee schedule that varies depending on the amount of time involved in preparing the claims report for the company.

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
Debra Lulich, President	Insurance Agent	Mason, WI	2012
Blaze Tody, Vice Pres.	Retired Carpentry Contractor	Ashland, WI	2011
Willard Ogren, Sec./Treas.	President, Security State Bank	Iron River, WI	2011
Verlyn Peterson	Farmer	Poplar, WI	2011
Richard Plunkett	Retired Farmer	Poplar, WI	2013
Martin Skaj	Farmer	Mason, WI	2013
Gary Peterson	Farmer	Poplar, WI	2012

No directors are agents for the company.

Members of the board currently receive $135.00 for each meeting attended 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 Compensation
Debra Lulich	President	$1,290
Blaze Tody	Vice-President	795
Willard Ogren	Secretary/Treasurer	530
Scott Ogren *	Manager	795

* Scott Ogren is not a board member but is an employee of and receives compensation from the Security State Agency, Inc.

Reported compensation is the total compensation paid by the insurer for the year and includes salary and director fees. The president is the only board member that receives a salary, which was $625 for the year shown.

The company has formally contracted with the Security State Agency, Inc., an affiliate of the Security State Bank, for the provision of management services since 1984. All day-to-day operations of the company are handled by officers and employees of the Security State Bank. Day-to-day administration of the company is managed by Scott Ogren. He is also an agent for the company. As of the date of this examination, the company paid the Security State Agency, Inc., a monthly management fee of $5,120.43 plus monthly rent of $900.00. This agreement runs through July 9, 2011. Commissions paid to the agency in 2010 were $25,488.73. Security State Agency, Inc., produced 65% of Tri-County Mutual's business in 2010.

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:

Adjusting Committee
Debra Lulich, Chair
Blaze Tody
Gary Peterson
Willard Ogren
Verlyn Peterson

Any three of the four of the above listed committee members, in addition to Chair Debra Lulich, may act as an adjustment committee. Direct contact with at least one member of the adjustment committee is required on all losses over $2,000.

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
2010	$211,654	647	$ (79,386)	$791,500	$645,632
2009	212,803	652	47,637	894,667	716,779
2008	216,186	665	78,777	838,962	690,734
2007	220,406	681	37,763	740,558	600,705
2006	223,306	694	109,674	692,951	549,202
2005	180,405	723	40,671	555,974	427,465

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
2010	$369,814	$213,293	$645,632	33%	57%
2009	355,967	208,010	716,779	29	50
2008	362,289	218,527	690,734	32	52
2007	352,005	213,149	600,705	35	59
2006	361,768	247,995	549,202	45	66
2005	353,944	181,138	427,465	42	83

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
2010	$214,475	$118,241	$211,654	101%	56%	157%
2009	97,265	111,873	212,803	46	53	99
2008	74,493	113,495	216,186	34	52	86
2007	117,550	116,680	220,406	53	55	108
2006	28,647	120,814	223,306	13	49	62
2005	66,163	103,844	180,405	37	57	94

During the period under examination, the company continued to improve its underwriting standards. This is reflected in the increase in gross premiums and a decrease in policies in force. Gross premiums increased by 2% to $369,814 and policies in force have decreased from 694 to 647. The company reported underwriting gains in three out of five years and net income in four out of the past five years. The company’s net loss of $79,386 in 2010 came as a result of unusually high loss claims from two severe wind/hailstorm events in the area.

The previous examination noted that the company surplus had increased by 30% during the five years between 2001 and 2005; during the current five-year period surplus has increased by 18% to $645,632. The composite ratio for 2010 was 157% and the five-year average is 102%. The particularly high loss experience in 2010 tended to skew that figure upward; for the five years 2005 to 2009, the composite ratio averaged 90%.

II. REINSURANCE

The examiners' review of the company's reinsurance portfolio revealed there is currently one ceding treaty. The treaty did contain 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, 2011
Termination provisions:	Until terminated by either party.

The coverages provided under this treaty are summarized as follows:

1.	Type of contract:	Class A: Casualty Quota Share Reinsurance
	Lines reinsured:	Liability
	Company's retention:	0%
	Coverage:	100% of each and every loss, including loss adjustment expense
	Reinsurance premium:	100% of premium written
	Ceding commission:	20% of premium paid Annual deposit premium: $59,000
2.	Type of contract:	Class B: First Surplus
	Lines reinsured:	Property
	Company's retention:	$150,000
	Coverage:	$800,000 excess of $150,000 0% per loss retention
	Reinsurance premium:	Pro rata portion of premium
	Ceding commission:	Commission rate: 15% Profit commission: 15%
3.	Type of contract:	Class C1: First Per Risk Excess of Loss
	Lines reinsured:	Property
	Company's retention:	$35,000
	Coverage:	$45,000 excess of $35,000 $0 aggregate deductable

	Reinsurance premium:	Minimum rate: 6% Maximum rate: 20% Annual deposit premium: $24,489 Current rate: 7.86%
4.	Type of contract:	Class C2: Second Per Risk Excess of Loss
	Lines reinsured:	Property
	Company's retention:	$80,000
	Coverage:	$70,000 excess of $80,000
	Reinsurance premium:	4.50% of written premium Annual deposit premium: $14,020
5.	Type of contract:	Class D/E: First Aggregate Excess of Loss
	Lines reinsured:	All business written by the company
	Company's retention:	70%
	Coverage:	100% of all losses exceeding the attachment point
	Reinsurance premium:	Minimum rate: 6.5% Maximum rate: 20.0% Annual deposit premium: $20,252 Current rate: 6.5%
	Est. attachment point:	$218,095

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, 2010, 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."

Tri-County Mutual Town Insurance Company
Statement of Assets and Liabilities
As of December 31, 2010

Assets	Ledger	Nonledger	Not Admitted	Net Admitted
Cash in checking	$ 31,772	$	$	$ 31,772
Cash deposited at interest	550,071			550,071
Bonds				
Stocks and mutual fund investments	150,088			150,088
Mortgage loans on real estate				
Real estate				
Premiums, agents' balances and installments:				
In course of collection	27,778			27,778
Investment income accrued		824		824
Reinsurance recoverable on paid losses and LAE	8,500			8,500
Electronic data processing equipment	1,549			1,549
Reinsurance premium recoverable	13,321			13,321
Reinsurance commission receivable	5,087			5,087
Prepaid insurance	560			560
Sundry receivable	1,950			1,950
Totals	$790,676	$824	$0	$791,500

Liabilities and Surplus

Net unpaid losses	$ 5,677
Unpaid loss adjustment expenses	1,500
Fire department dues payable	77
Unearned premiums	130,254
Reinsurance payable	8,240
Other liabilities:	
Expense-related:	
Accounts payable	120
Total Liabilities	145,868
Policyholders' surplus	645,632
Total Liabilities and Surplus	$791,500

Tri-County Mutual Town Insurance Company
Statement of Operations
For the Year 2010

Net premiums and assessments earned		$ 211,654
Deduct:		
Net losses incurred	$182,203	
Net loss adjustment expenses incurred	32,272	
Net other underwriting expenses incurred	118,241	
Total losses and expenses incurred		332,716
Net underwriting gain (loss)		(121,062)
Net investment income:		
Net investment income earned	8,937	
Net realized capital gains (losses)	0	
Total investment gain (loss)		8,937
Other income (expense):		
Administrative fees	22,732	
Wood stove fees	9,984	
Other income	23	
Gain (loss) on disposal of fixed assets		
Total other income		32,739
Net Income (Loss)		$ (79,386)

Tri-County Mutual Town Insurance Company
Reconciliation and Analysis of Surplus as Regards Policyholders
For the Five-Year Period Ending December 31, 2010

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:

	2010	**2009**	**2008**	**2007**	**2006**
Surplus, beginning of year	$716,779	$690,734	$600,705	$549,202	$427,465
Net income	(79,386)	47,637	78,777	37,763	109,674
Net unrealized capital gain or (loss)	8,239	(21,592)	11,252	13,740	12,063
Change in nonadmitted assets					
Change in surplus notes					
Other gains and (losses) in surplus:					
Surplus, End of Year	$645,632	$716,779	$690,734	$600,705	$549,202

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, 2010, annual statement			$645,632
Item	**Increase**	**Decrease**	
Deferred premium balance	$6,259	$	
Deferred commission payable		939	
Total	$6,259	$939	
Increase to Surplus per Examination			5,320
Policyholders' Surplus per Examination			$650,952

IV. SUMMARY OF EXAMINATION RESULTS

Compliance with Prior Examination Report Recommendations

The prior examination resulted in three recommendations as follows:

1. Board of Directors—It is recommended that the company comply with s. 612.13, Wis. Stat., regarding the size of the classes of board members.

   Action—Compliance

2. Affiliated Companies—It is recommended that the company notify OCI 30 days prior to the effective date of any contracts with affiliates or amendments thereof, pursuant to s. Ins 40.04 (2), Wis. Adm. Code.

   Action—Compliance

3. Cash and Invested Cash—It is again recommended that the company diversify its investments such that no more than $100,000 is invested in any one financial institution in accordance with the objectives of town mutual insurance company regulations pursuant to s. Ins 6.20 (6) (b) 2, Wis. Adm. Code.

   Action—Compliance

NOTE: The amount noted in the earlier recommendation, $100,000, was changed by congressional action in 2008 to $250,000. This level was made permanent by a provision of the Dodd-Frank Wall Street Reform and Consumer Protection Act in 2010. The company had acted to be in compliance with the lower level of $100,000, but this point was also mitigated by the increase in FDIC insurance coverage.

Current Examination Results

Board of Directors

During 2010, a board member was replaced by a new member. The new member was a named policyholder on a policy that also named his father, who is also a board member. It is recommended that the company establish a policy requiring each director to have a separate policy with the company. The purpose of this policy is to fulfill the town mutual requirement that each director be a policyholder of the company in accordance with ss. 612.10 (1) and 612.13, Wis. Stat. As the company does not have a bylaw that addresses this point, it would be clearer for each board member to be named separately on their own policy

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 unreported conflicts being noted. A discussion of the conflicts can be found in the “Affiliated Companies” section of this report.

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:	
Forgery, larceny, and fraud; theft, embezzlement, misapplication, misappropriation, dishonesty	$ 50,000
Worker's compensation and employer liability:	
Bodily injury by accident (each accident)	$100,000
Bodily injury by disease (each employee)	100,000
Bodily Injury by disease (policy limit)	500,000
Commercial property and liability:	
Business personal property (EDP equipment)	23,240
Damage to premises rented (fire damage)	50,000
Medical payments (any one person)	5,000
General aggregate limit	1,000,000
Products/completed operations aggregate	1,000,000
Each occurrence limit	1,000,000
Professional liability:	
Insurance company professional liability	1,000,000
Directors and officers	1,000,000
ICPL and D&O max aggregate for policy period	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 an independent inspector and then discussed during board meetings. Adjusting committee members of the board are independent of the risk under consideration and review.

Claims Adjusting

The company has an adjusting committee consisting of at least three directors as required by s. 612.13 (4), Wis. Stat. The company's adjusting committee requires at least three of the four committee members who are not the board President and the board President for deliberation. 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 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, 2010.

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

It was discovered that the company voided a check paid to an individual as a donation for speaking at an event representatives of the company attended. It was voided because the company found out that the individual had deceased before cashing the check and thought it was appropriate to do so under this circumstance. According to s. 177.01 (1), Wis. Stat., all intangible property that is issued or owing in the ordinary course of a "holder's" business and that has remained unclaimed by the "owner" for more than five years after it became distributable is presumed abandoned. In this circumstance the company paid an individual as part of its ordinary course of business with the intent that the individual was going to cash the check. Therefore, by voiding the issued check because the individual that it was issued to deceased before cashing it is not in compliance with s. 177, Wis. Stat. It is recommended that the company comply with the determination and reporting of unclaimed property in accordance with s. 177, Wis. Stat.

The examination noted that the affiliated agency's office assistant performs the accounting function and has check-writing authorization. The assistant also has access to open mail, handle cash receipts and make deposits in a bank. It is a sound accounting control to segregate the duties of writing checks and handling of cash from those of performing accounting functions. However, the agency has inadequate staffing currently to better segregate the cash handling function. It is recommended that the company, given the small number of employees involved, have a board member review the check register and bank reconciliation at each board meeting so as to add a level of oversight to the check/cash accounting function in accordance with s. Ins 13.05 (4), Wis. Adm. Code.

The checking account's signature card describes that all checks/disbursements require only one individual listed on the account signature card, which means that there is no limit placed on the amount that any one named signer can write. The requirement of having two individuals sign checks that meet a threshold established by the board is a sound control that would help prevent possible fraudulent activities. It is recommended that the company require two signers for checks whose amounts meet a threshold established by its board of directors, pursuant to s. Ins 13.05 (4) (b), Wis. Adm. Code. Note that this procedure is recommended since it was found during the examination process that the company utilizes a signature stamp for one of its signers that is not properly safeguarded.

The insurance agency that the company utilizes to perform its day-to-day operations has not properly safeguarded the company's blank checks or a signature stamp utilized by one of its signers. It was found that blank manual checks and a signature stamp of one of the authorized signers on the company's checking account are kept in an unlocked desk, which leaves the company at a greater risk of possible fraudulent activity. It is recommended that the company require the agency that performs its day-to-day operations to properly safeguard its blank checks and signature stamp utilized by one of the authorized signers on the account.

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 computer hard drives monthly. Data cartridge back up is done every two months and the backed-up data is kept on-site in a vault and a second copy off-site.

The company has manuals documenting the use of its software and outlining the steps to complete specific tasks. The company's staff also has access to the vendor's Web site and phone support. Software updates are automatically downloaded to the system. Training is offered to users of the system by the vendor on a regular basis.

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 examiners discussed the continuity of the business with company management, considering the age of several of its key employees. Responses were adequate. Given the small number of employees who work on company-related business, management has attempted to have adequate backup for key operations.

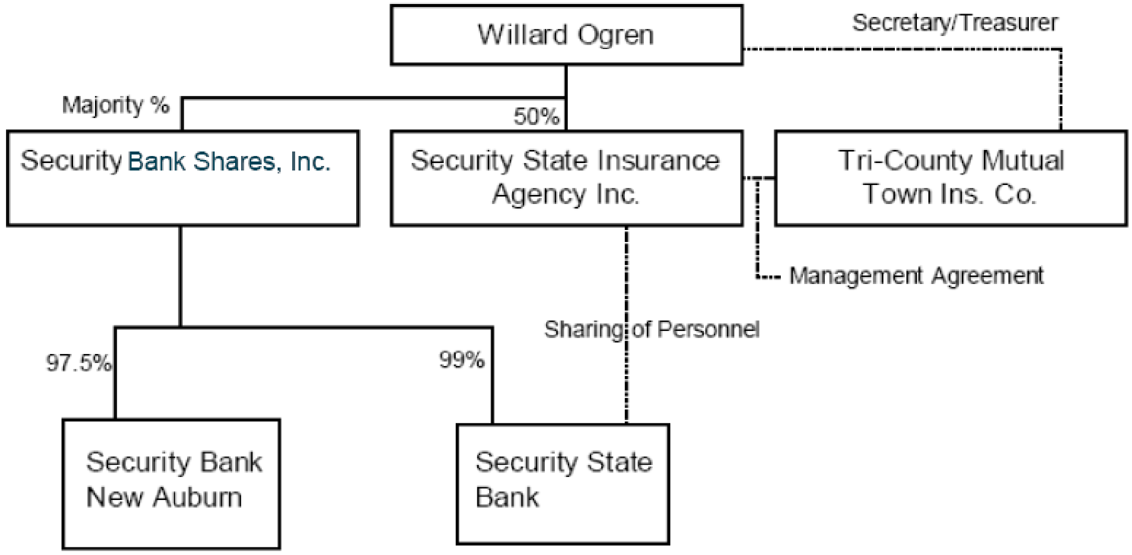
Affiliated Companies

Tri-County Mutual Town Insurance Company is a member of an insurance holding company system as defined by s. Ins 40.01, Wis. Adm. Code, the principal controlling person of which is Willard Ogren, secretary-treasurer of Tri-County Mutual. Pursuant to s. 600.03 (1), Wis. Stat., an "affiliate of a person means any other person who controls, is controlled by, or is under common control with, the first person. A corporation is an affiliate of another corporation, regardless of ownership, if substantially the same group of persons manages the two corporations." Pursuant to s. 600.03 (13), Wis. Stat., "control" means the possession, directly or indirectly, of the power to direct or cause the direction of management and policies of a person, whether through ownership of voting securities, by contract, by company management, or otherwise.

In light of the statutes cited, Tri-County Mutual is affiliated with certain companies under the direction of its secretary-treasurer, Willard Ogren. Willard Ogren owns 50% of the Security State Insurance Agency, Inc. The agency provided copies of its financial statements to examiners; however, it requested they not be disclosed in this report because the agency does not report its financial statements to the public. This agency has a contract to manage Tri-County Mutual for a flat monthly fee as was previously disclosed in this report. This agency also writes business for the company. Tri-County Mutual represents approximately 30% of the agency's total business, while Security State Insurance Agency produces approximately 65% of Tri-County Mutual's business.

Willard Ogren is president and majority stockholder of Security Bank Shares, Inc., a bank holding company domiciled in Wisconsin. Security Bank Shares, Inc., reported assets of $19,230,570, liabilities of $849,627, and stockholders' equity of $18,380,943 for fiscal year ending September 30, 2010. Net loss of $123,879 was reported for this same fiscal period. Security Bank Shares, Inc., is the majority stockholder of Security State Bank and Security Bank, New Auburn. Security State Bank reported assets of $92,152,000, liabilities of $80,929,000, and total capital and surplus of $11,223,000. The bank had a net income of $909,000 in 2010. Both subsidiaries are Wisconsin corporations. As of December 31, 2010, approximately 17% of Tri-County Mutual's admitted assets consisted of financial products of Security State Bank. In addition, Tri-County Mutual's manager, Security State Insurance Agency, Inc., makes use of employees of Security State Bank in the conduct of Tri-County Mutual's operations. Affiliation with these corporate entities is through the common management control of Willard Ogren, augmented by financial and operational reliance on Security State Bank.

The following chart depicts the organizational structure of the holding company.



Security State Insurance Agency, Inc.'s management contract is reviewed annually by the board of directors. According to the Wisconsin Administrative Code, the company should notify this office 30 days prior to any changes to an affiliated contract on a Form D filing.

The company's management contract with Security State Insurance Agency, Inc., was changed a number of times during the examination period. These were primarily to adjust the management fees. However, it has not been the company's practice to notify this office of the changes to the contract. It is recommended that the company notify the Office of the Commissioner of Insurance (OCI) 30 days prior to the effective date of any contracts with affiliates or amendments thereof, pursuant to s. Ins 40.04 (2), Wis. Adm. Code.

The company utilizes the Security State Bank's equipment and paper to make photocopies, send faxes and to provide postage. The company reimburses the bank for use of the copy machine and fax machine based on rates set by the bank and reimburses for postage used. However, there is no executed agreement between the bank and the company outlining the use of the banks equipment and associated reimbursement rates. Company employees reported that the board does review the rates charged by the bank but does not formally have these rates approved by the board. This should also be included in the agreement. It is recommended that the company execute an equipment use and services agreement with the Security State Bank covering use of the bank's copy machine and faxes as well as postage services which would need to be approved by the company's board of directors.

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	$445,868
2.	Liabilities plus 33% of gross premiums written	267,907
3.	Liabilities plus 50% of net premiums written	252,515
4.	Amount required (greater of 1, 2, or 3)	445,868
5.	Amount of Type 1 investments as of 12/31/2010	581,843
6.	Excess or (deficiency)	$135,975

The company has sufficient Type 1 investments. The level of insurance provided by the FDIC to account holders was raised from $100,000, the level in place during the previous examination, to $250,000 currently.

The investment rule prescribes that a town mutual shall divest of any investment which does not comply with the rule within three years of its noncompliance unless the Commissioner permits a longer period or requires a shorter period. Currently the company has permission to hold certain investments, with a statement value of $150,088, which are in compliance with the new investment rule.

ASSETS

Cash and Invested Cash **$581,843**

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

Cash in company's office	$ 0
Cash deposited in banks—checking accounts	31,772
Cash deposited in banks at interest	550,071
Total	$581,843

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 balance was made by obtaining confirmations directly from the auditor and reconciling the amounts shown thereon to company records.

Cash deposited in banks represents the aggregate of ten deposits in five depositories. Deposits were verified by obtaining confirmations from the auditor and by an actual count and inspection of certificates and/or passbooks. Interest received during the year 2010 totaled $11,725 and was verified to company cash records. Rates of interest earned on cash deposits ranged from 0.75% to 2.72%. Accrued interest on cash deposits totaled $824 at year-end.

Stocks and Mutual Fund Investments **$150,088**

The above asset consists of the aggregate market value of stocks and mutual funds held by the company as of December 31, 2010. Stocks owned by the company are located in the company's safe deposit box.

Stock certificates 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 2010 on stocks and mutual funds amounted to $1,038 and were traced to cash receipts records. There were no accrued dividends at December 31, 2010.

Premiums, Agents' Balances in Course of Collection **$27,778**

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 individual agency accounts verified the accuracy of this asset.

Premiums Deferred and Not Yet Due **$5,320**

This asset represents modal premium installments (such as monthly, quarterly, etc.) that are not yet due. Deferred premiums as reported in the company's deferred premium report as of December 31, 2010, are accurate.

In 2010 the company began offering its policyholders an option to pay annual policy premiums on an installment basis. However, it was discovered that the company did not report as an asset its deferred premiums of $6,259 at year-end 2010. Since the deferred amount exceeds tolerable error set for this examination, an examination recommendation is warranted as well as an adjustment to surplus (shown as an increase on page 12). Note that 15% of the deferred premium balance would be reported as a deferred commissions' payable liability ($939). As a result of this recommendation and adjustment to surplus, $6,259 was added as an asset to the company's balance sheet and $939 to liabilities, for a net effect of this change to increase company surplus by $5,320. It is recommended that the company report deferred premiums in accordance with the Town Mutual Annual Statement Instructions.

Investment Income Accrued **$824**

Interest due and accrued on the various assets of the company at December 31, 2010, relates to Cash Deposited at Interest.

Reinsurance Recoverable on Paid Losses and LAE **$8,500**

The above asset represents an estimate made by the auditor of recoveries due the company from reinsurance on losses and loss adjusting expenses which were paid on or prior to December 31, 2010. A review of year-end accountings with the reinsurer, which was received by the company in May, reported the actual amount to be $10,023.47. The letter from the reinsurer showing this calculation verified the amount actually received.

Electronic Data Processing Equipment **$1,549**

The above balance consists of computer hardware and operating system software, net of depreciation as of December 31, 2010. A review of the auditor's work papers calculating EDP equipment depreciation verified the balance. Non-operating system software was properly nonadmitted.

Other Assets – Prepaid Insurance **$560**

The company pays for a portion of its commercial insurance when it is invoiced. The payment made in the amount of $560 was paid prior to year-end 2010 and should have been nonadmitted as an asset in the company's annual statement. It is recommended that the company properly nonadmit any prepaid insurance premium in its annual statement in future years in accordance with the Town Mutual Annual Statement Instructions.

Other Assets – Sundry Receivable **$1,950**

The company issued a duplicate check in the amount of $1,950 for the payment of a claim, believing that the first check that it had written for the claim had been voided and not cashed. It later learned that both checks were in fact cashed and was able to recover repayment for the second check which it deposited after fiscal year-end. We note that this duplicate payment, while not rising to the level of an exam recommendation, could have created problems for the company if they were not able to recover the amount of the duplicate payment. While apparently caused by an inadvertent error, the company should re-examine its procedures for issuing duplicate checks in the event that it believes that a check has been voided or lost, including necessary steps to stop payment on the original check.

LIABILITIES AND SURPLUS

Net Unpaid Losses **$5,677**

This liability represents losses incurred on or prior to December 31, 2010, 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, 2010, with incurred dates in 2010 and prior years. To the actual paid loss figure was added an estimated amount for 2010 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	$29,177	$9,470	$19,707
Less: Reinsurance recoverable on unpaid losses	23,500	5,582	17,918
Net Unpaid Losses	$ 5,677	$3,888	$ 1,789

The above difference of $1,789 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 not maintained.
2. Claim files contained sufficient investigatory data and documentation to verify settlement payments or reserve estimates.
3. Proofs of loss were properly signed.

It was noted by the examiners that the company's manual claims register does not estimate a reserve for a loss for all claims that are filed. This became apparent upon observing open claims at the end of 2010. A more through examination of the company's claim register indicated that in about half of the cases, the company did establish a reserve estimate for the claim, and in the other half no reserve was established. At present, it seems that loss reserving is done on an inconsistent basis, with some claims having a reserve established, and others not. It is recommended that the company institute a policy of establishing a reserve for loss for all claims that are filed with the company, in compliance with s. Ins 13.05 (3) (f), Wis. Adm. Code.

Unpaid Loss Adjustment Expenses **$1,500**

This liability represents the company's estimate of amounts necessary to settle losses which were incurred prior to December 31, 2010, but which remained unpaid as of year-end. The methodology used by the company in establishing this liability is an estimate by the CPA using a percentage of losses based on historical data.

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.

Fire Department Dues Payable **$77**

This liability represents the fire department dues payable to the State of Wisconsin as of December 31, 2010.

The examiners reviewed the company's fire department dues calculation and found this liability to be correctly calculated. The actual amount due was verified to dues payable records of OCI.

Unearned Premiums **$130,254**

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 50% of the net premium in force methodology.

Reinsurance Payable **$8,240**

This liability consists of amounts due to the company's reinsurer at December 31, 2010, relating to transactions which occurred on or prior to that date.

Class A: Liability	$3,666
Class B: Property Pro Rata	1,831
Class C: Property EOL	1,091
Class D: Stop Loss	1,455
Estimated Premium Adjustment	197
Total	$8,240

Accounts Payable **$120**

This liability consists of three invoices due to the company's computer consultants due and unpaid at year-end.

V. CONCLUSION

Tri-County Mutual Town Insurance Company is a town mutual insurer covering an eight-county area. The company has been in business for more than 102 years providing property and liability insurance to its policyholders.

The company has reported underwriting gains for three of the five years during the examination period and net income for four out of five years during the examination period. The company recorded a net loss of $79,386 in 2010. As noted earlier, the company experienced an unusually high level of claims in 2010 due to several severe weather events in the region. Gross premiums written have increased since 2006, while net premiums written have declined and policies in force have decreased from 694 to 647. Surplus increased 18% over the five-year period since the last examination to $645,632. The previous examination report noted that surplus increased 30% between 2001 and 2005.

The examination resulted in ten recommendations. These recommendations are listed in the next section of this report. All three recommendations from the prior examination report have been complied with by the company.

VI. SUMMARY OF COMMENTS AND RECOMMENDATIONS

1. Page 14 - Board of Directors—It is recommended that the company establish a policy requiring each director to have a separate policy with the company.

2. Page 16 - Accounts and Records—It is recommended that the company comply with the determination and reporting of unclaimed property in accordance with s. 177, Wis. Stat.

3. Page 17 - Accounts and Records—It is recommended that the company, given the small number of employees involved, have a board member review the check register and bank reconciliation at each board meeting so as to add a level of oversight to the check/cash accounting function in accordance with s. Ins 13.05 (4), Wis. Adm. Code.

4. Page 17 - Accounts and Records—It is recommended that the company require two signers for checks whose amounts meet a threshold established by its board of directors, pursuant to s. Ins 13.05 (4) (b), Wis. Adm. Code. Note that this procedure is recommended since it was found during the examination process that the company utilizes a signature stamp for one of its signers that is not properly safeguarded.

5. Page 17 - Accounts and Records—It is recommended that the company require the agency that performs its day-to-day operations to properly safeguard its blank checks and signature stamp utilized by one of the authorized signers on the account.

6. Page 20 - Affiliated Companies—It is recommended that the company notify the Office of the Commissioner of Insurance (OCI) 30 days prior to the effective date of any contracts with affiliates or amendments thereof, pursuant to s. Ins 40.04 (2), Wis. Adm. Code.

7. Page 20 - Affiliated Companies—It is recommended that the company execute an equipment use and services agreement with the Security State Bank covering use of the bank's copy machine and faxes as well as postage services which would need to be approved by the company's board of directors.

8. Page 24 - Premiums Deferred and Not Yet Due—It is recommended that the company report deferred premiums in accordance with the Town Mutual Annual Statement Instructions.

9. Page 25 - Other Assets – Prepaid Insurance—It is recommended that the company properly nonadmit any prepaid insurance premium in its annual statement in future years in accordance with the Town Mutual Annual Statement Instructions.

10. Page 27 - Net Unpaid Losses—It is recommended that the company institute a policy of establishing a reserve for loss for all claims that are filed with the company, in compliance with s. Ins 13.05 (3) (f), Wis. Adm. Code.

VII. ACKNOWLEDGMENT

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

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

Respectfully submitted,

Richard Janosik
Examiner-in-Charge