

Report
of the
Examination of
Wisconsin Municipal Mutual Insurance Company
Madison, Wisconsin
As of December 31, 2012

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State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

Scott Walker, Governor
Theodore K. Nickel, Commissioner

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April 28, 2014

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Honorable Theodore K. Nickel
Commissioner of Insurance
State of Wisconsin
125 South Webster Street
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Commissioner:

In accordance with your instructions, a compliance examination has been made of the affairs and financial condition of:

WISCONSIN MUNICIPAL MUTUAL INSURANCE COMPANY
Madison, Wisconsin

and this report is respectfully submitted.

I. INTRODUCTION

The previous examination of Wisconsin Municipal Mutual Insurance Company (WMMIC or the company) was conducted in 2009 as of December 31, 2008. The current examination covered the intervening period ending December 31, 2012, and included a review of such 2013 transactions as deemed necessary to complete the examination.

The examination was conducted using a risk-focused approach in accordance with the NAIC Financial Condition Examiners Handbook, which sets forth guidance for planning and performing an examination to evaluate the financial condition and identify prospective risks of an insurer. This approach includes the obtaining of information about the company including corporate governance, the identification and assessment of inherent risks within the company, and the evaluation of system controls and procedures used by the company to mitigate those risks. The examination also included an assessment of the principles used and significant estimates made by management, as well as an evaluation of the overall financial statement presentation and management's compliance with statutory accounting principles, annual statement instructions, and Wisconsin laws and regulations.

The examination consisted of a review of all major phases of the company's operations and included the following areas:

- History
- Management and Control
- Corporate Records
- Conflict of Interest
- Fidelity Bonds and Other Insurance
- Employees' Welfare and Pension Plans
- Territory and Plan of Operations
- Growth of Company
- Reinsurance
- Financial Statements
- Accounts and Records
- Data Processing

Emphasis was placed on the audit of those areas of the company's operations accorded a high priority by the examiner-in-charge when planning the examination. Special attention was given to the action taken by the company to satisfy the recommendations and comments made in the previous examination report.

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

II. HISTORY AND PLAN OF OPERATION

In 1987, the company was incorporated under s. 66.30, Wis. Stat., as a “joint powers authority” rather than under the Wisconsin insurance statutes. The company was organized due to significant premium increases being experienced by municipalities and the inability of certain municipalities to obtain insurance in the mid-1980s. On December 22, 1987, the company was issued a certificate of authority to operate as a mutual insurance company under ch. 611, Wis. Stat., for the purpose of providing automobile liability and general liability insurance at a reasonable cost to its members. WMMIC began offering worker’s compensation insurance coverage in 2000. The company discontinued the program in 2010 and resumed offering worker’s compensation coverage in January of 2013. Administrative services for worker’s compensation claims are performed mainly by various third parties with WMMIC providing worker’s compensation claims administrative services for three members. All of the company’s members are counties, cities or other municipal entities within the state of Wisconsin, and the company is licensed only in Wisconsin.

In Wisconsin, municipalities have limited exposure to large general liability and automobile liability claims due to a tort cap of \$50,000 on general liability and \$250,000 on automobile liability pursuant to ss. 893.80 (3) and 345.05 (3), Wis. Stat., respectively. However, no tort cap is effective for miscellaneous liability actions, such as those brought in federal court, or for worker’s compensation.

Currently, WMMIC is comprised of 18 members which include 2 cities, 15 counties and 1 special-use district which is not an equity member. WMMIC members may purchase general liability, auto liability, and public official’s errors and omission liability coverage. WMMIC also resumed offering worker’s compensation coverage in 2013.

Of WMMIC’s members, 17 were required to contribute capital to the company when they became members. One member, the Brown County Stadium District (SUD), has purchased public officials error and omission liability coverage since 2004, but was not required to contribute capital. At the July 12, 2013, meeting, the board of directors approved the SUD’s request to

purchase general liability coverage from the company, effective January 1, 2004. The SUD remains a non-equity member.

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

Line of Business	Direct Premium	Reinsurance Assumed	Reinsurance Ceded	Net Premium
Other liability – occurrence	\$2,735,049	\$0	\$491,940	\$2,243,109
Commercial auto liability	<u>1,506,038</u>	<u>0</u>	<u>276,717</u>	<u>1,229,321</u>
Total All Lines	<u>\$4,241,087</u>	<u>\$0</u>	<u>\$768,657</u>	<u>\$3,472,430</u>

Capital Structure

Initial capitalization of \$13.3 million was obtained through the company’s public offering of tax-exempt serial revenue bonds. In order to count the bonds as surplus and to have an assured revenue source with respect to payment of principal and interest, the following occurred:

1. A letter of credit was obtained to assure payment of the bond obligations.
2. Each member policyholder issued a promissory note to the bank as collateral for the letter of credit, which in total equaled the principal and interest payments.

Payments of the principal and interest were funded by member payments on the promissory notes and dividends from the company. In the event that funding requirements were not met to cover the bond obligations, the letter of credit could have been called. The letter of credit was renewed in 1996 to match the outstanding debt for the years 1997 through 2007.

In an order issued by the Commissioner, the company is exempt from several provisions of the statutes and insurance administrative code. Pursuant to s. 611.23, Wis. Stat., the Commissioner has waived the following statutes:

- Sections 611.74 and 181.50, Wis. Stat. Section 8.01 (e) of the articles of incorporation is more restrictive regarding dissolution.
- Section 611.32 (2), Wis. Stat., but s. 66.066, Wis. Stat., is applicable to bonds issued.

- Sections 620.22 and 620.23, Wis. Stat., but s. 66.04, Wis. Stat., is applicable regarding investment limitations.
- Sections 645.72 (4) (e) and 611.74 (4), Wis. Stat. Section 8.02 of the articles of incorporation, which provides for the distribution of assets in rehabilitation or liquidation, is applicable.

The order allows the company to exclude its revenue bond obligation from the initial capitalization as a liability on the balance sheet, due to the bonds being supported by a letter of credit. The order also allows the company to accept general obligation securities issued by new members as capital contributions. However, such securities shall not be counted towards compulsory and security surplus calculations. Except for capital contributions from new members, the company shall not invest in any securities issued by member municipalities at any time. WMMIC had established an investment program, which matched its obligations with program earnings.

Membership Structure

Each municipality has a self-insured retention (SIR) limit and an annual aggregate retention limit, which is based on an actuarial valuation. Each member is obligated to fund losses until the SIR limit is reached. A list of the current members' 2012 single and aggregate retentions for casualty and liability claims is as follows:

Member	Single	Aggregate
Brown County	\$250,000	\$1,075,000
Brown County Stadium Dist.*	5,000	50,000
Chippewa County	100,000	300,000
City of Eau Claire	200,000	400,000
City of Madison	300,000	1,550,000
Dane County	250,000	1,500,000
Dodge County	100,000	450,000
Eau Claire County	150,000	400,000
Jefferson County	150,000	525,000
Kenosha County	200,000	925,000
La Crosse County	150,000	475,000
Manitowoc County	125,000	400,000
Marathon County	250,000	1,050,000
Outagamie County	200,000	750,000
Rock County	200,000	850,000
St. Croix County	500,000	1,500,000
Walworth County	200,000	650,000
Waukesha County	400,000	1,300,000

* Brown County Stadium District's SIR of 5,000/50,000 was effective on January 1, 2014. All other SIRs listed above are as of the examination date.

All new members joining the company may be required to contribute equity based on an actuarially determined risk level that each member brings to the company. New members' contributions may either be distributed back to the existing members based on their equity percentage, or the contributions can be used to increase surplus. To date, all members except the SUD, explained above, have contributed capital to WMMIC. No new members were added since the prior examination. The table below shows each member's equity investment in WMMIC as of December 31, 2012.

Member	Amount	Percent
Brown County	\$ 2,725,827	7.13%
Chippewa County	1,266,493	3.31
City of Eau Claire	1,280,391	3.35
City of Madison	6,087,350	15.93
Dane County	3,562,106	9.32
Dodge County	1,473,366	3.85
Eau Claire County	1,441,147	3.77
Jefferson County	925,452	2.42
Kenosha County	2,345,175	6.14
La Crosse County	1,369,947	3.58
Manitowoc County	2,181,104	5.71
Marathon County	2,281,858	5.97
Outagamie County	2,373,547	6.21
Rock County	1,636,185	4.28
St. Croix County	1,548,836	4.05
Walworth County	1,849,453	4.84
Waukesha County	<u>3,872,513</u>	<u>10.13</u>
Total	<u>\$38,220,750</u>	<u>100.00%</u>

III. MANAGEMENT AND CONTROL

Board of Directors

The board of directors consists of seven members. Five of the directors are elected to serve three-year staggered terms, while two directors are elected annually to serve one-year terms. Officers are elected at the board's annual meeting. Currently, the board members are not compensated for serving on the board. However, board members receive reimbursement for meals, lodging, and mileage at the state government rate for travel expenses when attending meetings. Currently the board of directors consists of the following persons:

Name and Residence	Principal Occupation	Term Expires
Daniel Lowndes Madison, WI	Risk Manager Dane County	2014
Connie Goss Eau Claire, WI	Risk Manager Chippewa County	2014
Colleen Schian Eau Claire, WI	Risk Manager City of Eau Claire	2014
Eric Veum Sun Prairie, WI	Risk Manager City of Madison	2014
Kristi Kordus Mosinee, WI	Finance Director Marathon County	2015
Laura Stauffer Waukesha, WI	Risk/Purchasing Manager Waukesha County	2015
James Olson Pleasant Prairie, WI	Risk Manager and Personnel Analyst Kenosha County	2016

Officers of the Company

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

Name	Office	2012 Compensation
Dean Boes	Executive Director	\$131,299
Kristi Kordus	Chairman	0
Mary Jo Maly	Secretary	0
Norman A. Cummings	Treasurer	0

Committees of the Board

The company's bylaws allow for the formation of certain committees by the board of directors. The committees at the time of the examination are listed below:

Claims Committee

Connie Goss, Chair
Daniel Lowndes
Colleen Schian
Laura Stauffer

Underwriting Committee

Laura Stauffer, Chair
Connie Goss
James Olson
Colleen Schian
Eric Veum

Finance Committee

Kristi Kordus, Chair
Daniel Lowndes
Eric Veum

Each committee consists of at least three directors, as well as representatives of member municipalities who are not directors. Only WMMIC board members are included in the committees listed above. Since the prior examination the company amended its bylaws to make any committee resolution advisory only. According to the amended bylaws only the board of directors has authority to pass binding resolutions; committee resolutions are only to advise the board.

IV. REINSURANCE

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

Ceding Contracts

1. Type: Excess of Loss

Reinsurer: Government Entities Mutual (GEM) 33%
General Reinsurance Corporation 67%

Scope: Casualty Excess of Loss
 - General liability (includes law enforcement activities) written on an occurrence basis
 - Auto liability (includes uninsured motorists) written on an occurrence basis
 - Public officials' errors and omissions liability (includes employee benefits liability) written on an occurrence basis
Retention: \$1,000,000 per any one loss occurrence per member

Coverage: \$9,000,000 per occurrence in respect of all lines of coverage/per member. Loss adjustment expense related to public officials' errors and omissions liability is included in net loss. Loss adjustment expense related to other coverages is paid proportionate to the reinsurer's share of net loss.

Company policy limits should not exceed:

General liability: \$10,000,000 each occurrence
30,000,000 aggregate per member

Automobile liability: \$10,000,000 each accident

Public officials E&O liability: \$10,000,000 each claim
30,000,000 aggregate per member

Premium: \$764,546

Effective date: January 1, 2013, to January 1, 2014

Termination: By either party at any time with 120 days' advance written notice
2. Type: Excess of Loss

Reinsurer: Safety National Casualty Corporation

Scope: Excess worker's compensation and employers' liability

V. FINANCIAL DATA

The following financial statements reflect the financial condition of the company as reported to the Commissioner of Insurance in the December 31, 2012, annual statement. Also included in this section are schedules that reflect the growth of the company, NAIC Insurance Regulatory Information System (IRIS) ratio results for the period under examination, and the compulsory and security surplus calculation. Adjustments made as a result of the examination are noted at the end of this section in the area captioned "Reconciliation of Surplus per Examination."

Wisconsin Municipal Mutual Insurance Company
Assets
As of December 31, 2012

	Assets	Nonadmitted Assets	Net Admitted Assets
Bonds	\$43,271,752	\$	\$43,271,752
Cash, cash equivalents, and short-term investments	1,409,477		1,409,477
Other invested assets	914,880		914,880
Receivables for securities			
Investment income due and accrued	154,346		154,346
Write-ins for other than invested assets:			
Investments held for self-insured retention member accounts	7,450,880		7,450,880
Accounts receivable	3,000		3,000
Prepaid expense	<u>3,424</u>	<u>3,424</u>	<u> </u>
Total Assets	<u>\$53,207,759</u>	<u>\$3,424</u>	<u>\$53,204,335</u>

Wisconsin Municipal Mutual Insurance Company
Liabilities, Surplus, and Other Funds
As of December 31, 2012

Losses		\$ 4,734,422
Loss adjustment expenses		724,791
Other expenses (excluding taxes, licenses, and fees)		141,634
Dividends declared and unpaid:		
Policyholders		1,931,858
Write-ins for liabilities:		
Amount withheld for member SIR accounts		<u>7,450,880</u>
Total liabilities		14,983,585
Gross paid in and contributed surplus	\$24,043,665	
Unassigned funds (surplus)	<u>14,177,085</u>	
Surplus as regards policyholders		<u>38,220,750</u>
Total Liabilities and Surplus		<u>\$53,204,335</u>

**Wisconsin Municipal Mutual Insurance Company
Summary of Operations
For the Year 2012**

Underwriting Income		
Premiums earned		\$3,472,430
Deductions:		
Losses incurred	\$(809,684)	
Loss adjustment expenses incurred	6,472	
Other underwriting expenses incurred	<u>865,360</u>	
Total underwriting deductions		<u>62,148</u>
Net underwriting gain (loss)		3,410,282
Investment Income		
Net investment income earned	610,950	
Net realized capital gains (losses)	<u>584,921</u>	
Net investment gain (loss)		1,195,871
Net income (loss) before dividends to policyholders and before federal and foreign income taxes		
		4,606,153
Dividends to policyholders		<u>1,931,858</u>
Net income (loss) after dividends to policyholders but before federal and foreign income taxes		
		2,674,295
Federal and foreign income taxes incurred		<u> </u>
Net Income		<u>\$2,674,295</u>

Wisconsin Municipal Mutual Insurance Company
Cash Flow
For the Year 2012

Premiums collected net of reinsurance		\$3,472,430
Net investment income		<u>926,591</u>
Total		4,399,021
Benefit- and loss-related payments	\$ 724,466	
Commissions, expenses paid, and aggregate write-ins for deductions	1,171,013	
Dividends paid to policyholders	<u>1,879,998</u>	
Total deductions		<u>3,775,477</u>
Net cash from operations		623,544
Proceeds from investments sold, matured, or repaid:		
Bonds	<u>\$17,264,465</u>	
Total investment proceeds		17,264,465
Cost of investments acquired (long-term only):		
Bonds	<u>18,502,085</u>	
Total investments acquired	<u>18,502,085</u>	
Net cash from investments		(1,237,620)
Cash from financing and miscellaneous sources:		
Other cash provided (applied)	<u>(6,424)</u>	
Net cash from financing and miscellaneous sources		<u>(6,424)</u>
Reconciliation:		
Net change in cash, cash equivalents, and short-term investments		(620,500)
Cash, cash equivalents, and short-term investments:		
Beginning of year		<u>2,029,977</u>
End of Year		<u>\$1,409,477</u>

**Wisconsin Municipal Mutual Insurance Company
Compulsory and Security Surplus Calculation
December 31, 2012**

Assets		\$53,204,335
Less liabilities		<u>14,983,585</u>
Adjusted surplus		38,220,750
Annual premium:		
Lines other than accident and health	\$1,540,572	
Factor	<u>20%</u>	
Compulsory surplus (subject to a minimum of \$2 million)		<u>2,000,000</u>
Compulsory Surplus Excess (or Deficit)		<u>\$36,220,750</u>
Adjusted surplus (from above)		\$38,220,750
Security surplus: (140% of compulsory surplus, factor reduced 1% for each \$33 million in premium written in excess of \$10 million, with a minimum factor of 110%)		<u>2,800,000</u>
Security Surplus Excess (or Deficit)		<u>\$35,420,750</u>

**Wisconsin Municipal Mutual Insurance Company
Analysis of Surplus
For the Four-Year Period Ending December 31, 2012**

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

	2012	2011	2010	2009
Surplus, beginning of year	\$35,440,579	\$34,348,345	\$33,666,191	\$33,611,655
Net income	2,674,295	717,031	466,038	(158,209)
Change in net unrealized capital gains/losses	109,300	375,203	153,385	87,745
Change in nonadmitted assets	(3,424)			
Change in provision for reinsurance				125,000
Surplus adjustments: Paid in	_____	_____	62,731	_____
Surplus, End of Year	<u>\$38,220,750</u>	<u>\$35,440,579</u>	<u>\$34,348,345</u>	<u>\$33,666,191</u>

**Wisconsin Municipal Mutual Insurance Company
Insurance Regulatory Information System
For the Four-Year Period Ending December 31, 2012**

The company's NAIC Insurance Regulatory Information System (IRIS) results for the period under examination are summarized below. Unusual IRIS results are denoted with asterisks and discussed below the table.

Ratio	2012	2011	2010	2009
#1 Gross Premium to Surplus	11%	12%	13%	13%
#2 Net Premium to Surplus	9	9	9	9
#3 Change in Net Premiums Written	3	4	3	4
#4 Surplus Aid to Surplus	0	0	0	0
#5 Two-Year Overall Operating Ratio	61	90	101*	107*
#6 Investment Yield	1.4*	1.7*	2.8*	4.0
#7 Gross Change in Surplus	8	3	2	0
#8 Change in Adjusted Surplus	8	3	2	0
#9 Liabilities to Liquid Assets	33	37	39	38
#10 Agents' Balances to Surplus	0	0	0	0
#11 One-Year Reserve Development to Surplus	(10)	(4)	(1)	(2)
#12 Two-Year Reserve Development to Surplus	(11)	(5)	(1)	2
#13 Estimated Current Reserve Deficiency to Surplus	0	0	0	0

Ratio No. 5 measures the company's profitability over the previous two-year period. The company reported the exceptional results for 2009 and 2010 despite the fact that it reported an underwriting gain in each of these two years. However, WMMIC consistently distributes large dividends to its members, which, in combination with smaller than usual underwriting gains in 2009 and 2010 and an underwriting loss in 2008, produced the exceptional results.

Ratio No. 6 measures the average return on the company's investments. The exceptional results for 2012, 2011 and 2010 were mainly due to low interest rate environment of recent years.

Growth of Wisconsin Municipal Mutual Insurance Company

Year	Admitted Assets	Liabilities	Surplus as Regards Policyholders	Net Income
2012	\$53,204,335	\$14,983,585	\$38,220,750	\$2,674,295
2011	51,718,259	16,277,680	35,440,579	717,031
2010	51,674,560	17,326,215	34,348,345	466,038
2009	49,621,839	15,955,648	33,666,191	(158,209)
2008	48,414,583	14,802,928	33,611,655	(284,811)

Year	Gross Premium Written	Net Premium Written	Premium Earned	Loss and LAE Ratio	Expense Ratio	Combined Ratio
2012	\$4,241,087	\$3,472,430	\$3,472,430	(23.1)%	24.9%	1.8%
2011	4,097,802	3,358,490	3,358,490	23.7	25.8	49.5
2010	4,378,998	3,225,940	3,225,940	48.4	24.1	72.5
2009	4,308,459	3,133,423	3,133,423	64.4	26.1	90.5
2008	4,141,986	3,013,097	3,013,097	75.2	27.2	102.4

Over the past four years, WMMIC has experienced steady growth in both net premium written and premium earned. Each balance has increased \$459,333, or 15.2% since 2008. In addition, WMMIC's loss and LAE ratio, expense ratio, and combined ratio have all improved since the prior examination. The combined ratio has been under 100% in each year during the period under examination. WMMIC's loss and LAE ratio was negative in 2012. This result was largely due to WMMIC's favorable reserve development for 2012.

Reconciliation of Surplus per Examination

No adjustments were made to surplus as a result of the examination. The amount of surplus reported by the company as of December 31, 2012, is accepted.

VI. SUMMARY OF EXAMINATION RESULTS

Compliance with Prior Examination Report Recommendations

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

1. Committees of the Board—It is recommended that the company develop changes to its committee structure and process which will result in compliance with s. 611.56 (1), Wis. Stat. **Error! Reference source not found.**

Action—Compliance

2. Investments—It is recommended that the company either enter into a new custodial agreement or amend the current one to reflect the actual investment advisor.

Action—Compliance

3. Investments—It is recommended that the company strive to coordinate board investment policies with any related agreements.

Action—Compliance

4. Loss Adjustment Expense—It is suggested that the company re-evaluate how it allocates DCC and AO expenses on the annual statement.

Action—Partial compliance; see comments in the “Summary of Current Examination Results” section of this report.

Summary of Current Examination Results

This section contains comments and elaboration on those areas where adverse findings were noted or where unusual situations existed. Comment on the remaining areas of the company's operations is contained in the examination work papers.

Loss Adjustment Expense

Current NAIC guidelines require allocating loss adjustment expense between defense cost and containment (DCC) and adjusting and other expenses (AO). The prior examination found that the company did not properly allocated loss adjustment expenses between the DCC and AO categories, but reported loss adjustment expenses to be all DCC. It was suggested that the company re-evaluate how it allocates DCC and AO expenses on the annual statement. Since the prior examination, WMMIC began to report AO expenses for paid losses. However, during the current examination, it was discovered that company did not include an estimate for unpaid adjusting and other expenses as part of its reserves for unpaid loss adjustment expenses. The liability for unpaid losses and loss adjustment expenses should include estimates for costs to be incurred in connection with adjusting losses, maintaining records, and other overhead costs. It is recommended that the company include an estimate for adjusting and other expenses as part of the loss adjustment expense reserve in all future annual statements, as required by SSAP No. 55, par. 5.

VII. CONCLUSION

Wisconsin Municipal Mutual Insurance Company reported assets of \$53,204,335, liabilities of \$14,983,585, and policyholders' surplus of \$38,220,750, as of December 31, 2012. During the period under examination, the company's admitted assets, liabilities, and surplus have increased by 9.9%, 1.2%, and 13.7%, respectively.

Since the prior examination, WMMIC premium growth has been steady. In addition, WMMIC's operating results were positive for four of the last five years with their largest underwriting gain reported in 2012 of \$3,410,282. Along with positive underwriting results, WMMIC has reported an investment gain every year since the prior examination. These investment gains ranged between \$901,545 and \$1,906,382.

The examination resulted in one recommendation relating to the company not reporting an estimate for adjusting and other expenses as a part of their estimate for loss adjustment expense. The examination did not result in any surplus adjustments or account reclassifications. The company complied with all of the recommendations and partially complied with the suggestion made by the prior examination.

VIII. SUMMARY OF COMMENTS AND RECOMMENDATIONS

1. Page 20 - Loss Adjustment Expense—It is recommended that the company include an estimate for adjusting and other expenses as part of the loss adjustment expense reserve in all future annual statements, as required by SSAP No. 55, par. 5.

IX. ACKNOWLEDGMENT

The courtesy and cooperation extended during the course of the examination by the officers and employees of the company are acknowledged.

In addition to the undersigned, the following representatives of the Office of the Commissioner of Insurance, State of Wisconsin, participated in the examination:

Name	Title
John Ebsen	Insurance Financial Examiner
David Jensen	IT Specialist
Jerry DeArmond	Reserve Specialist

Respectfully submitted,

Mike Miller
Examiner-in-Charge