

EXAMINATION REPORT OF
LEE COUNTY MUTUAL INSURANCE ASSOCIATION
LEE COUNTY, WEST POINT, IOWA
AS OF DECEMBER 31, 2017

HONORABLE DOUG OMMEN
Commissioner of Insurance
State of Iowa
Des Moines, Iowa

West Point, Iowa
June 27, 2018

Commissioner Ommen:

In accordance with your instructions and pursuant to Iowa statutory provisions, an examination has been made of the

LEE COUNTY MUTUAL INSURANCE ASSOCIATION

LEE COUNTY, WEST POINT, IOWA

AS OF DECEMBER 31, 2017

at its Home Office, 322 4th Street, West Point, Iowa. The report, containing applicable comments and financial data, is presented herein.

INTRODUCTION

Lee County Mutual Insurance Association, hereinafter referred to as the "Association", was last examined as of December 31, 2014. The examination reported herein was conducted by the Iowa Insurance Division.

SCOPE OF EXAMINATION

This examination covers the intervening period from December 31, 2014 to December 31, 2017. The examination was conducted in accordance with procedures established by the Iowa Insurance Division as recommended by the Financial Condition (E) Committee of the National Association of Insurance Commissioners, and other generally accepted insurance examination standards. A general review and survey was made of the Association's operations and business transactions conducted during the stated period. Accounting methods, internal control procedures, records and other supporting evidences were examined or tested by appropriate methods to the extent deemed adequate. The Association's assets were verified and evaluated and the liabilities determined to reflect herein a statement of its financial condition as of December 31, 2017.

HISTORY

The Association was incorporated in 1894 for the purpose of insuring the property of its members against hazards and risks as permitted by Chapter 518, Code of Iowa. The corporate existence was made perpetual in 1955.

MANAGEMENT AND CONTROL

MEMBERSHIP

The membership consists of those persons or organizations having insurance written by the Association which is in full force and effect.

The annual meeting of the members is held at West Point, Iowa on the second Tuesday in January at 10:00 a.m. Special meetings may be called by the Board of Directors as provided in the Articles of Incorporation. Due notice of the time and place of special meetings shall be given the membership. Each member present is entitled to one vote on any question to be decided. Voting by proxy is not permitted. The number of directors plus one constitute a quorum for any membership meeting.

BOARD OF DIRECTORS

The corporate powers of the Association are vested in a Board of not less than five nor more than fifteen directors, each elected by a majority vote at the annual meeting of the members for terms of three years. Any vacancy on the Board may be filled for the unexpired term by a majority vote of the remaining directors.

Directors serving at December 31, 2017 were:

<u>Name</u>	<u>Address</u>	<u>Term Expires</u>
Shannon McGowan	West Point, Iowa	2019
Gary Thompson	Houghton, Iowa	2019
April Johnson	Montrose, Iowa	2019
Daniel Kempker	West Point, Iowa	2020
Brian Burk	Wever, Iowa	2021
Mark Hunter	Hillsboro, Iowa	2021

The annual meeting of the Board is held immediately following the annual meeting of the members, and thereafter on the call of the Secretary. A majority present constitutes a quorum for the transaction of business.

Directors receive a fee of \$300 for each meeting attended and reimbursement of travel expense. The President receives a fee of \$350 per meeting attended.

OFFICERS

At its annual meeting, the Board of Directors shall elect for a term of one year a President, Treasurer and Secretary, who, when so designated by the Board, may also serve as Treasurer and such additional officers as it deems necessary. The Board may also elect a Vice-President.

Officers serving at December 31, 2017 were:

<u>Name</u>	<u>Office</u>
Daniel Kempker	President
Gary Thompson	Vice President
April Johnson	Secretary/Treasurer

April Johnson replaced Barbara Boeding as Secretary/Treasurer upon her retirement on January 1, 2016. Salaries and remunerations of officers are shown on Exhibit A following this report.

CONFLICT OF INTEREST

Conflict of interest statements were signed annually by all officers and directors. Conflicts were disclosed to the Board by the director and officer who was also an agent for the Association.

CORPORATE RECORDS

The Articles of Incorporation and Bylaws were not amended or substituted during the period covered by this examination.

The recorded minutes of the membership and Board of Directors meetings were read and noted. The minutes of the Board of Directors reflected that the Examination Report as of December 31, 2014 was reviewed and accepted during the October 13, 2015 Board meeting.

FIDELITY BONDS AND OTHER INSURANCE

The Association is protected by a blanket bond in the amount of \$100,000 for any one loss occurrence. The bond is written for an annual period and the indemnity is noncumulative.

Policies for other coverages are as follows:

- Employment practices liability
- Officers' and directors' liability
- Professional liability
- Building and contents
- General liability
- Business auto liability
- Cyber liability
- Equipment breakdown

Adequate insurance is placed with authorized insurers except professional liability and officers' and directors' liability which is written by a surplus lines insurer permitted to write in Iowa.

EMPLOYEES' WELFARE

The Association has no full time employees. Secretary/Treasurer contracts through Southern Iowa Insurance Services, Inc. with Association to perform management services for Association.

TERRITORY AND PLAN OF OPERATION

The Association is authorized to transact business in Lee, Henry, Van Buren and Des Moines counties. It was noted, from a review of numerous applications of policies in force, that risks appeared to be located within the authorized territory.

Policies are written or renewed for a one-year period with premiums payable quarterly, annually or semi-annually. The Association underwrites these policies every five years.

At the present time, business is produced by ten licensed agents.

UNDERWRITING EXPERIENCE

THREE-YEAR PERIOD ENDED DECEMBER 31, 2017

<u>Classification</u>	<u>2015</u>	<u>2016</u>	<u>2017</u>	<u>Total</u>
Premiums earned	<u>\$618,432</u>	<u>\$636,018</u>	<u>\$695,904</u>	<u>\$1,950,354</u>
Incurred deductions:				
Losses	\$217,588	\$317,650	\$570,600	\$1,105,838
Loss adjustment expense	9,082	15,598	23,518	48,198
Commissions	118,142	120,951	128,573	367,666
Salaries	48,625	53,427	(35,920)	66,132
Taxes, licenses and fees	15,166	8,212	8,702	32,080
Other underwriting expenses	<u>80,639</u>	<u>78,889</u>	<u>159,330</u>	<u>318,858</u>
Total deductions	<u>\$489,242</u>	<u>\$594,727</u>	<u>\$ 854,803</u>	<u>\$1,938,772</u>
Underwriting gain or (loss)	<u>\$129,190</u>	<u>\$ 41,291</u>	<u>\$(158,899)</u>	<u>\$ 11,582</u>

Expressed in ratios of expenses incurred to premiums earned, the percentages would be:

	<u>2015</u>	<u>2016</u>	<u>2017</u>	<u>Total</u>
Incurred deductions:				
Losses	35.18%	49.94%	81.99%	56.70%
Loss adjustment expense	1.47	2.45	3.38	2.47
Commissions	19.10	19.02	18.48	18.85
Salaries	7.86	8.41	(5.16)	3.39
Taxes, licenses and fees	2.46	1.29	1.24	1.65
Other underwriting expenses	<u>13.04</u>	<u>12.40</u>	<u>22.90</u>	<u>16.35</u>
Total deductions	<u>79.11%</u>	<u>93.51%</u>	<u>122.83%</u>	<u>99.41%</u>
Underwriting gain or (loss)	<u>20.89%</u>	<u>6.49%</u>	<u>(22.83)%</u>	<u>0.59%</u>

REINSURANCE

The Association has reinsurance contracts in force as of December 31, 2017 with an authorized insurer which provide the following:

Per Risk Excess of Loss

First \$100,000 of ultimate net loss per risk is retained by Association. First layer is reinsurer will pay 100 percent of net loss in excess of retention. The maximum recovery for first layer is \$1,000,000. Second layer has a recovery of \$4,000,000 in excess of \$1,000,000 for each risk. Third layer has a maximum recovery of \$15,000,000 in excess of \$5,000,000. Association is required to provide a timely notification to reinsurer of any risks exceeding \$10,000,000.

Aggregate Excess of Loss

First \$525,000 of ultimate net losses in aggregate, net of all other reinsurance recoveries is retained by Association. 100 percent of ultimate net loss in excess of retention is covered by the reinsurer. Reinsurance recovery is unlimited. Reinsurance applies to new and renewal and in-force policies of the Association effective and becoming effective at and after the effective date of the contract until expiration of the contract.

CLAIMS

From a review of numerous claims, it appeared that the Association made equitable settlements which were in keeping with the terms of the policy contracts. As of the end of the Examination period, Association was subcontracting the adjusting of claims.

AFFILIATED AGENCY

The Association owns its Home Office building and shares a portion of the space with Southern Iowa Insurance Services, Inc (SIIS). Upon her retirement on January 1, 2016, the former Association Manager Barbara Boeding, sold her interest in SIIS to her partner Randy Woodruff. SIIS writes 85 percent of the Association's premiums. Current officers and directors have no ownership of SIIS after January 1, 2016.

A management contract is in place whereby SIIS provides the daily management and oversees the operations of the Association. A management fee is established and approved by the Board of Directors annually, and paid to SIIS for the services provided by the Association's Manager, April Johnson (an SIIS employee). The management fee was \$49,500 for 2017. In addition, the Association pays for certain expenses incurred in the course of the management duties such as educational and travel related costs.

In accordance with a written agreement in lieu of rent, SIIS pays long distance phone calls, electric and heat bills, custodial labor, lawn mowing and snow removal service. Also, copier and copy paper is shared 50/50. SIIS occupies approximately 67 percent of the building.

ACCOUNTS AND RECORDS

Office copies of the filed annual statements for the years under review were found to be in agreement with or reconciled to the general ledger balances of assets, liabilities, income and disbursements.

Cash receipts recorded during the period were checked and traced to the Association's depository. Checks paid during selected months were compared to the disbursement records and were scrutinized as to payees, amounts, authorized

signatures and proper endorsements. Cash receipts and disbursements were proven by comparison and reconciliation to the monthly bank statements.

In accordance with Section 518.25, Code of Iowa, surplus must be maintained at a level of not less than fifty thousand dollars or one-tenth of one percent of the gross risk in force, whichever is greater. At December 31, 2017, the Association's gross risk in force was \$229,031,798. The Association's statutory minimum surplus level as December 31, 2017 was \$229,032. It is noted the Association's surplus level to minimum surplus level ratio was 19.3/1. The reported surplus/statutory minimum ratio average for the Chapter 518 licensed industry at December 31, 2017 was 8.4/1.

It was noted that eighteen checks that were outstanding at December 31, 2017 were written over three years, since the examination field work date. Nine of these were written over 15 years ago. This was addressed on prior examination report.

F I N A N C I A L S T A T E M E N T S
A N D C O M M E N T S T H E R E O N

NOTE: Except as otherwise stated, the financial statements immediately following reflect only the transactions for the period ending December 31, 2017 and the assets and liabilities as of this date. Schedules may not add or tie precisely due to rounding.

STATEMENT OF ASSETS AND LIABILITIES

ASSETS

	<u>Ledger</u>	<u>Nonledger</u>	<u>Not Admitted</u>	<u>Admitted</u>
Bonds	\$1,607,396	\$	\$	\$1,607,396
Stocks	1,953,335	892,776		2,846,111
Bank balances:				
Subject to check	114,405	2,704		117,109
On interest	156,442			156,442
Real estate	47,781			47,781
Unpaid premiums:				
Due before November 1	2,418		2,418	
Due after November 1	65,340		51,568	13,772
Accrued interest		16,747		16,747
Federal income tax recoverable		500	500	
Other assets	<u> </u>	<u>6,520</u>	<u> </u>	<u>6,520</u>
Total	<u>\$3,947,117</u>	<u>\$ 919,247</u>	<u>\$ 54,486</u>	<u>\$4,811,878</u>

LIABILITIES AND SURPLUS

Losses	\$ 162,431
Unpaid adjusting expenses	7,143
Ceded reinsurance balances payable	13,592
Unpaid salaries and commissions	(79,767)
Amounts withheld for others	2,334
Taxes payable	1,666
Other unpaid expenses	603
Premiums collected for other companies - not remitted	948
Premiums received in advance	26,931
Unearned premium reserve	<u>317,479</u>
Total liabilities	\$ 453,360
Surplus as regards policyholders	<u>\$4,358,518</u>
Total liabilities and surplus	<u>\$4,811,878</u>

INCOME AND DISBURSEMENTS
AND
RECONCILIATION OF LEDGER ASSETS

Ledger assets, December 31, 2016		\$3,840,303
	<u>INCOME</u>	
Net premiums and fees		\$ 697,250
Net interest received on bonds		56,906
Increase (Decrease) by adjustment - bonds		(409)
Dividends received		156,735
Interest received on bank deposits		1,933
Profit on sale of investments		1,012
Rents received		3,600
Premiums collected for other companies		14,935
Total income		<u>\$ 931,962</u>
Total assets and income		<u>\$4,772,265</u>
	<u>DISBURSEMENTS</u>	
Net losses paid		\$ 427,669
Operation Expense		
Loss adjustment expenses	\$ 17,375	
Commissions	128,573	
Advertising	9,646	
Boards, bureaus and associations	1,125	
Inspection and loss prevention	3,579	
Salaries of officers	49,500	
Insurance	11,373	
Directors' compensation	9,250	
Rent and rent items	3,600	
Equipment	602	
Printing, stationery and supplies	3,167	
Postage and telephone	4,993	
Legal and auditing	14,875	
State insurance taxes	8,198	
Insurance Division licenses and fees	155	
Real estate expenses	38	
Real estate taxes	998	
Miscellaneous	3,458	
Investment Expense	2,050	
Donations/contributions	3,489	
Data processing	<u>5,390</u>	
Total operating expense		\$ 281,434
<u>Non-Operating Expense</u>		
Depreciation on real estate		2,879
Loss on sale of investment		8,252
Federal income tax		8,858
Premium collections transmitted to other companies		11,892
Decrease in ledger liabilities		<u>84,164</u>
Total disbursements		<u>\$ 825,148</u>
Balance - ledger assets, December 31, 2017		<u>\$3,947,117</u>

UNDERWRITING AND INVESTMENT EXHIBIT

ONE YEAR PERIOD ENDED DECEMBER 31, 2017

STATEMENT OF INCOME

Underwriting Income

Premiums earned \$ 695,904

Deductions

Losses incurred \$570,600

Loss expenses incurred 23,518

Other operating expenses incurred 260,685

Total underwriting deductions 854,803

Net underwriting gain (loss) \$ (158,899)

Investment Income

Net investment income earned 209,070

Other Income

Premiums collected for other companies 3,003

Net income before Federal income tax \$ 53,174

Federal income tax incurred 8,998

Net income \$ 44,176

CAPITAL AND SURPLUS ACCOUNT

Surplus as regards policyholders, December 31, 2016 \$4,004,600

Gains and (Losses) in Surplus

Net income \$ 44,176

Unrealized capital change 309,742

Change in surplus as regards policyholders for the year \$ 353,918

Surplus as regards policyholders, December 31, 2017 \$4,358,518

UNDERWRITING AND INVESTMENT EXHIBIT

THREE-YEAR PERIOD ENDED DECEMBER 31, 2017

STATEMENT OF INCOME

Underwriting Income

Premiums earned \$1,950,354

Deductions

Losses incurred \$1,105,838

Loss expenses incurred 48,198

Other operating expenses incurred 784,736

Total underwriting deductions \$1,938,772

Net underwriting gain (loss) \$ 11,582

Investment Income

Net investment income earned 558,151

Other Income

Premiums collected for other companies 3,127

Net income before Federal income tax \$ 572,860

Federal income tax incurred 152,889

Net income \$ 419,971

CAPITAL AND SURPLUS ACCOUNT

Surplus as regards policyholders, December 31, 2014 \$3,655,936

Gains and (Losses) in Surplus

Net income \$ 419,971

Change in not admitted assets 2,289

Unrealized capital change 280,322

Change in surplus as regards policyholders for the year \$ 702,582

Surplus as regards policyholders, December 31, 2017 \$4,358,518

SURPLUS AS REGARDS POLICYHOLDERS

The changes which resulted in the net decrease are shown in the following statement of differences:

<u>Classification</u>	<u>Association Annual Statement</u>	<u>Examination Financial Statement</u>	<u>Surplus Increase (Decrease)</u>
<u>Assets</u>			
Stocks	\$2,819,551	\$2,846,111	\$ 26,560
Bank balances: subject to check	114,405	117,109	2,704
<u>Liabilities</u>			
Losses	67,504	162,431	(94,927)
Unpaid adjusting expenses	1,127	7,143	(6,016)
Taxes payable: Federal income		140	<u>(140)</u>
Net change to surplus			\$ (71,819)
Surplus per Association			<u>\$4,430,337</u>
Surplus per examination			<u>\$4,358,518</u>

During the period under review, surplus funds increased \$702,582 from the amount of \$3,655,936 as shown in the last previous examination report. An operating statement reflecting that increase is contained in the financial section.

COMMENTS

The major changes in the Association's financial statement were due to the following:

Stocks \$2,846,111

This asset increased by \$26,560 due to stocks included in custodial account records yet not reported in statutory statement.

Bank balances: Subject to check \$ 117,109

This asset increased by \$2,704 to account for funds in custodial records yet not reported in statutory statement.

Losses \$ 162,431

A review of paid and reserved claims subsequent to the end of 2017 that were incurred prior to 2018 resulted in a \$94,927 increase to loss reserves.

Unpaid adjustment expenses \$ 7,143

An analysis of paid adjusting expenses to paid losses increased the liability by \$6,016.

CONCLUSION

The cooperation and assistance extended by the officers and personnel of the Association is hereby acknowledged.

Respectfully submitted,

 /s/ Jerry Cihota
Jerry P. Cihota, CPA, CFE
Examiner Specialist
Insurance Division
State of Iowa