

EXAMINATION REPORT OF
MFS MUTUAL INSURANCE COMPANY
BURLINGTON, IOWA
AS OF DECEMBER 31, 2016

Burlington, Iowa
November 29, 2017

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

Commissioner:

In accordance with your authorization and pursuant to Iowa statutory provisions, an examination has been made of the records, business affairs and financial condition of

MFS MUTUAL INSURANCE COMPANY

BURLINGTON, IOWA

AS OF DECEMBER 31, 2016

at its Home Office located at 365 West Burlington Avenue, Burlington, Iowa.

INTRODUCTION

MFS Mutual Insurance Company, hereinafter referred to as "Company", was previously examined as of December 31, 2011. The examination reported herein was conducted by the Iowa Insurance Division examiners.

SCOPE OF EXAMINATION

This is the regular comprehensive examination of the Company covering the intervening period from January 1, 2012 to the close of business on December 31, 2016, including any material transactions and/or events occurring and noted subsequent to the examination period.

The examination was conducted in accordance with the National Association of Insurance Commissioners Financial Condition Examiners Handbook. The Handbook requires the examination to be planned and performed to evaluate the financial condition and identify prospective risks of the Company by obtaining information about the Company, including corporate governance, identifying and assessing inherent risks within the organization, and evaluating system controls and procedures used to mitigate those risks. An examination also includes assessing the principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation, management's compliance with Statutory Accounting Principles and annual statement instructions, when applicable to domestic state regulations.

All accounts and activities of the organization were considered in accordance with the risk-focused examination process. The Company's assets were verified and evaluated and the liabilities determined to reflect herein a statement of its financial condition as of December 31, 2016.

HISTORY

The Company was originally organized in 1889 by members of the Evangelical Synod of North America as a post-loss assessment association to insure its members of the German Evangelical Church against loss from the hazards of fire and storm. The writing of business began in March 1893 on risks originating only within the Evangelical Synod. This church denomination was founded in the St. Louis, Missouri area and also had a large concentration of churches in the Mississippi River Valley into Texas and along the Gulf

Coast of Louisiana and Mississippi. The Company made insurance available to churches, their members and ministers.

The Company was incorporated in March 1921 under the name of "Mutual Fire and Storm Insurance Association of the Evangelical Synod of North America," as a state mutual assessment association.

On December 4, 1945, amended and substituted Articles of Incorporation were filed converting the Company from a state mutual assessment association to a mutual insurance company and was then authorized to write insurance business under Sections 515.48 and 515.49, Code of Iowa. The Company's corporate existence was made perpetual and the corporate title of "Mutual Fire and Storm Insurance Company" was adopted. Although the structure of the Company was changed and the affiliation with the church was severed, the purpose of the Company remained the same, to provide coverage for the same clientele.

The Articles of Incorporation were amended effective June 12, 1962 in order to authorize the Company to write insurance business in all lines except life and title insurance.

Protestant Mutual Fire Insurance Association of Burlington, Iowa was merged into the Company on April 27, 1989 with the Company the surviving entity.

The Company entered into two separate Assumption and Reinsurance agreements effective January 1, 2004, whereby Company assumed assets and liabilities arising from insurance policies written by Wayne County Mutual Insurance Association and Davison Farm Mutual Insurance Company from South Dakota while receiving in exchange all the rights under said policies.

On June 1, 2006, Company amended the Articles of Incorporation and the Bylaws to change the name of the Company to MFS Mutual Insurance Company.

Effective March 26, 2012, the Company sold its Corydon, Iowa building and book of business to an agent who writes business for the Company. The Company's remaining operations, not including underwriting were consolidated in the Burlington office. Underwriting continues to be conducted in Osceola, Iowa as of the examination date.

MANAGEMENT AND CONTROL

MEMBERSHIP

Article VII of the Articles of Incorporation states that "any person or corporation now holding or hereafter obtaining insurance in this corporation shall be a member thereof, but only while such policy is in force".

The annual meeting of the members shall be held on the third Wednesday of the month of March at 1:30 p.m. at the Company's principal place of business. A notice of the time and place of such annual meeting shall be set forth in all policies issued by the Company and be published in the newspaper of the general circulation of the county where the Company has physical facilities at least thirty (30) days prior to the meeting, or, as an alternative, actual notice shall be mailed by the Secretary to each member not less than thirty (30) days prior to the date of the said meeting.

Special meetings of the members may be called by the President or Board of Directors and shall be called upon written demand of a group of at least fifteen percent or more members and shall state the purpose for which said meeting is to be called. The time of the special meeting shall be at 1:30 p.m. upon thirty (30) days notice provided to the members when a request for special meeting has been made and shall take place at the principal place of the Company.

Each member present is entitled to one vote at any regular or special meeting of the members on each matter of business submitted to a vote, regardless as to how many policies each member may own. Voting by proxy is not permitted. At any meeting of the members, eight members shall constitute a quorum of the voting group for the transaction of business.

The Company was not able to locate the minutes for the 2015 members meeting.

BOARD OF DIRECTORS

The Company shall be managed by a Board of no less than five (5) or more than seven (7) directors. The general control and management of the Company is currently vested in a Board of six directors.

Directors are elected for a three (3) year term at the annual meeting by the majority vote of the members. No more than three directors shall be elected at each annual meeting to allow the Board terms to be staggered.

The Board meets immediately following the adjournment of the member's annual meeting. Other meetings of the Board will be held as is deemed necessary by the President or Secretary, but no less than one (1) time each year. When it is determined that the Board will meet for the transaction of business, the meetings will be held on the second Monday of the month at 4:00 p.m., or at such time determined by the President or Secretary. Directors will be notified at least thirty (30) days prior to the meeting. A majority of the directors shall constitute a quorum for the transaction of business at any meeting of the directors.

The Board of Directors may establish one or more committees including an executive committee with each committee to consist of two or more directors appointed by the Board. Any such committee shall serve at the will of the Board.

The directors qualified and serving at December 31, 2016 were:

<u>Name and Address</u>	<u>Principal Occupation</u>	<u>Term Expires</u>
Craig Cornic Burlington, Iowa	Retired Speech Pathologist	2017
David Gunzenhauser Humeston, Iowa	Retired Farmer	2017
Mitchell L. Taylor Burlington, Iowa	Attorney Cray Law Firm LLP	2018
Theresa Thielen Burlington, Iowa	Funeral Home Director Thielen Funeral Home	2018
Joseph E. Deal Burlington, Iowa	Retired Business Owner Central Duplicating Company	2019
Stephen Paugh Humeston, Iowa	Retired Farm Mutual Manager	2019

Directors receive a fee of \$200 for each meeting attended. Mr. Deal and Mr. Gunzenhauser served as directors and as officers for 2016, but were not listed as directors on the 2016 Annual statement.

OFFICERS

At the first directors meeting following the annual members meeting, the Board of Directors shall elect for a term of one year a President, one or more Vice Presidents, Secretary and Treasurer. One person may hold two (2) offices and perform the duties of those officers. The Board of directors may leave unfilled any office except those of President, Secretary, or Treasurer for such period of time as it may fix.

Officers elected and serving at December 31, 2016 were:

<u>Name</u>	<u>Title</u>
Joseph E. Deal	President
David Gunzenhauser	Vice President
G. William Miles	Secretary
Robert Parmeter	Treasurer

The salaries and other remuneration of officers and directors are shown in Exhibit A, found immediately after the signature page of this report.

CONFLICT OF INTEREST

The Company has adopted a policy statement to ensure prompt disclosure of any possible conflict of interest on the part of its directors, officers and employees. Disclosures were indicated on the statements.

Two directors did not timely sign a conflict of interest statement for 2013.

CORPORATE RECORDS

Articles of Incorporation and Bylaws were neither amended nor substituted during the period covered by this examination. The Board approved the prior exam report at their January 30, 2013 meeting.

FIDELITY BONDS AND OTHER INSURANCE

The Company is protected by a blanket bond in the amount of \$250,000 for any one loss occurrence. The bond is written for an annual period and the indemnity is noncumulative.

Policies for other coverages, placed with authorized insurers, were as follows:

- Workers' compensation and employers' liability
- Commercial umbrella
- Commercial property
- General liability
- Commercial auto
- Equipment breakdown
- Professional liability

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

Full-time eligible employees are provided medical, dental, vision, term life, accidental death and dismemberment, and long-term disability insurance on a non-contributory basis.

The Board approved a Simple IRA plan for full-time employees in 2012. The Company made contributions of 5 percent in 2012 and 3 percent in 2013.

REINSURANCE

Reinsurance ceded treaties in force as of December 31, 2016 with an authorized insurer providing coverage for all property and casualty business written by the Company were as follows:

Casualty Excess of Loss Reinsurance

The reinsurer shall be liable for 100 percent in excess on a retention of \$5,000 for all casualty exposure not to exceed \$995,000 for each loss occurrence. This agreement provides for reinstatement coverage.

Property Per Risk Excess of Loss

<u>Layer</u>	<u>Company Retention</u>	<u>Per Risk Coverage</u>	<u>Per Occurrence Coverage</u>
First	\$125,000	\$125,000	\$ 375,000
Second	250,000	250,000	750,000
Third	500,000	500,000	1,500,000

This agreement provides for reinstatement coverage.

Property First Aggregate Excess of Loss

The reinsurer shall be liable for 100 percent of the annual aggregate net losses in excess of 75 percent of the Company's annual net earned premium.

Property Second Aggregate Excess of Loss

The reinsurer shall be liable for 100 percent of the annual aggregate net losses in excess of 130 percent of the Company's annual net earned premium not to exceed 70 percent of the Company's annual net earned premium.

TERRITORY AND PLAN OF OPERATION

The Company held a certificate of authority authorizing the transaction of business in Iowa. The Company writes policies for fire, homeowners and farm multiple peril insurance.

Policies are written or renewed for a continuous period with premiums payable annually, semi-annually, quarterly or monthly by means of electronic funds transfer. The Company inspects 100-120 of its approximately 1900 policies annually. Selection is determined judgmentally based in part on claims experience.

MARKET CONDUCT

PRODUCER LICENSING

The Company was unable to provide a listing of its appointed agents. According to Iowa Insurance Division record, the Company has 112 licensed agents and forty-four agencies as of the examination date.

COMPLAINT HANDLING

The Company had three complaints filed during the exam period and documented complaints in the register. The complaints were properly and fairly resolved.

CLAIMS

Early in the examination period, the Company processed claims out of two offices, Corydon, Iowa and the home office in Burlington, Iowa. As of March 26, 2012, the Corydon building and book of business was sold and its remaining claims operations were consolidated in the Burlington office.

Adjustment of property claims is handled by a third party vendor through an annual fixed fee contract up to a set limit of claims. Claims in excess of this limit remain at the same fixed fee. Based on review of claims, it appears that the Company made timely, prompt and equitable settlements which were in keeping with the terms of the policy contracts.

UNDERWRITING EXPERIENCE

Underwriting experience during the past five years, as taken from amounts contained in copies of the Company's filed annual statements, are as follows:

	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>	<u>Total</u>
Premiums earned	\$ 600,159	\$ 679,697	\$ 908,228	\$1,041,929	\$1,149,429	\$ 4,379,442
<u>Incurred Deductions</u>						
Losses	\$ 473,531	\$ 528,890	\$ 552,556	\$ 574,876	\$ 682,945	\$ 2,812,798
Loss adjustment expenses	83,567	104,120	83,204	101,499	99,128	471,518
Commissions	110,567	154,155	188,064	208,829	221,329	882,944
Salaries	193,193	200,787	213,686	208,447	178,031	994,144
Taxes, licenses and fees	38,665	26,767	28,797	27,413	20,291	141,933
Other underwriting expenses	<u>145,030</u>	<u>135,815</u>	<u>201,049</u>	<u>186,034</u>	<u>224,099</u>	<u>892,027</u>
Total deductions	<u>\$1,044,553</u>	<u>\$1,150,534</u>	<u>\$1,267,356</u>	<u>\$1,307,098</u>	<u>\$1,425,823</u>	<u>\$ 6,195,364</u>
Net underwriting gain (loss)	<u>\$ (444,394)</u>	<u>\$ (470,837)</u>	<u>\$ (359,128)</u>	<u>\$ (265,169)</u>	<u>\$ (276,394)</u>	<u>\$(1,815,922)</u>

Expressed in percentage of incurred deductions to earned premiums for the five year period:

	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>	<u>TOTAL</u>
<u>Incurred Deductions</u>						
Losses	78.90%	77.81%	60.84%	55.17%	59.42%	64.23%
Loss adjustment expenses	13.92	15.32	9.16	9.74	8.62	10.77
Commissions	18.42	22.68	20.71	20.04	19.26	20.16
Salaries	32.19	29.54	23.53	20.01	15.49	22.70
Taxes, licenses and fees	6.45	3.94	3.16	2.64	1.76	3.23
Other underwriting expenses	<u>24.17</u>	<u>19.98</u>	<u>22.14</u>	<u>17.85</u>	<u>19.50</u>	<u>20.37</u>
Total deductions	<u>174.05%</u>	<u>169.27%</u>	<u>139.54%</u>	<u>125.45%</u>	<u>124.05%</u>	<u>141.46%</u>
Net underwriting gain (loss)	<u>(74.05)%</u>	<u>(69.27)%</u>	<u>(39.54)%</u>	<u>(25.45)%</u>	<u>(24.05)%</u>	<u>(41.46)%</u>

FINANCES OF COMPANY

The following historical financial data, taken from annual statements for the years indicated, reflects the growth of the Company:

<u>Year</u>	<u>Net Admitted</u>	<u>Net Premiums</u>		<u>Losses</u>	<u>Investment</u>
	<u>Assets</u>	<u>Surplus</u>	<u>Earned</u>	<u>Incurred</u>	<u>Income</u>
2012	3,524,412	2,856,518	579,953	448,425	44,345
2013	3,640,646	2,721,876	679,697	528,890	35,767
2014	3,598,907	2,648,147	908,228	552,556	93,235
2015	3,666,228	2,621,499	1,041,929	574,876	95,522
2016	3,945,629	2,826,257	1,149,429	682,945	103,442

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 balance of assets, liabilities, income and disbursements.

The Company appears to consistently not comply with their underwriting guidelines. In a test of policies, six of twenty policies had homes at least forty years old with wiring that was over twenty years old. Underwriting guidelines require that older homes have timely wiring updates or are not eligible for coverage. Renewal applications prepared by policyholders or agents do not inquire about acquisitions of aggressive dogs or swimming pools with diving boards nor lack of updating of roof, plumbing and heating systems. Each of the aforementioned risks result in properties being uninsurable according to the underwriting guidelines.

Best business practices suggest timely inspections of member's property. The Company independently inspects a small percentage of total policies. The number of policies inspected annually are approximately 120.

The Company uses credit scores as a factor in determining rates. It is recommended that the Company follow the Iowa Code in regards to retaining evidence of proper notification when premiums are increased due to credit scores, usage of recently obtained credit scores and the periodic review of credit scoring used by the Company.

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, 2016, and the assets and liabilities as of that date. Schedules may not add or tie precisely due to rounding.

STATEMENT OF ASSETS AND LIABILITIES

ASSETS

	<u>Assets</u>	<u>Not Admitted</u>	<u>Net Admitted</u>
Bonds	\$ 989,335	\$	\$ 989,335
Stocks:			
Common stocks	2,004,209		2,004,209
Real estate:			
Properties occupied by the Association	546,045		546,045
Cash and short-term investment	169,726		169,726
Investment income due and accrued	13,999		13,999
Premiums and considerations:			
Uncollected premiums and agents' balances in the course of collection	2,725		2,725
Deferred premiums, agents' balances and installments booked but deferred and not yet due	218,770		218,770
Net deferred tax asset	126,600	126,600	
Electronic data processing equipment and software	820		820
Furniture and equipment	<u>3,177</u>	<u>3,177</u>	<u>0</u>
 Total Assets	 <u>\$4,075,406</u>	 <u>\$129,777</u>	 <u>\$3,945,629</u>

LIABILITIES, SURPLUS AND OTHER FUNDS

Losses			\$ 151,069
Loss adjusting expenses			15,400
Commissions payable, contingent commissions and other similar charges			45,708
Other expenses			9,981
Taxes, licenses and fees			11,993
Unearned premiums			854,292
Advance premiums			18,948
Ceded reinsurance premiums payable			3,801
Amounts withheld or retained by company for account of others			<u>8,180</u>
 Total liabilities			 <u>\$1,119,372</u>
 Surplus as regards policyholders			 <u>2,826,257</u>
 Total Liabilities and Surplus			 <u>\$3,945,629</u>

STATEMENT OF INCOME

ONE-YEAR PERIOD ENDING DECEMBER 31, 2016

Underwriting Income

Premiums earned \$1,149,429

Deductions:

Losses incurred	\$682,945	
Loss expenses incurred	99,128	
Other underwriting expenses incurred	<u>643,750</u>	
Total underwriting deductions		<u>\$1,425,823</u>
Net underwriting gain (loss)		\$ (276,394)

Investment Income

Net investment income earned	\$103,442	
Net realized capital gain (loss)	<u>7,194</u>	
Net investment gain (loss)		110,636

Other Income

Finance and service charges not included in premiums	\$116,864	
Miscellaneous Income	<u>497</u>	
Other income		<u>117,361</u>

Net income before federal income taxes \$ (48,397)

Federal income taxes incurred 0

Net income \$ (48,397)

CAPITAL AND SURPLUS ACCOUNT

Surplus as regards policyholders, December 31, 2015 \$2,621,499

Gains and (losses) in surplus

Net income		\$ (48,397)
Net unrealized capital gains (losses)		252,462
Change in non-admitted assets		28,493
Change in net deferred income tax		<u>(27,800)</u>
Change in surplus as regards policyholders		<u>\$ 204,758</u>

Surplus as regards policyholders, December 31, 2016 \$2,826,257

CASH FLOW STATEMENT

Cash from Operations

Premiums collected net of reinsurance	\$1,149,517
Net investment income	110,074
Miscellaneous income	<u>117,361</u>
Total	<u>1,376,952</u>

Benefit and loss related payments	\$ 639,977
Commissions, expenses paid and aggregate write-ins	<u>737,359</u>
Total	<u>1,377,336</u>

Net cash from operations	<u>\$ (384)</u>
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Cash from Investments

Proceeds from investments sold, matured and repaid:	
Bonds	\$ 220,380
Stocks	35,032
Real estate	1,300
Miscellaneous proceeds	<u>13,364</u>
Total investment proceeds	<u>270,076</u>

Cost of investments acquired (long-term) only:	
Bonds	\$ 176,288
Stocks	<u>13,654</u>
Total investments acquired	<u>189,942</u>

Net cash from investments	<u>\$ 80,134</u>
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Cash from Financing and Miscellaneous Sources

Other cash provided (applied)	<u>\$ 1,790</u>
Net cash from financing and miscellaneous sources	<u>\$ 1,790</u>

Reconciliation of Cash and Short-Term Investments

Net change in cash and short-term investments	\$ 81,540
Cash and short-term investments:	
Beginning of year	<u>\$ 88,186</u>
End of year	<u>\$ 169,726</u>

STATEMENT OF INCOME

FIVE-YEAR PERIOD ENDING DECEMBER 31, 2016

Underwriting Income

Premiums earned		\$ 4,379,442
 <u>Deductions</u>		
Losses incurred	\$2,812,798	
Loss expenses incurred	471,518	
Other underwriting expenses incurred	2,908,827	
Aggregate write-ins for underwriting deductions:		
Loss on sale of equipment	<u>2,221</u>	
Total underwriting deductions		<u>6,195,364</u>
 Net underwriting gain (loss)		 <u>\$ (1,815,922)</u>

Investment Income

Net investment income earned	\$ 373,952	
Net realized capital gain (loss)	<u>211,511</u>	
Net investment gain (loss)		585,463

Other Income

Finance and service charges not included in premiums	\$ 407,237	
Aggregate write-ins for miscellaneous income:		
Miscellaneous income	2,416	
Sale of customer list	<u>32,000</u>	
Other income		<u>441,653</u>
 Net income before federal income taxes		 \$ (788,806)
 Federal income taxes incurred		 <u>0</u>
 Net income		 <u>\$ (788,806)</u>

CAPITAL AND SURPLUS ACCOUNT

Surplus as regards policyholders, December 31, 2011		\$ <u>3,049,241</u>
<u>Gains and (losses) in surplus</u>		
Net income		\$ (788,806)
Net unrealized capital gains (losses)		545,017
Change in deferred income tax		126,600
Change in non-admitted assets		<u>(105,795)</u>
Change in surplus as regards policyholders		<u>\$ (222,984)</u>
Surplus as regards policyholders, December 31, 2016		<u>\$ 2,826,257</u>

CONCLUSION

The cooperation and assistance extended by the officers and employees of the Company is hereby acknowledged.

Respectfully submitted,

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

EXHIBIT A