

**STATE OF NORTH DAKOTA
BISMARCK, NORTH DAKOTA**

REPORT OF EXAMINATION

OF

SOUTHWEST MUTUAL INSURANCE COMPANY

NEW SALEM, NORTH DAKOTA

**AS OF
DECEMBER 31, 2021**

STATE OF NORTH DAKOTA
INSURANCE DEPARTMENT

I, the undersigned, Commissioner of Insurance of the State of North Dakota do hereby certify that I have compared the annexed copy of the Report of Examination of the

Southwest Mutual Insurance Company

New Salem, North Dakota

as of December 31, 2021, with the original on file in this Department and that the same is a correct transcript therefrom and of the whole of said original.


IN WITNESS WHEREOF, I have hereunto

set my hand and affixed my official seal at my

office in the City of Bismarck, this 19th day of

June, 2023.





Jon Godfread
Insurance Commissioner

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May 9, 2023
New Salem, North Dakota

Honorable Jon Godfreed
Commissioner of Insurance
North Dakota Insurance Department
600 East Boulevard Avenue
Bismarck, ND 58505-0320

Dear Commissioner:

Pursuant to your instructions and statutory requirements, an examination has been made of the books, records, and financial condition of

**Southwest Mutual Insurance Company
New Salem, North Dakota**

hereinafter referred to as the "Company" was last examined as of December 31, 2016, by representatives of the North Dakota Insurance Department, hereinafter referred to as the "Department".

SCOPE OF STATUTORY EXAMINATION

This examination was a financial condition examination conducted in accordance with North Dakota Century Code ("N.D.C.C.") § 26.1-03-19.3 and the guidelines and procedures contained in the NAIC Financial Condition Examiners Handbook. The examination was conducted to determine the Company's financial condition, its compliance with statutes, and to review its corporate affairs and insurance operations. This statutory examination covers the period from January 1, 2017 through December 31, 2021, including any material transactions and/or events occurring subsequent to the examination date and noted during the course of this statutory examination.

STATUS OF PRIOR EXAM FINDINGS

Our examination included a review to determine the current status of the 4 exception conditions commented upon in our preceding Report on Examination which covered the period from January 1, 2012, to December 31, 2016. We determined that the Company had satisfactorily addressed all of these items, except the following:

Recommendation

It is again recommended that the Company collect and retain board reviewed conflict of interest disclosures from its officers and directors.

Response

The Company did not comply. Conflict of Interest Statements were only completed during 2019. **It is again recommended that Conflict of Interest Statements be completed on an annual basis, that those**

statements be retained, and any noted conflicts be reviewed by the board.

The finding and recommendation related to the above area is addressed under the appropriate caption below for the current period under examination.

SUBSEQUENT EVENTS

The meeting minutes and general ledger were reviewed through March 2022. The 12/31/2022 Annual Statement was also reviewed. No material subsequent events were noted.

HISTORY

The Company was incorporated on April 16, 1900, as "The Morton County Mutual Fire and Lightning Insurance Company" and commenced business on July 21, 1900. At a later date, the Company's operating rights were extended to include the County of Oliver and the name was amended to "The Morton and Oliver Counties Mutual Fire and Lightning Insurance Company."

Effective January 1, 1997, the Company merged with Adams Farm Mutual Insurance Company located in Hettinger, North Dakota. The two companies formed a new company called Southwest Mutual Insurance Company located at New Salem, North Dakota.

The Company's term of existence is perpetual as provided by N.D.C.C. § 26.1-13-03.

MANAGEMENT AND CONTROL

Membership

The Company is controlled by its membership. Any person owning property within the Company's authorized territorial limits may become a member of the Company and be entitled to all the rights and privileges accorded each member. No person who does not reside within such territorial limits shall become a director of the Company.

The date and place of the annual meeting of the members is set by the Board of Directors. The annual meeting is followed with a reorganizational meeting to address the appointment of Directors. Notice of the annual meeting is mailed to all policyholders at least 10 days in advance of the meeting.

Directors

The Bylaws provide that the general management of the Company's affairs, business, and property is vested in a Board of Directors consisting of five members to be elected by the membership at an annual meeting, a majority of whom shall constitute a quorum to do business. Directors shall be elected by members of the Company at the annual meeting for a period of three years or until their successors are elected and qualified; one-third of said directorate shall be elected at each annual meeting. No person who does not reside within such territorial limits

shall become a director of the Company. Directors serving as of December 31, 2021, were as follows:

<u>Name and Residence</u>	<u>Term Expires</u>	<u>Occupation</u>
Ronald Gunsch Zap, ND	2023	Farmer
Darrel Suchy Mandan, ND	2024	Farmer
Kelli Mattern Beach, ND	2022	Insurance Agent
Marcus Erhardt New Salem, ND	2022	Retired Farmer/Agent
Randy John New Salem, ND	2023	Dairy Farmer

Officers

The Bylaws provide that the directors shall elect from their number a President, Vice-President, Second Vice President, and Secretary/Treasurer of which the Secretary/Treasurer position may be held by one person. All Officers shall hold their office for one year and until successors are elected and qualified. Officers serving as of December 31, 2021 were as follows:

<u>Officer</u>	<u>Title</u>
Ronald Gunsch	President
Randy John	First Vice President
Darrel Suchy	Second Vice President
Lisa Strom	Secretary-Treasurer

Committees

At December 31, 2021, the Company had one standing committee, the Investment Committee. The committee, however, did not meet during the examination period.

Those members serving on this Committee as of December 31, 2021 were as follows:

Ronald Gunsch	Randy John
Darrel Suchy	Kelli Mattern (Alternate)

CORPORATE RECORDS

The minutes of the meetings held by the membership and directors during the years under examination were reviewed for compliance with the Articles of Incorporation, Bylaws, and statutory requirements.

Articles of Incorporation and Bylaws

There were no amendments to the Articles of Incorporation during the period under review.

Two amendments were approved by the members to the Bylaws in 2021. The amendments decreased the number of directors from seven to five and removed the assessment language to conform with legislative changes.

Members

During the period under examination the annual meetings of the membership were held on the following dates: April 20, 2017, April 5, 2018, June 4, 2019, September 29, 2020 and October 4, 2021.

Directors

During the period under examination, the Board of Directors held 10 meetings in 2019, 11 meetings in 2017 and 2021 and 12 meetings in 2018 and 2020.

Conflict of Interest

The Company indicated in its Corporate Governance Annual Disclosure that Conflict of Interest Statements are completed on an annual basis. It was noted in a review of the board minutes that the Conflict of Interest Statements were only completed in 2019. **It is again recommended that Conflict of Interest Statements be completed on an annual basis, that those statements be retained, and any noted conflicts be reviewed by the board.**

Multiple Director claims were noted during the examination period. The Company does not have a formal process for reviewing and approving related party claims during board meetings. **It is recommended that all related party claims be approved by the full Board of Directors.**

FIDELITY BOND AND OTHER INSURANCE

The Company has a fidelity bond in force which provides \$500,000 coverage for losses associated with employee dishonesty. The Company also has \$25,000 in coverage for employee dishonesty and forgery and alteration under its business owners policy. The coverage meets the minimum amount of fidelity insurance suggested in the NAIC's *Financial Examiners Handbook*.

The Company also has in force a Directors and Officers Liability Insurance Policy providing a \$2,000,000 limit subject to a \$10,000 deductible. The policy provides coverage for errors or omissions in the performance of professional services and wrongful acts of a director or officer while acting solely in their individual or collective capacities as directors and officers.

TERRITORY AND PLAN OF OPERATION

At December 31, 2021, the Company was authorized to transact business in the following counties:

Adams	Billings	Bowman	Burleigh	Dunn
Golden Valley	Grant	Hettinger	Kidder	McKenzie
McLean	Mercer	Morton	Mountrail	Oliver
Sioux	Slope	Stark	Williams	

MARKET CONDUCT ACTIVITY

Treatment of Policyholders

Claims

Based on a limited review of claim files, the Company pays claims fairly within policy provisions upon receipt of satisfactory proof of loss or damage. It was noted at December 31, 2021, the Company had 74 unpaid claims, the average age of which was over 414 days; the oldest two exceeded 1,000 days. As of April 10, 2023, 56 of these claims were still open with an average age of 837 days. Per N.D.C.C. § 26.1-04-03(9)(c)&(d):

Unfair claim settlement practices. Committing any of the following acts, if done without just cause and if performed with a frequency indicating a general business practice:

- (c) Failing to adopt and implement reasonable standards for the prompt investigation of claims arising under insurance policies.
- (d) Not attempting in good faith to effectuate prompt, fair and equitable settlements of claims submitted in which liability has become reasonably clear.

It is recommended that the Company adopt, implement and execute reasonable standards for prompt investigation and settlement of claims as required by N.D.C.C. § 26.1-04-03(9)(c)&(d).

Advertising

The Company's advertising consists primarily of newspaper, radio, and miscellaneous ads (i.e., county fair). The advertising material was reviewed and no violations of N.D.C.C. § 26.1-04-03(2) were noted.

OPERATING AGREEMENTS

Loss Adjusting Service

During the examination period, the Company contracted with Grinnell Advisory Company, a subsidiary of Grinnell Mutual Reinsurance Company, to perform claims adjusting services.

Subsequent to the examination period, the Company began using the claims adjusting services of True Claim, LLC.

REINSURANCE

The following is a summary of the Company's most significant reinsurance contracts in force at December 31, 2021:

Nonaffiliated Ceding Contract:

Type:	Excess of Loss
Reinsurer:	Grinnell Mutual Reinsurance Company
Scope:	All policy forms and endorsements issued by the Company
	(A) Property Per Risk Excess of Loss – Covers up to \$20 million in losses from fire and windstorm risks written by the Company in excess of a \$175,000 retention.
	(B) Property Catastrophe Excess of Loss – Covers 100 percent of the Company's net losses incurred from windstorm, hail, or tornado loss occurrences within a period of 96 consecutive hours, in excess of a \$500,000 retention.
	(C) Property Aggregate Excess of Loss - Provides coverage for 100 percent of the Company's aggregate net losses in excess of a defined annual retention limit. The retention limit for 2021 was \$1,000,000.
Premium:	(A) Property Per Risk Excess of Loss - The 2021 annual premium was \$177,096 or \$14,758 per month.
	(B) Property Catastrophe Excess of Loss – The 2021 annual premium was \$96,000 or \$8,000 per month.
	(C) Aggregate Excess - The 2021 annual premium was \$79,104 or \$6,592 per month.
Termination Date:	The agreement may be terminated by either party with a written 90 day notice.

The contract contained the insolvency clause required by N.D.C.C. § 26.1-02-21 and all of the clause's required by the NAIC's *Accounting Practices and Procedures Manual*.

ACCOUNTS AND RECORDS

The Company's accounting procedures, internal controls, and transaction cycles were reviewed during the course of the examination and a trial balance as of December 31, 2021, was obtained and traced to the appropriate schedules of the Company's 2021 Annual Statement. Revenues and expenses were test checked to the extent deemed necessary.

Custodial Agreement

The Company's securities are held under an agreement executed with Fidelity Investments. This agreement was reviewed and found to be in compliance with N.D. Admin Code § 45-03-23-02.

FINANCIAL STATEMENTS

The following pages present a Statement of Assets, Liabilities, and Surplus as of December 31, 2021, and a Statement of Income for 2021.

These financial statements are based on the statutory financial statements filed by the Company with the Department and present the financial condition of the Company for the period ending December 31, 2021. The accompanying comments on financial statements reflect any examination adjustments to the amounts reported in the annual statement and should be considered an integral part of the financial statements.

**Southwest Mutual Insurance Company
Statement of Assets, Liabilities, and Surplus
December 31, 2021**

ASSETS:

LEDGER ASSETS:

Bonds	\$ 2,138,531	
Stocks	548,698	
Real Estate	86,161	
Cash on Hand and Checking Accounts	151,117	
Cash on Deposit	115,954	
Furniture, Fixtures, and Equipment	11,587	
TOTAL LEDGER ASSETS		\$3,052,048

NONLEDGER ASSETS:

Interest Due and Accrued on Bonds	\$ 15,307	
Interest Due and Accrued on Certificates of Deposit and Passbook Savings	230	
Assessments or Premiums in Course of Collection	156,941	
Market Value of Stocks Over Book Value	272,777	
Reinsurance Recoverable on Paid Losses	2,502	
TOTAL NONLEDGER ASSETS		447,757

DEDUCT: ASSETS NOT ADMITTED

Furniture, Fixtures, Automobiles	\$ 11,587	
Premiums over 90 Days Past Due	1,458	
TOTAL NONADMITTED ASSETS		(13,045)

TOTAL NET ADMITTED ASSETS

\$3,486,760

LIABILITIES:

Unpaid Losses	\$ 285,203	
Incurred But Not Reported Claims (IBNR)	4,500	
Unpaid Loss Adjustment Expense	6,500	
Advanced Premiums	25,904	
Unearned Premium Reserve	872,693	
Commissions Due and Payable to Agents	22,354	
Unpaid Taxes	8,565	
Unpaid Salaries	0	
Unpaid General Expenses	8,027	
Reinsurance Premiums Due and Payable	42,760	
Premiums Written for Others	8,395	
Federal Income Taxes	2,000	
TOTAL LIABILITIES		\$1,286,901

SURPLUS TO POLICYHOLDERS

\$2,199,859

TOTAL LIABILITIES AND SURPLUS

\$3,486,760

**Southwest Mutual Insurance Company
Statement of Income
For the Year 2021**

INCOME:

Gross Premium Income	\$1,649,537	
Less: Return Premiums	17,169	
Premiums for Reinsurance Ceded	358,783	
NET PREMIUM INCOME	<u> </u>	\$1,273,585
Interest on Bonds		38,355
Dividends on Stocks		19,858
Interest on Cash on Deposit (Banks and Savings & Loan Deposits)		7,915
Profit on sale or Maturity of Ledger Assets		8,045
Commissions and Service Fees Received		9,103
Miscellaneous Income		8,310
TOTAL INCOME RECEIPTS		<u> </u> <u>\$1,365,171</u>

DISBURSEMENTS:

Gross Losses Paid and Incurred in 2021	543,213	
Gross losses paid current year but occurred in previous years	81,191	
Deduct: Subrogation received	0	
Deduct: Reinsurance recovered	61,108	
NET LOSSES PAID		\$ 563,296
Claim Adjustment Expenses		41,570
Commissions Paid to Agents		281,110
Directors Fees and Expenses		15,804
Salaries to Employees		159,021
Printing, Stationery and Office Supplies		10,675
Real Estate Expenses (other than taxes)		9,621
Taxes on Real Estate		1,034
State and Local Insurance Taxes		24,805
Insurance Dept. Licenses & Fees		945
Payroll Taxes		19,977
Federal Income Taxes		4,414
Legal Fees and Auditing		4,150
Travel and Travel Items		4,052
Advertising		9,420
Dues and Donations		9,811
Equipment purchased (or depreciation on same)		3,850
Insurance and Bonds		14,725
Postage, Telephone, Internet and Bank charges		20,704
Employee Relations and Welfare		30,750
Data Processing Expenses		22,666
Risk Reviews and Other Underwriting Expenses		11,652
Investment Fees		18,896
Miscellaneous Expense		4,550
Change in Ledge Liabilities		(19,302)
TOTAL FUNDS DISBURSED		<u> </u> <u>1,268,196</u>
NET INCOME		<u> </u> <u>\$ 96,975</u>

COMMENTS ON FINANCIAL STATEMENTS

Financial statement balances at December 31, 2021, are commented upon only if financial changes, recommendations, or special explanations are considered necessary.

Liabilities

Loss Reserves

At December, 31, 2021, the Company had 74 open claims. The reserves on three of these claims have subsequent development through April 10, 2023 that was materially deficient; two of these claims remain open. Due to other errors noted during the subsequent claims runout, no adjustments will be made to surplus as the aggregate reserves have developed redundantly, thus far. It is noteworthy that 54 of these 74 open claims remain open and 41 have had no activity or updates between December 31, 2021 and April 10, 2023 (465 days) so it is likely that numerous additional claims will develop materially deficient due to supply chain and general materials cost inflation concerns which have occurred since these claims were first opened.

It was also noted that on the December 31, 2021 open claims reserve report, eight claims had \$1 reserves; two of these claims were materially deficient by April 10, 2023.

It is recommended that the Manager review each open claim and ensure case reserve adequacy monthly prior to presenting a status report to the Board of Directors during the monthly meetings. The Board should review the open claims reserve amounts and settlement timeliness against the policies referenced within N.D.C.C. § 26.1-04-03(9)(c)&(d).

Loss Adjustment Expenses

At December 31, 2021, the Company estimated its unpaid loss adjusting expenses ("ULAE") to \$6,500, but only had support for ULAE that met the definition of liabilities per SSAP 5R totaling \$3,437.50.

It is recommended that the Company only report ULAE matching the fixed contract rate when participating in annual adjusting subscription programs.

Reinsurance Premiums Due and Payable

Reinsurance premiums due and payable as determined by this examination consisted of the following items and amounts:

<u>Description</u>	<u>Company</u>	<u>Examination</u>
Due to Grinnell Mutual Reinsurance Company	\$27,233	\$27,233
Due to Hartford Steam Boiler	\$29,350	\$15,527
Total	<u>\$56,583</u>	<u>\$42,760</u>

At December 31, 2021, the Company reported \$56,583 in Reinsurance Premiums Due and Payable. The Company overreported the amount due to Hartford Steam Boiler ("HSB"). It was noted that during the 6-month period from July 2021 through December 2021 the Company did not remit payment to HSB. The payment was made in May 2022. The delay in payment was due

to deficiencies in the Company's process for calculating the amount owed to HSB under the reinsurance contract.

It is recommended that the Company implement procedures for remitting amounts owed to HSB on a monthly basis.

Surplus to Policyholders

Surplus to policyholders was determined by this examination to be \$2,199,859 or \$13,823 more than the amount reported by the Company. Adjustments to surplus are shown in the following schedule:

Description	Company	Examination	Increase (Decrease) to Surplus
Liabilities:			
Reinsurance Premiums Due and Payable	\$56,583	\$42,760	\$13,823
Net Increase			<u>\$13,823</u>
Surplus to Policyholders as reported by Company	\$2,186,724		
Increase (Decrease) to Surplus from above			<u>13,823</u>
Surplus to Policyholders per Examination			<u>\$2,199,859</u>

CONCLUSION

The financial condition of Southwest Mutual Insurance Company, New Salem, North Dakota, as determined by this examination is summarized as follows:

TOTAL ADMITTED ASSETS		<u>\$3,486,760</u>
Liabilities	\$1,286,901	
Surplus to Policyholders	<u>2,199,859</u>	
TOTAL LIABILITIES AND SURPLUS		<u>\$3,486,760</u>

Since the last examination conducted as of December 31, 2016, the Company's admitted assets have increased \$884,742, its total liabilities have increased \$405,291, and its surplus as regards policyholders has increased \$479,451.

In addition to the undersigned, North Dakota Insurance Department Examiner Rebekkah Boubin and Supervising Examiner Colton Schulz, CFE, CFE (Fraud), CISA participated in this examination.

The Examiners express their appreciation for the courteous cooperation extended them during the course of this examination.

Respectfully submitted,



Matt Fischer, CFE
Chief Examiner
North Dakota Insurance Department

COMMENTS AND RECOMMENDATIONS

It is again recommended that Conflict of Interest Statements be completed on an annual basis, that those statements be retained, and any noted conflicts be reviewed by the board.

It is recommended that all related party claims be approved by the full Board of Directors.

It is recommended that the Company adopt, implement and execute reasonable standards for prompt investigation and settlement of claims as required by N.D.C.C. § 26.1-04-03(9)(c)&(d).

It is recommended that the Manager review each open claim and ensure case reserve adequacy monthly prior to presenting a status report to the Board of Directors during the monthly meetings. The Board should review the open claims reserve amounts and settlement timeliness against the policies referenced within N.D.C.C. § 26.1-04-03(9)(c)&(d).

It is recommended that the Company only report ULAE matching the fixed contract rate when participating in annual adjusting subscription programs.

It is recommended that the Company implement procedures for remitting amounts owed to HSB on a monthly basis.