

STATE OF MISSOURI



DEPARTMENT OF INSURANCE, FINANCIAL INSTITUTIONS AND PROFESSIONAL REGISTRATION

P.O. Box 690, Jefferson City, Mo. 65102-0690

RE: Examination Report of Keystone Mutual Insurance Company for the period ended December 31, 2013

ORDER

After full consideration and review of the report of the financial examination of Keystone Mutual Insurance Company for the period ended December 31, 2013, together with any written submissions or rebuttals and any relevant portions of the examiner's workpapers, I, John M. Huff, Director, Missouri Department of Insurance, Financial Institutions and Professional Registration pursuant to section 374.205.3(3)(a), RSMo., adopt such examination report. After my consideration and review of such report, workpapers, and written submissions or rebuttals, I hereby incorporate by reference and deem the following parts of such report to be my findings and conclusions to accompany this order pursuant to section 374.205.3(4), RSMo: summary of significant findings, subsequent events, company history, corporate records, management and control, fidelity bond and other insurance, pension, stock ownership and insurance plans, territory and plan of operations, growth of the company and loss experience, reinsurance, accounts and records, statutory deposits, financial statements, analysis of examination changes, comments on financial statement, and general comments or recommendations.

Based on such findings and conclusions, I hereby ORDER, that the report of the Financial Examination of Keystone Mutual Insurance Company as of December 31, 2013 be and is hereby ADOPTED as filed and for Keystone Mutual Insurance Company to take the following action or actions, which I consider necessary to cure any violation of law, regulation or prior order of the Director revealed by such report: (1) implement, and verify compliance with each item, if any, mentioned in the Comments on Financial Statement Items and/or Summary of Recommendations section of such report; (2) account for its financial condition and affairs in a manner consistent with the Director's findings and conclusions.

So ordered, signed and official seal affixed this 10th day of April, 2015.



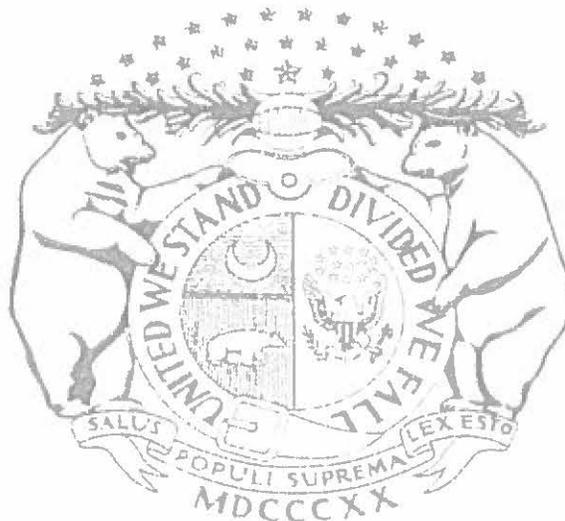
John M. Huff, Director
Department of Insurance, Financial Institutions
and Professional Registration

REPORT OF
FINANCIAL EXAMINATION

Keystone Mutual Insurance Company

As of:
DECEMBER 31, 2013

FILED
APR 20 2015
DIRECTOR OF INSURANCE,
FINANCIAL INSTITUTIONS &
PROFESSIONAL REGISTRATION



STATE OF MISSOURI

DEPARTMENT OF INSURANCE, FINANCIAL INSTITUTIONS
AND PROFESSIONAL REGISTRATION

JEFFERSON CITY, MISSOURI

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November 18, 2014
St. Louis, MO

Honorable John M. Huff, Director
Missouri Department of Insurance, Financial
Institutions and Professional Registration
301 West High Street, Room 530
Jefferson City, MO 65101

Director Huff:

In accordance with your financial examination warrant, a comprehensive financial examination has been made of the records, affairs and financial condition of

Keystone Mutual Insurance Company

hereinafter referred to as “Keystone”, or the “Company”. The Company's home office is located at 366 West Fourth Street, St. Louis, Missouri 63025; telephone number (636)549-3744. Examination fieldwork began on March 17, 2014, and concluded on the above date.

SCOPE OF EXAMINATION

Period Covered

We have performed a single-state examination of Keystone Mutual Insurance Company. The last examination was completed as of December 31, 2010. This examination covers the period of January 1, 2011, through December 31, 2013. This examination also included material transactions or events occurring subsequent to December 31, 2013.

Procedures

This examination was conducted using guidelines set forth in the Financial Condition Examiners Handbook (Handbook) of the NAIC, except where practices, procedures and applicable regulations of the Department of Insurance, Financial Institutions and Professional Registration (“Department” or “DIFP”) or statutes of the state of Missouri prevailed. The Handbook requires that we plan and perform the examination to evaluate the financial condition and to identify prospective risks of the Company. This process involves obtaining information about the Company, including corporate governance, identifying and assessing inherent risks within the Company, and evaluating the systems controls and procedures used by the Company to mitigate those risks. The examination also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation, compliance with Statutory Accounting Principles and Annual Statement instructions when applicable to domestic state regulations.

All accounts and activities of the Company were considered in accordance with the risk-focused examination process. The following key activities were identified: Claims and Reserving, Expenses, Investments and Treasury, Premiums and Underwriting, Reinsurance and Taxes.

SUMMARY OF SIGNIFICANT FINDINGS

An examination change was made to reclassify the cumulative capital contributions made by policyholders of \$161,883 from Gross paid in and contributed surplus to Aggregate write-ins for other than surplus funds.

SUBSEQUENT EVENTS

None.

COMPANY HISTORY

General

Keystone Mutual Insurance Company was incorporated under the laws of the state of Missouri on December 31, 2007 pursuant to Chapter 383, RSMo (Malpractice Insurance) as an assessable medical malpractice company with authority to write medical malpractice insurance in Missouri only. The Company is not subject to Chapter 382, RSMo (Insurance Holding Companies).

Capital Stock

The Company is a mutual insurance company and has no capital stock.

Dividends

The Company has not paid any dividends to its members since its inception.

Acquisitions, Mergers and Major Corporate Events

There have been no mergers or acquisitions involving the Company.

Surplus Debentures

The Company has issued the following Surplus Notes:

<u>Date Issued</u>	<u>Interest Rate</u>	<u>Carrying Value</u>	<u>Accrued Interest</u>	<u>Total</u>
9/30/2009	7%	\$ 220,000	\$ 65,705	\$ 285,705
11/30/2009	7%	50,000	14,340	64,340
12/31/2009	7%	10,000	2,810	12,810
12/31/2010	7%	80,000	16,878	96,878
12/31/2010	7%	90,000	18,988	108,988
11/30/2011	7%	110,000	16,029	126,029
12/30/2011	7%	100,000	14,000	114,000
12/30/2011	7%	40,000	5,600	45,600
		<u>\$ 700,000</u>	<u>\$ 154,350</u>	<u>\$ 854,350</u>

All of the Surplus Notes were issued to Keystone Mutual Holding Company, with the exception of the \$100,000 note issued on December 30, 2011. This note is held by the Company's CEO, and is administered by Sunwest Trust Inc.

CORPORATE RECORDS

Corporate Documents

The Articles of Association and the Bylaws were reviewed. Effective January 5, 2011, the Articles were amended to change the term "initial assessments" paid by policyholders to "initial capital contributions" and to implement an ongoing annual capital contribution of 2.5% of each member's annual premium. No amendments were made to the Bylaws during the examination period.

Meeting Minutes

Minutes of the meetings of the Board of Directors and committees were reviewed for the period under examination. The minutes documented evidence of the overall guidance provided by the Board of Directors.

MANAGEMENT AND CONTROL

Board of Directors

As of December 31, 2013, the following eleven members comprised the Board of Directors:

Name	Principal Occupation
James R. Bowlin Wildwood, MO	Chairman and CEO Keystone Mutual Insurance Company
Scott B. Lakin Kansas City, MO	Principal Lakin Consulting, LLC
Jerry N. Middleton, MD, FACOG St. Louis, MO	Obstetrician and Gynecologist Obstetrical Associates of St. Louis, Inc.
Craig S. McPartlin Wildwood, MO	CEO and Treasurer Con-Tech Carpentry, LLC
Jerry D. Kennett, MD, FACC Columbia, MO	Cardiologist Missouri Cardiovascular Specialists, LLP
Katie Steele Danner Jefferson City, MO	Director Missouri Division of Tourism
Joel D. Hassien, MD Hannibal, MO	Radiologist; President Hannibal Imaging Service
Dennis A. Nahnsen Saint Louis, MO	Retired President Missouri Valley Partners
Bruce C. Oetter Clayton, MO	Partner Bryan Cave LLP
George K. Parkins Prairie Village, KS	Orthopedic Surgeon Drisko, Fee & Parkins, PC
Matthew J. Spellman, MD Richmond Heights, MO	Urologist; President Urology Consultants, Ltd.

Committees

Committee assignments as of December 31, 2013 were as follows:

Rate & Underwriting

Dr. Matthew J. Spellman
Katie Steele Danner
Dr. Jerry N. Middleton

Claims

Dr. Jerry D. Kennett
Dr. Jerry N. Middleton
Bruce C. Oetter

Reinsurance

Dr. Jerry N. Middleton
Craig S. McPartlin
Dr. Joel D. Hassien

Marketing

Dr. George K. Parkins
Scott B. Lakin
Dr. Matthew J. Spellman

Governmental Affairs

Dr. Jerry D. Kennett
Scott B. Lakin
Dr. Jerry N. Middleton

Investment/Finance

Dennis A. Nahnsen
Craig S. McPartlin
Bruce C. Oetter

Compensation

Katie Steele Danner
Dr. Joel D. Hassien
Dr. Matthew J. Spellman

Audit

Dr. Jerry D. Kennett
Dennis A. Nahnsen
Dr. George K. Parkins

Appellate

Dr. Joel D. Hassien
Scott B. Lakin
Dr. George K. Parkins

Nominating

Dr. Joel D. Hassien
Dr. George K. Parkins
Bruce C. Oetter

Officers

The officers of the Company elected and serving as of December 31, 2013 were as follows:

<u>Name</u>	<u>Office</u>
James R. Bowlin	Chairman and CEO
Scott B. Lakin	President
Dr. Jerry N. Middleton	Vice-President
Craig S. McPartlin	Treasurer
Dr. Jerry D. Kennett	Secretary

Organizational Structure

The Company is a single entity, owned by the membership with no equity holdings of its own. The Company has issued a series of Surplus Notes to Keystone Insurance Holding Company and has entered into a management agreement with Keystone Insurance Holding Company for underwriting and general management. Keystone Insurance Holding Company is owned by the Chairman and CEO of Keystone Mutual Insurance Company.

Intercompany Transactions

The Company is a party to the following two affiliated agreements.

Management Agreement

Parties: Keystone Mutual Insurance Company and Keystone Insurance Holding Company.

Effective: January 1, 2010

Services: Keystone Insurance Holding Company provides underwriting, claims and other corporate management services.

Rate(s): The Company incurred \$72,000 in management fees in 2013 per this agreement.

Lease Agreement

Parties: Keystone Mutual Insurance Company and McPartlin Realty, LLC.

Effective: January 1, 2013

Services: The Company leases office space at 366 W. 4th Street, Eureka, MO, 63025, from McPartlin Realty, LLC, which is owned by Craig S. McPartlin. The lease is for a one year term at a monthly rent of \$490. Under the lease, McPartlin Realty, LLC is responsible for all utilities, repairs and maintenance, and property taxes associated with the building.

Rate(s): The Company incurred \$5,880 in fees in 2013 per this agreement.

FIDELITY BOND AND OTHER INSURANCE

The Company is a named insured on a fidelity bond with a coverage limit of \$100,000 and a deductible of \$20,000. The coverage exceeds the minimum amount of fidelity insurance recommended by the NAIC.

Keystone is also a named insured on policies which provide the following types of coverage: general liability, employer's liability, automobile liability, directors and officers liability, commercial property damage, and personal property. In addition, the Company has a key-man life insurance policy on the Chairman and Chief Executive Officer, James R. Bowlin. The Company's level of insurance coverage appears adequate.

PENSIONS, STOCK OWNERSHIP AND INSURANCE PLANS

Keystone has a total of eight employees, including the Chief Executive Officer, Chief Financial Officer, a Member Relations Manager, an Underwriter and four sales agents. The Chief Financial Officer and Underwriter are part-time while the remaining positions are full-time.

Employees receive a comprehensive benefits package, which includes health and disability insurance coverage, paid time off, holidays, and a SIMPLE IRA.

TERRITORY AND PLAN OF OPERATIONS

The Company is organized as an assessable mutual insurance company, licensed to write medical malpractice insurance under Chapter 383 RSMo. The Company writes business in the state of Missouri only. Currently, Keystone only insures doctors who practice in one of 12 select specialties that it has identified as being low-risk, based on past claims experience in the industry. Coverage is issued primarily on a claims-made basis with a coverage limit of \$1 million/\$3 million. Members can also purchase an extended reporting endorsement which provides coverage on an occurrence basis with the same coverage limits. Free tail coverage (occurrence-based) is also offered in the event of death, disability, or retirement.

The Company produces the majority of its business through 4 licensed captive agents. A small amount of business is also produced through 2 non-exclusive insurance agencies; Missouri Rural Services Corporation, and Carpenter & Company.

GROWTH OF COMPANY

The table below shows various indicators of the Company's growth over the past four years.

	2010	2011	2012	2013
Gross Written Premiums	\$ 983,936	\$ 1,058,594	\$ 1,414,800	\$ 1,493,242
Total Admitted Assets	837,321	1,212,772	1,518,553	1,717,433
Other Underwriting Expenses Incurred	462,266	743,100	766,566	857,080
Total Capital and Surplus	(12,616)	123,311	114,024	156,606

The Company has experienced moderate, steady growth in written premiums and total assets. Operating expenses have also increased as premium has grown. Capital and surplus increased by a total of \$169,222 during the examination period. A series of surplus notes with a total par value of \$700,000 were issued in the period 2009-2011 to improve the Company's capital and surplus position.

LOSS EXPERIENCE

The following exhibit illustrates Keystone's underwriting results for each of the last four years.

	2010	2011	2012	2013
Premiums Earned	\$ 717,887	\$ 928,747	\$ 967,231	\$ 1,284,364
Losses Incurred	312,000	101,469	9,553	227,578
Loss Adjustment				
Expenses Incurred	162,989	258,959	275,757	237,534
Net Underwriting Gain	(219,368)	(174,781)	(84,645)	(37,828)
Net Income	(196,195)	(145,111)	(95,355)	12,859

The Company experienced poor operating results during its first few years in existence. This is not unusual for a new startup insurer. Surplus has been maintained with several infusions of funds through surplus notes. Operating performance has gradually improved in recent years, and the Company reported positive net income for the first time in 2013. Losses and loss adjustment expenses remained at a reasonable level during the examination period. The Company did not make any indemnity payments from its inception in 2008 through 2011. Loss payments of \$170,000 and \$140,000 were made in 2012 and 2013 respectively.

REINSURANCE

General

Premiums written during 2010 through 2013 were as follows:

<u>Premiums</u>	2010	2011	2012	2013
Direct Business	\$ 983,936	\$ 1,058,594	\$ 1,414,800	\$ 1,493,242
Reinsurance Assumed	-	-	-	-
Reinsurance Ceded	222,776	98,839	240,124	221,983
Net Premiums	<u>\$ 761,160</u>	<u>\$ 959,755</u>	<u>\$ 1,174,676</u>	<u>\$ 1,271,259</u>

Assumed

The Company does not assume any reinsurance.

Ceded

Keystone has one reinsurance agreement, a Medical Professional Liability Excess of Loss Contract. The original agreement has been in effect since the Company began operations in 2008 and it has since been subsequently renewed through a number of addenda. The reinsurance intermediary, Guy Carpenter, manages the program and the participating reinsurers are Hannover Ruchversicherung AG (15%), Catlin Insurance Company Ltd. (35%) and various Lloyd's Syndicates (50%).

The Company's retention limit under the agreement is \$200,000 per occurrence. The reinsurers' maximum liability is equal to 300% of the ceded reinsurance premium for the current underwriting year.

The provisional premium under the agreement is equal to 20% of net written premium for the current underwriting year. The Company pays the reinsurers an annual deposit premium of \$350,000, payable in four quarterly installments. The deposit premium is then adjusted to the provisional premium amount within 60 days after the end of the underwriting year.

The agreement also has a "swing-rate" premium adjustment feature under which a final adjusted premium is calculated based on several factors, including the reinsurers' loss experience and the Company's net earned premiums for the underwriting year.

Effective July 1, 2012, all losses incurred by the Company under policies allocated to the first underwriting year of the agreement (defined as the period from March 1, 2008 through February 28, 2010) were commuted in exchange for \$126,164. This commutation constitutes a complete and final release of both parties with respect to claims under policies allocated to the first underwriting year.

Effective July 1, 2013, all losses incurred by the Company under policies allocated to the second underwriting year of the agreement (defined as the period from March 1, 2010 through June 30, 2011) were commuted in exchange for \$150,619.

To date, Keystone has not had a claim that has reached the \$200,000 retention limit attachment point.

ACCOUNTS AND RECORDS

General

The Company uses Peachtree Accounting Software and various Microsoft Excel spreadsheets to maintain its general ledger. The Company also uses Microsoft Excel for underwriting, policy administration, premiums, and claims management functions. Annual and quarterly financial data are compiled by the external accounting firm of Mountjoy Chilton Medley LLP, and used to prepare the statutory financial statements.

Independent Auditor

The Company's financial statements are audited annually by the accounting firm of Brown Smith Wallace, LLC. The workpapers and reports of the 2012 independent audit were reviewed for this examination. These workpapers and reports were used in the course of this examination as deemed appropriate.

Independent Actuaries

Reserves and related actuarial items reported in the financial statements were reviewed and certified by Ronald T. Kuehn, FCAS, MAAA, of Huggins Actuarial Services, Inc.

Consulting actuary, Robert P. Daniel, ACAS, MAAA, of Merlinos & Associates, Inc. was retained by the Department to review the adequacy of the Company's reserves and other related liabilities. He concluded that the Company's reserves and other related liabilities, as of the examination date, were reasonable.

STATUTORY DEPOSITS

The Company writes only in Missouri and, as a Chapter 383 company, is not required to maintain any deposits with the state.

FINANCIAL STATEMENTS

The following financial statements, with supporting exhibits, present the financial condition of the Company as of December 31, 2013, and the results of operations for the year then ended. Any examination adjustments to the amounts reported in the financial statements and/or comments regarding such are made in the "Comments on Financial Statements" section, which follow the financial statements.

There may have been additional differences found in the course of this examination that are not shown in the "Comments on Financial Statements." These differences were determined to be immaterial in relation to the financial statements and therefore were only communicated to the Company and noted in the workpapers for each individual annual statement item.

ASSETS

	Assets	Non- Admitted Assets	Net Admitted Assets
Bonds	\$ 102,099	\$ -	\$ 102,099
Cash and short-term investments	1,156,204	-	1,156,204
Investment income due and accrued	477	-	477
Uncollected premiums	48,315	-	48,315
Deferred premiums	167,543	-	167,543
Other amounts receivable on reinsurance	104,845	-	104,845
Current federal income tax recoverable	33,583	-	33,583
Net deferred tax asset	77,268	35,732	41,536
Electronic data processing equipment	14,692	14,692	-
Prepaid expenses	7,831	7,831	-
Prepaid reinsurance	12,831	-	12,831
Insurance proceeds receivable	50,000	-	50,000
TOTAL ASSETS	\$ 1,775,688	\$ 58,255	\$ 1,717,433

LIABILITIES, SURPLUS AND OTHER FUNDS

Losses	\$ 340,600
Loss adjustment expenses	429,399
Other expenses	120,111
Taxes, licenses and fees	5,342
Unearned premiums	549,695
Advance premium	115,680
TOTAL LIABILITIES	<u>\$ 1,560,827</u>
Aggregate Write-Ins for Other Than Special Surplus Funds (Note 1)	\$ 174,250
Surplus notes	854,350
Gross paid in and contributed surplus (Note 1)	-
Unassigned funds (surplus)	<u>(871,994)</u>
SURPLUS AS REGARDS POLICYHOLDERS	<u>\$ 156,606</u>
TOTAL LIABILITIES AND SURPLUS	<u><u>\$ 1,717,433</u></u>

STATEMENT OF INCOME

Underwriting Income:

Premiums earned		\$ 1,284,364
Deductions:		
Losses incurred	\$ 227,578	
Loss expenses incurred	237,534	
Other underwriting expenses incurred	<u>857,080</u>	
Total underwriting deductions		<u>1,322,192</u>
Net Underwriting Gain (Loss)		\$ (37,828)

Investment Income:

Net investment income earned	\$ 5,235	
Net realized capital gains	<u>-</u>	
Net Investment Gain (Loss)		\$ 5,235

Other Income:

Net loss from agents or premium balances charged off	\$ -	
Finance and service charges	45,875	
Gain/(Loss) on sale of assets	<u>(1,351)</u>	
Total Other Income		<u>\$ 44,524</u>

Net income before dividends and FIT \$ 11,931

Dividends to policyholders	-	
Federal income taxes incurred	<u>(928)</u>	
Net income		<u>\$ 12,859</u>

RECONCILIATION OF SURPLUS

Changes from December 31, 2010 to December 31, 2013

	<u>2011</u>	<u>2012</u>	<u>2013</u>
Surplus as regards policyholders; December 31 prior year	\$ (12,616)	\$ 123,311	\$ 114,024
Net income	(145,111)	(95,355)	12,859
Change in net deferred income tax	-	65,189	12,079
Change in nonadmitted assets	2,849	(20,898)	(22,060)
Change in surplus notes	282,607	49,000	49,000
Surplus adjustments: Paid in	28,190	41,777	39,704
Transferred from capital	-	(5,293)	(12,367)
Accrued interest on surplus notes	(32,608)	(49,000)	(49,000)
Legacy Plan	-	5,293	12,367
Change in surplus as regards policyholders for the year	<u>135,927</u>	<u>(9,287)</u>	<u>42,582</u>
Surplus as regards policyholders; December 31 current year	<u>\$ 123,311</u>	<u>\$ 114,024</u>	<u>\$ 156,606</u>

ANALYSIS OF EXAMINATION CHANGES

Surplus as Reported by Company			\$156,606
	Increase in Surplus	Decrease in Surplus	
Aggregate write-ins for other than special surplus funds (Note 1)	161,883		
Gross paid in and contributed surplus (Note 1)		161,883	
Total Changes	161,883	161,883	
Net Change in Surplus			-
Surplus Per Examination			\$156,606

COMMENTS ON FINANCIAL STATEMENTS

Note 1	Aggregate write-ins for other than special surplus funds	\$174,250
	Gross paid in and contributed surplus	\$0

Keystone's Articles of Association require policyholders to pay initial and annual capital contributions to the Company. The cumulative balance of these contributions were reported on the Gross paid in and contributed surplus line on the Annual Statement. Per SSAP No. 72 (Surplus and Quasi-Reorganizations), gross paid-in and contributed surplus is the amount of capital received in excess of the par value of the stock issued. This does not appear to be applicable since Keystone is a mutual company instead of a stock company. The capital contributions appear to more closely meet the definition of other than special surplus funds per SSAP No. 72. As a result, an adjustment was made to reclassify the cumulative capital contributions of \$161,883 from Gross paid in and contributed surplus to Aggregate write-ins for other than special surplus funds.

GENERAL COMMENTS OR RECOMMENDATIONS

Comments on Financial Statements

Page 15

The Company should report the cumulative balance of policyholder contributions on the Aggregate write-ins for other than special surplus funds line on the Annual Statement in the future.



April 9, 2015

Via Email

Leslie Nehring, CPA, CFE
Acting Chief Financial Examiner
Missouri Department of Insurance, Financial Institutions
& Professional Registration
301 W. High St., Room 530
P.O. Box 690
Jefferson City, MO 65102-0690

RE: Examination Report, dated November 18, 2014 (the "Report")

Dear Ms. Nehring:

Thank you for your March 31, 2015 correspondence.

Please find enclosed our Company's response to the Report included with your letter. We ask that this response be included with the Report as a public document.

Please let me know if you have any questions or comments.

Sincerely,


James R. Bowlin
CEO

Encl. - 1

c: Craig S. McPartlin, CFO (w/Encl.)

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**Missouri Department of Insurance, Financial Institutions & Professional Registration (the
"Department") Missouri Financial Examination
Keystone Mutual Insurance Company (NAIC #13073)
Company Response – Examination Report dated 11/18/14 (the "Report")**

COMMENTS ON FINANCIAL STATEMENTS

Note 1 – Reclassification of Cumulative Capital Contribution

The Company has reclassified \$161,883 in cumulative capital contributions received from its policyholders, from Gross Paid-In and Contributed Surplus to Aggregate Write-Ins for Other than Special Surplus Funds, as set forth in Note 1.

GENERAL COMMENTS OR RECOMMENDATIONS

Comment on Financial Statements

The Report stated:

The Company should report the cumulative balance of policyholder contributions on the Aggregate write-ins for other than special surplus funds line on the Annual Statement in the future.

Company Response:

This relates to the same issue referenced in Note 1, above, and the Company agrees with this recommendation.