

# STATE OF MISSOURI



## DEPARTMENT OF INSURANCE, FINANCIAL INSTITUTIONS AND PROFESSIONAL REGISTRATION

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

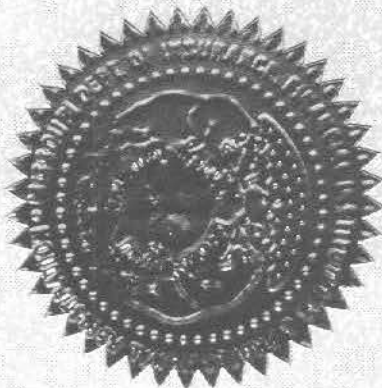
RE: Examination Report of Shelter Mutual Insurance Company as of December 31, 2007

### ORDER

After full consideration and review of the report of the financial examination of Shelter Mutual Insurance Company for the period ended December 31, 2007, 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 report. After my consideration and review of such report, workpapers, and written submissions or rebuttals, the findings and conclusions of the examination report are incorporated by reference and deemed to be my findings and conclusions to accompany this order pursuant to section 374.205.3(4), RSMo.

Based on such findings and conclusions, I hereby ORDER Shelter 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 mentioned in the General Comments and/or 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 May 7, 2009.



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

REPORT OF THE  
ASSOCIATION FINANCIAL EXAMINATION OF  
**SHELTER MUTUAL INSURANCE COMPANY**

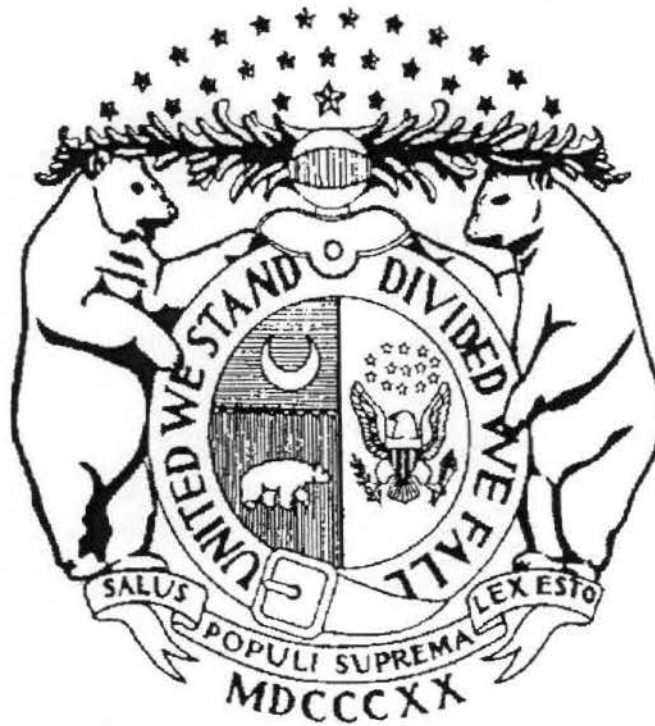
AS OF

**FILED**

DECEMBER 31, 2007

MAY 17 2009

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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Columbia, Missouri  
April 10, 2009

Honorable Alfred W. Gross, Commissioner  
Virginia Bureau of Insurance  
Chairman of Financial Condition (EX4) Subcommittee

Honorable Merle D. Scheiber, Commissioner  
South Dakota Division of Insurance  
Midwestern Zone Secretary

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

Gentlemen:

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

**Shelter Mutual Insurance Company**

hereinafter referred to as such, as Shelter Mutual, or as the Company. Its administrative office is located at 1817 West Broadway, Columbia, Missouri 65218, telephone number (573) 445-8441. This examination began on August 18, 2008, fieldwork was completed on March 5, 2009 and the examination report was concluded on the above date.

## SCOPE OF EXAMINATION

### Period Covered

The prior full scope association financial examination of Shelter Mutual Insurance Company was made as of December 31, 2004, and was conducted by examiners from the State of Missouri representing the Midwestern Zone of the National Association of Insurance Commissioners (NAIC).

The current full scope association financial examination covered the period from January 1, 2005, through December 31, 2007, and was conducted by examiners from the State of Missouri, representing the Midwestern Zone of the NAIC, with no other zones participating.

This examination was performed concurrently with the examinations of the Company's subsidiaries, Shelter General Insurance Company (Shelter General), Shelter Reinsurance Company (Shelter Re) and Shelter Life Insurance Company (Shelter Life), collectively constituting the Shelter Insurance Companies.

This examination also included the material transactions and/or events occurring subsequent to the examination date, which are noted in this report.

### Procedures

This examination was conducted using the guidelines set forth in the Financial Condition Examiners Handbook of the NAIC, except where practices, procedures and applicable regulations of the Missouri Department of Insurance, Financial Institutions and Professional Registration (DIFP) and statutes of the State of Missouri prevailed.

The examiners relied upon information supplied by the Company's independent auditor, Ernst & Young, LLP, of Kansas City, Missouri, for its audit covering the period from January 1, 2007, through December 31, 2007. Information relied upon included paid losses and schedule P analysis and reconciliation, attorney letters, review and documentation of review of fraud, tests of controls and system walk-throughs, narrative descriptions of processes and controls, etc.

### Comments - Previous Examination

Listed below are comments, recommendations and notes of the previous examination report dated as of December 31, 2004, and the subsequent response or action taken by the Corporation.

### **Reinsurance Agreement with ERC**

*Comment:* The Company's excess reinsurance agreement with ERC, originally effective January 1, 1975, was determined to be disjointed with over 50 amendments and containing confusing

terminology. It was recommended that the agreement should be restated in its entirety so that the reinsured lines of business, retentions, and limits are clearly defined.

*Company's Response:* The Company disagreed with the characterization of the agreement terms, insisting that neither the Company nor the reinsurer have had any disagreements or difficulty arising from terms of the agreement or the amendments.

*Current Findings:* The agreement was revised during the course of this examination, accordingly, no other issue was indicated.

### **Voided Drafts**

*Comment:* The Company was directed to maintain a running balance of voided claim drafts that have not been reissued at the end of each month. The Company was also directed to record as liabilities in the Losses line the amount of unpaid claims relating to voided drafts in accordance with an applicable Statement of Statutory Accounting Principle (SSAP).

*Company's Response:* The Company indicated that items of this nature are included in its IBNR. The Company further indicated that it will continue to conservatively report loss reserves in accordance with applicable standards.

*Current Findings:* No additional problems were indicated during the current examination period.

## **HISTORY**

### **General**

Shelter Mutual Insurance Company was incorporated on August 31, 1945 and was originally named M.F.A. Mutual Insurance Company. It was issued a Certificate of Authority on December 31, 1945 and commenced business on January 1, 1946. The Company's name was changed to Shelter Mutual Insurance Company on July 1, 1981. The Company operates as a mutual property and casualty insurer under the insurance laws of Chapter 379 RSMo (Insurance Other Than Life).

### **Capital Stock**

The Company was organized as a mutual entity and therefore, does not have any capital stock ownership. The Company is owned 100% by its policyholders.

**Dividends**

Shelter Mutual does not have any stockholders. The Company's Bylaws allow for dividends to be paid to its policyholders. However, no dividends were declared or paid during the examination period.

**Management**

The management of the Company is vested in a Board of Directors that are appointed by the policyholders. The Company's Articles of Incorporation and Bylaws specify that the number of directors shall be nine. Each director must also be a policyholder of Shelter Mutual. The Board of Directors appointed and serving, as of December 31, 2007, were as follows:

<u>Name and Address</u>	<u>Principal Occupation and Business Affiliation</u>
John D. Duello Rocheport, MO	Chairman of the Board and Retired Executive Shelter Insurance Companies
John D. Moore Columbia, MO	President and CEO Shelter Insurance Companies
Raymond E. Jones Columbia, MO	Retired Executive Shelter Insurance Companies
Gerald T. Brouder Columbia, MO	President Columbia College
Ann K. Covington Columbia, MO	Vice Chairman Shelter Insurance Companies Attorney / Partner Bryan Cave, LLP
Andres Jimenez* Madrid, Spain	Vice President and Chief Executive Officer Mapfre Re Compania de Reaseguros, S.A.
Don A. McCubbin Sturgeon, MO	Executive Vice President Shelter Insurance Companies
Barry L. McKuin Morrilton, AR	Retired President Morrilton Area Chamber of Commerce
Phillip K. Marblestone University Park, FL	Retired Partner PriceWaterhouseCoopers LLP

\* Effective August 1, 2008, Mr. Jimenez retired and was replaced as a Board member by Randall C. Ferguson, Jr.

**Committees**

The Bylaws require an Executive and Compensation Committee, Audit Committee, and an Investment Committee of the Board of Directors. The Bylaws also allow for other committees to



be appointed by the Board of Directors as needed. As of December 31, 2007, the members of each committee were as follows:

**Executive and Compensation Committee**

Ann K. Covington, Chairman  
John D. Duello  
Barry L. McQuin  
John D. Moore  
Gerald T. Brouder

**Investment Committee**

John D. Duello, Chairman  
Raymond E. Jones  
Thomas N. Fischer#  
Ann K. Covington  
John D. Moore  
Don A. McCubbin  
Gerald T. Brouder

**Audit Committee**

Barry L. McQuin, Chairman  
Ann K. Covington  
Phillip K. Marblestone

# Resigned effective March 1, 2008, and was replaced by Jerry L. French

**Officers**

The officers of the Company shall be a Chairman of the Board, Vice Chairman of the Board, a President and Chief Executive Officer, an Executive Vice President, Vice Presidents, Secretary and a Treasurer, all of whom shall be elected by the Board of Directors. The officers elected by the Board of Directors and serving as of December 31, 2007, were as follows:

John. D. Duello	Chairman
Ann K. Covington	Vice Chairman
John D. Moore	President and Chief Executive Officer
Randa Rawlins	Secretary and General Counsel
Don A. McCubbin	Executive Vice President
Gary D. Myers	Executive Vice President
Ricky L. Means	Executive Vice President
Jerry L. French	Executive Vice President, Treasurer, and Assistant Secretary
William C. Keithley*	Vice President – Information Services
Max T. Dills	Vice President – Administration
Joe L. Moseley	Vice President – Public Affairs
Gary L. Ford	Vice President – Planning and Research
C. Tyler Bailey	Vice President – Marketing
Madison M. Moore	Vice President – Claims
S. Daniel Clapp	Vice President – Actuarial
Terry L. Dykes	Vice President – General Services
Thomas N. Fischer#	Vice President – Investments
L. Gerald Brooks@	Assistant Treasurer

# Thomas N. Fischer resigned as Vice President of Investments effective March 31, 2008. Investment duties will be performed by Jerry L. French, Executive Vice President, Treasurer, and Assistant Secretary.

\* William C. Keithley was appointed Executive Vice President as of January 1, 2008, and was replaced by Yvette M. Gonzales as Vice President of Information Services effective as of the same date.

@ L. Gerald Brooks retired on November 21, 2008 and was replaced by Christina M. Workman as Assistant Treasurer. Ms. Workman was also appointed Vice President of Accounting as of January 1, 2008.

### **Conflict of Interest**

The Company has a policy that requires all officers, directors, and key employees to complete a conflict of interest statement each year. Signed statements of officers and directors were reviewed for the examination period. No significant exceptions were noted.

### **Corporate Records**

A review was made of the Articles of Incorporation and Bylaws for the examination period. There were no amendments or changes to the Articles of Incorporation during the period under examination.

The Bylaws were amended and restated effective February 24, 2005, to specify the indemnification guidelines for employees, officers, and directors that are subject to litigation proceedings. The Bylaws were further amended effective October 10, 2005, to add the Investment Committee as a required committee of the Board of Directors, revise the duties and requirements of elected officers, and other minor changes. The bylaws were also amended effective December 18, 2006, to change the title of Chairman of the Board and CEO to simply Chairman of the Board, and to change the title of President and Chief Operating Officer to President and Chief Executive Officer.

The minutes of the Board of Directors' meetings, committee meetings, and policyholders' meetings were reviewed for proper approval of corporate transactions. In general, the minutes appear to properly reflect and approve the Company's major transactions and events for the period under examination.

### **Acquisitions, Mergers and Major Corporate Events**

There was no major corporate event or acquisition during the examination period. However, subsequent to the examination date, Shelter Mutual contracted to purchase 100% of the issued and outstanding stock of a Tennessee domiciled insurer, Haulers Insurance Company (Haulers Insurance) for \$50,705,595, pursuant to a purchase agreement. The transaction closed on June 30, 2008, with Shelter Mutual acquiring 100% of the issued and outstanding share of Haulers Insurance. Haulers Insurance is a property and casualty insurer licensed in 18 states and sells

insurance primarily for private and commercially owned automobiles. The transaction was accounted for as a statutory purchase. On June 30, 2008, Haulers Insurance recorded surplus was \$31,065,859, resulting in goodwill in the amount of \$19,639,736 in Shelter Mutual's books. This amount will be amortized over 10 years in accordance with the applicable statutory accounting standards.

### **Surplus Debentures**

No surplus debentures were issued or outstanding for the period under examination.

## **AFFILIATED COMPANIES**

### **Holding Company, Subsidiaries and Affiliates**

The Company is a member of an Insurance Holding Company System as defined by Section 382.010, RSMo (Definitions). An Insurance Holding Company System Registration Statement was filed by Shelter Mutual, on behalf of itself, and its insurance subsidiaries, for each year of the examination period. Shelter Mutual is organized as a mutual entity, accordingly, it does not have any stockholders or controlling entity. The Company is ultimately owned by its policyholders.

As of December 31, 2007, Shelter Mutual directly or indirectly wholly-owned the following entities:

- Shelter General Insurance Company (Shelter General), a State of Missouri property and casualty insurer specializing in automobile insurance coverage.
- Shelter Life Insurance Company (Shelter Life), a State of Missouri life insurer that specializes in providing ordinary life insurance, annuities and accident and health insurance.
- Shelter Reinsurance Company (Shelter Re), a State of Missouri reinsurer that specializes in providing property and casualty reinsurance and earthquake reinsurance coverage on an excess of loss basis.
- Shelter Financial Corporation (SFC), a holding company for Shelter Financial Bank.
- Shelter Financial Bank (SFB), a savings and loan company that sells certificates of deposits and provides auto loans and mortgage loans. It does not have any demand accounts (checking or savings). Its customers are mainly policyholders of Shelter Mutual and Shelter General, but customers may also come from the general public.
- Shelter Financial Services, Inc. (SFS), a holding company for Shelter Benefits Management, Inc.
- Shelter Benefits Management, Inc. (Shelter Benefits), a benefit management company that manages various agent and employee services for Shelter Mutual employees. Services provided include human resource functions, payroll services, and benefits administration for the employees, agents, and retirees of Shelter Mutual.

- Shelter Enterprises, LLC (Shelter Enterprises) – Leases property and equipment to affiliates, including Shelter Mutual, and other non-affiliated entities.
- Daniel Boone Agency, LLC (DBA, LLC). – An insurance broker that places risks from leads generated by agents of Shelter Mutual and its insurance subsidiaries.

**Organizational Chart**

The following table depicts the holding company system of Shelter Mutual and its subsidiaries, as of December 31, 2007:

<u>Company</u>	<u>Parent or Controlling Entity</u>	<u>Ownership</u>
<b>Shelter Mutual Insurance Company</b>	Policyholders	100%
Shelter General Insurance Company	Shelter Mutual Insurance Company	100%
Shelter Enterprises, LLC	Shelter Mutual Insurance Company Shelter General Insurance Company Shelter Life Company Shelter Reinsurance Company	13% 39% 39% 9%
Shelter Life Insurance Company	Shelter Mutual Insurance Company	100%
Shelter Reinsurance Company	Shelter Mutual Insurance Company	100%
Shelter Financial Corporation	Shelter Mutual Insurance Company	100%
Shelter Financial Bank	Shelter Financial Corporation	100%
Shelter Financial Services, Inc.	Shelter Mutual Insurance Company Shelter General Insurance Company Shelter Life Insurance Company	79% 11% 10%
Shelter Benefits Management, Inc.	Shelter Financial Services, Inc.	100%
Daniel Boone Agency, L.L.C.	Shelter Mutual Shelter General Shelter Life	40% 40% 20%
Haulers Insurance Company*	Shelter Mutual	100%

\*Haulers Insurance Company (Haulers Insurance) was acquired on June 30, 2008, subsequent to the examination date.

**Intercompany Transactions**

The Company is a party to the intercompany agreements outlined below.

- 1. Type:** Agreement for Management Services and Facilities (9 separate agreements)
- Parties:** Shelter General, Shelter Life, Shelter Re, SFC, SFS, Daniel Boone Agency, LLC, Daniel Boone Agency, Inc. Daniel Boone Underwriters, Inc., Shelter Enterprises, LLC, (collectively referred to as the "Subsidiaries").
- Effective:** January 1, 1997 for Daniel Boone Agency, LLC  
January 1, 1997 for Shelter Life, Shelter Re, and SFS  
April 10, 1998 for SFC  
October 1, 2003 for DBA, Inc., DBU, Inc., and Shelter Enterprises and December 5, 2005, for Shelter General
- Terms:** All 9 agreements contain the following nearly identical terms. Shelter Mutual agrees to provide the employees to operate all aspects of the Subsidiaries. Services to be provided include recordkeeping, processing, planning, budgeting, receipt and disbursement activities, and all work incidental to the operation of the Subsidiaries' business. Shelter Mutual agrees to provide office space, utilities, computer systems, office equipment, and supplies. In exchange for the services and facilities provided by Shelter Mutual, the Subsidiaries will make monthly payments to Shelter Mutual. Payments will be calculated in accordance with the Joint Expense Allocation Agreement between Shelter Mutual and the Subsidiaries. These agreements were amended effective September 22, 2006, to prohibit payments no later than 89 days after the billing date.

The agreement with Shelter General also contains a processing clause wherein Shelter Mutual agrees to process and service outstanding claims drafts of Shelter General.

- 2. Type:** Agreement for Management Services and Facilities
- Parties:** Shelter Financial Bank
- Effective:** April 12, 1999
- Terms:** Shelter Mutual agrees to provide Shelter Bank with the following services: loan processing, payroll processing, human resources, employee benefit administration, investment management and treasury, training for employees and agents, facilities management, legal, tax, internal controls, and administrative support. Shelter Mutual agrees to provide office space, utilities, computer systems, and telephone systems. Shelter Bank will pay Shelter Mutual the lower of actual costs or the fair market price for the services and facilities provided. Actual costs shall be determined on an allocation basis as defined in Exhibit D and with the Joint Expense Allocation Agreement between Shelter Mutual and certain subsidiaries.

- 3. Type:** Joint Expense Allocation Agreement
- Parties:** Shelter General, Shelter Life, Shelter Re, SFS, Daniel Boone Agency, LLC, Shelter Enterprises, LLC, Shelter Benefits
- Effective:** May 19, 1999 (original Agreement)  
December 1, 2004 (amended and restated)  
September 22, 2006 Amended
- Terms:** Each party agrees to pay its direct expenses in instances when each entity's actual usage can be determined. The parties agree to allocate any joint expenses for instances in which the identification and segregation of each entity's actual share is not practically feasible. The allocation methodologies for each category of joint expenses are as follows:
- (1) Personnel – estimated or actual time
  - (2) Real Estate – square footage and employee count
  - (3) Investment – portfolio value
  - (4) Claims Adjustment (applicable to Shelter Mutual and Shelter General only) – incurred losses
  - (5) Reinsurance (applicable to Shelter Mutual and Shelter General only) – actual premiums and claims of each entity
  - (6) Other Expenses – assets, employee count, or written premium.

This agreement was amended effective September 22, 2006, to strengthen the original settlement period of 30 days by prohibiting payment of later than 89 days after billing date.

- 4. Type:** Management Services Agreement
- Parties:** Shelter Benefits Management, Inc.
- Effective:** May 19, 1999
- Terms:** Shelter Benefits will provide all human resource functions, payroll processing, and benefits administration for the employees and agents of Shelter Mutual. The costs of Shelter Benefits providing services will be allocated in accordance with the Joint Expense Allocation Agreement.
- 5. Type:** Transfer and Assumption Agreement
- Parties:** Shelter General, Shelter Life and Shelter Benefits
- Effective:** May 19, 1999
- Terms:** Shelter Mutual transferred certain of its agent and employee benefit liabilities to Shelter Benefits in 1999. The liabilities transferred included agents termination benefits, post-retirement benefits, accrued vacation benefits, and director's retirement plan benefits. In exchange, Shelter Mutual assigned its rights to a promissory note issued to it by Shelter Life to Shelter Benefits. Shelter Benefits also issued shares of preferred stock to Shelter Mutual, as part of the 1999 transactions. Shelter Benefits agrees to assume future agent liabilities and employee benefit liabilities from Shelter Mutual. Each year, Shelter Mutual

makes a payment to Shelter Benefits for the incurred expenses for the agent and employee benefits under its administration.

6. **Type:** Tax Allocation Agreement
- Parties:** Shelter General, Shelter Life, Shelter Re, SFS, SFC, Shelter Benefits, SFB and Haulers Insurance
- Effective:** Effective May 19, 1999; amended September 23, 2008, to include Haulers Insurance Company. Agreement is applicable to 1999 and subsequent tax years.
- Terms:** Shelter Mutual will file a consolidated federal income tax return on behalf of itself and its subsidiaries. The tax liability for each company will be the amount that would have been determined on a separate filing basis. The subsidiaries will pay their share of tax payments to Shelter Mutual within 10 days following any tax payments made by Shelter Mutual. Shelter Mutual will refund any amount due to the subsidiaries within 10 days after filing the consolidated return.
7. **Type:** Lease Agreement
- Parties:** Shelter Enterprises
- Effective:** March 1, 1994 to February 28, 1999 (original Lease terms)  
March 1, 1999 to February 28, 2002 (per Addendum dated August 3, 1999)  
March 1, 2002 to February 29, 2004 (per Extension dated January 10, 2002)  
March 1, 2004 to February 28, 2006 (per Extension dated January 7, 2004)  
March 1, 2006 to February 28, 2009 (per Extension dated January 24, 2006)
- Terms:** Shelter Enterprises leases storage space in Columbia, Missouri from Shelter Mutual. The lease rates to be paid by Shelter Enterprises were \$705 per month, as of December 31, 2004, and through the period ending February 28, 2006. The lease rates will remain at \$705 per month through February 28, 2009 per the Lease Extension Agreement dated January 24, 2006.
8. **Type:** Commercial Lease Agreement (three separate agreements)
- Parties:** Shelter Financial Bank (SFB)
- Effective:** April 12, 2002 to April 12, 2005  
April 13, 2005 to April 30, 2008  
May 1, 2008 to April 30, 2011
- Terms:** Shelter Financial Bank leases office space in Columbia, Missouri from Shelter Mutual for the years 2002 to 2011. The lease rates paid by SFB were \$4,232 per month for the duration of the lease term from April 12, 2002 to April 12, 2005. A new lease was executed in 2005 with lease rates of \$5,030 per month for the period April 13, 2005 to April 30, 2008. A new lease was executed in 2008 with lease rates to be paid by SFB at \$5,333.70 per month for the duration of the lease term from May 1, 2008 to April 30, 2011.

9. **Type:** Lease of Aircraft  
**Parties:** Shelter Enterprises  
**Effective:** November 7, 2005 for a ten year lease term, expiring on November 6, 2015  
**Terms:** A new lease agreement for a 2005 Beechcraft, King Air 350 aircraft was executed in 2005 to replace an earlier lease for a 1990 airplane from Shelter Enterprises. Shelter Mutual pays Shelter Enterprises a rental lease of \$44,242 per month for the aircraft. In addition, Shelter Mutual is responsible for paying certain taxes identified in the lease.
10. **Type:** Lease Agreement – Agent Signs, Office Furniture and Office Equipment  
**Parties:** Shelter Enterprises  
**Effective:** March 14, 2004  
**Terms:** Shelter Mutual leases agent signs, office furniture, and office equipment from Shelter Enterprises for the purposes of subleasing the property to its agents. The lease rents to be paid by Shelter Mutual were to be equal to the sublease rents paid by the agents.
11. **Type:** Promissory Note  
**Parties:** Shelter Enterprises  
**Effective:** November 7, 2005  
**Terms:** Shelter Mutual loaned \$3,876,600 to Shelter Enterprises in exchange for a promissory note. Shelter Enterprises used the proceeds to purchase a new airplane. Shelter Enterprises will pay 6% interest on the principal balance of the note. Principal and interest totaling \$43,038 will be paid each month by Shelter Enterprises for a period of ten years to repay the note. The outstanding balance was \$3,248,338 as of December 31, 2007.
12. **Type:** Line of Credit Promissory Note  
**Parties:** Shelter Financial Corporation  
**Effective:** September 19, 2001  
**Terms:** Shelter Financial Corporation extends credit to allow Shelter Mutual to borrow up to \$3,000,000, as needed. Shelter Mutual pays interest on loan amounts at a rate of 0.25% over the Targeted Federal Funds Rate on an “interim reset date”, which is mutually agreed upon at the time of the advance. The principal amounts are to be paid upon demand. The outstanding loan balance was \$2,875,000, as of December 31, 2007.
13. **Type:** Line of Credit Promissory Note  
**Parties:** Shelter Financial Services, Inc.  
**Effective:** September 19, 2001



**Terms:** SFS extends credit to allow Shelter Mutual to borrow up to \$8,000,000, as needed. Shelter Mutual pays interest on loan amounts at a rate of 0.25% over the Targeted Federal Funds Rate on an "interim reset date", which is mutually agreed upon at the time of the advance. The principal amounts are to be paid upon demand. The outstanding loan balance was \$2,620,000, as of December 31, 2007.

In addition to the above listed agreements, Shelter Mutual had the following additional intercompany transactions during and subsequent to the examination period:

- The Company received cash dividend payments of \$3,000,000, \$1,000,000 and \$2,000,000 from Shelter General in 2005, 2006, and 2007, respectively. The Company received cash dividend payments of \$3,000,000, \$2,000,000, and \$5,000,000 in 2005, 2006, and 2007 respectively, from Shelter Life. The Company also received cash distribution of \$400,000, \$500,000 and \$1,600,000 in 2005, 2006, and 2007, respectively, from Daniel Boone Agency, LLC. Note that Daniel Boone Agency, LLC changed its name from Daniel Boone Underwriters, LLC, effective January 1, 2006.
- Shelter Mutual and Shelter General purchased structured settlement annuities from Shelter Life during the examination period. The structured settlements were used to provide periodic payouts of claim payments due under the terms of policies issued by Shelter Mutual and Shelter General. The claimants are the beneficiaries of the contracts. The present value of the structured settlements collectively paid by Shelter Mutual and Shelter General to Shelter Life was \$32,299,620, \$30,912,892, and \$29,206,385 during 2005, 2006, and 2007, respectively.
- The Company entered into an excess of loss reinsurance contract with Shelter Reinsurance Company, a subsidiary, which provides excess of loss reinsurance coverage. See further details in the Reinsurance section of this report.
- Shelter Mutual and its active subsidiaries are named insureds on a general liability insurance policy issued by Shelter Mutual. Premiums are charged to the subsidiaries through intercompany allocations under the Joint Expense Allocation Agreement.
- Shelter Re provides earth movement coverage on all real and personal property at locations owned or used by Shelter Mutual. The premium is paid directly to Shelter Re upon receipt of renewal notice.
- Shelter Mutual became a member of Shelter Enterprises, LLC, effective December 31, 2005, by contributing two separate tracts of real estate resulting in a capital contribution of \$921,605. The percentage of ownership of Shelter Enterprises, as of December 31, 2007, was as follows: Shelter General – 39.11%, Shelter Life – 39.11%, Shelter Mutual – 13.08%, and Shelter Reinsurance – 8.70%.

The following table summarizes the payments made during the examination period, between Shelter Mutual and its subsidiaries, pursuant to the intercompany agreements summarized above:

Subsidiary	Agreement	Net Paid / (Received)		
		2007	2006	2005
Shelter Financial Corp	Mgmt. Services and Facilities	(\$ 40,014)	(\$ 45,552)	(\$ 43,000)
Shelter Re	Joint Expense Allocation	(1,357,219)	(1,077,569)	(953,629)
Shelter General	Joint Expense Allocation	(18,984,189)	(17,361,513)	(16,009,350)
Shelter Life	Joint Expense Allocation	(10,986,371)	(8,980,509)	(8,279,052)

DBU, Inc.	Joint Expense Allocation	NA	NA	(19,569)
DBA, Inc.	Joint Expense Allocation	NA	NA	(13,451)
DBU, LLC	Joint Expense Allocation	NA	NA	(171,593)
DBA, LLC	Joint Expense Allocation	(264,418)	(232,664)	NA
SFS	Joint Expense Allocation	0	0	0
Shelter Enterprises	Joint Expense Allocation	(252,027)	(143,878)	(115,401)
Shelter Benefits	Joint Expense Allocation	(1,025,277)	(607,974)	(639,366)
Shelter Benefits	Transfer and Assumption	4,536,970	3,573,235	3,506,190
Shelter Benefits	Management Services	5,807,497	5,270,059	5,715,934
Shelter Reinsurance	Tax Allocation	(9,512,563)	(8,269,865)	1,296,403
Shelter General	Tax Allocation	(4,399,711)	(3,814,796)	(4,523,665)
Shelter Life	Tax Allocation	(7,189,960)	(5,281,512)	(7,162,797)
SFB	Tax Allocation	(318,177)	(356,888)	(353,006)
SFS	Tax Allocation	(59,564)	(60,940)	(37,025)
SFC	Tax Allocation	(57,594)	(58,444)	(32,806)
Shelter Benefits	Tax Allocation	602,936	(133,902)	216,925
SFC	Promissory Note	154,088	129,935	11,926
SFS	Promissory Note	140,398	143,083	20,565
Shelter Enterprise	Promissory note	(514,902)	(221,733)	3,814,297
SFB	Commercial Lease	(60,360)	(60,360)	(57,847)
Shelter Enterprises	Leases	855,261	83,7569	332,898
<b>TOTALS</b>		<b><u>(\$42,925,196)</u></b>	<b><u>(\$36,754,218)</u></b>	<b><u>(\$23,496,419)</u></b>

*NA: The Agreement indicated was either terminated or not in effect at the time period under review.*

### FIDELITY BOND AND OTHER INSURANCE

Shelter Mutual, along with various subsidiaries is a named-insured on a financial institution bond with a liability limit of \$2,500,000 and a deductible of \$100,000. This level of coverage complies with the suggested minimum amount of fidelity insurance according to NAIC guidelines.

Shelter Mutual is also a named-insured on the following insurance policies: General Liability, Excess Umbrella, Automobile, Property and Equipment (including Boiler and Machinery coverage), Fiduciary and Excess Fiduciary, Workers Compensation and Earth Movement Policy coverages.

### PENSION, STOCK OWNERSHIP AND INSURANCE PLANS

As of December 31, 2007, the Company had approximately 1,733 employees and 1,580 agents. The employees work on the operations of Shelter Mutual and several subsidiaries. The agents produce business for Shelter Mutual, Shelter General, and Shelter Life. Benefit costs for employees and agents are allocated from the Company to the subsidiaries, pursuant to agreements that are described in the Intercompany Transactions section of this report.

A variety of standard benefits are provided to the employees and agents. These benefits include, but are not limited to, the following: medical insurance, dental insurance, life insurance, personal accident insurance, disability insurance, sick leave, and tuition reimbursement. Employees are also provided with a defined benefit pension plan and a 401(k) savings and profit sharing plan. Certain highly compensated employees are provided with a Supplemental Employee Retirement Plan (SERP). As of December 31, 2007, the defined benefit pension plan was over funded by \$61,751,699. As of December 31, 2007, SERP was underfunded by \$2,275,195 and its liability was \$3,214,290.

Employees of Shelter Benefits Management, Inc., a subsidiary, provide various human resource functions for Shelter Mutual and its subsidiaries. Benefit costs for the Shelter Benefits employees, agents, directors, and retirees, are allocated to Shelter Mutual and its subsidiaries, pursuant to agreements that are described in the Intercompany Transactions section of this report. These benefits include postretirement health benefits, agents' termination benefits, directors' retirement benefits, nonqualified separation benefits, and vacation benefits. Shelter Benefits manages these benefits for Shelter Mutual. Shelter Mutual makes payments to Shelter Benefits each year for these benefits.

## STATUTORY DEPOSITS

### Deposits with the State of Missouri

The funds on deposit with the Missouri Department of Insurance, Financial Institutions and Professional Registration as of December 31, 2007, as reflected below, were sufficient to meet the capital deposit requirement for the State of Missouri in accordance with Section 379.098 RSMo (Securities Deposit). The funds on deposit as of December 31, 2007, were as follows:

<u>Type of Security</u>	<u>Par Value</u>	<u>Fair Value</u>	<u>Statement Value</u>
U.S. T-Bonds	\$2,005,000	\$2,108,260	\$2,080,513

### Deposits with Other States

The Company also has funds on deposit with other states. Those funds on deposit, as of December 31, 2007, were as follows:

<u>State</u>	<u>Type of Security</u>	<u>Par Value</u>	<u>Fair Value</u>	<u>Statement Value</u>
Arkansas	U.S. Treasury Bonds	\$300,000	\$307,923	\$294,217
Louisiana	U.S. Treasury Bonds	100,000	102,641	98,072
Nevada	Fed Home Loan Note	<u>250,000</u>	<u>291,199</u>	<u>279,492</u>

<b>TOTALS</b>	<b><u>\$650,000</u></b>	<b><u>\$701,763</u></b>	<b><u>\$671,781</u></b>
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**Other Deposits**

The Company has pledged assets to UMB Bank, N.A. as collateral for letters of credit in support of some of its assumed business, some of which is retroceded to its subsidiary, Shelter Re. The pledged funds on deposit, as of December 31, 2007, were as follows:

<u>Type of Security</u>	<u>Par Value</u>	<u>Fair Value</u>	<u>Statement Value</u>
General Obligation Bonds	\$6,175,000	\$6,474,472	\$6,271,986

**INSURANCE PRODUCTS AND RELATED PRACTICES****Territory and Plan of Operation**

Shelter Mutual Insurance Company (Shelter Mutual) is licensed as a property and casualty insurer by the Missouri Department of Insurance, Financial Institutions and Professional Registration (DIFP) under Chapter 379 RSMo (Insurance Other than Life). The Company is licensed and writes business in Missouri and 13 other Midwestern states, as follows:

Arkansas	Indiana	Kentucky	Nebraska
Colorado	Iowa	Louisiana	Oklahoma
Illinois	Kansas	Mississippi	Tennessee
Nevada			

The Company is licensed, but does not currently write business, in the following states: Maryland, Ohio, Texas, and Vermont. The Company is also licensed to provide reinsurance *only* in the following states: Alabama, Delaware, Georgia, Idaho, Massachusetts, Minnesota, Montana, New Hampshire, New Jersey, New York, North Carolina, Pennsylvania, South Carolina, South Dakota, Virginia, and Wisconsin.

The states with the largest percentage of 2007 direct written premiums were Missouri (31%), Arkansas (19%), and Oklahoma (11%). The major lines of business for Shelter Mutual, based upon 2007 direct written premiums, are as follows:

<u>Line of Business</u>	<u>Percentage of Total Direct Written Premiums</u>
Private Passenger Auto Liability	32.0%
Homeowners	28.8%
Auto Physical Damage	22.5%
All Other	<u>16.7%</u>
Total	<u>100.0%</u>

Shelter Mutual and its subsidiaries, Shelter General and Shelter Life, are marketed as a single business operation under the “Shelter Insurance” brand name. The property and casualty products are underwritten by Shelter Mutual and Shelter General. Shelter Mutual writes all of the homeowners policies, commercial property, and commercial liability risks for the Shelter Insurance Companies. Automobile policies for insureds with higher credit scores are assigned to Shelter Mutual; insureds with lower credit scores are assigned to Shelter General. One exception is that Shelter Mutual does not write any auto business in Illinois and Tennessee since those states do not allow credit scoring for determining premium rates. Thus, Shelter General writes all auto business in Illinois and Tennessee.

The Company’s business is produced by approximately 1,311 captive agents, who also produce business for Shelter General and Shelter Life subsidiaries. The Company has a marketing staff that uses various methods of advertising and direct mailings to promote the products of Shelter Mutual and its subsidiaries.

**Policy Forms & Underwriting**

**Advertising & Sales Materials**

**Treatment of Policyholders**

The DIFP has a market conduct staff that performs a review of these issues and generates a separate market conduct report. The most recent DIFP market conduct examination report was dated April 25, 2002, and covered the period from October 1, 2000 to September 30, 2001. No significant problems were noted from the review of this report. The Company also had market conduct examinations from Illinois and Oklahoma during the examination period. Reports for these examinations were reviewed and no significant problems were noted.

## REINSURANCE

### General

The Company's premium activity on a direct written, assumed and ceded basis, for the period under examination, is detailed below:

	<u>2007</u>	<u>2006</u>	<u>2005</u>
Direct Business	\$914,054,589	\$903,284,080	\$898,347,587
Reinsurance Assumed:			
Affiliates	719,052	789,277	0
Non-affiliates	35,435,354	27,176,765	17,178,953
Reinsurance Ceded:			
Affiliates	(35,054,043)	(26,382,719)	(15,186,324)
Non-affiliates	<u>(28,892,402)</u>	<u>(39,046,171)</u>	<u>(22,603,710)</u>
<b>Net Written Premiums</b>	<b><u>\$886,262,550</u></b>	<b><u>\$865,821,232</u></b>	<b><u>\$877,736,506</u></b>

### Assumed

Shelter Mutual assumes a small amount of business under a fronting arrangement with its subsidiary, Shelter Re. The arrangement exists because Shelter Mutual can obtain more favorable contract terms by utilizing its A.M. Best rating of "A" (Excellent), in comparison to Shelter Re's lower rating of "A-" (Excellent). The Company assumes business from several U.S. and foreign companies and the business is retroceded 100% to Shelter Re. This retrocession activity with Shelter Re accounted for \$35,054,000 or 97% of total assumed premiums in 2007. The only other business assumed by Shelter Mutual is from involuntary pools and associations.

### Ceded

The Company is contingently liable for all reinsurance losses ceded to others. This contingent liability would become an actual liability in the event that an assuming reinsurer fails to perform its obligations under the reinsurance agreement.

In general, Shelter Mutual retains nearly all of the risks from the auto and homeowners policies that it writes on a direct basis. The Company's reinsurance program is designed to protect the Company against very large risks and catastrophes.

Shelter Mutual has several joint ceded reinsurance agreements in which the Company's subsidiary, Shelter General, is also a named-reinsured. Shelter General does not directly pay reinsurance premiums to the reinsurers and does not directly receive loss recoveries. Rather, Shelter Mutual pays the total premium to the reinsurers on behalf of itself and Shelter General. Likewise, any loss recoveries are paid directly to Shelter Mutual. Shelter General is allocated reinsurance premiums and loss recoveries, pursuant to terms of the Joint Expense Allocation Agreement that is described in the Intercompany Agreements section of this report.

Shelter Mutual and Shelter General maintain a Property Per Risk and Automatic Facultative Treaty with General Reinsurance Corporation (Gen Re). Under this treaty, the net amount retained on any one risk is \$750,000. The per risk coverage is in two layers with the first layer attaching at \$750,000. The per risk limit is \$1.25 million subject to a per occurrence limit of \$3.75 million on any one event. The second layer attaches at \$2 million with a per risk limit of \$1.5 million subject to an occurrence limit of \$3 million. The Automatic Facultative Treaty with Gen Re extends property per risk coverage by an additional \$12 million for losses in excess of \$3.5 million per risk.

Shelter Mutual and Shelter General have a five-layer catastrophe program with several participating reinsurers. The catastrophe program covers all property risks including auto physical damage. The first four layers are contained in a catastrophe excess of loss agreement effective January 1 of each year. The participation of each reinsurer is defined under an Interest and Liabilities Agreement with each reinsurer. The two catastrophe agreements are renewed on an annual basis and provide coverage for losses up to \$210 million with a retention of \$50 million. The major reinsurers are XL Re Ltd., Tokio Millennium Re Ltd., and Renaissance Reinsurance Ltd. The remaining reinsured loss limit placed with Mutual Reinsurance Bureau's Regional Reciprocal Catastrophe Pool.

Shelter Mutual and Shelter General are reinsured by a multi-line casualty reinsurance treaty with Swiss Reinsurance Company (Swiss Re) (formerly, Employers Reinsurance Corporation). The agreement is in two layers with an aggregate limit of \$4 million. The treaty attaches at \$600,000 and \$2 million for losses in excess of \$2.6 million. Personal umbrella coverage with Swiss Re provides up to \$2 million in coverage in excess of underlying policy limits. In 2008, the multi-line casualty reinsurance coverage was combined with personal umbrella coverage. This coverage attaches at \$1 million and \$5 million for losses up to \$9 million per occurrence.

Shelter Mutual has an agreement, effective January 1, 1987, with its subsidiary, Shelter Reinsurance Company, in which Shelter Mutual acts as a fronting company for Shelter Re. Shelter Mutual retrocedes 100% of the risks from its entire book of assumed business to Shelter Re, except for business from involuntary pools and associations. The fronting arrangement is described in the Assumed section of this report.

## ACCOUNTS AND RECORDS

### Independent Auditor

The Company's financial statements were audited by the CPA firm, Ernst & Young, LLP, of Kansas City, Missouri, for all the years under examination.

### Appointed Actuary

Loss and Loss Adjustment Expense reserves were reviewed and certified by Robert H. Wainscott, FCAS, MAAA, who is employed by Ernst & Young, LLP, of Chicago, Illinois for each of the years under examination.

## FINANCIAL STATEMENTS

The following financial statements, with supporting exhibits, present the financial condition of Shelter Mutual for the period ending December 31, 2007. Any examination adjustments to the amounts reported in the financial statements and/or comments regarding such are made in the "Notes to the Financial Statements." The failure of any column of numbers to add to its respective total is due to rounding or truncation.

There may have been additional differences found in the course of this examination, which are not shown in the "Notes to the Financial Statements." These differences were determined to be immaterial concerning their effect on the financial statements, and therefore were only communicated to the Corporation and noted in the workpapers for each individual Annual Statement item.



**Assets**

	<u>Assets</u>	<u>Non-Admitted Assets</u>	<u>Net Admitted Assets</u>
Bonds	\$1,075,880,691	\$0	\$1,075,880,691
Common Stocks	712,876,847		712,876,847
Mortgage Loans on Real Estate	3,248,339		3,248,339
Real Estate	38,474,271		38,474,271
Cash and Short-Term Investments	72,037,741		72,037,741
Other Invested Assets	225,475,790	44,198,985	181,276,805
Receivable for Securities	5,966,099		5,966,099
Investment Income Due and Accrued	16,523,122		16,523,122
Uncollected Premiums and Agents' Balances in the Course of Collection	3,326,603	81,618	3,244,985
Deferred Premiums, Agents' Balances Booked But Deferred and Not Yet Due	49,037,798		49,037,798
Amounts Recoverable from Reinsurers	3,591,137		3,591,137
Funds Held by or Deposited with Reinsured Companies	266,000		266,000
Other Amounts Receivable Under Reinsurance	1,886,837		1,886,837
Net Deferred Tax Asset	16,206,255		16,206,255
Guaranty funds Receivable or on Deposit	2,963,226		2,963,226
EDP Equipment and Software	4,414,184	482,778	3,931,406
Furniture and Equipment	2,882,007	2,882,007	0
Receivables from Parent, Sub., and Affiliates	14,758,320		14,758,320
Aggregate Write-ins for Assets:			
Company Owned Vehicles	6,617,222		6,617,222
Equities and Deposits in Pools	270,438		270,438
General Accounts Receivable	99,085	83,360	15,725
Other Non-Admitted Assets	63,077,201	63,077,201	0
<b>TOTAL ASSETS</b>	<b><u>\$2,319,879,213</u></b>	<b><u>\$110,805,949</u></b>	<b><u>\$2,209,073,264</u></b>

## Liabilities, Surplus and Other Funds

Losses	\$ 259,862,307
Reinsurance Payable on Paid Loss and LAE	1,450,586
Loss Adjustment Expenses	68,190,379
Commissions Payable	36,156,407
Other Expenses	19,652,707
Taxes, Licenses and Fees	7,182,824
Current Federal Income Taxes	3,189,817
Unearned Premiums	320,934,548
Advance Premium	24,607,570
Ceded Reinsurance Premiums Payable	774,113
Funds held by Company under Reinsurance Treaties	83,108
Amount Withheld or Retained by Company	6,680,669
Remittances and Items Not Allocated	2,027,462
Provision for Reinsurance	177,596
Drafts Outstanding	28,061,136
Payable to Parent, Subsidiaries and Affiliates	6,668,424
Aggregate Write-In Liabilities:	
Catastrophe Reserve – Earthquake	58,583,727
Catastrophe Reserve – General	12,419,139
Deferred Gain on Intercompany Sales	263,748
Miscellaneous Accounts Payable	188,747
Premium Deficiency Reserve – Involuntary Assumptions	1,504
Accounts Payable-Escheatable Checks	7,904
<b>TOTAL LIABILITIES</b>	<b>\$857,164,422</b>
Aggregate Write-ins for Other than Special Surplus Funds:	
Missouri Minimum Capital Requirements	1,250,000
Unassigned Funds (Surplus)	<u>1,350,658,840</u>
Capital and Surplus	<b><u>\$1,351,908,840</u></b>
<b>TOTAL LIABILITIES AND SURPLUS</b>	<b><u>\$2,209,073,262</u></b>

## Summary of Operations

### Underwriting Income

<b>Premiums Earned</b>	<b>\$877,003,973</b>
Losses Incurred	463,792,438
Loss Expenses Incurred	74,064,283
Other Underwriting Expenses Incurred	263,246,795
Aggregate Write-ins for Underwriting Deductions:	
Change in Catastrophe Reserve-Earthquake	6,475,203
Change in Premium Deficiency Reserves – Involuntary Assumptions	(4,502)
Change in Catastrophe Reserve – General	<u>12,419,139</u>
<b>Total Underwriting Deductions</b>	<b><u>\$819,993,356</u></b>
<b>Net Underwriting Gain/(Loss)</b>	<b>\$57,010,617</b>

### Investment Income

Net Investment Income Earned	80,546,496
Net Realized Capital Gains or (Losses)	<u>28,948,653</u>
<b>Net Investment Gain or (Loss)</b>	<b>\$109,495,149</b>

### Other Income

Finance and Service Charges not Included in Premiums	8,733,196
Miscellaneous Other Income	<u>519,767</u>
<b>Total Other Income</b>	<b><u>\$9,252,963</u></b>
Net Income Before Dividends to Policyholders and Federal Income Taxes	\$175,758,729
Federal and Foreign Income Taxes Incurred	<u>(36,834,589)</u>
<b>Net Income or (Loss)</b>	<b><u>\$138,924,140</u></b>

### Capital and Surplus Account

Capital and Surplus, December 31, 2006	\$1,144,321,363
Net Income or (Loss)	138,924,140
Change in Net Unrealized Capital Gains or (Losses)	101,044,832
Change in Non-Admitted Assets	(49,384,007)
Change in Provision for Reinsurance	257,805
Change in Net Deferred Income Tax	18,286,474
Change in Net Unrealized Foreign Exchange Capital Gain (Loss)	(1,541,768)
<b>Net Change in Capital and Surplus</b>	<b><u>\$207,587,476</u></b>
 <b>CAPITAL AND SURPLUS, DECEMBER 31, 2007</b>	 <b><u>\$1,351,908,839</u></b>

### NOTES TO THE FINANCIAL STATEMENTS

None

### EXAMINATION CHANGES

None

### GENERAL COMMENTS AND/OR RECOMMENDATIONS

None

### **SUBSEQUENT EVENTS**

On June 30, 2008, Shelter Mutual purchased 100% of the issued and outstanding common stock of Tennessee domiciled Haulers Insurance Company (Haulers Insurance) for \$50,705,595 in cash pursuant to a purchase agreement. Haulers Insurance is a property and casualty insurer and is licensed in 18 states. Goodwill on the purchase was \$19,639,736, which will be amortized over year in accordance with the applicable statutory accounting standards.

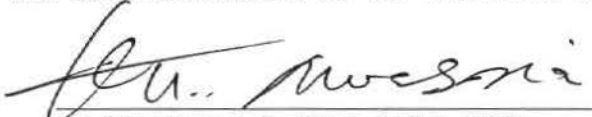
**ACKNOWLEDGMENT**

The assistance and cooperation extended by the officers and the employees of Shelter Mutual Insurance Company during the course of this examination is hereby acknowledged and appreciated. In addition to the undersigned, Larry Kleffner, CFE, Shawn Hernandez, CFE, Karen Baldree, CPA, CFE, Steven Koonse, CFE and Valerie Hastings, examiners for the Missouri Department of Insurance, Financial Institutions and Professional Registration also participated in this examination. Angela Campbell CFE, Computer Audit Specialist for the Missouri Department of Insurance, Financial Institutions and Professional Registration performed a review of the information system environment. Jon Michelson, FCAS, MAAA of Expert Actuarial Services, LLC also participated as a consulting actuary.

**VERIFICATION**

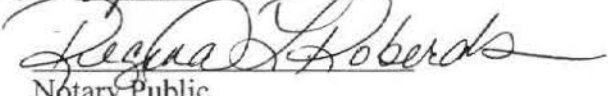
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                                          )  
County of                     )

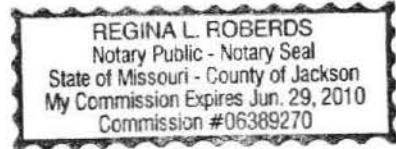
I, Levi N. Nwasoria, CPA, MSA, CFE on my oath swear that to the best of my knowledge and belief the above examination report is true and accurate and is comprised of only facts appearing upon the books, records or other documents of the Company, its agents or other persons examined or as ascertained from the testimony of its officers or agents or other persons examined concerning its affairs and such conclusions and recommendations as the examiners find reasonably warranted from the facts.



Levi N. Nwasoria, CPA, MSA, CFE  
Examiner-In-Charge  
Missouri Department of Insurance, Financial  
Institutions and Professional Registration

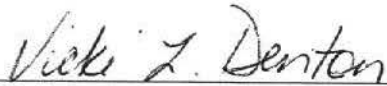
Sworn to and subscribed before me this 7<sup>th</sup> day of April, 2009.

My commission expires: 06/26/10   
Notary Public



**SUPERVISION**

The examination process has been monitored and supervised by the undersigned. The examination report and supporting workpapers have been reviewed and approved. Compliance with NAIC procedures and guidelines as contained in the Financial Condition Examiners Handbook has been confirmed.

  
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Vicki L. Denton, CFE  
Audit Manager  
Missouri Department of Insurance, Financial  
Institutions and Professional Registration