

# CERTIFICATION

June 10, 2014

I, Bruce R. Ramage, Director of Insurance of the State of Nebraska, do hereby certify that the attached is a full and correct copy of the

Financial Examination Report of  
**PHYSICIANS LIFE INSURANCE COMPANY**

as of

December 31, 2012

The report is now on file and forming a part of the records of this Department.

I hereto subscribe my name under the seal of my office at Lincoln, Nebraska.



STATE OF NEBRASKA  
DEPARTMENT OF INSURANCE

JUN 10 2014

FILED

*Bruce R. Ramage*

DIRECTOR OF INSURANCE

CERTIFICATE OF ADOPTION

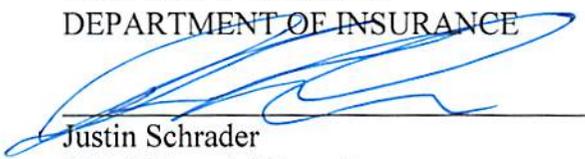
Take notice that the proposed report of the financial examination of

**PHYSICIANS LIFE INSURANCE COMPANY**

dated as of December 31, 2012, verified under oath by the examiner-in-charge on May 22, 2014, and received by the company on May 22, 2014, has been adopted without modification as the final report pursuant to Neb. Rev. Stat. § 44-5906(3)(a).

Dated this 9 day of June, 2014.

STATE OF NEBRASKA  
DEPARTMENT OF INSURANCE

  
Justin Schrader  
Chief Financial Examiner

**STATE OF NEBRASKA**

**Department of Insurance**

**EXAMINATION REPORT**

**OF**

**PHYSICIANS LIFE INSURANCE COMPANY**

**as of**

**December 31, 2012**



## TABLE OF CONTENTS

| <u>Item</u>  | <u>Page</u> |
|--|-------------|
| Salutation .....                                   | 1           |
| Introduction.....                                  | 1           |
| Scope of Examination.....                          | 2           |
| <b>Description of Company:</b>                     |             |
| History.....                                       | 4           |
| <b>Management and Control:</b>                     |             |
| Holding Company .....                              | 4           |
| Shareholder .....                                  | 5           |
| Board of Directors.....                            | 5           |
| Officers .....                                     | 7           |
| Committees .....                                   | 7           |
| <b>Transactions with Affiliates:</b>               |             |
| Service Agreement.....                             | 9           |
| Net Worth Agreement.....                           | 9           |
| Reinsurance Agreement.....                         | 10          |
| Territory and Plan of Operation.....               | 10          |
| <b>Reinsurance:</b>                                |             |
| Assumed.....                                       | 12          |
| Ceded .....  | 12          |
| General.....                                       | 13          |
| <b>Body of Report:</b>                             |             |
| Growth .....                                       | 13          |
| Financial Statements .....                         | 13          |
| Examination Changes in Financial Statements.....   | 17          |
| Compliance with Previous Recommendations .....     | 17          |
| <b>Commentary on Current Examination Findings:</b> |             |
| Custodial Agreement .....                          | 17          |
| Schedule Y .....                                   | 18          |
| Summary of Comments and Recommendations.....       | 18          |
| Acknowledgment.....                                | 19          |

Omaha, Nebraska  
May 1, 2014

Honorable Joseph Torti, III  
Chairman, Financial Condition (E) Committee, NAIC  
Deputy Director and Superintendent of Insurance  
Rhode Island Division of Insurance  
1511 Pontiac Avenue, Bldg. #69-2  
Cranston, Rhode Island 02920

Honorable Ted Nickel  
Chair, Midwestern Zone, NAIC  
Commissioner of Insurance  
State of Wisconsin Office of the Commissioner of Insurance  
125 South Webster Street  
GEF III – 2<sup>nd</sup> Floor  
Madison, Wisconsin 58703-3474

Honorable Bruce R. Ramage  
Director of Insurance  
Nebraska Department of Insurance  
941 "O" Street, Suite 400  
Lincoln, Nebraska 68508

Dear Sirs:

Pursuant to your instruction and authorizations, and in accordance with statutory requirements, an examination has been conducted of the financial condition and business affairs of:

**PHYSICIANS LIFE INSURANCE COMPANY**  
**2600 Dodge Street**  
**Omaha, NE 68131-2671**

(hereinafter also referred to as the "Company") and the report of such examination is respectfully presented herein.

### **INTRODUCTION**

The Company was last examined as of December 31, 2008 by the State of Nebraska. The current financial condition examination covers the intervening period to, and including, the close

of business on December 31, 2012, and includes such subsequent events and transactions as were considered pertinent to this report. The State of Nebraska participated in this examination and assisted in the preparation of this report.

The same examination staff conducted a concurrent financial condition examination of the Company's parent, Physicians Mutual Insurance Company (PMIC). PMIC is under common management with the Company.

### **SCOPE OF EXAMINATION**

This examination was conducted pursuant to and in accordance with both the NAIC Financial Condition Examiners Handbook (Handbook) and Section §44-5904(1) of the Nebraska Insurance Statutes. The Handbook requires that examiners plan and perform the examination to evaluate the financial condition and identify prospective risks of the Company by obtaining information about the Company including, but not limited to: corporate governance, identifying and assessing inherent risks within the Company, and evaluating system controls and procedures used to mitigate those risks. The examination also includes assessing the principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation and management's compliance with Statutory Accounting Principles and Annual Statement Instructions, when applicable to domestic state regulations.

A general review was made of the Company's operations and the manner in which its business has been conducted in order to determine compliance with statutory and charter provisions. The Company's history was traced and has been set out in this report under the caption "Description of Company." All items pertaining to management and control were reviewed, including provisions for disclosure of conflicts of interest to the Board of Directors and the departmental organization of the Company. The Articles of Incorporation and By-Laws

were reviewed, including appropriate filings of any changes or amendments thereto. The minutes of the meetings of the shareholders, Board of Directors and committees, held during the examination period, were read and noted. Attendance at meetings, proxy information, election of Directors and Officers, approval of investment transactions and authorizations of salaries were also noted.

The fidelity bond and other insurance coverages protecting the Company's property and interests were reviewed, as were plans for employee welfare and pension. Certificates of Authority to conduct the business of insurance in the various states were inspected and a survey was made of the Company's general plan of operation.

Data reflecting the Company's growth during the period under review, as developed from the Company's filed annual statements, is reflected in the financial section of this report under the caption "Body of Report."

The Company's reinsurance facilities were ascertained and noted, and have been commented upon in this report under the caption "Reinsurance." Accounting records and procedures were tested to the extent deemed necessary through the risk-focused examination process. The Company's method of claims handling and procedures pertaining to the adjustment and payment of incurred losses were also noted.

All accounts and activities of the Company were considered in accordance with the risk-focused examination process. This included a review of workpapers prepared by Deloitte & Touche LLP, the Company's external auditors, during their audit of the Company's accounts for the years ended December 31, 2011 and 2012. Portions of the auditor's workpapers have been incorporated into the workpapers of the examiners and have been utilized in determining the

scope and areas of emphasis in conducting the examination. This utilization was performed pursuant to Title 210 (Rules of the Nebraska Department of Insurance), Chapter 56, Section 013.

Any failure of items to add to the totals shown in schedules and exhibits appearing throughout this report is due to rounding.

## **DESCRIPTION OF COMPANY**

### **HISTORY**

The Company was incorporated under the laws of the State of Nebraska as a capital stock life insurance company on January 15, 1970, and was licensed to commence business on January 28 of that same year. It was and has remained a wholly owned subsidiary of Physicians Mutual Insurance Company since the date of incorporation. The Amended and Restated Articles of Incorporation provide that the Company shall have perpetual existence. Under provisions of its current charter, and in conformity with Nebraska Statutes, the Company is authorized to write the kinds of insurance prescribed in Section 44-201, Subsections (1) and (4), of the Nebraska Insurance Statutes (life and sickness and accident).

### **MANAGEMENT AND CONTROL**

#### **Holding Company**

The Company is a member of an insurance holding company system as defined by Nebraska Statute. An organizational listing flowing from the "Ultimate Controlling Person," as reported in the 2012 Annual Statement and amended during the examination, is represented by the following (subsidiaries are denoted through the use of indentations, and unless otherwise indicated, all subsidiaries are 100% owned):

Physicians Mutual Insurance Company  
Physicians Life Insurance Company  
MD45 Transport, LLC  
Physicians Mutual Insurance Company Foundation  
Physicians Mutual Employee Benefit Trust  
Physicians Mutual Services Corporation  
Seniors Information Network, LLC  
National Association of Medicare Members, Inc.

**Shareholder**

Article IV of the Company's Amended and Restated Articles of Incorporation states that, "the aggregate number of shares which the Company shall have authority to issue is One Million Five Hundred Thousand (1,500,000) shares of common stock, and the par value of each said share is One Dollar and 67/100 (\$1.67)." As of the examination date, Company records indicate that 1,500,000 shares are issued and outstanding for capital of \$2,505,000, and are all owned by Physicians Mutual Insurance Company (PMIC). As of the examination date the Company's paid-in surplus is \$102,487,905, which is unchanged since the previous examination. There have been stock dividends totaling \$200,000 and cash dividends totaling \$5,800,000 paid since inception of the Company. There were no dividends paid during this examination period.

The Amended and Restated By-Laws state that, "the annual Meeting of the shareholders shall be held on the third Saturday in the month of February in each year...at the principal office of the Company, for the purposes of receiving the reports of the Officers, electing Directors and for the transaction of such other business as may properly come before the meeting."

**Board of Directors**

Article III of the Amended and Restated By-Laws states that, "the Board of Directors shall consist of not less than five (5), nor more than twelve (12) members, divided into three (3) groups as nearly equal in number as is possible."

The following persons were serving as Directors at December 31, 2012:

| <b><u>Name and Residence</u></b>                       | <b><u>Principal Occupation</u></b>   | <b><u>Term Expires</u></b> |
|--|--|----------------------------|
| <b>William R. Hamsa, Jr., M.D.<br/>Omaha, Nebraska</b> | <b>Retired Physician and Chairman<br/>of the Board of the Company</b>  | <b>2013</b>                |
| <b>Martin M. Mancuso, M.D.<br/>Omaha, Nebraska</b>     | <b>Practicing Physician and Associate<br/>Medical Director of the Company<br/>and Chairman of the Claims<br/>Committee</b> | <b>2013</b>                |
| <b>James T. Canedy, M.D.<br/>Omaha, Nebraska</b>       | <b>Practicing Physician and Secretary<br/>of the Company</b>   | <b>2014</b>                |
| <b>John D. Woodbury, M.D.<br/>Omaha, Nebraska</b>      | <b>Retired Physician, Associate Medical<br/>Director of the Company and<br/>Chairman of the Underwriting<br/>Committee</b> | <b>2014</b>                |
| <b>Robert A. Reed, Jr.<br/>Omaha, Nebraska</b>         | <b>Executive Vice President, Chief<br/>Operating Officer and Assistant<br/>Secretary of the Company</b>                    | <b>2014</b>                |
| <b>Dale E. Brett, M.D.<br/>Omaha, Nebraska</b>         | <b>Retired Physician and Treasurer<br/>of the Company</b>  | <b>2015</b>                |
| <b>Robert A. Reed<br/>Omaha, Nebraska</b>              | <b>President and Chief Executive<br/>Officer of the Company</b>  | <b>2015</b>                |

The Amended and Restated By-Laws state that, “the Directors may be paid their expenses, if any, of attendance at each meeting of the Board of Directors, and may be paid a fixed sum for attendance at each meeting of the Board of Directors or a stated salary as a Director. No such payment shall preclude any Director from serving the Company in any other capacity and receiving compensation therefor.”

**Officers**

Article VI of the Amended and Restated Articles of Incorporation states that, “the Officers of the Company shall consist of a President, a Secretary and a Treasurer who shall be elected by the Directors and who shall hold office until their successors are elected and qualified. The Directors may select one or more Vice Presidents and may designate one or more other offices, and assign their duties and responsibilities.”

The Officers are nominated by the Compensation Committee on an annual basis, with the exception of Robert Reed, Sr. and Robert Reed, Jr., who are under contract with the Company.

The following is a listing of Officers elected and serving the Company at December 31, 2012:

| <b><u>Name</u></b>    | <b><u>Office</u></b>   |
|-----------------------|--|
| Robert A. Reed        | President and Chief Executive Officer                                      |
| Dale E. Brett, M.D.   | Treasurer  |
| James T. Canedy, M.D. | Secretary  |
| Robert A. Reed, Jr.   | Executive Vice President – Chief Operating Officer and Assistant Secretary |
| Steven A. Scanlan     | Senior Vice President – Chief Investment Officer and Assistant Treasurer   |
| Michael J. Wade       | Senior Vice President – Finance Group and Chief Financial Officer          |
| Benjamin T. Baldwin   | Senior Vice President – Agency Group                                       |
| Melissa J. Crawford   | Senior Vice President – Market, Products and Technology                    |
| Howard G. Daubert     | Senior Vice President – Corporate Services                                 |
| Robert L. Gunia       | Senior Vice President – Public Affairs Group                               |
| Michael J. Taylor     | Senior Vice President – Strategic Development                              |

**Committees**

According to Article III of the Company’s Amended By-Laws, the Board of Directors may designate from its members an executive committee, which shall consist of at least three (3) Directors, together with the Chairman of the Board, the President, and the Secretary, which shall

have and may exercise all the authority of the Board of Directors when the entire Board of Directors are not in session.

The following persons were serving on the Executive Committee at December 31, 2012:

|                                  |                        |
|----------------------------------|------------------------|
| William R. Hamsa, M.D., Chairman | Dale E. Brett, M.D.    |
| James T. Canedy, M.D.            | Robert A. Reed         |
| Robert A. Reed, Jr.              | John D. Woodbury, M.D. |

The Company's Amended and Restated By-Laws also state that, "the Board of Directors may also designate one (1) or more other committees consisting of at least (2) Directors, each of which committees, to the extent provided in the resolution designating such committee, shall have such designated authority of the Board of Directors when the entire Board is not in session." The Board of Directors has elected to establish several standing committees consisting of the following persons at December 31, 2012:

**Compensation**

William R. Hamsa, M.D., Chairman  
Dale E. Brett, M.D.  
Terrence D. O'Hare, General Counsel  
Robert A. Reed  
Robert A. Reed, Jr.  
John D. Woodbury, M.D.

**Claims**

Martin M. Mancuso, M.D., Chairman  
Dale E. Brett, M.D.  
James T. Canedy, M.D.  
William R. Hamsa, M.D.  
Edward J. Kaspar  
Robert A. Reed  
Robert A. Reed, Jr.  
John D. Woodbury, M.D.

**Audit**

William R. Hamsa, M.D., Chairman  
Dale E. Brett, M.D.  
Robert A. Reed  
Robert A. Reed, Jr.  
Michael J. Wade  
John D. Woodbury, M.D.

**Underwriting**

John D. Woodbury, M.D., Chairman  
Dale E. Brett, M.D.  
James T. Canedy, M.D.  
John C. Clark  
William R. Hamsa, M.D.  
Martin M. Mancuso, M.D.  
Robert A. Reed  
Robert A. Reed, Jr.

**Investment**

Dale E. Brett, M.D., Chairman  
James T. Canedy, M.D.  
William R. Hamsa, M.D.  
Robert A. Reed  
Robert A. Reed, Jr.  
Steven A. Scanlan  
Michael J. Wade  
John D. Woodbury, M.D.

**Benefits**

Howard G. Daubert  
Melissa J. Crawford  
Mark Peters  
Jane R. Phillips  
Michael J. Taylor  
Debra L. Walton

**TRANSACTIONS WITH AFFILIATES****Service Agreement**

Physicians Mutual Insurance Company (PMIC) provides equipment, space and personnel necessary for the operations of its subsidiaries. By agreement dated June 24, 1997 and amended January 1, 2004, PMIC agrees to perform all reasonable services necessary in connection with the solicitation, issuance, and servicing of policies and claims in connection with policies previously issued and hereafter issued by the Company. Compensation for these services is the actual salary represented by the time spent in the performance of such services, and costs and expenses associated with respect to equipment, office space and other overhead expenses represented by the time and use devoted to such services. PMIC is also to receive payment for any direct expenses paid on behalf of the Company. Upon 60 day's prior written notice to the other party, either party may terminate the Agreement. The total expenses allocated under this agreement to the Company during 2012 and 2011 were \$33,808,657 and \$33,242,499, respectively.

**Net Worth Agreement**

The Company entered into a Net Worth Agreement with PMIC effective January 1, 1993, whereby PMIC agrees to take any actions necessary to maintain the Company's financial position with a surplus level in excess of Risk Based Capital requirements.

This agreement can be canceled by either party with a written 90 day notice provided such termination does not eliminate the obligation of PMIC to infuse cash into the Company with respect to the obligation to support, supplement, or permit the timely payment of contractual claims received by the Company from policyholders of insurance contracts or annuity contracts during the term of the agreement.

#### **Reinsurance Agreement**

Effective January 1, 2004, the Company entered into a reinsurance agreement with PMIC, that replaced the previous reinsurance agreement effective January 1, 2003. Per the January 1, 2004 agreement, the Company cedes 100% of the liabilities associated with Medicare Supplement insurance. The Company is paid a "front fee allowance" of 3% of premiums. PMIC paid approximately \$2,600,000 and \$2,800,000 in fees related to this agreement in 2012 and 2011, respectively. The Company terminated sales of its Medicare Supplement in 2009.

Medicare Supplement business is currently sold through PMIC.

#### **TERRITORY AND PLAN OF OPERATION**

As evidenced by current or continuous Certificates of Authority, the Company is licensed to transact business in all states, with the exception of New York, and the District of Columbia.

The Company currently writes life, pre-need, accident and health insurance, and fixed annuities. During the period covered by this examination, business was produced by direct mail, television, radio, newspaper, email and internet advertisement through the Company's direct marketing channels and by personal solicitation through the Agency and Pre-need Divisions. The Brokerage Division was terminated in July, 2006. The Company continues to receive renewal premiums on policies sold by brokers. The direct marketing channels produced approximately 70% of the Company's net written premium during 2012. The Agency Division

produced approximately 26% of net written premium. The Pre-need Division produced approximately 4% with the brokerage renewal premium accounting for less than 1%.

The direct marketing channels include the Direct Marketing Group, the Telesales Department and the eCommerce Department. These departments are each under the direction of an Officer of the Company and focus on both the acquisition of new customers and gaining additional sales from existing customers.

The Agency Division is under the direction of the Agency Senior Vice President who is assisted by two Vice Presidents of Agency Administration. In addition, the Company utilizes the services of three salaried full-time field employees as Regional Managers. Each such manager has a proportionate number of Division Managers under his or her supervision. The Division Managers are full-time employees and act exclusively for the Company. They are authorized to recruit, appoint and train agents within their territories, subject to Home Office approval. They receive remuneration in the form of overwrite commissions on business produced by agents under their supervision.

At December 31, 2012, the Company's agency force was comprised of the following:

|                   |     |
|-------------------|-----|
| Division Managers | 19  |
| Contracted Agents | 898 |

The contracted agents are independent contractors who act as career agents for the Company. All contracted agents receive commissions and can also earn cash bonuses and lead or advertising credits by meeting production and persistency requirements.

## **REINSURANCE**

### **Assumed**

The Company entered into an automatic 50% coinsurance life agreement with AAA Life Insurance Company (AAA), effective January 1, 1999 and amended January 1, 1999; September 27, 2001; and July 31, 2002. The third amendment added PMIC as a party to the agreement.

Effective February 1, 2003, the Company entered into a retrocession agreement whereby Transamerica International Re, retroceded 20% of the yearly renewable term business to the Company under a quota share agreement.

### **Ceded**

Effective February 1, 2003 the Company reinsured its new 10 and 20-year term plans with Transamerica Reinsurance Company (Transamerica) under a series of three treaties. The first treaty was a 100% first dollar quota share arrangement. Treaty two was a retrocession agreement whereby Transamerica's Bermuda affiliate, Transamerica International Re, retroceded 20% of the business back to the Company under a quota share arrangement. Under treaty three, the Company reinsured any excess above face amounts of \$100,000 to Transamerica. Because Transamerica was also the underwriter, a facultative agreement was not needed.

The Company ceded approximately \$90,854,000 in premiums in 2012. Approximately \$88,100,000 was to PMIC (see discussion under "Transactions with Affiliates" above). The Company also ceded an immaterial amount of life insurance to various reinsurers. Premiums ceded to various reinsurers were approximately \$2,754,000 in 2012.

## **General**

All contracts reviewed contained standard insolvency, arbitration, errors and omissions, and termination clauses where applicable. All contracts contained the clauses necessary to assure reinsurance credits could be taken.

## **BODY OF REPORT**

### **GROWTH**

The following comparative data reflects the growth of the Company during the period covered by this examination:

|  | <b><u>2009</u></b> | <b><u>2010</u></b> | <b><u>2011</u></b> | <b><u>2012</u></b> |
|--|--------------------|--------------------|--------------------|--------------------|
| Bonds                                  | \$1,138,407,595    | \$1,124,229,044    | \$1,148,839,886    | \$1,167,949,194    |
| Admitted assets                        | 1,252,705,969      | 1,257,469,499      | 1,268,942,225      | 1,284,977,580      |
| Aggregate reserves for life contracts  | 981,070,959        | 1,000,984,209      | 1,019,171,026      | 1,048,726,961      |
| Total liabilities                      | 1,151,199,530      | 1,151,347,634      | 1,160,219,520      | 1,169,139,668      |
| Capital and surplus                    | 101,506,439        | 106,121,865        | 108,722,705        | 115,837,912        |
| Premium income                         | 193,798,846        | 197,467,017        | 200,859,560        | 211,177,239        |
| Net investment income                  | 65,719,725         | 64,213,187         | 62,767,518         | 62,219,823         |
| Death benefits and annuity benefits    | 131,660,630        | 127,770,859        | 132,172,123        | 134,645,104        |
| Net income                             | 6,278,932          | 5,013,356          | 4,383,458          | 8,716,430          |
| Life insurance in-force (in thousands) | 3,888              | 3,826              | 3,739              | 3,716              |

### **FINANCIAL STATEMENTS**

The following statement of admitted assets and liabilities, together with the accompanying summary of operations, reflects the financial condition of the Company at December 31, 2012 and its transactions during the year 2012 as determined through this examination. A reconciliation of the capital and surplus account for the period under review is also included.

**FINANCIAL STATEMENT**  
**December 31, 2012**

| <b><u>Assets</u></b>                                    | <b><u>Assets</u></b>          | <b><u>Assets Not<br/>Admitted</u></b> | <b><u>Net<br/>Admitted<br/>Assets</u></b> |
|---|-------------------------------|---------------------------------------|---|
| Bonds   | \$1,167,949,194               |                                       | \$1,167,949,194                           |
| Preferred stocks  | 12,770,075                    |                                       | 12,770,075                                |
| Common stocks   | 2,991,378                     |                                       | 2,991,378                                 |
| Cash and short-term investments                         | 33,943,620                    |                                       | 33,943,620                                |
| Contract loans  | 28,455,725                    | \$ 6,664                              | 28,449,061                                |
| Derivatives   | 4,133,374                     |                                       | 4,133,374                                 |
| Other invested assets                                   | 4,678,194                     |                                       | 4,678,194                                 |
| Receivable for securities                               | <u>99,746</u>                 |                                       | <u>99,746</u>                             |
| <b>Subtotal, cash and invested assets</b>               | <b>\$1,255,021,307</b>        | <b>\$ 6,664</b>                       | <b>\$1,255,014,643</b>                    |
| Investment income due and accrued                       | 13,734,982                    |                                       | 13,734,982                                |
| Amounts recoverable from insurers                       | 75,204                        |                                       | 75,204                                    |
| Other amounts receivable under<br>reinsurance contracts | 396,387                       |                                       | 396,387                                   |
| Current federal income tax recoverable                  | 149,325                       |                                       | 149,325                                   |
| Net deferred tax asset                                  | 40,033,051                    | 24,659,014                            | 15,374,037                                |
| Guaranty funds receivable or on deposit                 | 233,003                       |                                       | 233,003                                   |
| Other amounts receivable                                | 387,411                       | 387,411                               |   |
| Debit suspense  | <u>1,318,388</u>              | <u>1,318,388</u>                      |   |
| <b>Totals</b>   | <b><u>\$1,311,349,057</u></b> | <b><u>\$26,371,477</u></b>            | <b><u>\$1,284,977,580</u></b>             |

**Liabilities, Surplus, and Other Funds**

|   |                               |
|---|-------------------------------|
| Aggregate reserve for life contracts                                  | \$1,048,726,961               |
| Liability for deposit-type contracts                                  | 49,901,780                    |
| Contract claims – life  | 16,007,553                    |
| Premiums and annuity considerations for contracts received in advance | 2,013,855                     |
| Other amounts payable on reinsurance                                  | 283,933                       |
| Interest maintenance reserve  | 8,481,392                     |
| Commissions to agents due or accrued                                  | 90,212                        |
| General expenses due or accrued                                       | 649,285                       |
| Taxes, licenses and fees due or accrued                               | 879,969                       |
| Unearned investment income  | 906,908                       |
| Amounts withheld or retained by company                               | 1,625,164                     |
| Remittances and items not allocated                                   | 741,124                       |
| Borrowed money  | 18,099,243                    |
| Asset valuation reserve   | 9,551,192                     |
| Payable to parent, subsidiaries and affiliates                        | 410,298                       |
| Drafts outstanding  | 9,488,237                     |
| Payable for securities  | 1,219,298                     |
| Miscellaneous interest  | <u>63,264</u>                 |
| <b>Total liabilities</b>  | <b><u>\$1,169,139,668</u></b> |
| <b>Common capital stock</b>   | <b>\$ 2,505,000</b>           |
| <b>Gross paid in and contributed surplus</b>                          | <b>102,487,905</b>            |
| <b>Unassigned funds (surplus)</b>                                     | <b><u>10,845,007</u></b>      |
| <b>Total capital and surplus</b>                                      | <b><u>\$ 115,837,912</u></b>  |
| <b>Totals</b>   | <b><u>\$1,284,977,580</u></b> |

## SUMMARY OF OPERATIONS – 2012

|  |                             |
|--|-----------------------------|
| Premiums and annuity considerations for life and accident and health contracts         | \$211,177,239               |
| Considerations for supplementary contracts with life contingencies                     | 3,153,790                   |
| Net investment income  | 62,219,823                  |
| Amortization of interest maintenance reserve   | 1,645,513                   |
| Commissions and expense allowances on reinsurance ceded                                | 2,261,903                   |
| Income on derivatives  | 3,442,810                   |
| Miscellaneous income   | 3,087,159                   |
| Change in market value of derivatives  | <u>1,912,494</u>            |
| <b>Totals</b>  | <b><u>\$288,900,732</u></b> |
| <br>   |                             |
| Death benefits   | \$117,633,367               |
| Matured endowments   | 170,044                     |
| Annuity benefits   | 14,541,353                  |
| Surrender benefits and withdrawals for life contracts                                  | 34,005,963                  |
| Interest and adjustments on contract or deposit-type contract funds                    | 1,190,792                   |
| Payments on supplementary contracts with life contingencies                            | 2,300,340                   |
| Increase in aggregate reserves for life and accident and health contracts              | <u>29,555,936</u>           |
| <b>Totals</b>  | <b><u>\$199,397,796</u></b> |
| <br>   |                             |
| Commissions on premiums, annuity considerations, and<br>deposit type contract funds    | \$ 5,796,751                |
| Commissions and expense allowances on reinsurance assumed                              | 650,135                     |
| General insurance expenses   | 63,000,339                  |
| Insurance taxes, licenses and fees   | 5,953,567                   |
| Amortization of derivatives  | 3,328,967                   |
| Payment on swaps   | <u>36,141</u>               |
| <b>Totals</b>  | <b><u>\$278,163,695</u></b> |
| <br>   |                             |
| Net gain from operations before federal income taxes<br>and net realized capital gains | \$ 10,737,037               |
| <br>   |                             |
| Federal income taxes incurred  | \$ 2,092,335                |
| Net realized capital gains (losses)  | <u>71,729</u>               |
| <br>   |                             |
| Net income   | <b><u>\$ 8,716,430</u></b>  |

## CAPITAL AND SURPLUS ACCOUNT

|   | <u>2009</u>          | <u>2010</u>          | <u>2011</u>          | <u>2012</u>          |
|---|----------------------|----------------------|----------------------|----------------------|
| Capital and surplus, beginning                                | \$ <u>87,607,333</u> | <u>\$101,506,442</u> | <u>\$106,121,872</u> | <u>\$108,722,709</u> |
| Net income  | \$ 6,278,932         | \$ 5,013,356         | \$ 4,383,458         | \$ 8,716,430         |
| Change in net unrealized<br>capital gains                     | (432,264)            | 186,265              | (691,587)            | 558,682              |
| Change in net deferred income tax                             | (1,726,312)          | 2,488,253            | 95,125               | (1,628,222)          |
| Change in nonadmitted assets                                  | 10,538,559           | (10,770,710)         | (850,363)            | 1,804,073            |
| Change in asset valuation reserve                             | (759,806)            | (1,331,429)          | (610,707)            | (2,335,755)          |
| Cumulative effect of changes in<br>accounting principles      |                      |                      | 100,000              |                      |
| Additional deferred tax assets<br>admissible through SSAP 10R | _____                | <u>9,029,695</u>     | <u>174,911</u>       | _____                |
| Net change for the year                                       | \$ <u>13,899,108</u> | <u>\$ 4,615,431</u>  | <u>\$ 2,600,837</u>  | <u>\$ 7,115,207</u>  |
| Capital and surplus, ending                                   | <u>\$101,506,442</u> | <u>\$106,121,872</u> | <u>\$108,722,709</u> | <u>\$115,837,916</u> |

### EXAMINATION CHANGES IN FINANCIAL STATEMENTS

Unassigned funds (surplus) in the amount of \$10,845,007, as reported in the Company's 2012 Annual Statement, has been accepted for examination purposes. Examination findings, in the aggregate, were considered to have no material effect on the Company's financial condition.

### COMPLIANCE WITH PREVIOUS RECOMMENDATIONS

No recommendations were made as a result of the previous examination.

### COMMENTARY ON CURRENT EXAMINATION FINDINGS

#### Custodial Agreement

Some provisions of Nebraska Regulation Title 210, Chapter 81 were missing, or only partially covered, in the Company's custodial agreement with the Federal Home Loan Bank of Topeka (FHLB of Topeka).

It is recommended that the Company revise its custodial agreement with FHLB of Topeka to include all provisions related to safeguards and controls of securities pursuant to Title 210 (Nebraska Department of Insurance Rules and Regulations), Chapter 81.

### **Schedule Y**

The Company did not disclose the Physicians Mutual Insurance Company Foundation or the Company's trusts for the benefit of employees on its Schedule Y Part 1 - Organizational Chart, Schedule Y Part 1A - Detail of Insurance Holding Company System and Schedule Y Part 2 - Summary of Insurer's Transactions with any Affiliates, in accordance with SSAP No. 25, *Accounting for and Disclosures about Transactions with Affiliates and Other Related Parties* and NAIC Annual Statement Instructions.

It is recommended the Company disclose the Physicians Mutual Insurance Company Foundation and the Company's trusts for the benefit of employees in its Schedule Y in each of the individual annual statements in accordance with NAIC Annual Statement Instructions and SSAP No. 25.

## **SUMMARY OF COMMENTS AND RECOMMENDATIONS**

The following comments and recommendations have been made as a result of this examination:

**Custodial Agreement** – It is recommended that the Company revise its custodial agreement with FHLB of Topeka to include all provisions related to safeguards and controls of securities pursuant to Title 210 (Nebraska Department of Insurance Rules and Regulations), Chapter 81.

**Schedule Y** – It is recommended that the Company disclose the Physicians Mutual Insurance Company Foundation and the Company's trusts for the benefit of employees in its Schedule Y in accordance with NAIC Annual Statement Instructions and SSAP No. 25.

**ACKNOWLEDGMENT**

The courteous cooperation extended by the Officers and employees of the Company during this examination is hereby acknowledged.

In addition to the undersigned, Derek Petersen, CFE, Brian Davis and Kim Shannon, Financial Examiners; Linda Scholl, CFE, Information Systems Specialist; and Dan Eckstein, ASA, CIB, Life and Health Actuarial Specialist; all with the Nebraska Department of Insurance, participated in this examination and assisted in the preparation of this report.

Respectfully submitted,

A handwritten signature in black ink, appearing to read 'S. Carroll', with a long horizontal flourish extending to the right.

**Susan L. Carroll, CPA, CFE  
Examiner-in-Charge  
Department of Insurance  
State of Nebraska**

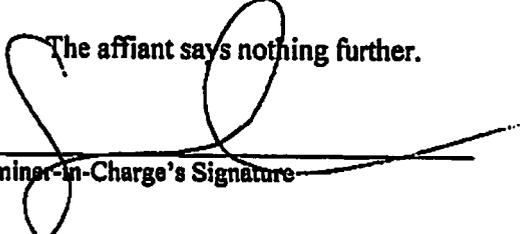
State of Nebraska,

County of Lancaster,

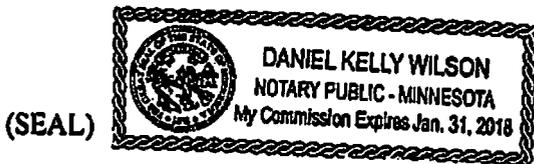
Susan Carroll, being duly sworn, states as follows:

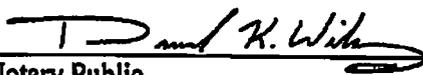
1. I have authority to represent the Department of Insurance of the State of Nebraska in the examination of Physicians Mutual Insurance Company and Physicians Life Insurance Company.
2. The Department of Insurance of the State of Nebraska is accredited under the National Association of Insurance Commissioners Financial Regulation Standards and Accreditation.
3. I have reviewed the examination work papers and examination report, and the examination of Physicians Mutual Insurance Company and Physicians Life Insurance Company was performed in a manner consistent with the standards and procedures required by the Department of Insurance of the State of Nebraska.

The affiant says nothing further.

  
Examiner-in-Charge's Signature

Subscribed and sworn before me by Susan L. Carroll on this 22<sup>nd</sup> day of May, 2014.



  
Notary Public

My commission expires 01/31/2018 [date].



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I have received a copy of the Physicians Life Insurance Company Association Report of ~~Financial Condition Examination~~ as of December 31, 2012.

Dale E. Brett  
Dale E. Brett, MD

6/10/14  
Date

James T. Canedy  
James T. Canedy, MD

6/10/14  
Date

William R. Hamsa, Jr.  
William R. Hamsa, Jr., MD

6/10/14  
Date

Martin M. Mancuso  
Martin M. Mancuso, MD

6/10/14  
Date

Robert A. Reed  
Robert A. Reed

6-10-14  
Date

Robert A. Reed, Jr.  
Robert A. Reed, Jr.

6/10/14  
Date

John D. Woodbury  
John D. Woodbury, MD

6-10-14  
Date

