

EXAMINATION REPORT OF
FARMERS MUTUAL INSURANCE ASSOCIATION
CRAWFORD COUNTY, SCHLESWIG, IOWA
AS OF DECEMBER 31, 2018

Schleswig, Iowa
November 27, 2019

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

Commissioner Ommen:

In accordance with your instructions and pursuant to Iowa statutory provisions, an examination has been made of the

FARMERS MUTUAL INSURANCE ASSOCIATION

CRAWFORD COUNTY, SCHLESWIG, IOWA

AS OF DECEMBER 31, 2018

at its Home Office, 106 Second Street, Schleswig, Iowa. The report, containing applicable comments and financial data, is presented herein.

SCOPE OF EXAMINATION

This examination covers the period from January 1, 2016 to December 31, 2018. The examination was conducted in accordance with procedures established by the Iowa Insurance Division. The Association's assets were verified and evaluated and the liabilities determined to reflect herein a statement of its financial condition as of December 31, 2018.

HISTORY

The Association was incorporated in 1879 for the purpose of insuring the property of its members against hazards and risks as permitted by Chapter 518, Code of Iowa. The corporate existence was made perpetual in 1946.

MANAGEMENT AND CONTROL

MEMBERSHIP

The membership consists of those persons or organizations having insurance written by the Association which is in full force and effect.

The annual meeting of the members is held at Schleswig, Iowa on the second Saturday in February. Special meetings may be called by the Board of Directors as provided in the Articles of Incorporation. Due notice of the time and place of special meetings shall be given the membership. Each member present is entitled to one vote on any question to be decided. Voting by proxy is not permitted. Ten members present constitute a quorum for any membership meeting.

BOARD OF DIRECTORS

The corporate powers of the Association are vested in a Board of not less than nine nor more than fifteen directors, each elected by a majority vote at the annual meeting of the members for terms of three years. Any vacancy on the Board may be filled for the unexpired term by a majority vote of the remaining directors. As of December 31, 2018, the Association had only six directors serving on its board.

Directors serving at December 31, 2018 were:

<u>Name</u>	<u>Address</u>	<u>Term Expires</u>
Grant Snyder	Odebolt, Iowa	2019
Alan Weiss	Schleswig, Iowa	2019
Steve Vary	Arion, Iowa	2019
Jason Schultz	Schleswig, Iowa	2020
Douglas Soellner	Holstein, Iowa	2021
Larry Abbe	Schleswig, Iowa	2021

The annual meeting of the Board is held immediately following the annual meeting of the members, and thereafter on the call of the Secretary. A majority present constitutes a quorum for the transaction of business.

Directors receive a fee of \$100 for each meeting attended.

Remuneration of directors are shown on Exhibit A following this report.

OFFICERS

At its annual meeting, the Board of Directors elects for a term of one year a President, Vice President, Treasurer and Secretary, who, when so designated by the Board, may also serve as Treasurer and such additional officers as it deems necessary.

Officers serving at December 31, 2018 were:

<u>Name</u>	<u>Office</u>
Jason Schultz	President
Douglas Soellner	Vice President
Alan Weiss	Secretary/Treasurer

Remuneration of officers are shown on Exhibit A following this report.

CONFLICT OF INTEREST

Conflict of interest statements were signed annually by all officers, directors and key employees. Greater care should be taken to ensure all proper interests and affiliations are disclosed.

CORPORATE RECORDS

The Articles of Incorporation and Bylaws were not amended or substituted during the period covered by this examination.

The recorded minutes of the membership and Board of Directors meetings were read and noted. The minutes of the Board of Directors reflected that the Examination Report as of December 31, 2015 was read and accepted at the February 11, 2017 Board meeting.

FIDELITY BONDS AND OTHER INSURANCE

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

Policies for other coverages are as follows:

- Workers' compensation and employers' liability
- Professional liability
- Officers' and directors' liability
- Business property and personal property
- Business liability

It appears adequate insurance is placed with authorized insurers, except professional liability and officers' and directors' liability which is written by a surplus lines insurer permitted to write in Iowa.

EMPLOYEES' WELFARE

Contributions to a pension trust retirement plan are made at a level of five percent of salary. Contributions paid by the Association for 2016, 2017, and 2018 were \$9,836, \$9,203, and \$9,823, respectively.

TERRITORY AND PLAN OF OPERATION

The Association is authorized to transact business in the State of Iowa as a county mutual insurance association under the provisions of Chapter 518, Code of Iowa. It is currently authorized to transact business in nine counties in the State of Iowa. The permitted writing territory is composed of the following counties: Audubon, Carroll, Crawford, Harrison, Ida, Monona, Sac, Shelby, and Woodbury counties. It was noted, from a review of numerous applications of policies in force, that risks appeared to be located within the authorized territory.

Policies are written or renewed for a one-year period with premiums payable quarterly, annually or semi-annually. The Association underwrites these policies every three years.

At the present time, business is produced by twenty-six licensed agents.

UNDERWRITING EXPERIENCE

THREE-YEAR PERIOD ENDED DECEMBER 31, 2018

<u>Classification</u>	<u>2016</u>	<u>2017</u>	<u>2018</u>	<u>Total</u>
Premiums earned	<u>\$2,360,982</u>	<u>\$2,164,925</u>	<u>\$2,247,196</u>	<u>\$6,773,103</u>
Incurred deductions:				
Losses	\$1,427,616	\$1,090,577	\$1,862,877	\$4,381,070
Loss adjustment expenses	90,418	80,559	109,493	280,470
Commissions	479,033	489,235	477,338	1,445,606
Salaries	111,007	111,939	116,736	339,682
Taxes, licenses and fees	47,663	47,300	54,917	149,880
Other underwriting expenses	<u>114,054</u>	<u>97,276</u>	<u>106,817</u>	<u>318,147</u>
Total deductions	<u>\$2,269,791</u>	<u>\$1,916,886</u>	<u>\$2,728,178</u>	<u>\$6,914,855</u>
Underwriting gain or (loss)	<u>\$ 91,191</u>	<u>\$ 248,039</u>	<u>\$ (480,982)</u>	<u>\$ (141,752)</u>

Expressed in ratios of expenses incurred to premiums earned, the percentages would be:

	<u>2016</u>	<u>2017</u>	<u>2018</u>	<u>Total</u>
Incurred deductions:				
Losses	60.47%	50.37%	82.90%	64.68%
Loss adjustment expenses	3.83	3.72	4.87	4.14
Commissions	20.29	22.60	21.24	21.34
Salaries	4.70	5.17	5.19	5.02
Taxes, licenses and fees	2.02	2.18	2.44	2.21
Other underwriting expenses	<u>4.83</u>	<u>4.50</u>	<u>4.76</u>	<u>4.70</u>
Total deductions	<u>96.14%</u>	<u>88.54%</u>	<u>121.40%</u>	<u>102.09%</u>
Underwriting gain or (loss)	<u>3.86%</u>	<u>11.46%</u>	<u>(21.40%)</u>	<u>(2.09%)</u>

REINSURANCE

The Association has reinsurance contracts in force as of December 31, 2018 with an authorized insurer which provides the following:

Per Risk Excess of Loss

First \$150,000 of ultimate net loss per risk is retained by the Association. First layer is reinsurer will pay 100 percent of net loss in excess of retention. The maximum recovery for first layer is \$1,000,000. Second layer has recovery of \$4,000,000 in excess of \$1,000,000 for each risk. Third layer has maximum recovery of \$15,000,000 in excess of \$5,000,000. The Association is required to provide a timely notification to reinsurer of any risks exceeding \$10,000,000.

Catastrophe Excess of Loss

First \$700,000 of ultimate net loss per catastrophe, which is any period of 96 consecutive hours arising out of and directly occasioned by the same event, is retained by the Association. One-hundred percent of ultimate net loss in excess of retention is covered by the reinsurer.

Aggregate Excess of Loss

First \$1,925,000 of ultimate net losses in aggregate, net of all other reinsurance recoveries is retained by the Association. One-hundred percent of ultimate net loss in excess of retention is covered by the reinsurer. Reinsurance recovery is unlimited. Applies to new and renewal and in-force policies of the Association effective and becoming effective at and after the effective date of the contract until expiration of the contract.

Facultative

While facultative reinsurance is available, no risks were identified which would warrant a facultative agreement.

Reinsurance - General

Reinsurance attachments appear to be in compliance with Iowa statutes.

CLAIMS

From a review of numerous claims, it appeared that the Association made prompt settlements which were in keeping with the terms of the policy contracts.

AFFILIATED AGENCY

The Association owns its Home Office building and shares a portion of the space with Farmers Mutual Direct Agency. The agency is 100 percent owned by the Association. This agency produced approximately two percent of the Association's business during 2018.

The agency paid \$750 monthly rent to the Association in addition to a \$750 monthly management fee in 2018. The rental charge and the expense allocation between the agency and Association do not appear to be unreasonable.

ACCOUNTS AND RECORDS

Office copies of the filed annual statements for the years under review were found not to be in agreement with or could not be reconciled to the general ledger balances of assets, liabilities, income and disbursements. Greater care should be exercised to ensure that the annual statement agrees with and reconciles to the general ledger.

Selected cash receipts recorded during the period were checked and traced to the Association's depository. Checks paid during selected months were compared to the disbursement records and were scrutinized as to payees, amounts, and authorized signatures. Cash receipts and disbursements for selected months were proven by comparison and reconciliation to the monthly bank statements.

The Association was in compliance with the Commissioner's Bulletin 97-6 at December 31, 2018 relative to security custodial requirements.

In accordance with Section 518.25, Code of Iowa, surplus must be maintained at a level of not less than fifty thousand dollars or one-tenth of one percent of the gross risk in force, whichever is greater. At December 31, 2018, the gross risk in force for the Association was \$964,574,118. The Association's statutory minimum surplus level as December 31, 2018 was \$964,574. It is noted the Association's surplus level to minimum surplus level ratio was 3.96/1. The reported surplus/statutory minimum ratio average for the Chapter 518 licensed industry at December 31, 2018 was 7.90/1.

Investment transactions do not appear to be properly classified and reported. It is suggested that greater care be exercised to report investment securities according to their proper classification, CUSIP, purchase dates, call or maturity dates, and interest rates.

At the March 15, 2019 board meeting, Larry Abbe stepped down from the Manager position with the Association. Scott March was promoted to Interim Manager.

F I N A N C I A L S T A T E M E N T S
A N D C O M M E N T S T H E R E O N

NOTE: Except as otherwise stated, the financial statements immediately following reflect only the transactions for the period ending December 31, 2018 and the assets and liabilities as of this date. Schedules may not add or tie precisely due to rounding.

STATEMENT OF ASSETS AND LIABILITIES

ASSETS

	<u>Ledger</u>	<u>Nonledger</u>	<u>Not Admitted</u>	<u>Admitted</u>
Bonds	\$4,795,611	\$	\$ 125,655	\$4,669,956
Stocks	46,004	68,712	28,710	86,006
Bank balances:				
Subject to check	120,982			120,982
On interest	856,837			856,837
Real estate	8,821			8,821
Cash in office	100			100
Unpaid premiums:				
Due before November 1		2,036	2,036	
Due after November 1		40,477		40,477
Reinsurance receivable		35,162		35,162
Accrued interest		32,767		32,767
Supplies		2,500	2,500	
Federal income tax recoverable		40,000	40,000	
Subrogation recoverable		64,466		64,466
Commission receivable		24,379		24,379
Iowa Fair Plan partnership	3,231		3,231	
	\$5,831,586	\$ 310,499	\$ 202,132	\$5,939,953
Total				

LIABILITIES AND SURPLUS

Losses	\$ 407,018
Unpaid adjusting expenses	26,747
Ceded reinsurance balances payable	212,070
Unpaid salaries and commissions	38,634
Taxes payable	3,914
Other unpaid expenses	3,503
Suspense	810
Premiums collected for other companies - not remitted	23,821
Premiums received in advance	40,498
Employee benefits payable	9,823
Unearned premium reserve	1,357,158
	\$2,123,996
Total liabilities	
Surplus as regards policyholders	3,815,957
	\$5,939,953
Total liabilities and surplus	

INCOME AND DISBURSEMENTS
AND
RECONCILIATION OF LEDGER ASSETS

Ledger assets, December 31, 2017			<u>\$5,867,637</u>
	<u>INCOME</u>		
Net premiums and fees			\$2,451,728
Net interest received on bonds			173,253
Increase (decrease) by adjustment - bonds			(8,306)
Dividends received			184
Interest received on bank deposits			17,778
Other interest			19
Profit on sale of investments			961
Rents received			9,000
Increase in ledger liabilities			8
Miscellaneous income			847
GMRC direct liability premium adjustment			76,835
Total income			<u>\$2,722,307</u>
Total assets and income			<u>\$8,589,944</u>
	<u>DISBURSEMENTS</u>		
Losses paid			\$1,777,177
<u>Operating Expense</u>			
Adjusting expense	\$	92,576	
Commissions	493,607		
Advertising	7,385		
Boards, bureaus and associations	10,753		
Inspection and loss prevention	805		
Salaries of officers	59,274		
Salaries of office employees	57,462		
Employee welfare	8,648		
Insurance	11,681		
Directors' compensation	7,900		
Rent and rent items	2,954		
Printing and stationary	7,381		
Postage, telephone	15,269		
Legal and auditing	10,125		
State insurance taxes	36,220		
Insurance Division licenses and fees	240		
Payroll taxes	15,432		
Real estate expenses	7,009		
Real estate taxes	1,922		
Miscellaneous	4,159		
Registration fees	2,840		
Data processing	11,874		
Travel and travel items	1,168		
Meals and lodging	1,640		
Total operating expense		<u>868,324</u>	\$ 868,324
<u>Non-Operating Expense</u>			
Depreciation on real estate			315
Loss on sale of investments			3,348
Federal income tax			108,962
Iowa Fair Plan - net loss			232
Total disbursements			<u>\$2,758,358</u>
Balance - ledger assets, December 31, 2018			<u>\$5,831,586</u>

UNDERWRITING AND INVESTMENT EXHIBIT

ONE-YEAR PERIOD ENDED DECEMBER 31, 2018

STATEMENT OF INCOME

<u>Underwriting Income</u>	
Premiums earned	\$2,247,196
<u>Deductions</u>	
Losses incurred	\$1,862,877
Loss expenses incurred	109,493
Other operating expenses incurred	755,808
Total underwriting deductions	<u>2,728,178</u>
Net underwriting gain (loss)	\$ (480,982)
<u>Investment Income</u>	
Net investment income earned	178,919
<u>Other Income</u>	
Premiums collected for other companies (net)	68,381
Miscellaneous income	<u>148</u>
Net loss before Federal income tax	\$ (233,534)
Federal income tax incurred	<u>39,926</u>
Net loss	<u>\$ (273,460)</u>

CAPITAL AND SURPLUS ACCOUNT

Surplus as regards policyholders, December 31, 2017	<u>\$4,087,512</u>
<u>Gains and (Losses) in Surplus</u>	
Net loss	\$ (273,460)
Change in net unrealized gains/losses	<u>1,905</u>
Change in surplus as regards policyholders for the year	<u>\$ (271,555)</u>
Surplus as regards policyholders, December 31, 2018	<u>\$3,815,957</u>

UNDERWRITING AND INVESTMENT EXHIBIT

THREE-YEAR PERIOD ENDED DECEMBER 31, 2018

STATEMENT OF INCOME

<u>Underwriting Income</u>		
Premiums earned		\$6,773,103
<u>Deductions</u>		
Losses incurred	\$4,381,070	
Loss expenses incurred	280,470	
Other operating expenses incurred	2,253,315	
Total underwriting deductions	<u>6,914,855</u>	<u>6,914,855</u>
Net underwriting gain (loss)		\$ (141,752)
<u>Investment Income</u>		
Net investment income earned		513,566
<u>Other Income</u>		
Premiums collected for other companies (net)		67,825
Miscellaneous income		<u>12,814</u>
Net income before Federal income tax		\$ 452,453
Federal income tax incurred		<u>226,287</u>
Net income		<u>\$ 226,166</u>

CAPITAL AND SURPLUS ACCOUNT

Surplus as regards policyholders, December 31, 2015		<u>\$3,548,210</u>
<u>Gains and (Losses) in Surplus</u>		
Net income		\$ 226,166
Change in net unrealized gains/losses		<u>41,581</u>
Change in surplus as regards policyholders for the period		<u>\$ 267,747</u>
Surplus as regards policyholders, December 31, 2018		<u>\$3,815,957</u>

SURPLUS AS REGARDS POLICYHOLDERS

The changes which resulted in the net decrease are shown in the following statement of differences:

<u>Classification</u>	<u>Association Annual Statement</u>	<u>Examination Financial Statement</u>	<u>Surplus Increase (Decrease)</u>
<u>Assets</u>			
Bonds	\$4,735,611	\$4,669,956	\$ (65,655)
Stocks	17,294	86,006	68,712
Unpaid premiums	41,286	40,477	(809)
Federal income tax recoverable	40,000	0	(40,000)
Subrogation recoverable	90,000	64,466	(25,534)
<u>Liabilities</u>			
Losses	402,050	407,018	(4,968)
Unpaid adjusting expenses	16,500	26,747	(10,247)
Ceded reinsurance balances payable	203,910	212,070	(8,160)
Unpaid salaries and commissions	33,415	38,634	(5,219)
Premiums collected for other companies	31,981	23,821	8,160
Premiums received in advance	37,140	40,498	(3,358)
Unearned premium reserve	1,358,825	1,357,158	1,667
Net change to surplus			\$ (85,411)
Surplus per Association			<u>\$3,901,368</u>
Surplus per examination			<u>\$3,815,957</u>

During the period under review, surplus funds increased \$267,747 from the amount of \$3,548,210 as shown in the last previous examination report. An operating statement reflecting that increase is contained in the financial section.

COMMENTS

The major changes in the Association's financial statement were due to the following:

Bonds \$4,669,956

This asset was decreased by \$65,655 to adjust for recalculation of bond amortization and re-classification of two preferred stocks that were incorrectly classified.

Stocks \$ 86,006

This asset was increased by \$68,712 to reflect the proper valuation of the wholly owned subsidiary agency and re-classification of two preferred stocks that were incorrectly classified.

Unpaid premiums \$ 40,477

This asset was decreased by \$809 to reflect the actual amount of premiums received in 2019.

Federal income tax recoverable \$ 0

This asset was decreased by \$40,000 to reflect the income tax refund not received and credited to 2019 tax.

Subrogation recoverable \$ 64,466

This asset was decreased by \$25,534 to reflect the actual amount received in 2019.

Losses \$ 407,018

Losses was increased by \$4,968 to reflect actual loss development.

Unpaid adjusting expenses \$ 26,747

An analysis of paid expenses to paid losses increased the liability by \$10,247.

Ceded reinsurance balances payable \$ 212,070

This liability was increased by \$8,160 to correct the presentation of this liability.

Unpaid salaries and commissions \$ 38,634

This liability was increased by \$5,219 to reflect the actual commissions paid on premiums receivable.

Premiums collected for other companies \$ 23,821

This liability was decreased by \$8,160 to correct the presentation of this liability.

Premiums received in advance \$ 40,498

This liability was increased by \$3,358 to remove liability premiums previously included in the calculation.

Unearned premium reserve \$ 1,357,158

A recalculation of unearned premium reserve using examination adjustments decreased this liability by \$1,667.

CONCLUSION

The cooperation and assistance extended by the officers and personnel of the Association is hereby acknowledged.

Respectfully submitted,

/s/Abby Kramer
Abby Kramer
Cain Ellsworth & Co., LLP
Representing the State of Iowa