

EXAMINATION REPORT OF
FARMERS MUTUAL INSURANCE ASSOCIATION
MITCHELL COUNTY, OSAGE, IOWA
AS OF DECEMBER 31, 2018

Osage, Iowa
November 8, 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

MITCHELL COUNTY, OSAGE, IOWA

AS OF DECEMBER 31, 2018

at its Home Office, 708 Chase Street, Osage, 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 1874 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 1949.

On January 1, 2006, the Association entered into an Assumption & Reinsurance Agreement with St. Ansgar Mutual Insurance Association, with Farmers Mutual Insurance Association of Osage being the surviving entity.

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 Osage, Mitchell County, Iowa on the third Monday in February at 1:30 p.m. 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. One more member than the number of directors authorized by the Articles of Incorporation or Bylaws present constitute a quorum for any membership meeting.

BOARD OF DIRECTORS

The corporate powers of the Association are vested in a Board of seven 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.

Directors serving at December 31, 2018 were:

<u>Name</u>	<u>Address</u>	<u>Term Expires</u>
Steve Follmuth	Stacyville, Iowa	2019
Jerry Newton	Osage, Iowa	2019
Sam Kruse	McIntire, Iowa	2019
Roger Frank	St. Ansgar, Iowa	2020
Kenneth Pitzen	Stacyville, Iowa	2020
William Brandau	Floyd, Iowa	2021
Doug Uthe	Osage, 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 \$150 for each meeting attended and reimbursement of travel expense.

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

OFFICERS

At its annual meeting, the Board of Directors shall elect for a term of one year a President, Chairman, Vice Chairman, 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>
Roger Frank	Chairman
Jerry Newton	Vice Chairman
William Brandau	Secretary
TJ Crandall	President/Treasurer/Manager

Remuneration of officers are reflected in Exhibit A following this report.

In 2017, Steve Tervo resigned as President/Treasurer/Manager and TJ Crandall was hired to fill those positions.

CONFLICT OF INTEREST

Conflict of interest statements were signed annually by all officers, directors and key employees during the exam period.

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 not discussed in the Board of Directors meeting minutes.

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
- Building and contents
- General liability
- Business auto
- Cyber liability and data breach response

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

No health, life, or dental coverage is provided by the Association.

The Association provides \$450 per month for auto allowance and \$40 per month for cell phone allowance for sales agents.

The Association does not have a formal profit share arrangement, but offers 0.5 percent profit share to all employees each year. Employees received \$788 in 2016 and \$6,636 in 2018.

Retirement benefit contributions were made to a pension trust plan based on ten percent of the full-time eligible employee's salary. Contributions were paid by the Association of \$22,882, \$12,084, and \$16,200 for 2016, 2017, and 2018, respectively.

TERRITORY AND PLAN OF OPERATION

The Association is authorized to transact business in Mitchell, Worth, Howard, Cerro Gordo, Floyd, and Chickasaw 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 monthly (only for EFT/ACH), quarterly, semi-annually or annually. The Association underwrites these policies every five years.

At the present time, business is produced by thirty-five 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>\$1,609,139</u>	<u>\$1,584,680</u>	<u>\$1,494,647</u>	<u>\$4,688,466</u>
Incurred deductions:				
Losses	\$ 846,514	\$1,468,832	\$ 594,444	\$2,909,790
Loss adjustment expense	38,976	36,855	38,568	114,399
Commissions	328,801	249,977	278,869	857,647
Salaries	222,040	186,587	233,823	642,450
Taxes, licenses and fees	43,068	38,123	41,755	122,946
Other underwriting expenses	<u>104,415</u>	<u>174,879</u>	<u>163,920</u>	<u>443,214</u>
Total deductions	<u>\$1,583,814</u>	<u>\$2,155,253</u>	<u>\$1,351,379</u>	<u>\$5,090,446</u>
Underwriting gain or (loss)	<u>\$ 25,325</u>	<u>\$ (570,573)</u>	<u>\$ 143,268</u>	<u>\$ (401,980)</u>

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

<u>Classification</u>	<u>2016</u>	<u>2017</u>	<u>2018</u>	<u>Total</u>
Incurred deductions:				
Losses	52.61%	92.69%	39.77%	62.06%
Loss adjustment expense	2.42	2.33	2.58	2.44
Commissions	20.43	15.77	18.66	18.29
Salaries	13.80	11.77	15.64	13.70
Taxes, licenses and fees	2.68	2.41	2.79	2.62
Other underwriting expenses	<u>6.49</u>	<u>11.04</u>	<u>10.97</u>	<u>9.45</u>
Total deductions	<u>98.43%</u>	<u>136.01%</u>	<u>90.41%</u>	<u>108.56%</u>
Underwriting gain or (loss)	<u>1.57%</u>	<u>(36.01%)</u>	<u>9.59%</u>	<u>(8.56%)</u>

REINSURANCE

The Association has reinsurance contracts in force as of December 31, 2018 with an authorized insurer which provide 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 a recovery of \$4,000,000 in excess of \$1,000,000 for each risk. Third layer has a 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.

Property 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 \$1,500,000 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, 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 Quota Share

While facultative reinsurance as 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.

The Association owns 100 percent of the Mitchell County Mutual Insurance Agency, Inc. dba Town & Country Insurance Agency. This agency produced approximately 52 percent of the Association's business during 2018. The Association shares no portion of Home Office building space with the agency. There are no expenses being shared. The Association's manager also manages the wholly-owned agency. Agency remuneration relating to that individual are paid directly by the agency. Starting in 2015, the agency began paying the mutual a management fee of \$2,500 per month.

ACCOUNTS AND RECORDS

Office copies of the filed annual statements for the years under review were found to be in agreement with or reconciled to the general ledger balances of assets, liabilities, income and disbursements.

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.

As stated in last exam, investment purchases and sales should be recorded at the trade date. Care should be taken to properly record these transactions.

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 \$582,904,770. The Association's statutory minimum surplus level as of December 31, 2018 was \$582,905. It is noted the Association's surplus level to minimum surplus level ratio was 7.05/1. The reported surplus/statutory minimum ratio average for the Chapter 518 licensed industry at December 31, 2018 was 7.90/1.

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	\$2,864,797	\$	\$	\$2,864,797
Stocks	1,379,292	308,925		1,688,217
Bank balances:				
Subject to check	13,450			13,450
On interest	518,886			518,886
Real estate	73,264		22,131	51,133
Cash in office	100			100
Unpaid premiums:				
Due after November 1		48,085		48,085
Accrued interest		27,170		27,170
Equipment and furniture	3,807		3,807	
Federal income tax recoverable		27,522		27,522
EDP equipment	5,498		1,866	3,632
Premium tax credit receivable		898		898
Contingency receivable		7,311		7,311
	<hr/>	<hr/>	<hr/>	<hr/>
Total	\$4,859,094	\$ 419,911	\$ 27,804	\$5,251,201

LIABILITIES AND SURPLUS

Losses	\$ 125,461
Unpaid adjusting expenses	2,708
Ceded reinsurance balances payable	61,083
Unpaid salaries and commissions	6,150
Amounts withheld for the account of others	2,966
Taxes payable	4,434
Other unpaid expenses	5,647
Employee benefits payable	7,487
Premiums collected for other companies - not remitted	8,677
Premiums received in advance	38,817
Unearned premium reserve	878,000
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Total liabilities	\$1,141,430
Surplus as regards policyholders	4,109,771
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Total liabilities and surplus	\$5,251,201

INCOME AND DISBURSEMENTS
AND
RECONCILIATION OF LEDGER ASSETS

Ledger assets, December 31, 2017			<u>\$4,527,278</u>
	<u>INCOME</u>		
Net premiums and fees			\$1,438,312
Net interest received on bonds			98,548
Increase (Decrease) by adjustment - bonds			(9,016)
Dividends received			33,247
Interest received on bank deposits			2,727
Profit on sale of investments			62,661
Rents received			6,175
Premiums collected for other companies			130,823
Federal income tax refund			145,655
Miscellaneous income			32,500
Total income			<u>\$1,941,632</u>
Total assets and income			<u>\$6,468,910</u>
	<u>DISBURSEMENTS</u>		
Losses paid			\$ 662,233
<u>Operating Expense</u>			
Adjusting expense	\$ 39,760		
Commissions	273,673		
Advertising	8,641		
Boards, bureaus and associations	7,810		
Inspection and loss prevention	4,269		
Salaries of officers	105,000		
Salaries of office employees	128,823		
Employee welfare	18,816		
Insurance	15,103		
Directors' compensation	9,450		
Directors' expenses	598		
Rent and rent items	6,175		
Equipment	28,650		
Printing and stationary and supplies	4,828		
Postage and telephone	22,854		
Legal and auditing	13,787		
State insurance taxes	22,084		
Insurance Division licenses and fees	415		
Payroll taxes	17,916		
All other taxes (excluding federal income)	597		
Real estate expenses	10,179		
Real estate taxes	2,336		
Miscellaneous	22		
Donations	2,600		
Annual meeting and conventions	6,371		
Travel and travel items	844		
Over and short	(5)		
Total operating expense			751,596
<u>Non-Operating Expense</u>			
Depreciation on real estate			2,932
Loss on sale of investments			17,559
Federal income tax			42,500
Premium collections transmitted to other companies			109,117
Commissions paid agents for other companies			23,771
Decrease in ledger liabilities			108
Total disbursements			<u>\$1,609,816</u>
Balance - ledger assets, December 31, 2018			<u>\$4,859,094</u>

UNDERWRITING AND INVESTMENT EXHIBIT

ONE-YEAR PERIOD ENDED DECEMBER 31, 2018

STATEMENT OF INCOME

<u>Underwriting Income</u>	
Premiums earned	\$1,494,647
<u>Deductions</u>	
Losses incurred	\$ 594,444
Loss expenses incurred	38,568
Other operating expenses incurred	718,367
Total underwriting deductions	<u>1,351,379</u>
Net underwriting gain (loss)	\$ 143,268
<u>Investment Income</u>	
Net investment income earned	166,670
<u>Other Income</u>	
Premiums collected for other companies (net)	(1,931)
Miscellaneous income	<u>39,811</u>
Net income before Federal income tax	\$ 347,818
Federal income tax incurred	<u>(130,677)</u>
Net income	<u>\$ 478,495</u>

CAPITAL AND SURPLUS ACCOUNT

Surplus as regards policyholders, December 31, 2017	<u>\$3,680,520</u>
<u>Gains and (Losses) in Surplus</u>	
Net income	\$ 478,495
Change in not admitted assets	1,225
Change in net unrealized gains/losses	<u>(50,469)</u>
Change in surplus as regards policyholders for the year	<u>\$ 429,251</u>
Surplus as regards policyholders, December 31, 2018	<u>\$4,109,771</u>

UNDERWRITING AND INVESTMENT EXHIBIT

THREE-YEAR PERIOD ENDED DECEMBER 31, 2018

STATEMENT OF INCOME

<u>Underwriting Income</u>		
Premiums earned		\$4,688,466
<u>Deductions</u>		
Losses incurred	\$2,909,790	
Loss expenses incurred	114,399	
Other operating expenses incurred	2,066,257	
Total underwriting deductions	<u>5,090,446</u>	
Net underwriting gain (loss)		\$ (401,980)
<u>Investment Income</u>		
Net investment income earned		492,770
<u>Other Income</u>		
Premiums collected for other companies (net)		(2,524)
Miscellaneous income		<u>100,127</u>
Net income before Federal income tax		\$ 188,393
Federal income tax incurred		<u>(119,481)</u>
Net income		<u>\$ 307,874</u>

CAPITAL AND SURPLUS ACCOUNT

Surplus as regards policyholders, December 31, 2015		<u>\$3,487,246</u>
<u>Gains and (Losses) in Surplus</u>		
Net income	\$ 307,874	
Change in not admitted assets	7,886	
Change in net unrealized gains/losses	<u>306,765</u>	
Change in surplus as regards policyholders for the period		<u>\$ 622,525</u>
Surplus as regards policyholders, December 31, 2018		<u>\$4,109,771</u>

SURPLUS AS REGARDS POLICYHOLDERS

The changes which resulted in the net increase 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>			
Stocks	\$1,707,918	\$1,688,217	\$ (19,701)
Unpaid premiums	27,735	48,085	20,350
Federal income tax recoverable		27,522	27,522
Premium tax credit receivable		898	898
<u>Liabilities</u>			
Losses	115,600	125,461	(9,861)
Unpaid adjusting expenses	5,000	2,708	2,292)
Unpaid salaries and commissions	3,421	6,150	(2,729)
Premiums received in advance	39,642	38,817	825
Unearned premium reserve	870,000	878,000	(8,000)
Net change to surplus			\$ 11,596
Surplus per Association			<u>4,098,175</u>
Surplus per examination			<u>\$4,109,771</u>

During the period under review, surplus funds increased \$622,525 from the amount of \$3,487,246 as shown in the last previous examination report. An operating statement reflecting the increase is contained in the financial section.

COMMENTS

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

Stocks \$1,688,217

This asset was decreased by \$19,701 to reflect the proper valuation of the wholly owned subsidiary agency.

Unpaid premiums \$ 48,085

This asset was increased by \$20,350 to reflect the actual amount of premiums received in 2019.

Federal income tax recoverable \$ 27,522

This asset of \$27,522 was established to reflect the income tax refund received in 2019.

Premium tax credit receivable \$ 898

This asset of \$898 was established to reflect the premium tax credit applied to 2019.

Losses \$ 125,461

This liability was increased by \$9,861 to reflect actual loss development.

Unpaid adjusting expenses \$ 2,708

An analysis of paid adjusting expenses to paid losses decreased this liability by \$2,292.

Unpaid salaries and commissions \$ 6,150

This liability was increased by \$2,729 to reflect the actual commissions paid on premiums receivable.

Premiums received in advance \$ 38,817

This liability was decreased by \$825 to remove liability premiums previously included in the calculation.

Unearned premium reserve \$ 878,000

A recalculation of unearned premium reserve using examination adjustments increased this liability by \$8,000.

CONCLUSION

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

Respectfully submitted,

 /s/ Jessica Jensen
Jessica Jensen
Cain Ellsworth & Co. LLP
Representing the State of Iowa