

EXAMINATION REPORT OF
FARM AND HOME SECURITY MUTUAL INSURANCE ASSOCIATION
WASHINGTON COUNTY, WASHINGTON, IOWA
AS OF DECEMBER 31, 2013

Washington, Iowa
August 26, 2014

HONORABLE NICK GERHART
Commissioner of Insurance
State of Iowa
Des Moines, Iowa

Commissioner Gerhart:

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

FARM AND HOME SECURITY MUTUAL INSURANCE ASSOCIATION

WASHINGTON COUNTY, WASHINGTON, IOWA

AS OF DECEMBER 31, 2013

at its Home Office, 102 South Iowa Street, Washington, Iowa. The report, containing applicable comments and financial data, is presented herein.

INTRODUCTION

The Farm and Home Security Mutual Insurance Association, hereinafter referred to as the "Association", was last examined as of December 31, 2009. The examination reported herein was conducted by the Iowa Insurance Division.

SCOPE OF EXAMINATION

This examination covers the period from December 31, 2009 to December 31, 2013. The examination was conducted in accordance with the procedures established by the Insurance Division of Iowa and generally accepted insurance examination standards.

The examination was conducted in accordance with procedures recommended by the Financial Condition (E) Committee of the N.A.I.C., and other generally accepted insurance examination standards. A general review and survey was made of the Association's operations and business transactions conducted during the stated period. Accounting methods, internal control procedures, records and other supporting evidences were examined or tested by appropriate methods to the extent deemed adequate. 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, 2013.

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 1955.

Effective January 1, 2008, the Articles of Incorporation were amended and substituted to change the corporate structure to a state mutual insurance association under Chapter 518A, Code of Iowa. At the same time the name was changed from Farmers Mutual Insurance Association of Washington, Iowa to Farm and Home Security Mutual Insurance Association.

MANAGEMENT AND CONTROL

MEMBERSHIP

The membership consists of every individual, co-partnership, public or private corporation, board or association, trustee, administrator, executor, organization or other legal entity having insurance herein by the Association which is in full force and effect.

The annual meeting of the members is held at Washington, Iowa on the second Friday in March of each year at 1:30 p.m. Special meetings shall be called by the President upon request of the majority of the members of the Board of Directors or upon written request of one-fourth of the members of the Association. Due notice of the time and place of special meetings shall be given the membership as specified in the Bylaws. The private property of the members shall be exempt from Association debts. Each member present at any meeting shall be entitled to one vote on each question voted on at any membership meeting regardless of the number of policies owned by the member. Voting by proxy is not permitted. A quorum shall be one more member than the number of directors fixed by Resolution of the Board of Directors.

BOARD OF DIRECTORS

The corporate powers of the Association are vested in a Board of not less than five nor more than ten directors, each elected by a majority vote at the annual meeting of the members for a term not to exceed three years. Any vacancy on the Board may be filled for the unexpired term by a majority vote of the remaining directors or the office declared vacant. Upon the death or resignation, or expiration of term of office of any director, the Board, by Resolution, may decrease the size of the Board and vacate the office, in which case no successor shall be elected; but in no event shall the Board at any time consist of less than five members.

Directors serving at December 31, 2013 were:

<u>Name</u>	<u>Address</u>	<u>Term Expires</u>
Michael I. Wood	Washington, Iowa	2015
Susan N. Fisher	Washington, Iowa	2015
Charles Limoges	Ainsworth, Iowa	2016
Tammy J. Roth	Washington, Iowa	2017
Roger L. Adam	Washington, Iowa	2017

The annual meeting of the Board shall be held immediately after the adjournment of the annual meeting of the membership, and thereafter on the call of the President. A majority of the number of directors fixed by Resolution shall constitute a quorum for the transaction of business, unless a greater number is required by the Bylaws.

Directors receive a fee of \$600 for each regular meeting attended and reimbursement for travel expense.

The directors approved the fee of \$100 per special meeting, executive and investment committee meetings fee at \$100 and other committee meetings at \$50 per meeting, plus mileage.

OFFICERS

At its annual meeting, the Board of Directors shall elect for a term of one year a President, Vice President, Secretary/Chief Executive Officer and Treasurer. Any of such offices may be combined, except the offices of President and Secretary.

Officers serving at December 31, 2013 were:

<u>Name</u>	<u>Office</u>
Michael I. Wood	President
Susan N. Fisher	Vice President
Charles Limoges	Treasurer
Barbara J. Wood	Secretary/Chief Executive Officer

Salaries and remunerations are shown in Exhibit A following this report.

COMMITTEES

The Board of Directors at its annual March re-organizational meeting appoints an Executive and Investment Committee. The Executive Committee is comprised of the entire board. The Executive Committee shall meet on the call of the Secretary. In such meetings, a majority shall constitute a quorum.

Serving on the Investment Committee at December 31, 2013 were:

Barbara Wood - Secretary/Chief Executive Officer
Michael I. Wood - President
Charles Limoges - Treasurer

CONFLICT OF INTEREST

Conflict of interest statements were signed annually by all officers, directors and key employees. Disclosures were indicated on the statements. One form was missing proper disclosure.

CORPORATE RECORDS

The Bylaws were amended during the period covered by this examination.

On March 9, 2012, the Bylaws were amended by unanimous vote to eliminate the age 72 restriction.

The Articles of Incorporation were not amended 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 were silent regarding approval of the Examination Report as of December 31, 2009.

AFFILIATED AGENCY

The Association owns its Home Office building and shares a portion of the space with Associated Insurance Services, Inc.

Associated Insurance Services, Inc., a wholly owned subsidiary, was formed in June of 2009 with the initial capitalization of \$5,000 representing 10 shares of common stock at \$500 par value. The subsidiary's officers and directors are the same as those for the Association.

The agency writes office walk-in business directly with the Association. The agency produced 9 percent of the Association's business during 2013.

The Association does not have a written and signed Agency contract with Associated Insurance Services, Inc.

The Board of Directors for the agency approved monthly payments of \$50 rent and \$50 management fee to be paid to the Association. The Association did not receive such payments during 2013 due to the limited business volume and funds availability of the agency. All rents and management fees have been waived.

FIDELITY BONDS AND OTHER INSURANCE

The Association is protected by a blanket bond in the amount of \$150,000 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 business personal property
- Business liability
- Employment practices liability
- Commercial liability umbrella
- Commercial inland marine
- Business automobile

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

Regular full-time eligible employees and their dependents are reimbursed for health insurance premiums. The amount is set by the board on an individual basis.

The eligible employee may elect to participate in the flexible pretax plan including non-employee sponsor premiums, medical expense and child care. The pretax plan includes but is not limited to long-term disability, short-term disability, dental, vision, individual life and accidental death and dismemberment insurance which the premiums are paid by the employee. The eligible employees are also offered group life insurance. These premiums are paid by the Association.

Retirement benefit to a Simplified Employee Pension/Individual Retirement Account (SEP/IRA) fund was also provided to full-time eligible employees whereby the Association contributed eight percent of the employee's gross salary or wage, exclusive of overtime, to the employee selected retirement fund. Contributions of \$19,542 (2010), \$15,760 (2011), \$18,769 (2012), and \$20,049 (2013) were paid by the Association.

REINSURANCE

The Association has reinsurance contracts in force as of December 31, 2013 with an authorized insurer which provide the following:

Individual Occurrence of Loss Excess

Fire, Lightning and Extended Coverage (Other Than Windstorm and Hail)

One hundred percent in excess of \$75,000 at one location, arising out of one event, insured on one or more policies, up to the limit stated in the coverage schedule.

Windstorm and Hail (Excluding Hail on Growing Crops)

One hundred percent in excess of \$75,000 at one location, arising out of one windstorm or hailstorm, insured on one or more policies; and/or the total of losses occurring on items insured on one policy at multiple locations arising out of one windstorm or hailstorm.

Aggregate Excess of Loss

Fire, Windstorm and Extended Coverages:

One hundred percent of the amount in excess of \$602,776 for the net aggregate loss occurring during the 2013 contract year subject to the following limitations:

Livestock/Poultry/Horse Operations: including swine and poultry confinements, dairy, beef and veal operations, and horse training and boarding facilities. \$1,000,000

Commercial and Public Property: including community halls, schools, churches, agribusiness risks and other commercial type risks. \$1,000,000

Farm Product Storage Structures: including farm product storage buildings and grain storage operations. This class does **not** include livestock, poultry, horse operations or farm machinery and equipment storage buildings. \$1,000,000

Farm Machinery and Equipment Storage Buildings: including farm outbuildings or other structures used to store mobile farm machinery and/or other farm equipment and tools. This class does **not** include livestock, poultry, horse operations or farm product storage structures. \$2,000,000

Dwelling: including dwelling, contents, additional living expense, other structures, and scheduled personal property coverages. \$1,000,000

Service Line

The reinsurer will reinsure 100 percent of the liability.

Earthquake

The reinsurer will reinsure 100 percent of each loss.

Pollution Clean Up and Removal

The reinsurer will reinsure 100 percent of the liability.

Facultative

Risks in excess of the Association's reinsurance contract limits may be ceded on a facultative basis. As of December 31, 2013, there were no risks identified that warranted facultative agreements.

Reinsurance - General

The Association appears to comply with current statutory standards relative to surplus exposure and reinsurance coverage.

MARKET CONDUCT

TERRITORY AND PLAN OF OPERATION

The Association is authorized to transact business in the State of Iowa as a state mutual insurance association under the provisions of Chapter 518A, Code of Iowa. It is currently authorized to transact business in sixteen counties in the State of Iowa. The permitted writing territory is composed of the following counties:

Johnson, Iowa, Keokuk, Washington, Louisa, Jefferson, Henry, Tama, Benton, Linn, Poweshiek, Cedar, Mahaska, Muscatine, Wapello, and Des Moines.

PRODUCER LICENSING

At the present time, business is produced by 28 licensed agents.

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

ADVERTISING

The Association's advertising material was reviewed during the examination period with no violations noted under the provisions of the Iowa Administrative Code.

RATING AND STATISTICAL REPORTING

The Association is neither a member of nor a subscriber to any rating bureau or statistical reporting agency.

POLICY FORMS AND UNDERWRITING PRACTICES

The Association has policies in force on farm personal property, homeowners and country homeowners classes in insurance covering fire, allied lines and inland marine.

Policy and endorsement forms have been filed and approved. The policies and endorsements utilized by the Association are approved by the Board of Directors prior to usage.

TREATMENT OF POLICYHOLDERS

CLAIMS

Adjustment of claims is handled primarily by the Association's salaried Home Office personnel. Numerous claims files were reviewed, including closed by

payment, closed without payment and open files to determine adequacy of loss reserves and the treatment of policyholders. Of the claims reviewed, 100 percent were paid within 30 days from the date sufficient information was received to pay the claim.

COMPLAINT REGISTER

A review was made of all written complaints received by the Association during the period under examination. The one formal insurance division complaint was handled fairly and in a timely manner.

GROWTH OF THE ASSOCIATION

The following historical financial data, taken from annual statements for the years indicated, reflects the growth of the Association:

<u>Year</u>	<u>Admitted Assets</u>	<u>Surplus to Policyholders</u>	<u>Net Premiums Earned</u>	<u>Net Losses Incurred</u>	<u>Investment Income Earned</u>
2010	4,279,550	3,548,105	983,575	232,327	62,338
2011	4,261,944	3,578,066	963,681	364,429	87,612
2012	4,600,389	3,849,178	911,169	229,650	71,679
2013	4,986,326	4,150,781	985,675	341,422	79,302

UNDERWRITING EXPERIENCE

Underwriting experience as reflected by the Association's annual statements for the four-year period ended December 31, 2013 was as follows:

	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>Total</u>
Premiums earned	\$983,575	\$963,681	\$911,169	\$ 985,675	\$3,844,100
<u>Incurred deductions:</u>					
Losses	232,327	364,429	229,650	317,747	1,144,153
Loss adjustment expenses	110,857	80,340	122,213	127,092	440,502
Commissions	169,430	164,783	166,828	192,834	693,875
Salaries	113,794	118,100	121,614	121,704	475,212
Taxes, licenses and fees	11,896	22,693	11,846	11,286	57,721
Other underwriting expenses	<u>202,491</u>	<u>192,132</u>	<u>212,016</u>	<u>249,551</u>	<u>856,190</u>
Total deductions	<u>\$840,795</u>	<u>\$942,477</u>	<u>\$864,167</u>	<u>\$1,020,214</u>	<u>\$3,667,653</u>
Net underwriting gain (loss)	<u>\$142,780</u>	<u>\$ 21,204</u>	<u>\$ 47,002</u>	<u>\$ (34,539)</u>	<u>\$ 176,447</u>

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

	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>Total</u>
<u>Incurred deductions:</u>					
Losses	23.6%	37.8%	25.2%	32.2%	29.8%
Loss adjustment expenses	11.3%	8.3%	13.4%	12.9%	11.5%
Commissions	17.2%	17.1%	18.3%	19.6%	18.1%
Salaries	11.6%	12.3%	13.3%	12.3%	12.4%
Taxes, licenses and fees	1.2%	2.4%	1.3%	1.1%	1.5%
Other underwriting expenses	<u>20.6%</u>	<u>19.9%</u>	<u>23.3%</u>	<u>25.3%</u>	<u>22.3%</u>
Total deductions	<u>85.5%</u>	<u>97.8%</u>	<u>94.8%</u>	<u>103.4%</u>	<u>95.6%</u>
Net underwriting gain (loss)	<u>14.5%</u>	<u> 2.2%</u>	<u> 5.2%</u>	<u>(3.4)%</u>	<u> 4.4%</u>

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 independent Board of Director members approved the salaries of the officers and employees. The remaining Board members did not ratify the salaries due to conflicts.

Management, Discussion and Analysis should be reported per the NAIC prescribed form.

A custodial agreement update is needed to recognize the change in name.

Health insurance premium reimbursements received by employees were not reported on the W-2. It is recommended the Association research IRS requirements in this regard.

In lieu of expense reports or credit cards, the Association issues debit cards to each employee to cover company expenses. During the exam it was noted that monthly bank reconciliations are not performed on this account. It was also noted that the balance on the bank statement did not tie to the general ledger. Greater care should be exercised to ensure this account is reconciled on a monthly basis. Upon review of debit card transactions it was noted that some receipts were missing to support and substantiate the business expense. Greater care should be exercised to ensure that receipts or other documents are obtained to substantiate the business expense.

The Association was in compliance with the Commissioner's Bulletin 97-6 at December 31, 2013 relative to security custodial requirements.

In accordance with Section 518A.37, Code of Iowa, surplus must be maintained at a level of not less than one hundred thousand dollars or one-tenth of one percent of the gross risk in force, whichever is greater. At December 31, 2013, the gross risk in force for the Association was \$307,466,520. The Association's statutory minimum surplus level as of December 31, 2013 was \$307,467. It is noted the Association's surplus level to minimum surplus level ratio was 13.57/1. The reported surplus/statutory minimum ratio average for the Chapter 518A licensed industry at December 31, 2013 was 9.87/1.

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, 2013 and the assets and liabilities as of this date. Schedules may not add or tie precisely due to rounding

STATEMENT OF ASSETS AND LIABILITIES

	<u>ASSETS</u>		
	<u>Assets</u>	Not <u>Admitted</u>	<u>Admitted</u>
Bonds	\$2,568,147	\$ 859	\$2,567,288
Common stocks	1,770,099	602	1,769,497
Cash	122,729	402	122,327
Short-term investments	109,963		109,963
Real estate			
Properties occupied by Company	160,780		160,780
Properties held for production of income			
Investment income due and accrued	30,344		30,344
Premiums and considerations:			
Uncollected premiums	28,288	2,146	26,142
Deferred premiums	170,253		170,253
Reinsurance receivable	5,085		5,085
Electronic data			
processing equipment	22,927	6,365	16,562
Furniture and equipment	5,917	5,917	0
Transportation equipment	13,476	13,476	0
Total	<u>\$5,008,008</u>	<u>\$ 29,767</u>	<u>\$4,978,241</u>

LIABILITIES AND SURPLUS

Losses	\$ 18,965
Loss adjustment expenses	9,821
Commissions payable	48,242
Other expense	26,630
Tax, license and fees	3,886
Unearned premiums	638,936
Advance premiums	23,355
Ceded reinsurance premiums payable	21,629
Amounts withheld or retained by Company for account of others	<u>14,536</u>
Total liabilities	\$ 806,000
Surplus as regards policyholders	<u>4,172,241</u>
Total liabilities and surplus	<u>\$4,978,241</u>

UNDERWRITING AND INVESTMENT EXHIBIT

ONE YEAR PERIOD ENDED DECEMBER 31, 2013

STATEMENT OF INCOME

<u>Underwriting Income</u>	
Premiums earned	\$ 985,675
<u>Deductions</u>	
Losses incurred	\$317,747
Loss expenses incurred	127,092
Other operating expenses incurred	<u>575,375</u>
Total underwriting deductions	<u>1,020,214</u>
Net underwriting gain (loss)	\$ (34,539)
<u>Investment Income</u>	
Net investment income earned	59,561
Net realized capital gains	19,740
<u>Other Income</u>	
Premiums collected for other companies (net)	14,740
Miscellaneous income	<u>1,975</u>
Net income before Federal income tax	\$ 61,477
Federal income tax incurred	<u>(7,246)</u>
Net income	<u>\$ 68,723</u>

CAPITAL AND SURPLUS ACCOUNT

Surplus as regards policyholders, December 31, 2012	<u>\$3,849,178</u>
<u>Gains and (Losses) in Surplus</u>	
Net income	\$ 68,723
Change in not admitted assets	(2,837)
Change in net unrealized gains/losses	<u>257,177</u>
Change in surplus as regards policyholders for the year	<u>\$ 323,063</u>
Surplus as regards policyholders, December 31, 2013	<u>\$4,172,241</u>

UNDERWRITING AND INVESTMENT EXHIBIT

FOUR YEAR PERIOD ENDED DECEMBER 31, 2013

STATEMENT OF INCOME

<u>Underwriting Income</u>	
Premiums earned	\$3,844,100
<u>Deductions</u>	
Losses incurred	\$1,144,153
Loss expenses incurred	440,502
Other operating expenses incurred	<u>2,082,998</u>
Total underwriting deductions	<u>3,667,653</u>
Net underwriting gain (loss)	<u>\$ 176,447</u>
<u>Investment Income</u>	
Net investment income earned	286,061
Net realized capital gains	14,870
<u>Other Income</u>	
Premiums collected for other companies (net)	26,588
Miscellaneous income	<u>8,395</u>
Net income before Federal income tax	\$ 512,361
Federal income tax incurred	<u>2,187</u>
Net income	<u>\$ 510,174</u>

CAPITAL AND SURPLUS ACCOUNT

Surplus as regards policyholders, December 31, 2010	<u>\$3,179,303</u>
<u>Gains and (Losses) in Surplus</u>	
Net income	\$ 510,174
Change in not admitted assets	471,563
Change in net unrealized gains/losses	<u>11,201</u>
Change in surplus as regards policyholders for the year	<u>\$ 992,938</u>
Surplus as regards policyholders, December 31, 2013	<u>\$4,172,241</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>			
Bonds	\$2,568,147	\$2,567,288	\$ (859)
Common Stocks	1,770,099	1,769,497	(602)
Cash	122,729	122,327	(402)
Uncollected premiums and agents' balances	25,999	26,142	143
Electronic data processing equipment & software	22,927	16,562	(6,365)
<u>Liabilities</u>			
Net unpaid claims	42,640	18,965	23,675
Unpaid adjusting expenses	18,800	9,821	8,979
Unpaid salaries and commissions	39,122	48,242	(9,120)
Taxes payable	5,717	3,886	1,831
Other unpaid expenses	20,551	26,630	(6,079)
Amounts withheld or retained by company for account of others	24,800	14,536	<u>10,264</u>
Net change to surplus			\$ 21,465
Surplus per Association			<u>4,150,776</u>
Surplus per examination			<u>\$4,172,241</u>

During the period under review, surplus funds increased \$932,873 from the amount of \$3,239,368 as shown in the last previous examination report. An operating statement reflecting that increase is contained in the financial section.

COMMENTS

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

Bonds \$2,567,288

The asset was decreased \$859 to properly value bonds below investment grade.

Common Stock \$1,769,497

The asset was decreased \$602 to reflect the proper valuation of the wholly owned subsidiary agency.

Cash \$122,327

The asset was decreased \$402 to reflect the correct reconciled balance.

Uncollected premiums and agents' balances \$26,142

The asset was increased \$143 to reflect the actual premiums received during 2014.

Electronic data processing equipment and software \$16,562

The asset was decreased \$6,365 to non-admit software.

Net unpaid claims \$18,965

The net unpaid claims were decreased \$23,675 to reflect current loss development.

Unpaid adjusting expense \$9,821

An analysis of paid adjusting expenses to paid losses decreased the liability by \$8,979.

Unpaid salaries and commission \$48,242

Salaries and commissions paid during 2014 but incurred in 2013 were compared to the year-end accrual amount increasing the liability \$9,120.

Taxes payable \$3,886

Taxes paid during 2014 but incurred in 2013 were compared to the year-end accrual amount increasing the liability \$1,831.

Other unpaid expenses \$26,630

Items paid during 2014 but incurred in 2013 were compared to the year-end accrual amount increasing the liability \$6,079.

Amounts withheld or retained by company for account of others \$14,536

The liability was decreased \$10,264 to adjust to actual amounts per reports.

CONCLUSION

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

Respectfully submitted,



Abby De Zeeuw, CPA
Cain Ellsworth & Co. LLP
Representing the State of Iowa