

MARKET CONDUCT
EXAMINATION REPORT OF
FARMERS MUTUAL HAIL INSURANCE COMPANY OF IOWA
WEST DES MOINES, IOWA
AS OF DECEMBER 31, 2011

West Des Moines, Iowa
November 26, 2012

HONORABLE SUSAN E. VOSS
Commissioner of Insurance
Insurance Division
State of Iowa
Des Moines, Iowa

Commissioner:

In accordance with your authorization and pursuant to Iowa statutory provisions, a market conduct examination has been made of the records, business and marketing practices of

FARMERS MUTUAL HAIL INSURANCE COMPANY OF IOWA

WEST DES MOINES, IOWA

AS OF DECEMBER 31, 2011

at its Home Office, 6785 Westown Parkway, West Des Moines, Iowa.

INTRODUCTION

The examination report, containing applicable comments, explanations and findings, is presented herein. In general, this is a report by exception. Comments regarding practices and procedures reviewed during the examination have been omitted from the report if no improprieties were found.

SCOPE OF EXAMINATION

Farmers Mutual Hail Insurance Company of Iowa, hereinafter referred to as the "Company", was previously examined as of December 31, 2006. This market conduct examination covers the intervening period from December 31, 2006 to the close of business on December 31, 2011. It was conducted and performed solely for the Iowa Insurance Division by its examiners. A general review and survey was made of the Company's marketing operations and treatment of policyholders for statutory compliance during the stated period. Other supporting evidences have been examined and evaluated to the extent deemed necessary.

In conjunction with the examination of Farmers Mutual Hail Insurance Company of Iowa, the Company's wholly owned subsidiary, Farmer Union Co-Operative Insurance Company, Inc., was examined by examiners of the Iowa Insurance Division.

HISTORY

The Company was incorporated on March 4, 1893 as a crop hail assessment insurance association under the name of Farmers Mutual Hail Association of Iowa, with its Home Office located in Early, Iowa. In 1941, the Company adopted its present name, Farmers Mutual Hail Insurance Company of Iowa and in 1950 the Company's existence was made perpetual. In addition, the issuance of non-assessable policies and the writing of multiple lines were approved.

In 1895, the Home Office was moved to Des Moines, Iowa and in 2005 the principle place of business was moved to West Des Moines, Dallas County, Iowa.

Through mergers, the General Mutual Insurance Company, Des Moines, Iowa and the Property Owners Mutual Insurance Company, St. Paul, Minnesota, were acquired in 1932 and 1957, respectively. In 1994, the Company executed a merger agreement with Wheat Growers Mutual Insurance Company, a Kansas insurer. The Company issued assumption of policy obligations and liability endorsement certificates to all Wheat Growers' policyholders.

On April 1, 2011, Central Iowa Mutual Insurance Association (CIM) merged into the Company. The Company issued assumption of policy obligations and liability endorsement certificates to all CIM policyholders. As a result of the statutory merger, the Company also owns 100% of the stock in C.I.M. Insurance Agency, Inc.

TERRITORY AND PLAN OF OPERATION

The Company is licensed to write business in 36 jurisdictions and is a qualified reinsurer in 8 jurisdictions. Direct written premiums totaled \$712,575,766 for 2011 with \$549,418,854, or 77%, written under the Multiple Peril Crop Insurance (MPCI) program. The remaining premium is primarily written in crop hail coverage with a small book of property/casualty business. The top five states representing direct written premiums are: Iowa 30%, Nebraska 11%, Kansas 11%, Minnesota 10% and Illinois 9%.

MPCI is a federally subsidized farm risk management program under the auspices of the Federal Crop Insurance Corporation (FCIC) and administered by the FCIC's Risk Management Agency (RMA). The program is designed to encourage farmers to share, through premium payments, in the federal government's risk management system. The current program, authorized by Congress in 1980 and modified in subsequent legislation, provides premium subsidies and reinsurance protection on eligible crop insurance contracts. The program is administered by the RMA and offered through private carriers pursuant to a Standard Reinsurance Agreement (SRA) contract.

The Company also assumes reinsurance, mainly from small to medium-sized regional companies. Direct products are marketed through a network of approximately 4,800 independent producers and its assumed reinsurance business through brokers.

LOSS PORTFOLIO ASSUMPTION

Prior to 2011, Farmers Union Co-Operative Insurance Company, Inc. (FUCIC) wrote private passenger auto and other liability lines of business for the county mutuals that the Company reinsures in Arkansas, Illinois, Iowa, Missouri, Nebraska and South Dakota. This business was written through approximately 230 independent agencies. FUCIC operated through a 100% quota share reinsurance agreement with the Company and therefore retained no premiums or underwriting liabilities. The Company entered into a loss portfolio assumption agreement for the FUCIC book of business that was in force as of April 1, 2011. As part of the novation, the Company booked \$1,519,229 of unearned premiums, \$3,754,354 of loss and loss adjustment reserves, and \$184,362 of commissions payable.

MARKETING AND SALES

The Company has implemented review and approval procedures for advertising materials. The Farmers Mutual Hail group utilizes various forms of marketing such as the internet, radio, magazine ads, and newspapers. The Company maintains a website at www.fmh.com. The advertising materials are primarily based on name recognition. The Company also offers a cost sharing program with the agency force.

PRODUCER LICENSING

The Company markets products through an independent agency force of approximately 4,800 producers associated with approximately 3,000 agencies. Upon the merger of Central Iowa Mutual Insurance Association and reinsurance assumption of Farmers Union Co-Operative Insurance Company, Inc. business, the Company failed to timely appoint approximately 470 Iowa producers writing the property and casualty business, in accordance with Iowa Administrative Code 191-10.15(1) and 191-10.15(6). For the period of time between April 1, 2011 and July 24, 2012, \$11,607,813 of premium was written by non-appointed producers and \$1,706,678 in commissions was paid associated with this business.

COMPLAINT HANDLING

The Company has complaint procedures and records that are in compliance with Iowa Administrative Code 191-15.13. Written and/or oral complaints received by the Company are reviewed by the appropriate adjuster, underwriter or legal counsel.

CLAIMS PRACTICES

The Company has written claims handling procedures and is required to follow federal regulations with respects to the adjudication of MPCCI claims. A study of claim practices found the Company to be in compliance with Iowa Administrative Code 191-15 and Iowa Code 507B.

UNDERWRITING EXPERIENCE

Direct underwriting experience, as taken from data filed with the N.A.I.C. for each of the years, is as follows:

<u>Classification</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>
Premiums earned	<u>\$369,906,425</u>	<u>\$544,031,551</u>	<u>\$472,551,769</u>
<u>Incurred deductions</u>			
Losses incurred	\$120,591,451	\$451,173,679	\$242,705,213
Defense and cost containment	(23,698)	191,013	271,285
Adjusting and other expenses	14,080,000	16,735,000	20,252,000
Commission and brokerage	77,621,937	105,287,485	98,246,770
Taxes, licenses and fees	1,168,385	2,312,044	1,971,532
Other acquisition expenses	10,257,000	11,022,000	13,091,000
General expenses incurred	<u>12,255,000</u>	<u>14,129,000</u>	<u>17,010,000</u>
Total deductions	<u>\$235,950,075</u>	<u>\$600,850,221</u>	<u>\$393,547,800</u>
Underwriting gain (loss)	<u>\$133,956,350</u>	<u>\$(56,818,670)</u>	<u>\$ 79,003,969</u>

<u>Classification</u>	<u>2010</u>	<u>2011</u>	<u>Total</u>
Premiums earned	<u>\$452,723,953</u>	<u>\$694,049,719</u>	<u>\$2,533,263,417</u>
<u>Incurred deductions</u>			
Losses incurred	\$208,435,881	\$441,411,126	\$1,464,317,350
Defense and cost containment	221,497	(871,664)	(211,567)
Adjusting and other expenses	20,702,000	22,889,000	94,658,000
Commission and brokerage	89,332,779	91,581,611	462,070,582
Taxes, licenses and fees	2,307,870	2,473,415	10,233,246
Other acquisition expenses	15,602,000	16,444,000	66,416,000
General expenses incurred	<u>23,525,000</u>	<u>26,852,000</u>	<u>93,771,000</u>
Total deductions	<u>\$360,127,027</u>	<u>\$600,779,488</u>	<u>\$2,191,254,611</u>
Underwriting gain (loss)	<u>\$ 92,596,926</u>	<u>\$ 93,270,231</u>	<u>\$ 342,008,806</u>

Expressed in the ratio of incurred deductions to premiums earned, the percentages are:

	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>Average</u>
<u>Incurred deductions</u>						
Losses incurred	32.6%	82.9%	51.3%	46.0%	63.6%	57.8%
Defense and cost containment	(0.0)	0.0	0.1	0.0	(0.1)	(0.0)
Adjusting and other expenses	3.8	3.1	4.3	4.6	3.3	3.7
Commission and brokerage	21.0	19.4	20.8	19.7	13.2	18.3
Taxes, licenses and fees	0.3	0.4	0.4	0.5	0.3	0.4
Other acquisition expenses	2.8	2.0	2.8	3.5	2.4	2.6
General expenses incurred	<u>3.3</u>	<u>2.6</u>	<u>3.6</u>	<u>5.2</u>	<u>3.9</u>	<u>3.7</u>
Total deductions	<u>63.8%</u>	<u>110.4%</u>	<u>83.3%</u>	<u>79.5%</u>	<u>86.6%</u>	<u>86.5%</u>
Underwriting gain (loss)	<u>36.2%</u>	<u>(10.4%)</u>	<u>16.7%</u>	<u>20.5%</u>	<u>13.4%</u>	<u>13.5%</u>

DIRECT UNDERWRITING EXPERIENCE BY STATE

<u>State</u>	<u>Five-Year Average Earned Premium</u>	<u>Five-Year Operating Ratio</u>	<u>2011 Earned Premium</u>	<u>2011 Operating Ratio</u>
Arkansas	\$ 4,510,378	89.7%	\$ 6,876,348	128.0%
Colorado	4,361,374	92.1	6,683,572	100.7
Illinois	48,773,999	71.5	64,613,760	58.4
Indiana	28,536,990	74.5	40,240,736	81.5
Iowa	151,905,784	84.3	214,275,120	60.7
Kansas	52,349,560	111.8	65,668,109	158.8
Michigan	2,157,763	64.9	4,578,166	70.8
Minnesota	55,109,722	78.2	71,168,516	87.8
Missouri	23,895,541	107.2	36,584,740	145.9
Nebraska	64,366,816	89.6	77,986,790	90.3
North Dakota	20,685,511	95.3	28,786,458	141.1
Ohio	7,293,080	70.6	11,345,158	59.6
Oklahoma	2,958,005	1.0	2,858,503	61.0
South Dakota	27,760,865	84.2	39,828,470	81.9
Wisconsin	11,987,297	71.8	22,555,273	41.1
Total	<u>\$506,652,685</u>	<u>86.5%</u>	<u>\$694,049,719</u>	<u>86.6%</u>

The Company is directly impacted by storm related losses and commodity pricing.

CONCLUSION

The cooperation and assistance extended by the officers and employees of the Company is hereby acknowledged.

In addition to the undersigned, Randy Guzman, Alex Matovu, and Bob Wong, CFE, Examiners for the Iowa Insurance Division, participated in the examination and preparation of this report.

Respectfully submitted,

/s/ Virginia West
VIRGINIA WEST, CFE
Examiner in Charge
Insurance Division
State of Iowa
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