



Report on Examination

of the

Farmers Mutual Fire Insurance Company of Warren County,
Tennessee

McMinnville, TN

as of

September 30, 2009

RECEIVED

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Dept. of Commerce & Insurance
Company Examinations

Department of Commerce and Insurance

State of Tennessee

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STATE OF TENNESSEE
DEPARTMENT OF COMMERCE AND INSURANCE
INSURANCE DIVISION
500 JAMES ROBERTSON PARKWAY - 4TH FLOOR
NASHVILLE, TENNESSEE 37243-1135

March 25, 2010

The Honorable Leslie A. Newman
Commissioner
Tennessee Department of Commerce and Insurance
500 James Robertson Parkway, 5th Floor
Nashville, Tennessee 37243

Commissioner Newman:

Pursuant to your instructions and in accordance with Tennessee statutes and regulations, and resolutions adopted by the National Association of Insurance Commissioners ("NAIC"), a financial examination has been made of the condition and affairs of

Farmers Mutual Fire Insurance Company of Warren County, Tennessee

671 River Cliff Road
P. O. Box 294
McMinnville, Tennessee 37111

("the Company") as of September 30, 2009, and the report thereon is hereby respectfully submitted.

SCOPE OF EXAMINATION

This examination commenced December 1, 2009, and covers the period from December 31, 2006, the date of the last examination, through September 30, 2009, in accordance with statutes, rules and procedures of the State of Tennessee. The examination was conducted at the Company's office, located at 671 River Cliff Road, McMinnville, Tennessee, 37111 and at the office of The Tennessee Department of Commerce and Insurance ("TDCI"). This examination was conducted by a duly authorized representative of the TDCI.

During the course of the examination, the assets of the Company were verified, and liabilities were determined or estimated as of September 30, 2009, in accordance with procedures as prescribed by Tenn. Code Ann. and Tenn. Comp. R. & Regs., of the State of Tennessee and the National Association of Insurance Commissioners (NAIC). The

Company's financial solvency and degree thereof was thus established. Test checks covering selected periods were made of income and disbursement items, and a general review was made of the Company's operations, practices and compliance with Tenn. Code Ann. and Tenn. Comp. R. & Regs., to the extent hereinafter set forth.

Location of Books and Records:

The Company maintains its books and records at the home of the Secretary / Treasurer, Ada Mai Church, which is located at 671 River Cliff Road, McMinnville, Tennessee, 37111.

In addition, the following topics were reviewed:

- Status of Prior Examination Findings
- Company History
- Charter and Bylaws
- Management and Control
- Pecuniary Interest Tenn. Code Ann. § 56-3-103
- Corporate Records
- Fidelity Bonds and Other Insurance
- Territory
- Plan of Operation
- Market Conduct Activities
- Reinsurance
- Loss Experience
- Accounts and Records
- Dividends
- Litigation and Contingent Liabilities
- Subsequent Events
- Financial Statement

Status of Prior Examination Findings

The previous examination of the Company was made as of December 31, 2006 by a TDCI examiner. The report of examination was dated June 2, 2008, and covered the period from January 1, 2002 through December 31, 2006. There were no recommendations made in the preceding Report on Examination pertaining to violations of Tennessee Code by the Company as of December 31, 2006. However, the Company, subsequent to the date of examination, was in violation of three (3) Tennessee statutes. A summary of each recommendation and the corrective actions taken by the Company are as follows:

Recommendations:

(1) The Company's "surplus over all liabilities" at no time since January 1, 2007 has met or exceeded \$200,000. Therefore, the Company was not in compliance with the minimum surplus requirements of Tenn. Code Ann. § 56-22-105(c) (effective January 1, 2007) as of the date this examination report was submitted to the Commissioner. It was recommended that the Company take the necessary steps to become compliant with Tenn. Code Ann. § 56-22-105(c).

Corrective Action: For the current period under review, the Company has yet to achieve compliance with the \$200,000 minimum surplus requirements of Tenn. Code Ann. § 56-22-105(c) (effective January 1, 2007).

(2) The Company has not maintained aggregate reinsurance coverage since 1997. As of January 1, 2007, Tenn. Code Ann. § 56-22-110 requires all county mutual insurance companies to carry an aggregate excess of loss insurance policy of no less than 5% of business in force. The amount required for such a policy shall be reduced by the county mutual insurance company's accumulated surplus. Therefore, the Company has not been in compliance with Tenn. Code Ann. § 56-22-110 since the January 1, 2007 effective date of this statute. It was recommended that the Company purchase the proper amount of aggregate reinsurance coverage in order to become compliant with Tenn. Code Ann. § 56-22-110.

Corrective Action: For the current period under review, the Company has not purchased aggregate reinsurance coverage in order to become compliant with Tenn. Code Ann. § 56-22-110 (effective January 1, 2007).

(3) The Company's agents as of December 31, 2006 were issued a special "Limited Insurance.Producer" agent's license specifically designed for those agents that worked for "county mutual" insurance companies. As of July 1, 2007 these "Limited Insurance Producer" agent's licenses were no longer effective. Tenn. Code Ann. § 56-22-113 requires agents to be licensed to sell property and/or casualty lines of insurance under Tenn. Code Ann. §§ 56-6-101, *et seq.* It was recommended that the Company's agents comply with Tenn. Code Ann. § 56-22-113 by taking the necessary steps in order to receive insurance licenses to write "property" and/or "casualty" lines of insurance coverage from the TDCI pursuant to Tenn. Code Ann. § 56-6-105, 106 and 107.

Corrective Action: As of September 30, 2009, the Company had one (1) agent that was licensed pursuant to Tenn. Code Ann. § 56-22-113 and Tenn. Code Ann. § 56-6-105, 106 and 107. However, effective December 18, 2009, a second agent of the Company was licensed pursuant to Tenn. Code Ann. § 56-22-113 and Tenn. Code Ann. § 56-6-105, 106 and 107.

History

The Company commenced business in 1910 under the statutes of Tennessee, as Farmers Mutual Fire Insurance Company of Warren County, Tennessee. The Company's Charter and first By-Laws were adopted in 1910. Also, the Company's first Board of Directors was elected and the Company's officers were appointed by the Board of Directors in 1910. Additionally, the Board of Directors established the following committees in 1910: Executive Committee, Adjusting Committee, Auditing Committee and Committee of Appeals. Finally, in 1910 the Board of Directors elected the Company's first General Agent.

The following historical information reflects an event that had a material negative impact on the Company's financial position. On October 22, 1977 a Special Meeting of the

Company's Board of Directors was held to decide how to handle a ruling by the I.R.S. concerning the Company's surplus. The I.R.S. informed the Company that it had accumulated an amount of surplus above an amount it considered acceptable. No documentation maintained by the Company noted a specific I.R.S. code that granted the I.R.S. the authority to require the Company to reduce its surplus. The Directors decided to create and maintain a minimum reserve or surplus fund of \$100,000. At that time \$100,000 was approximately 1% of insurance in force. Also, the Directors at the 1978 Annual Membership Meeting decided to return the entire surplus for the 1975 policy year to the policyholders on record as of December 31, 1975 in the form of a reduced premium. The total amount refunded was \$16,579.

The Company appointed Mr. Von Hall, First Vice President of the Company and employee of City Bank & Trust of McMinnville, TN to work with the I.R.S. on the excess surplus matter. Additional records related to this I.R.S. matter were kept by Mr. Hall. However, on September 30, 1996 he was killed in an automobile accident and the Company was unable to gain access to his records concerning this matter after his death.

Based upon verbal information provided by the Company's Secretary / Treasurer, Ada Mai Church, the Company contacted the TDCI regarding this matter sometime in 1977 or 1978.

The Company each year from 1978 through 1986 reduced policy premiums until the Company's surplus was at or below \$100,000.00.

Charter and Bylaws

There were no changes to the Company's Charter or Bylaws during the period of examination.

Management and Control

Management:

The Company's Charter and Bylaws require that the business and affairs of the Company shall be directed by a Board of Directors. As of September 30, 2009 the Board was composed of the following:

<u>NAME</u>	<u>TITLE</u>	<u>OCCUPATION</u>	<u>RESIDENCE</u>
Mrs. Anna Rhea Basham		Farmer	McMinnville, TN
Mrs. Ada Mai Church	Secretary & Treasurer	Farmer	McMinnville, TN
Mr. Robert Clendenon		Farmer	McMinnville, TN
Mr. Jerry Hildreth	Vice President	Farmer	Smithville, TN
Mr. Marvin Lusk		Farmer	McMinnville, TN
Mr. Jimmy Milstead		Farmer	McMinnville, TN
Mr. David Pendergraph		Farmer	McMinnville, TN
Mr. Phillip Prater		Farmer	McMinnville, TN
Mr. Richard Woods	President	Farmer	McMinnville, TN

Note: Officers of the Board of Directors are considered Officers of the Company.

Auditing Committee

NAME

Mr. Jerry Hildreth
Mr. Phillip Prater
Mr. Marvin Lusk

Adjusting Committee

NAME

Mr. Jerry Hildreth
Mr. David Pendergraph
Mr. Richard Woods

Committee of Appeal

NAME

Mrs. Anna Rhea Basham
Mr. Richard Woods
Mr. Jimmy Milstead
Mr. Robert Clendenon
Mr. Marvin Lusk
Mr. Phillip Prater
Mr. J. Morris Womack*

Note: Mr. J. Morris Womack was not an officer or director of the Company.

Control:

Control of a county mutual insurance company rests directly with its Board of Directors. However, the Company's policyholders pursuant to Tenn. Code Ann. § 56-22-107(a) are responsible for the election of the Board of Directors and decisions on issues brought before them by the Board of Directors.

The Company's Annual Meeting on the second Saturday in January is the venue for policyholders voting on the composition of the Board of Directors and any issues set before them by the Directors. The Company's Charter allows for special meetings of the policyholders as well as the Board of Directors.

PECUNIARY INTEREST - TENN. CODE ANN. § 56-3-103

The Company as of September 30, 2009 did not have a conflict of interest policy for its directors and officers. However, the Examiner found no instance of any officer or director having a pecuniary interest in the investment or disposition of Company funds in violation of Tenn. Code Ann. § 56-3-103.

CORPORATE RECORDS

Minutes of meetings of the Board of Directors of the Company were reviewed for the period under examination as well as minutes for meetings of various committees. In general, such minutes appear to be in proper order and accurately report the proceedings of each respective meeting.

FIDELITY BOND AND OTHER INSURANCE

Minimum fidelity bond coverage of \$15,000 to \$25,000 is suggested by guidelines published in the NAIC Financial Condition Examiners Handbook. The Company as of the September 30, 2009 date of examination had a \$10,000 Surety Bond in effect covering the Company's Secretary / Treasurer. Western Surety Company issued this Surety Bond and is a licensed property and casualty insurance company in the State of Tennessee. See the "Comments and Recommendations" section of this report for further discussion of fidelity bond coverage.

TERRITORY

As of September 30, 2009, and as of the date of this examination report, the Company was licensed to transact business in the State of Tennessee. The Company's Certificate of Authority was issued effective July 1, 1986 by the TDCI.

From January 1 through September 30, 2009, the Company wrote total direct premium of \$78,247 entirely in Warren County, Tennessee. Tenn. Code Ann. § 56-22-106(f)(1) allows the Company to "issue policies of insurance on property located in the county in which its principal place of business is located and in all those counties contiguous to the county in which its principal place of business is located".

PLAN OF OPERATION

The Company provides insurance against loss by fire, lightning, and wind. The Board of Directors on January 13, 2007 approved the addition of sinkhole collapse coverage without an increase in policy premium.

However, the Company's Charter and Bylaws did not reflect coverage for wind and sinkhole collapse. This finding is discussed further under the headings, "Comments and Recommendations".

Policies are typically written for two-thirds of the value of the property insured, subject to policy limits of \$14,000 per loss. The policy period for each policy was three (3) years. Premiums are paid annually and are due on February 1 of each year. There was a \$100 deductible for all wind losses. The agent performs the appraisal on the property prior to the issuance of a policy. Property eligible to be insured includes residential dwellings (and all household goods), barns, livestock, farm equipment, feed mills community centers and church buildings.

MARKET CONDUCT ACTIVITIES

A market conduct review was made of the Company as of September 30, 2009, in conjunction with this examination. The following items were addressed:

Policy Forms and Underwriting Practices

The Rating Section of the TDCI received a copy of the Company's application, policy form and premium rates on December 8, 2006. This documentation was stamped approved on January 8, 2007 pursuant to Tenn. Code Ann. § 56-22-109(b)(1) and Tenn. Code Ann. § 56-5-303, 304 and 305.

From January 1, 2002 through January 31, 2009 the Company charged its policyholders an annual rate of \$9.00 for each \$1,000.00 of coverage for all risks insured. Beginning February 1, 2009 the Company with the approval of its Board of Directors increased its premium rates to \$9.50 per \$1,000.00 of coverage for all risks insured on an annual basis.

Based upon the most recent rate filing approved by the P & C Section of the TDCI on January 8, 2007 the Company was only approved to bill and collect \$9.00 per thousand for all risks insured for the full policy period.

Therefore, the Company billed and collected premiums at a rate that was contrary to the rates filed and approved by the TDCI in violation of Tenn. Code Ann. § 56-22-109(b)(1) and Tenn. Code Ann. § 56-5-305. (See the Recommendations Section of this examination report for further discussion of this issue.)

Advertising

The Company during the period of examination did not engage in any advertising activities.

Privacy of Non-Public Personal Information

The Company's policy for the disclosure of privacy of non-public personal information was reviewed. The examiners noted no instances of non-compliance with Tenn. Comp. R. & Regs. 0780-1-72, "Privacy of Consumer Information Regulations."

REINSURANCE

Tenn. Code Ann. § 56-22-106(d) (effective January 1, 2007) states "A county mutual insurance company may secure reinsurance pursuant to Tenn. Code Ann. § 56-2-208(1)".

In 1997 the Company cancelled its Aggregate Excess of Loss and its Supplemental Aggregate Excess of Loss Reinsurance Agreements with the Erie Insurance Exchange.

Since 1997 the Company continued to maintain a Facultative Binding Authority Reinsurance Agreement and most recently a Property Facultative Pro Rata Reinsurance Agreement through Guy Carpenter and Company, Inc. of Albany, NY. Guy Carpenter and Company, Inc. is a wholly owned subsidiary of Marsh McLennan.

During the period of examination the Company ceded reinsurance through a consortium of carriers including Arch Reinsurance Company, Aspen Insurance U.K. Limited, Farmers Mutual Hail Insurance Company of Iowa, Hartford Steam Boiler Inspection and Insurance Company and The TOA Reinsurance Company of America. The aforementioned reinsurers were either a licensed carrier, approved surplus lines company or a non-licensed accredited reinsurer qualified to transact business in the State of Tennessee.

The Company as of September 30, 2009 had a Property Facultative Pro Rata Reinsurance Agreement which became effective January 1, 2009.

Type: Property Facultative Pro Rata Reinsurance

Reinsurance Broker: Guy Carpenter & Company, Inc. of Pennsylvania

Coverage: Pro-Rata Share – Property Business
Maximum Cession - \$100,000

Special Acceptance Clause above \$100,000

However, if the cession is greater than \$250,000, the maximum cession as respects any one animal shall not exceed \$250,000.

Minimum Retention - \$7,000

Term: Effective at 12:01 AM Standard Time, January 1, 2009 until 12:01 AM Standard Time, January 1, 2010

Deposit Premium: The Company receives a 15.0% ceding commission on all premiums ceded to the reinsurers. The Company shall allow the Reinsurer return commission on return premiums at the same rate.

Retention and Limit: Submissions hereunder shall be limited to eight (8) times the net retained liability of the Ceding Company, as defined herein, and shall be subject to a maximum cession of \$100,000 and a minimum retention of \$7,000 as respects any one (1) risk, covering business classified Fire and Allied Lines. The agreement stated that the Company may request reinsurance for limits greater than those set above.

Cessions covering perils other than fire, wherever the Company carries fire liability upon the same risk, shall be ceded at least in an equal proportion of such fire liability to this contract.

The reinsurer shall pay to the Company the reinsurer's proportional share of Loss and Extra Contractual Obligations, the sum of which shall be limited to eight (8) times the net retained liability of the ceding company. In addition, the reinsurer shall pay to the Company the reinsurer's proportional share of loss adjustment expense.

A review of the Company's 2007, 2008 and 2009 monthly bordereau reports filed with Guy

Carpenter revealed only new, renewed or endorsement added policies with a total insured value above \$14,000 were ceded to the Company's reinsurers. The Company's Directors during the period of examination established the Company's minimum retention at \$14,000 for any single risk. All new and renewal policies issued by the Company have a three (3) year policy term. Policies in-force not classified as new or renewal with a total insured value above \$14,000 were not ceded to the Company's reinsurers from 2007 through 2009.

The Company's failure to maintain reinsurance coverage on all specific risks above the Company's \$14,000.00 self-imposed retention limit caused the Company's risk exposure from 2007 – 2009 to be much higher than the Company's Directors intended and much higher than TN Code allowed. This finding is discussed further under the headings, "Comments and Recommendations".

LOSS EXPERIENCE

As developed from applicable amounts included in the Company's annual statements filed with the TDCI, the ratios of net losses incurred to net premiums earned for the period subject to this examination were as follows:

<u>Year</u>	<u>Claims Incurred</u>	<u>Net Premiums Earned</u>	<u>Loss Ratio</u>
2007	17,951	74,272	24.2%
2008	43,364	67,960	63.8%
2009*	<u>9,115</u>	<u>50,955</u>	17.9%
Total	\$70,430	\$193,187	36.5%

* 2009 data is through the September 30, 2009 date of examination.

ACCOUNTS AND RECORDS

During the course of examination, such tests and audit procedures were made as were considered necessary, including substantial verification of postings, extensions and footings and reconciliation of subsidiary ledgers to control accounts where necessary. General ledger trial balances were reconciled with copies of annual statements for the years 2007, 2008 and 2009.

Accounting records were maintained on a cash basis. The 2007 and 2008 Annual Statements submitted to the TDCI were not fully completed and inaccurate in that all of the annual statement instructions were not followed. Therefore, the 2007 and 2008 Annual Statements did not fully reflect the operations during the 2007 and 2008 policy years on a statutory accounting basis.

The Company's cash receipts and disbursements were recorded manually using written check registers and accounting ledger paper. Policy files were maintained in paper form and electronically. Premium billing and receipts for each policy were recorded

electronically using Lotus 1-2-3.

Books and records of the Company are kept at the home office location:

240 River Cliff Road
McMinnville, Tennessee 37228

DIVIDENDS OR DISTRIBUTIONS

No dividends or distributions have been declared or paid to the policyholders during the period of examination.

LITIGATION

As of September 30, 2009, the Company had no pending litigation which could have a material financial effect.

SUBSEQUENT EVENTS

1.) The 2009 Annual Statement filed by the Company with the TDCI disclosed "Policyholders Surplus" of \$175,805. The Company as of December 31, 2009 did not meet the minimum surplus requirements pursuant to Tenn. Code Ann. § 56-22-105(c) (effective January 1, 2007).

2.) As stated above, effective December 18, 2009, a second agent of the Company was licensed pursuant to Tenn. Code Ann. § 56-22-113 and Tenn. Code Ann. § 56-6-105, 106 and 107.

3.) On December 29, 2009 the Company filed a "Facultative Loss Bordereau" with its reinsurance broker, Guy Carpenter, for losses incurred in January, February, September & November 2008 totaling \$12,143.06 and March, April, June, September & November 2009 totaling \$5,235.09.

Two (2) of the five (5) claims incurred and paid in 2008 totaling \$3,855.05 and six (6) of the nine (9) claims incurred and paid in 2009 totaling \$4,559.65 were ceded to the Company's reinsurers for policies that were not disclosed on prior monthly Bordereau Reports with the payment of applicable premium. This error in the filing of "Facultative Loss Bordereau" was due to a misunderstanding by the Company related to its responsibility for reporting all policy cessions for single risks greater than \$14,000 each year and not just new, renewed or endorsement added policies. Because the Company had not properly disclosed these policies on their monthly "Facultative Reinsurance Bordereau" reports, with the appropriate amount of premium ceded, the re-insurers were not obligated to cover these losses per the terms of the Property Facultative Pro-Rata Reinsurance Contracts in place in 2008 and 2009.

However, the Company as of the signature date of this report had received three (3) separate payments from Guy Carpenter in the amount of \$4,324.87, \$9,251.48 and

\$2,471.13 for 2008 and 2009 paid losses submitted to Guy Carpenter. Documentation accompanying these payments verified that the reinsurers made full or partial payment on claim submissions without being obligated.

4.) The Company's Vice President, Jerry Hildreth, resigned effective, January 16, 2010. The Company's Board of Directors elected David Pendergraph to replace him as Vice President at the Company's January 16, 2010, Board of Directors Meeting.

FINANCIAL STATEMENT

There follows a statement of assets, liabilities and statement of income at September 30, 2009, together with a reconciliation of capital and surplus for the period under review, as established by this examination:

ASSETS

	<u>Current Year</u>
Cash and Cash Equivalents (Schedule E)	\$186,603.45
Reinsurance Recoverable on Paid Losses and Loss Adjustment Expenses	0.00
Interest, Dividends and Real Estate Income Due and Accrued	846.13
Electronic Data Processing Equipment and Software	<u>358.89</u>
Gross Assets	187,808.47
Total Assets Non-Admitted	<u>0.00</u>
Total Admitted Assets	<u>\$187,808.47</u>

LIABILITIES, SURPLUS, AND OTHER FUNDS

	<u>Current Year</u>
Total Unpaid Losses and Claims Net of Reinsurance	\$0.00
Loss Adjustment Expenses	0.00
Unearned Premiums	26,012.00
Ceded Reinsurance Premiums Payable	9,866.00
Accounts Payable and Accrued Expenses Payable	229.50
Taxes, Licenses & Fees (Excluding Federal Income Taxes)	<u>400.00</u>
Total Liabilities	<u>36,507.50</u>
Policyholders' Surplus	<u>151,300.97</u>
Total Liabilities and Policyholders' Surplus	<u>\$187,808.47</u>

STATEMENT OF INCOME & POLICYHOLDERS' SURPLUS ACCOUNT

UNDERWRITING INCOME

Net Premiums and Assessments Earned	<u>\$78,693.01</u>
DEDUCTIONS:	
Net Losses Incurred	\$9,115.21
Loss Expenses Incurred Including Claims Adjustment Expenses	\$1,200.99
Other Underwriting Expenses Incurred:	
Commissions and Brokerage:	
Directors and Officers Compensation and Allowances	\$0.00
Agents Compensation and Allowances	\$2,996.60
Commissions Received on Reinsurance Ceded	<u>\$171.00</u>
Net Commissions and Brokerage	\$2,825.60
Salaries and Related Items:	
Employee's Salaries	\$0.00
Directors & Officers Salaries	\$14,850.00
Payroll Taxes	<u>\$2,450.00</u>
Total Salaries and Related Items	\$17,300.00
Directors Fees	\$330.00
Boards, Bureaus and Association Dues	\$327.00
Insurance and Fidelity Bonds	\$100.00
Travel and Travel Items	\$1,276.35
Equipment	\$0.00
Cost or Depreciation of EDP Equipment of Software	\$170.00
Printing and Stationary	\$351.29
Postage, Telephone and Telegraph	\$168.00
Taxes, Licenses and Fees:	
State and Local Insurance Taxes	\$857.46
Insurance Department Licenses and Fees	<u>\$635.00</u>
Total Taxes, Licenses and Fees	\$1,492.46
Aggregate Write-Ins For Underwriting Expenses	<u>\$362.46</u>
Total Underwriting Expenses Incurred	\$24,703.16
Total Underwriting Deductions	<u>\$35,019.36</u>
Net Underwriting Gain or (Loss)	\$43,673.65

INVESTMENT INCOME

Net Investment Income Earned	\$1,121.72
Net Realized Capital Gains or (Losses) From Sale or Maturity of Assets	<u>\$0.00</u>
Net Investment Gain or (Loss)	\$1,121.72

OTHER INCOME

Finance & Service Charges Not Included In Premium (Policy Fees)	<u>\$0.00</u>
Total Other Income	\$0.00
Dividends To Policyholders	<u>\$0.00</u>
Net Income After Dividends To Policyholders and Before Federal Income Taxes	\$44,795.37

Federal Income Taxes Incurred	<u>\$0.00</u>
Net Income	<u>\$44,795.37</u>

POLICYHOLDERS' SURPLUS ACCOUNT

Policyholders' Surplus, December 31 of Previous Year	\$106,505.60
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GAINS AND (LOSSES) IN SURPLUS

Net Income (From Line 16)	\$44,795.37
Policyholders' Surplus as of September 30, 2009	\$151,300.97

COMMENTS AND RECOMMENDATIONS

Comments:

- The Company as of the September 30, 2009 date of examination had a \$10,000 Surety Bond in effect covering the Company's Secretary / Treasurer. Minimum fidelity bond coverage of \$15,000 to \$25,000 is suggested per the guidelines published in the NAIC Financial Condition Examiners Handbook.
- The Company's Charter and Bylaws did not reflect coverage provided for wind and sinkhole collapse. These key documents should be amended to disclose the Company insures against loss from wind and sinkhole collapse in addition to loss from fire and lightning as noted on the original Charter and Bylaws.
- As previously noted in the "Subsequent Events" section of this report the Company's reinsurers through Guy Carpenter made full or partial payment on claim submissions without being obligated per the terms of the Property Facultative Pro-Rata Reinsurance Contracts in place in 2008 and 2009. Representatives of Guy Carpenter have requested that the Company pay the appropriate amount of reinsurance premium for the two (2) claims incurred and paid in 2008 and the six (6) claims incurred and paid in 2009 that were ceded to the Company's reinsurers for policies that were not disclosed on prior monthly "Bordereau Reports". The Examiner determined that the amount of unpaid reinsurance premium on ceded losses incurred in 2008 was \$333.00 and the amount of unpaid reinsurance premium on ceded losses incurred in 2009 was \$1,275.00.

Recommendations:

- As previously stated, at no time since the January 1, 2007 effective date of Tenn. Code Ann. § 56-22-105(c) until the date of this examination report has the Company's "surplus over all liabilities" met or exceeded \$200,000. It is recommended that the Company take the necessary steps to become compliant with Tenn. Code Ann. § 56-22-105(c).
- Tenn. Code Ann. § 56-22-106(c)(1) restricts the Company from issuing "a policy of insurance covering those risks found in subsection (a) where the retained amount of risk by the county mutual insurance company on any single risk exceeds the lesser of: (A) twenty thousand dollars (\$20,000), plus three percent (3%) of the county mutual insurance company's surplus; or (B) one hundred thousand dollars (\$100,000)". The Company's surplus as determined by this examination as of September 30, 2009 was \$151,301. Three percent (3%) of \$151,301 equates to \$4,539. Therefore, the Company as of September 30, 2009 should not have exposure to any single risk above \$24,539.

A review of the Company's policies in force at September 30, 2009 revealed the Company had 85 policies covering a specific risk greater than \$24,539. Of these 85 policies the Company had not ceded any reinsurance premium covering 58 of these

policies during the 2009 policy year. The total amount of insurance in force for each of the single risks greater than \$24,539 covered by these 58 policies was \$2,539,100. Therefore, there were 58 policies in force covering single risks over \$24,539 in violation of Tenn. Code Ann. § 56-22-106(c)(1).

It is recommended that the Company properly reinsure all specific risks above \$24,539 in order become compliant with Tenn. Code Ann. § 56-22-106(c)(1).

- As mentioned above the Company has not maintained aggregate re-insurance coverage since 1997. Effective January 1, 2007, Tenn. Code Ann. § 56-22-110 required all county mutual insurance companies to carry an aggregate excess of loss insurance policy of no less than 5% of business in force. The amount required for such a policy shall be reduced by the county mutual insurance company's accumulated surplus. Therefore, the Company has not been in compliance with Tenn. Code Ann. § 56-22-110 since the January 1, 2007 effective date of this statute.

Five percent (5%) of the Company's documented \$8,377,600 total for insurance in force as of September 30, 2009 equates to \$418,880. \$418,880 less the Company's \$151,301 examination total for surplus is \$267,579. Therefore as of September 30, 2009 the Company was required to maintain an aggregate re-insurance policy covering \$267,579 of the Company's insurance pursuant to Tenn. Code Ann. § 56-22-110.

It is recommended that the Company purchase the proper amount of aggregate re-insurance coverage in order to become compliant with Tenn. Code Ann. § 56-22-110.

- As previously reported beginning February 1, 2009 the Company with the approval of its Board of Directors increased its premium rates to \$9.50 per \$1,000.00 of coverage for all risks insured on an annual basis. However, based upon the most recent rate filing approved by the P & C Section of the TDCI on January 8, 2007 the Company was only approved to bill and collect \$9.00 per thousand for all risks insured for the full policy period. Therefore, the Company billed and collected premiums at a rate that was contrary to the rates filed and approved by the TDCI in violation of Tenn. Code Ann. § 56-22-109(b)(1) and Tenn. Code Ann. § 56-5-305.

It is recommended that the Company seek approval from the TDCI to charge \$9.50 per \$1,000.00 of coverage for all risks insured.

CONCLUSION

Insurance examination practices and procedures, as promulgated by the National Association of Insurance Commissioners, have been followed in connection with the verification and valuation of assets and the determination of liabilities of Farmers Mutual Fire Insurance Company of Warren County, Tennessee of McMinnville, Tennessee.

In such manner, it was determined that, as of September 30, 2009, the Company had admitted assets of \$187,808 and liabilities, exclusive of a statutory contingency reserve and unassigned funds, of \$36,507. Thus, there existed for the additional protection of the policyholders unassigned funds (surplus) of \$151,301.

The courteous cooperation of the officers and directors of the Company extended during the course of the examination is hereby acknowledged.

Respectfully submitted,

James T. Pearce, Jr.

James T. Pearce, Jr.
Insurance Examiner
State of Tennessee
Southeastern Zone, N.A.I.C.

AFFIDAVIT

The undersigned deposes and says that he has duly executed the attached examination report of Farmers Mutual Fire Insurance Company of Warren County, Tennessee dated March 25, 2010, and made as of September 30, 2009, on behalf of the Department of Commerce and Insurance, State of Tennessee. Deponent further says he is familiar with such instrument and the contents thereof, and that the facts therein set forth are true to the best of his knowledge, information and belief.

James T. Pearce, Jr.

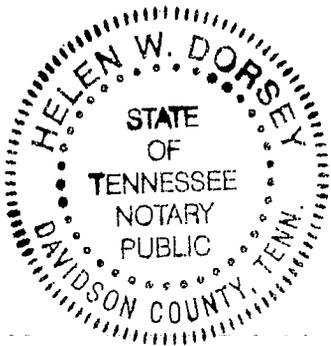
James T. Pearce, Jr.
Insurance Examiner
State of Tennessee
Southeastern Zone, N.A.I.C.

Subscribed and sworn to before me

this 25th day of
March, 2010

Notary *Helen W. Dorsey*
County *Davidson*
State *Tennessee*

Commission Expires *05/22/2010*



My Commission Expires MAY 22, 2010

FARMERS MUTUAL FIRE INSURANCE COMPANY OF WARREN COUNTY
ADA MAI CHURCH SEC'Y

P. O. Box 294
McMINNVILLE, TN 37111-0294
Phone 931- 473 2352
Fax 931- 474 2352
April 1, 2010

RECEIVED

APR 06 2010
Dept. of Commerce & Insurance
Company Examinations

Mr. Horace E. Gaddis, Jr., CFE
Insurance Examinations Director
State of Tennessee
Department of Commerce and Insurance
500 James Robertson Parkway
Nashville, TN 37243

RE: Report of Financial Examination as of September 30, 2009

Dear Mr. Gaddis:

Received the Financial Examination of September 30, 2009.

We are in agreement with it and do accept the report as printed.

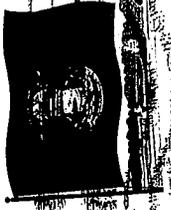
Sincerely,

Farmers Mutual Fire Insurance Company of Warren County Tennessee

Ada Mai Church

Ada Mai Church
Sec'y & Treas.

USA44



THE FARMERS' MUTUAL
FIRE INSURANCE COMPANY OF
WARREN COUNTY TENNESSEE
ADA MAI CHURCH, Sec.-Treas.
P.O. Box 294
McMINNVILLE, TN 37111-0294

McMINNVILLE TN 37111

03 APR 2010 11:32

RECEIVED

APR 06 2010
Dept. of Commerce & Insurance
Company Examinations



McMINNVILLE TN 37111