

# CERTIFICATION

June 4, 2014

I, Bruce R. Ramage, Director of Insurance of the State of Nebraska, do hereby certify that the attached is a full and correct copy of the

Financial Examination Report of

**KNOX COUNTY FARMERS MUTUAL INSURANCE COMPANY**

as of

December 31, 2012

The report is now on file and forming a part of the records of this Department.

I hereto subscribe my name under the seal of my office at Lincoln, Nebraska.

STATE OF NEBRASKA  
DEPARTMENT OF INSURANCE

JUN 04 2014

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STATE  
DEPARTMENT

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*Bruce R. Ramage*

DIRECTOR OF INSURANCE

STATE

DEPARTMENT

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CERTIFICATE OF ADOPTION

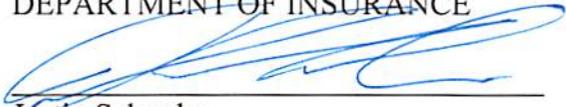
Take notice that the proposed report of the financial examination of

**KNOX COUNTY FARMERS MUTUAL INSURANCE COMPANY**

dated as of December 31, 2012, verified under oath by the examiner-in-charge on May 15, 2014, and received by the company on May 15, 2014, has been adopted without modification as the final report pursuant to Neb. Rev. Stat. § 44-5906(3)(a).

Dated this 2 day of June 2014.

STATE OF NEBRASKA  
DEPARTMENT OF INSURANCE

  
Justin Schrader  
Chief Financial Examiner

**STATE OF NEBRASKA**

**Department of Insurance**

**EXAMINATION REPORT**

**OF**

**Knox County Farmers Mutual Insurance Company**

**as of**

**December 31, 2012**



Bloomfield, Nebraska  
April 12, 2014

Honorable Bruce R. Ramage  
Director of Insurance  
Nebraska Department of Insurance  
941 "O" Street, Suite 400  
Lincoln, Nebraska 68508

Dear Sir:

Pursuant to your instruction and authorizations, and in accordance with statutory requirements, an examination has been conducted of the financial condition and business affairs of:

**Knox County Farmers Mutual Insurance Company  
212 N. Broadway  
Bloomfield, NE 68718**

(hereinafter also referred to as the "Company") and the report of such examination is respectfully presented herein.

### **INTRODUCTION**

The Company was last examined as of December 31, 2007 by the State of Nebraska. The current financial condition examination covers the intervening period to, and including, the close of business on December 31, 2012, and includes such subsequent events and transactions as were considered pertinent to this report. The State of Nebraska participated in this examination and assisted in the preparation of this report.

### **SCOPE OF EXAMINATION**

This examination was conducted pursuant to and in accordance with the provisions of Section §44-5904(1) of the Nebraska Insurance Statutes.

A general review was made of the Company's operations and the manner in which its business has been conducted in order to determine compliance with statutory and charter provisions. The Company's history was traced and has been set out in this report under the caption "Description of Company." All items pertaining to management and control were reviewed. The Articles of Incorporation and By-Laws were reviewed, including appropriate filings of any changes or amendments thereto. The minutes of the meetings of the members and Board of Directors held during the examination period, were read and noted. Attendance at meetings and election of Directors and Officers were also noted.

The fidelity bond and other insurance coverages protecting the Company's property and interests were reviewed. The Certificate of Authority to conduct the business of insurance in the state of Nebraska was inspected and a survey was made of the Company's general plan of operation.

The Company's reinsurance facilities were ascertained and noted, and have been commented upon in this report under the caption "Reinsurance." Accounting records and procedures were tested to the extent deemed necessary through the substantive examination process.

All accounts and activities of the Company were considered in accordance with the provisions of Section §44-5904(1) of the Nebraska Insurance Statues. The assets were verified and evaluated and the liabilities were determined in order to present the statement of the Company's financial condition as of December 31, 2012.

Any failure of items to add to the totals shown in schedules and exhibits appearing throughout this report is due to rounding.

## **DESCRIPTION OF COMPANY**

### **HISTORY**

The Farmers Mutual Fire Insurance Company of Knox County, Nebraska was organized under the laws of the State of Nebraska on March 18, 1893, as a mutual assessment company for the purpose of insuring farm properties, country school, country churches and parsonages and their contents against loss by fire and lightning. Dwellings, garages, barns and personal property of members living in fire protected towns and cities were also insured. Its amended Articles of Incorporation allowed for an existence of ninety-nine years from February 19, 1934, unless sooner dissolved by law. A sister company, namely Farmers Mutual Whirlwind and Tornado Insurance Company of Knox County, Nebraska, was organized on July 3, 1905, for the purpose of providing windstorm and tornado coverage on like properties. Its corporate existence likewise was for ninety-nine years from February 19, 1934, unless sooner dissolved by law.

These two companies were merged into a single consolidated corporation under and pursuant to the provisions of the applicable Nebraska Statutes. Said consolidation was effective March 29, 1984. The consolidated corporation was named Knox County Farmers Mutual Insurance Company, Incorporated. Its purpose is to continue the business of the two consolidated companies as an assessment insurance company insuring the properties of its members against loss as set forth in its By-Laws. The Company's Articles of Incorporation provide that, "the duration of this corporation shall be perpetual."

### **MANAGEMENT AND CONTROL**

#### **Members**

The Company's Articles of Incorporation state that, "every person, corporation, association or partnership insuring in this corporation shall be a member thereof and entitled to one vote which

may be cast in person or by proxy... the members present shall constitute a quorum for the transaction of business.” The Company's By-Laws provide that, “the regular annual meeting of said company shall be the first Tuesday in February in each year and shall be held in the City of Bloomfield, Knox County, Nebraska, at which time said corporation shall elect its Officers and transact other regular business.”

### **Board of Directors**

The Company's Articles of Incorporation state that, “the general management of this corporation shall be vested in a Board of not less than five nor more than nine Directors, who shall be elected at the annual meeting of the corporation and shall act as such Directors until their successors are elected and qualified. A Director of this corporation must be a member thereof and reside within the territory embraced by the By-Laws.”

The Company's By-Laws state that, “the Officers to be elected at said annual meeting shall consist of at least five Directors and no more than nine Directors in whom management of said corporation shall vest, and a majority of whom shall constitute a quorum for the transaction of business. Directors shall be elected for a term of one year. Vacancies in said board shall be filled by the other Directors, to serve until the next annual meeting. All members of the Board of Directors so chosen by the members of this corporation shall be members in good standing of this corporation. The Board of Directors so chosen at the regular meeting of said corporation shall hold a regular meeting of said board on or before the first Tuesday in March of each year in the City of Bloomfield, Knox County, Nebraska.”

The following persons were serving as Directors at December 31, 2012:

<u>Name</u>	<u>Residence</u>
Brian Eisenhauer	Bloomfield, Nebraska
Richard Eisenhauer	Bloomfield, Nebraska
Kenneth Gill	Bloomfield, Nebraska
Alvin Kathol	Hartington, Nebraska
Martin Kleinschmit	Hartington, Nebraska
Edward Lange Jr.	Hartington, Nebraska
Kevin Mackeparng	Bloomfield, Nebraska
Leland Vawser	Bloomfield, Nebraska
Donald Willats	Bloomfield, Nebraska

Each Director receives \$10 per meeting attended. They also receive a fee of \$15 plus 50 cents per mile for each appraisal or loss adjustment. In addition, Directors receive \$25 per day plus mileage of 50 cents per mile while attending to incidental business of the Company.

### Officers

The Company's By-Laws state that, "the Board shall choose from their own number a President, Secretary and a Treasurer."

The following is a listing of Officers elected and serving the Company at December 31, 2012:

<u>Name</u>	<u>Office</u>
Leland Vawser	President
Donald Willats	Secretary
Kenneth Gill	Treasurer

### TERRITORY AND PLAN OF OPERATION

As evidenced by a current Certificate of Authority, the Company is licensed to transact business in the state of Nebraska. The Company's By-Laws provide that, "the district in which this corporation may do business shall be limited to the State of Nebraska for which Knox Co Farmers Mutual Insurance Company is licensed to write insurance."

The Company's By-Laws also state that, "the purpose of this corporation is to insure for a term of four years or less, against loss or damage, the urban and rural buildings, including churches, parsonages, schools, dwelling houses, garages, barns and other outbuildings as well as personal property of members of this corporation, excluding commercial property...the Directors so chosen at the regular meeting of said corporation, if licensed to do so, shall be the agents of said corporation to solicit new members for this organization." The Company had three licensed agents as of December 31, 2012. The agents receive a 10 percent commission for each new policy and 9 percent on renewal policies written.

The Company, as a convenience for its policyholders and agents, makes available general liability insurance coverage written by Acceptance Casualty Insurance Company and Grinnell Mutual Reinsurance Company. Commissions received by the Company are transferred and disbursed to the agent responsible for the production of such business.

#### **FIDELITY BOND AND OTHER INSURANCE**

The Company's By-Laws state that, "the Treasurer so chosen by the Board of Directors shall give bond in the amount of \$100,000, conditioned for the faithful performance of his duties of his office and the accounting for all moneys coming through his hands." A fidelity bond on the Treasurer in the amount of \$100,000 was in-force at December 31, 2013.

#### **REINSURANCE**

##### **Ceded**

The Company has a reinsurance contract with Grinnell Mutual Reinsurance Company (Grinnell), which became effective January 1, 2011 and continues until terminated at the end of any calendar year with 90 days written notice. This contract establishes the Company as a

member of Grinnell. Coverage applies to all policy forms and endorsements issued by the Company once they are filed and accepted by Grinnell.

The Company is issued a coverage schedule each calendar year setting the premium rates, individual occurrence retention limit, individual occurrence coverage limits, and aggregate loss attachment point. Under the 2012 coverage schedule, the Company's individual occurrence retention is \$50,000. Grinnell is liable for losses in excess of the retention, up to a limit of \$1,000,000 for livestock/poultry/horse operations, commercial and public property, farm products storage structures, and dwelling, and up to a limit of \$2,000,000 for farm machinery and equipment storage buildings. The 2012 monthly premium rate is \$0.0407 of the adjusted gross fire risk in force per \$1,000 at the end of each month during the contract year.

Under the 2012 coverage schedule, the Company's aggregate net loss retention is \$256,599. Grinnell is liable for all aggregate losses in excess of this retention. The 2012 monthly premium rate is \$0.0773 of the adjusted gross fire risk in force per \$1,000 at the end of each month during the contract year.

Facultative coverage is available for exposures that exceed the individual occurrence limit. The Company does not have any exposures that are applicable.

### **General**

The contract reviewed contained standard insolvency, arbitration, errors and omissions, and termination clauses.

## **BODY OF REPORT**

### **FINANCIAL STATEMENTS**

The following financial statements reflect the Company's operations during the examination period and the financial condition of the Company at December 31, 2012. All amounts are based on the current examination:

#### **STATEMENT OF INCOME AND DISBURSEMENTS**

	<b><u>2008</u></b>	<b><u>2009</u></b>	<b><u>2010</u></b>	<b><u>2011</u></b>	<b><u>2012</u></b>
Balance, beginning of year	<b><u>\$1,184,622</u></b>	<b><u>\$1,323,813</u></b>	<b><u>\$1,410,732</u></b>	<b><u>\$1,290,493</u></b>	<b><u>\$1,245,038</u></b>
<b><u>Income</u></b>					
Gross receipts from assessments	\$ 390,554	\$ 393,685	\$ 413,730	\$ 457,428	\$ 604,431
Return on cancellations	<u>3,186</u>	<u>3,235</u>	<u>3,229</u>	<u>3,511</u>	<u>8,154</u>
Net received from members	\$ 387,368	\$ 390,450	\$ 410,501	\$ 453,917	\$ 596,277
Interest on investments and dividends	43,384	37,742	24,198	16,624	15,389
Liability sold for AIC	53,482	59,200	57,644	34,998	
Liability premium for Grinnell GMRC direct				19,443	
Salvage	1,500			1,464	
Tax refund		1,324	85		
Commissions from Grinnell Mutual					9,858
Refund on insurance					10
Refund from PIA	<u>80</u>				
Total revenue	<b><u>\$ 485,814</u></b>	<b><u>\$ 488,716</u></b>	<b><u>\$ 492,427</u></b>	<b><u>\$ 526,446</u></b>	<b><u>\$ 621,535</u></b>

**STATEMENT OF INCOME AND DISBURSEMENTS (continued)**

	<u>2008</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>2012</u>
<b><u>Disbursements</u></b>					
Gross losses paid	\$ 104,650	\$ 185,633	\$ 329,079	\$ 674,777	\$ 268,619
Less discount and salvage		200	2,500	15,822	5,415
Less reinsurance recovered	<u>                    </u>	<u>45,135</u>	<u>14,783</u>	<u>363,170</u>	<u>92,242</u>
Net losses paid	\$ 104,650	\$ 140,298	\$ 311,796	\$ 295,786	\$ 170,962
Adjusting expense	1,000	968	2,209	6,257	7,982
Commissions to agents	34,811	36,656	38,801	40,660	48,583
Expenses of agents	1,195	274	24		
Salaries and expenses of Directors and Officers	12,393	14,327	14,599	15,729	14,629
Rent	6,000	6,000	5,500	6,500	6,550
Insurance department licenses and fees	1,527	1,579	4,681	2,088	532
All other taxes	14,109	14,282	13,430	23,818	16,373
Advertising, printing and stationery	603	788	683	1,470	1,044
Telephone, postage and utilities	1,840	1,339	1,769	1,952	1,802
Reinsurance premiums paid	112,203	127,356	160,957	113,523	141,653
Interest on borrowed money	500				
Miscellaneous	1,543	638	674	1,645	3,308
GMRC direct				4,000	9,756
Liability premiums for AIC	50,267	53,550	53,988		
Liability premiums for Acceptance Casualty and Grinnell Mutual				58,474	57,896
Federal and state employee WH	<u>3,982</u>	<u>3,742</u>	<u>3,555</u>	<u>                    </u>	<u>8,367</u>
Total disbursements	<u>\$ 346,623</u>	<u>\$ 401,797</u>	<u>\$ 612,666</u>	<u>\$ 571,901</u>	<u>\$ 489,436</u>
Balance, end of year	<u>\$1,323,813</u>	<u>\$1,410,732</u>	<u>\$1,290,493</u>	<u>\$1,245,038</u>	<u>\$1,377,136</u>

**STATEMENT OF ASSETS AND LIABILITIES**  
**DECEMBER 31, 2012**

**ASSETS**

**Ledger Assets**

Certificates of deposit	\$1,110,197	
Cash deposited in banks	210,984	
Surplus note	<u>55,955</u>	
Total ledger assets		<b><u>\$1,377,136</u></b>

**Assets Not Admitted**

Non-admitted surplus note	\$ <u>55,955</u>	
Total assets not admitted		<b><u>\$ 55,955</u></b>
Total admitted assets		<b><u>\$1,321,181</u></b>

**LIABILITIES AND SURPLUS**

Losses adjusted and unpaid	\$ 57,501	
Claims reported but not adjusted	20,100	
Less reinsurance	<u>(57,501)</u>	
Net unpaid losses		\$ 20,100
Unearned premiums		241,463
Premium tax liability		<u>2,294</u>
Total liabilities		<b>\$ 263,857</b>
Surplus as regards policyholders		<b><u>\$1,057,324</u></b>
Total liabilities and surplus		<b><u>\$1,321,181</u></b>

**COMPLIANCE WITH PREVIOUS RECOMMENDATIONS**

The recommendation appearing in the previous report of examination is reflected below together with the remedial actions taken by the Company to comply therewith:

**Certificate of Deposit** – It is recommended that the Company utilize the services of a competitor of Kansas Bankers Surety, Co. (KBS) to provide a new guaranty bond, as KBS will no longer offer their guaranty bond program. Another option the Company

could employ would be to disperse the excessive Certificate of Deposit amongst various banks.

**Action:** The Company has complied with this recommendation.

## **COMMENTARY ON CURRENT EXAMINATION FINDINGS**

**Certificates of Deposit** **\$1,110,197**

The Company at December 31, 2012 had eleven certificates of deposit issued from various banking institutions. Each certificate of deposit was verified by direct confirmation from the respective bank officials. The Company erroneously reported a surplus note, valued at \$55,955, as a certificates of deposit on the 2012 Annual Statement.

**Other Cash Deposited in Banks** **\$ 210,984**

The Company maintains these funds in a checking account with a local bank. These deposits were verified by obtaining a direct confirmation from the bank. The amount indicated thereon for the checking account was reconciled to the Company's records as of December 31, 2012, by giving consideration to outstanding checks.

**Surplus Note** **\$ 55,955**

The note was issued by Nebraska Farmers Mutual Reinsurance Association. Statement of Statutory Accounting Principles No. 41, Paragraph 10(b)(b) states that, "holders of surplus notes shall value their investment in surplus notes as follows: by applying a 'statement factor' to the outstanding face amount of the capital or surplus notes. The 'statement factor' is equal to the total capital and surplus, including surplus notes, less the greater of 5% of admitted assets or \$6,000,000, divided by capital or surplus notes. If 'statement factor' is negative, the surplus note(s) shall be carried at zero."

Calculation of the Company's surplus note is as follows:

\$1,377,136	Admitted asset (including surplus note)
<u>261,563</u>	Less liabilities
\$1,115,573	Total capital, surplus and surplus note

\$ 1,377,136	
<u>5%</u>	of admitted assets
\$ 68,857	

Greater of \$68,857 or \$6,000,000

\$1,115,573	
<u>- 6,000,000</u>	
\$(4,884,427)/1,115,573	= -4.37 statement factor

With the statement factor a negative amount, the surplus note is considered \$0 per the Statement of Statutory Accounting Principles No. 41, Paragraph 10(b)(b), noted above.

It is recommended that the Company list the surplus note in Annual Statement page 5 line 11, "Other Assets." The note should then be non-admitted on Annual Statement page 5 line 22.

**Net Unpaid Losses** **\$ 20,100**

The Company reported a gross liability for unpaid losses amounting to \$77,601 in its December 31, 2012 Annual Statement. The Company also reported reinsurance recoverable for previous years in the amount of \$57,501, reflecting a net unpaid loss of \$20,100.

**Unearned Premiums** **\$ 241,463**

The Company reported unearned premium as \$241,463 in its Annual Statement. The amount is calculated by taking 45% of the premium received during the year. Liability premiums, which are forwarded on to Acceptance Casualty Insurance Company and Grinnell Mutual Reinsurance Company are not reserved for.

**Premium Tax Liability****\$ 2,294**

The Company did not report a premium tax liability in its Annual Statement. The liability amount reported in the 2012 State of Nebraska Annual Tax Return was \$2,294. It is recommended that this amount be accrued and reported within the Annual Statement on page 5 line 34, "Premium Tax Liability."

**Policyholder's Surplus****\$1,057,324**

Surplus as regards policyholders amounted to \$1,057,324 at December 31, 2012, as developed through this examination.

**Documentation Maintenance**

The Company does not maintain documentation used for the reporting of Annual Statement page 5 line 25, "Losses Adjusted and Unpaid," or Annual Statement page 5 line 26, "Claims Reported but not Adjusted." The documentation provided by the Company was current information, rather than data used to complete the Annual Statement.

The Company is not compliant with Nebraska Insurance Code 44-5905(b)(i)(A) which states that, "every company or person subject to the Insurers Examination Act shall retain all books, records, accounts, papers, documents, and computer or other recordings relating to the property, assets, financial accounts, and business of such company or person in a manner that permits examination of such books, records, accounts, papers, documents, and computer or other recordings for five years, or until the period of time in which the transaction took place has undergone a financial examination by the Director, whichever is later, following the completion of a transaction relating to the property, assets, financial accounts, and business of such company or person."

It is recommended that the Company maintain documentation in compliance with Nebraska Insurance Statute 44-5905(b)(i)(A).

### **SUMMARY OF COMMENTS AND RECOMMENDATIONS**

The following comments and recommendations have been made as a result of this examination:

**Surplus Note** – It is recommended that the Company list the surplus note on Annual Statement page 5 line 11, “Other Assets.” The note should then be non-admitted on Annual Statement page 5 line 22.

**Premium Tax Liability** - It is recommended that the Company accrue for premium taxes within the Annual Statement on page 5 line 34, “Premium Tax Liability.”

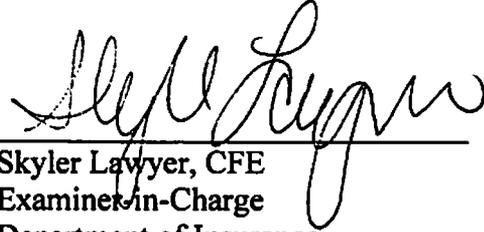
**Documentation Maintenance** - It is recommended that Company maintain documentation in compliance with Nebraska Insurance Statute 44-5905(b)(i)(A).

**ACKNOWLEDGEMENT**

The courteous cooperation extended by the Officers and employees of the Company during this examination is hereby acknowledged.

In addition to the undersigned, Kim Hurst, CFE, Financial Examiner with the Nebraska Department of Insurance, participated in this examination and assisted in the preparation of this report.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Skyler Lawyer", written over a horizontal line.

Skyler Lawyer, CFE  
Examiner-in-Charge  
Department of Insurance  
State of Nebraska

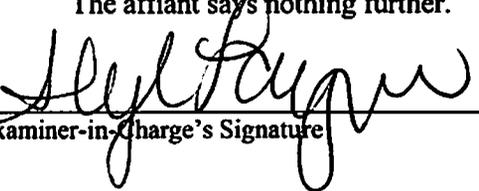
State of Nebraska,

County of Lancaster,

Skylar Lawyer, being duly sworn, states as follows:

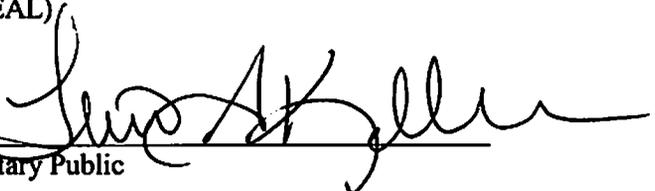
1. I have authority to represent the Department of Insurance of the State of Nebraska in the examination of    Knox County Farmers Mutual Insurance Company   .
2. The Department of Insurance of the State of Nebraska is accredited under the National Association of Insurance Commissioners Financial Regulation Standards and Accreditation.
3. I have reviewed the examination work papers and examination report, and the examination of    Knox County Farmers Mutual Insurance Company    was performed in a manner consistent with the standards and procedures required by the Department of Insurance of the State of Nebraska.

The affiant says nothing further.

  
Examiner-in-Charge's Signature

Subscribed and sworn before me by Skylar Lawyer on this 5<sup>th</sup> day of May, 2014.



(SEAL)  
  
Notary Public

My commission expires December 24, 2017 [date].