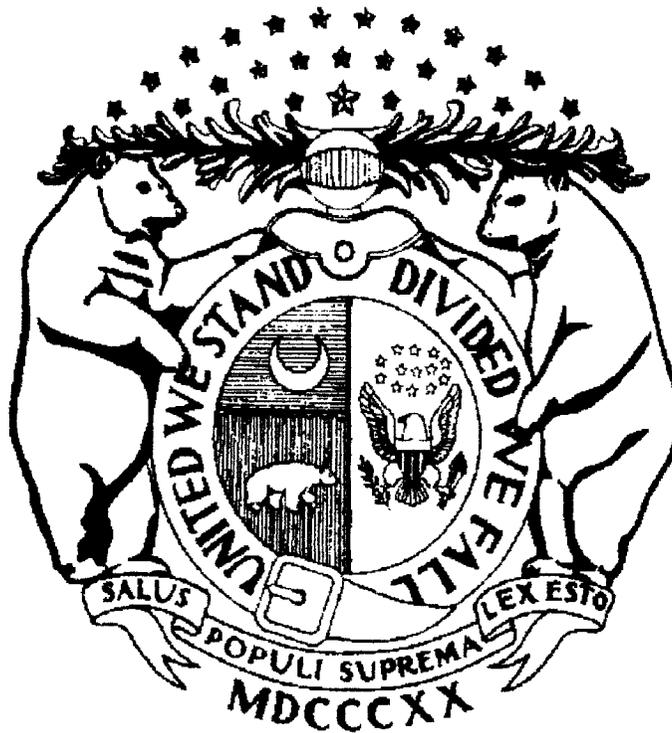


**REPORT OF THE  
FINANCIAL EXAMINATION OF  
CITIZENS MUTUAL INSURANCE COMPANY  
AS OF  
DECEMBER 31, 2005**



**STATE OF MISSOURI**

**DEPARTMENT OF INSURANCE, FINANCIAL INSTITUTIONS  
AND PROFESSIONAL REGISTRATION**

**JEFFERSON CITY, MISSOURI**

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January 22, 2007  
Columbia, Missouri

Honorable Douglas M. Ommen, Director  
Missouri Department of Insurance, Financial  
Institutions and Professional Registration  
301 West High Street, Room 530  
Jefferson City, Missouri 65101

Sir:

In accordance with your examination warrant, a full-scope examination has been made of the records, affairs and financial condition of

**CITIZENS MUTUAL INSURANCE COMPANY**

hereinafter referred to as such, or as "Citizens" or the "Company". The Company's administrative office is located at 2102 White Gate Drive, Columbia, Missouri 65202, telephone number (573) 474-6193. This examination began on January 12, 2007, and was concluded on January 22, 2007, and is respectfully submitted.

**SCOPE OF EXAMINATION**

**Period Covered**

The prior full-scope examination of the Company was made as of December 31, 2001, and was conducted by examiners from the State of Missouri. The current full-scope examination covers the period from January 1, 2002, through December 31, 2005, was conducted by examiners from the Missouri Department of Insurance, Financial Institutions and Professional Registration (DIFP) and concurrently with the examination of the Company's affiliate Columbia Mutual Insurance Company (CMIC).

This examination also included material transactions and/or events occurring subsequent to the examination date, which are noted in this report.

**Procedures**

This examination was conducted using the guidelines set forth in the Financial Examiners Handbook of the National Association of Insurance Commissioners (NAIC), except where practices, procedures and

applicable regulations of the DIFP and statutes of the State of Missouri prevailed.

**Comments-Previous Examination Report**

There were no previous examination report comments.

**HISTORY**

**General**

The Company was originally organized on May 11, 1901, as Citizens Mutual Fire and Lightning Insurance Society in Applecreek Township, Cape Girardeau County, Missouri. On December 27, 1932, the Company was incorporated under the general business laws of the State of Missouri as Citizens Mutual Fire Insurance Company. In January of 1970, the Company merged with Bollinger County Farmers Mutual Aid Society, with Citizens remaining as the surviving entity. In October of 1971, the Company amended its Articles of Incorporation, changing its name to Citizens Mutual Insurance Company.

The Company has a Certificate of Authority dated July 1, 1991, and is covered by Sections 380.201 through 380.611 RSMo. (Extended Missouri Mutual Companies). The Company's Certificate of Authority is renewed annually.

**Management**

In accordance with the Articles of Incorporation, the annual meeting of the Company's members is held on the Friday immediately following the first Saturday in March, at the home office of the Company or at such other place as may be designated by the Board of Directors. Special meetings of the members may be called by the Board of Directors at any time and shall be called upon petition of one-fourth of the members. Eight members shall constitute a quorum at any membership meeting. Proxy voting is permitted.

The management of the Company is vested in the Board of Directors, who are elected from the general membership. The Board of Directors consists of nine members, serving staggered, three-year terms. All directors must be policyholders of the Company. The Board of Directors meets approximately once a year.

Directors who are not also employees of Columbia Insurance Group, Inc. (CIG) receive an annual retainer of \$450 plus \$50 per each meeting attended.

Members serving on the Board of Directors as of December 31, 2005, were as follows:

<u>Name and Address</u>	<u>Occupation</u>	<u>Term</u>
Roger Ballard 8280 North Millsite Columbia, Missouri	Treasurer Columbia Insurance Group	2004-2007
Roger Birdsong 4808 Greenberry Court Columbia, Missouri	Senior Vice President Columbia Insurance Group	2003-2006
James E. Cunningham 1730 East Cedar Tree Lane Hartsburg, Missouri	Secretary & General Counsel Columbia Insurance Group	2003-2006
A. Ben Galloway 501 South Glenwood Avenue Columbia, Missouri	Vice-President – Investments Columbia Insurance Group	2005-2008
Robert A. Gerding 20 South Fifth Street Columbia, Missouri	President Gerding, Korte & Chitwood, CPA's	2005-2008
Betty J. Schuster 3109 Hill Haven Columbia, Missouri	Agent Principal Financial Group	2005-2008
Gary W. Thompson 3903 Keystone Court Columbia, Missouri	Senior Vice President Columbia Insurance Group	2004-2007
Robert J. Wagner 2 Lucern Court Columbia, Missouri	President & Chief Executive Officer Columbia Insurance Group	2003-2006
Alan G. Wills 612 West Main Street Jackson, Missouri	Agent Citizens Mutual Insurance Company	2004-2007

The Board of Directors appoints for a term of one year, the officers of the Company. The officers of the Company serving at December 31, 2005, were as follows:

Robert J. Wagner	Chairman of the Board
Robert J. Wagner	President & Chief Executive Officer
Gary W. Thompson	Executive Vice-President & Chief Operating Officer
James E. Cunningham	Secretary
Roger D. Ballard	Treasurer

### **Conflict of Interest**

The Company has written conflict of interest procedures for the disclosure of material conflicts of interest or affiliations by its directors and officers. The Company has its directors and officers sign conflict of interest statements on an annual basis, and no material potential conflicts were disclosed.

### **Corporate Records**

A review was made of the Articles of Incorporation and the Bylaws of the Company. No amendments were made to the Articles of Incorporation or Bylaws during the period under examination.

The minutes of the membership and the Board of Directors' meetings were reviewed for the period under examination. The minutes and records of the Company appear to properly reflect corporate transactions and events.

### **Affiliated Transactions**

Six of the nine directors of the Company are employees of Columbia Insurance Group, Inc. (CIG), a wholly-owned subsidiary of Columbia Mutual Insurance Company (CMI), a Missouri property and casualty insurer. CMI also owns two other insurance companies, Patrons Insurance Company (PIC), a Kansas property and casualty insurer, and Columbia National Insurance Company (CNI), a Nebraska property and casualty insurer. As such, Citizens is affiliated with the aforementioned companies by means of being controlled by the same management team.

The Company is party to a Personnel and Service Agreement with CIG. Under the agreement, CIG acts as an employer and common paymaster for Citizens and other affiliates and provides administrative and management functions, computer services, and facilities and equipment to the affiliates. The affiliates

reimburse CIG for expenses actually incurred in the provision of the facilities and services.

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

The Company and its affiliates are named insureds on a fidelity bond providing a limit of liability of \$1,000,000 and a \$10,000 deductible. The fidelity bond coverage of the Company meets the minimum amount suggested in the guidelines promulgated by the NAIC, which is between \$75,000 and \$100,000 in coverage. The fidelity bond is underwritten by CMI and reinsured under their multiple lines excess of loss reinsurance agreement.

The Company utilizes only independent producers, which are responsible for obtaining errors and omissions insurance.

The Company is also a named insured on policies issued by affiliates CMI, CNI or PIC, including property, general liability, commercial umbrella liability, automobile physical damage and liability, and workers compensation. These policies are subject to the reinsurance coverages obtained by the affiliates. In addition, the Company is a named insured on errors and omissions and directors and officers liability policies issued by non-affiliates.

The insurance coverage appears adequate.

### **EMPLOYEE BENEFITS**

The Company has no employees. Personnel services are provided by CIG pursuant to the Personnel and Service Agreement described in the “Affiliated Transactions” section of this report. CIG provides its employees with a variety of benefits, including group medical and dental, group long-term disability, group term and universal life, and accidental death and dismemberment insurance and a 401(k) savings plan.

In addition, CIG provides its employees with a qualified defined contribution pension plan. Citizens has no legal obligation for benefits under the plan; however, the Company’s share of the pension expense for

2005 was \$17,258. CIG has also established non-qualified deferred compensation and retirement plans for its officers and directors.

The Company appears to have made adequate provisions in the financial statements for these employee benefits.

## **INSURANCE PRODUCTS AND RELATED PRACTICES**

### **Territory and Plan of Operation**

The Company is licensed by the Missouri Department of Insurance as an Extended Missouri Mutual Company operating under Sections 380.201 through 380.611 RSMo. (Extended Missouri Mutual Companies). The Company is authorized to write fire, wind and liability insurance in all counties in the State of Missouri. The Company writes fire, wind and liability coverages. The Company's policies are sold by approximately 28 licensed agencies. Commissions paid to producers vary from ten to fifteen percent, depending on the line of business.

### **Policy Forms and Underwriting Practices**

The Company uses AAIS and ISO policy forms. The policies are written on a continuous period basis. Rates are determined by the Board of Directors. Renewal billings are mailed directly to the insured. Inspections and adjusting services are performed by CIG adjusters, territory managers or independent adjusters.

## **GROWTH AND LOSS EXPERIENCE OF THE COMPANY**

	<u>Admitted Assets</u>	<u>Liabilities</u>	<u>Gross Assessment</u>	<u>Gross Losses</u>	<u>Investment Income</u>	<u>Underwriting Income</u>	<u>Net Income</u>
2005	\$3,729,874	\$2,111,506	\$4,091,452	\$1,276,253	\$116,185	\$195,794	\$203,344
2004	3,241,838	1,841,578	3,652,952	1,547,694	107,649	129,447	163,509
2003	2,846,993	1,605,792	3,279,991	3,608,767	102,339	49,351	104,268
2002	2,530,607	1,408,003	2,998,357	2,145,968	121,628	(28,402)	66,208

At year-end 2005, 4,946 policies were in force.

## REINSURANCE

### General

Citizens, Columbia Mutual Insurance Company (CMI), Columbia National Insurance Company (CNI) and Patrons Insurance Company (PIC) participate in the Reinsurance and Cost Sharing Agreement. Under the terms of the agreement, CMI agrees to assume 100% of the premiums, expenses and loss reserves for all insurance policies issued and assumed by Citizens, CNI and PIC. The insurance policies issued and assumed by CMI are pooled with the business assumed from the participants. The pooled business of all four entities is ceded, pursuant to reinsurance agreements with non-affiliated reinsurers. The net premiums, expenses and loss reserves from the pooled business that remains is then retroceded back to the participants, per the following percentages: CNI – 18%, PIC – 5% and Citizens– 1%. CMI retains the remaining 76% of the net pooled business.

The Company's reinsurance premium activity on a direct-written, assumed and ceded basis for the period under examination is shown below:

	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>
Direct	\$1,459,958	\$1,594,534	\$1,856,928	\$2,235,867
Assumed	1,538,399	1,685,457	1,796,026	1,855,585
Ceded	<u>(1,459,958)</u>	<u>(1,594,534)</u>	<u>(1,856,928)</u>	<u>(2,235,867)</u>
Net	<u>\$1,538,399</u>	<u>\$1,685,457</u>	<u>\$1,796,026</u>	<u>\$1,855,585</u>

### Assumed

The Company assumes 1% of pooled business under the Reinsurance and Cost Sharing Agreement, described in the “Reinsurance – General” section above.

### Ceded

The Company cedes 100% of its business to CMI under the Reinsurance and Cost Sharing Agreement, described in the “Reinsurance – General” section above.

CMIC obtains reinsurance on the pool of business it assumes under the Reinsurance and Cost

Sharing Agreement. In general, CMI retains a maximum exposure of \$550,000 per risk on property losses and \$550,000 per occurrence on casualty losses. CMI is also party to various catastrophe and facultative reinsurance contracts.

The Company is contingently liable for all reinsurance losses ceded to others. This contingent liability would become an actual liability in the event that any assuming reinsurer should fail to perform its obligations under its reinsurance agreement with the Company.

### **ACCOUNTS AND RECORDS**

The accounting records are maintained by the Company on an accrual basis. The Company prepares its annual statement and tax filings.

### **FINANCIAL STATEMENTS**

The following financial statements, with supporting exhibits, present the financial condition of the Company for the period ending December 31, 2005, and the results of operations for the year then ended. Any examination adjustments to the amounts reported in the Annual Statement and/or comments regarding such are made in the "Notes to the Financial Statements," which follow the Financial Statements. (The failure of any column of numbers to add to its respective total is due to rounding or truncation.)

There may have been differences found in the course of this examination, which are not shown in the "Notes to the Financial Statements." These differences were determined to be immaterial, concerning their effect on the financial statements. Therefore, they were communicated to the Company and noted in the workpapers for each individual annual statement item.

**ANALYSIS OF ASSETS**  
**December 31, 2005**

Bonds	\$ 2,983,689
Cash and Short-Term Investments	132,081
Investment Income Due & Accrued	31,347
Uncollected Premium	169,892
Deferred Premium	267,373
Recoverable From Reinsurers	5,361
Funds on Deposit With Reinsurers	88
Other Amounts Receivable Under Reinsurance Contracts	54,591
Net Deferred Tax Asset	78,287
Guaranty Funds on Deposit	7,165
	-----
Total Assets	<u><u>\$ 3,729,874</u></u>

**LIABILITIES, SURPLUS AND OTHER FUNDS**  
**December 31, 2005**

Losses	\$ 818,285
Reinsurance Payable on Paid Losses	4,151
Loss Adjustment Expenses	178,036
Commissions Payable	85,169
Other Expenses	77,978
Taxes, Licenses & Fees	17,382
Current Federal Taxes	25,118
Unearned Premiums	860,141
Advance Premiums	22,967
Ceded Reinsurance Premiums Payable	19,146
Funds Held Under Reinsurance Treaties	718
Amounts Withheld for Account of Others	1,465
Remittances and Items Not Allocated	950
	-----
Total Liabilities	\$ 2,111,506
Unassigned Funds (Note 1)	\$ 1,618,368
	-----
Surplus As Regards Policyholders	\$ 1,618,368
	-----
Total Liabilities and Surplus	\$ 3,729,874
	=====

**STATEMENT OF INCOME**  
**December 31, 2005**

Premiums Earned	\$ 1,823,117
Losses Incurred	(890,806)
Loss Expenses Incurred	(163,320)
Other Underwriting Expenses Incurred	(573,197)
	-----
Net Underwriting Income (Loss)	\$ 195,794
	-----
Investment Income	\$ 116,185
Other Income	11,339
	-----
Net Income Before Tax	\$ 323,318
Federal Income Tax	(119,974)
	-----
Net Income (Loss)	\$ 203,344
	=====

**CAPITAL AND SURPLUS ACCOUNT**  
**December 31, 2005**

Policyholders' Surplus, December 31, 2004	\$ 1,400,260
Net Income (Loss)	203,344
Change in Net Deferred Income Tax	21,200
Change in Non-Admitted Assets	(6,436)
	-----
Policyholders' Surplus, December 31, 2005	\$ 1,618,368
	=====

## **NOTES TO THE FINANCIAL STATEMENTS**

### **Note 1 – Unassigned Funds**

The Unassigned Funds balance of \$1,618,368 includes a guaranty fund balance of \$150,000, in accordance with Section 380.271 RSMo. (Financial Reinsurance Requirements). The 2005 Property and Casualty Annual Statement filed by the Company does not contain a guaranty fund line in its format. The DIFP approved the Company's filing of this statement in lieu of the Missouri Mutual Annual Statement.

### **EXAMINATION CHANGES**

There were no examination changes.

### **GENERAL COMMENTS AND RECOMMENDATIONS**

There were no general comments or recommendations.

### **SUBSEQUENT EVENTS**

The Reinsurance and Cost Sharing Agreement was replaced by the Intercompany Reinsurance Agreement, effective January 1, 2006. The terms of the new agreement are similar to those of the former agreement.

Effective April 1, 2006, the affiliated company Patrons Insurance Company was merged into another affiliate, Columbia National Insurance Company.

