

# STATE OF MISSOURI



## DEPARTMENT OF INSURANCE, FINANCIAL INSTITUTIONS AND PROFESSIONAL REGISTRATION

P.O. Box 690, Jefferson City, Mo. 65102-0690

RE: Examination Report of Farmers and Laborers Cooperative Insurance Association of Audrain County as of December 31, 2010

### ORDER

After full consideration and review of the report of the financial examination of Farmers and Laborers Cooperative Insurance Association of Audrain County as of December 31, 2010, together with any written submissions or rebuttals and any relevant portions of the examiner's workpapers, I, John M. Huff, Director, Missouri Department of Insurance, Financial Institutions and Professional Registration pursuant to section 380.061, RSMo [if Part I], or 380.491, RSMo [if Part II], adopt such report. After my consideration and review of such report are incorporated by reference and deemed to be my findings and conclusions to accompany this order.

Based on such findings and conclusions, I hereby ORDER Farmers and Laborers cooperative Insurance Association of Audrain County to take the following action or actions, which I consider necessary to cure any violation of law, regulation or prior order of the Director revealed in such report: (1) implement, and verify compliance with, each item mentioned in the General Comments and/or Recommendations, if any, section of such report; (2) account for its financial condition and affairs in a manner consistent with the Director's findings and conclusions; and (3) submit a signed copy of the minutes of the meeting which reflect a corporate resolution to the effect the Examination Report has been reviewed and accepted.

So ordered, signed and official seal affixed this 10<sup>th</sup> day of February 2012.



A handwritten signature in black ink, appearing to read "John M. Huff".

John M. Huff, Director  
Department of Insurance, Financial Institutions  
and Professional Registration

REPORT OF THE  
FINANCIAL EXAMINATION OF

Farmers and Laborers Cooperative Insurance Association of  
Audrain County

AS OF  
DECEMBER 31, 2010



**FILED**  
FEB 10 2012  
DIRECTOR OF INSURANCE,  
FINANCIAL INSTITUTIONS &  
PROFESSIONAL REGISTRATION

STATE OF MISSOURI

DEPARTMENT OF INSURANCE, FINANCIAL INSTITUTIONS  
AND PROFESSIONAL REGISTRATION

JEFFERSON CITY, MISSOURI

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December 20, 2011  
Mexico, Missouri

Honorable John M. Huff, 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

**Farmers and Laborers Cooperative Insurance Association of Audrain County**

hereinafter referred to as such, or as the "Company". The Company's home office and principal place of business is located at 1005 West Monroe Street, Mexico, Missouri 65265, telephone number (573) 581-1360. This examination began on November 28, 2011, concluded on the above date, and is respectfully submitted.

**SCOPE OF EXAMINATION**

**Period Covered**

The prior full-scope examination was made as of December 31, 2005, and was conducted by examiners from the State of Missouri. The current full-scope examination covers the period from January 1, 2006 through December 31, 2010, and was conducted by examiners from the Missouri Department of Insurance, Financial Institutions and Professional Registration (DIFP).

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 by 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**

The general comments and/or recommendations of the previous examination report dated December 31, 2005, are listed below followed by the Company's response and the current examination findings regarding such general comments and/or recommendations.

### **Management and Control**

*Comment:* "The Board should develop a comprehensive policies and procedures manual to ensure consistent application of the Board's directions. An investment policy should be included that ensures compliance with statutory and regulatory requirements."

*Company Response:* "Action was taken and outlines were set forth to issue a policies and procedures manual."

*Current Findings:* The Company has not developed a policies and procedures manual.

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

*Comment:* "The Board should obtain written agreements with all its agents."

*Company Response:* "Written contracts for Company sales representatives were signed into effect between the sales persons and Company officers at the November 28, 2006 meeting."

*Current Findings:* The Company had written agreements with three of its four agents.

### **Growth and Loss Experience of the Company**

*Comment:* "The growth and size of this Company emphasizes the need for improvement in its organizational structure. The management agreement the Board developed in response to a previous examination recommendation lists several responsibilities of the manager. However, because all these duties are vested in one individual, there is no segregation of duties. This is a critical internal control that is missing in this Company. Implementation of this internal control is especially important since the Company does not have an annual independent audit."

*Company Response:* "Company does not agree with the Examiner's opinion that there is a critical internal control missing in the operation of the Company. There are three (3) people inside the Company office that oversees the operation of the business. There is no one person that could embezzle monies without one of two other people finding the cover-up."

*Current Findings:* There is no longer a written management agreement. However, the current manager's responsibilities are essentially the same as those noted in the previous examination.

*Comment:* "The Board should consider a separate claims adjusting function within the Company. The aggregate excess of loss reinsurance arrangement places a large portion of the loss payment responsibility directly on the Company. This responsibility, coupled with the increased reporting and operational responsibilities of the manager, illustrates the need for a separate adjuster. This would also help to improve the segregation of duties issue discussed above."

*Company Response:* "Our Company will be working with our Reinsurer about a coop shared claims adjuster. This is a project our Reinsurer is putting together to coop an adjuster among two or more Missouri Mutuals in our area."

*Current Findings:* The Company has a contract services agreement with its reinsurer for claims adjustment services.

## HISTORY

### General

The Company was organized and incorporated on April 6, 1891 as Farmers and Laborers Cooperative Insurance Association. On October 9, 1962, the Company amended its Articles of Incorporation and changed its name to Farmers and Laborers Cooperative Insurance Association of Audrain County. In February 1985, the Company amended its Articles of Incorporation to comply with Sections 380.201 through 380.591 RSMo (Extended Missouri Mutual Companies). The Company has a Certificate of Authority dated July 1, 1991, which was issued by the Missouri Department of Insurance, now known as the DIFP.

### Management

The annual meeting of the Company's members is held on the second Tuesday in February, at the home office of the Company, or at such other place as may be designated by the Executive Committee. 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. Ten members shall constitute a quorum at any membership meeting. Proxy voting was not addressed in the Articles of Incorporation, or Bylaws.

The management of the Company is vested in the Board of Directors, who are elected from the general membership. The Board of Director consists of seven members, serving staggered, three-year terms. All directors must be policyholders of the Company. The Board of Directors meet every quarter, and each director is compensated \$50 per hour with a \$100 minimum for each meeting attended.

The Board consisted of the following members as of December 31, 2010:

| <u>Name / Address</u>   | <u>Occupation</u>   | <u>Term</u> |
|---|---|-------------|
| Alvin Wagner<br>31715 Audrain Road 416<br>Rush Hill, MO 65280 | Farmer  | 2009-2012   |
| Harry Riechers<br>1626 Churchill Place<br>Mexico, MO 65265    | Farmer  | 2009-2012   |
| Lloyd Bruns<br>16969 Audrain Road 975<br>Thompson, MO 65285   | Farmer  | 2010-2013   |
| Dan Kilbourn<br>9573 Audrain Road 124<br>Centralia, MO 65240  | Building/Mechanical Maintenance<br>University of Missouri | 2010-2013   |
| Keith Dowell<br>80 Audrain Road 381<br>Mexico, MO 65265       | Farmer/Business Owner                                     | 2011-2014   |
| Douglas Erdel<br>1309 Cedar Ridge Cove<br>Mexico, MO 65265    | Retired   | 2009-2012   |
| Rennie Davis<br>45399 Audrain Road 548<br>Vandalia, MO 63382  | Farmer  | 2011-2014   |

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, 2010, were as follows:

|                |                     |
|----------------|---------------------|
| Lloyd Bruns    | President           |
| Harry Riechers | Vice-President      |
| Greg Sudbrock  | Secretary-Treasurer |

In addition to serving as an officer, Greg Sudbrock is also the Company's manager and one of its agents. The Manager is considered an independent contractor and receives a commission based on the Company's premiums. While approval was documented in the minutes of the membership and the Board of Directors' meetings, there is no written agreement. According to RSMo 380.611, an agreement of contract under which any person, organization or corporation is granted the

exclusive or dominant right to manage or control a Missouri mutual insurance company shall be filed with and approved by the director of the department of insurance, financial institutions and professional registration.

The Company does not have a policies and procedures manual as recommended in the two previous examinations.

### **Conflict of Interest**

The officers and directors sign a conflict of interest statement, annually. However, the Secretary-Treasurer did not complete this form. No potential material conflicts were noted based upon a review of the signed statements.

### **Corporate Records**

The Articles of Incorporation and Bylaws were reviewed. During the review, it was noted that the Bylaws state that the Company may levy and collect assessments, however the Articles of Incorporation and the insurance policies issued by the Company state that the Company is non-assessable. According to RSMo 380.431, members holding policies issued on the premium basis shall pay the stipulated premium at or before the time when the policy is issued and shall not be liable to assessment. Also, the Company could not locate a current signed and dated copy of its Bylaws.

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. The Board formally acknowledged the previous examination report during its February 13, 2007 meeting.

## **FIDELITY BOND AND OTHER INSURANCE**

The Company has fidelity bond coverage providing a liability limit of \$100,000 issued by Western Surety Company. The minimum amount recommended in the NAIC Financial Condition Examiners Handbook (Handbook) is \$125,000 for the Company's level of exposure.

The Company carries directors' and officers' liability coverage through the Missouri Association of Mutual Insurance Companies (MAMIC) with an aggregate limit of liability of \$3 million.

The Company provides errors and omissions liability insurance for its captive agents and requires proof of coverage from its independent agent. While the policies have various limits of liability, \$500,000 was the minimum amount of coverage.

The Company has property and liability insurance coverage for its office building through Grinnell Mutual Reinsurance Company (Grinnell) with limits of \$160,000 on the property, and liability limits of \$500,000 per occurrence and \$1 million aggregate.

The Company also has workers compensation and employers liability insurance with Grinnell. The workers compensation insurance applies to the Workers Compensation Laws of the state of Missouri. The policy has a limit of liability for bodily injury by accident of \$100,000 each accident and limits of liability for bodily injury by disease of \$100,000 per employee and a policy limit of \$500,000.

### **EMPLOYEE BENEFITS**

The Company has one full-time employee, who provides office support. The employee receives vacation and sick leave. No other benefits are provided.

### **INSURANCE PRODUCTS AND RELATED PRACTICES**

#### **Territory and Plan of Operations**

The Company is licensed by the DIFP as an Extended Missouri Mutual Insurance Company operating under Sections 380.201 through 380.611 RSMo (Extended Missouri Mutual Insurance Companies). The Company is authorized to write fire, windstorm and liability coverage in all Missouri counties. The Company does not write liability coverage for its policyholders, but does sell the coverage through Grinnell Mutual Reinsurance Company and receives a 20% commission. The majority of the Company's business is concentrated in Audrain and surrounding counties. Insurance is provided on a non-assessable basis. The Company advertises through local newspaper and radio advertisements, community involvement and with other promotional items such as pens, caps and calendars. The Company also has a web site at [www.farmersandlaborerscoop.com](http://www.farmersandlaborerscoop.com).

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

The Company writes continuous renewable policies. The Company uses forms supplied by Grinnell Mutual Reinsurance Company. Insurance products are sold by three captive agents and one independent agent. However, only three of the four agents had a written contract with the Company. It was also noted that the contracts lacked provisions requiring that insurance applications be fully completed and submitted to the Company within a specified time frame. The captive agents receive a 10.5% commission, with the exception of the manager, whose

commission is 11.5% as an agent. The Company's independent agent receives a 15% commission. New and renewal commissions are paid at the same rate. Property inspections are performed by the writing agent prior to the issuance of a policy and underwriting is performed by the Company's manager. Renewals are inspected approximately every third year. The Company primarily contracts with Grinnell Mutual Reinsurance Company for claims adjustment services. However, the Company uses a local independent adjuster for claims in the Licking, MO area, and minor claims are adjusted in-house.

### GROWTH AND LOSS EXPERIENCE OF THE COMPANY

|      | <u>Admitted<br/>Assets</u> | <u>Liabilities</u> | <u>Gross<br/>Premiums</u> | <u>Gross<br/>Losses</u> | <u>Investment<br/>Income</u> | <u>Underwriting<br/>Income</u> | <u>Net<br/>Income</u> |
|------|----------------------------|--------------------|---------------------------|-------------------------|------------------------------|--------------------------------|-----------------------|
| 2010 | \$ 12,028,191              | \$ 1,057,461       | \$ 1,782,919              | \$ 803,028              | \$ 565,354                   | \$ 294,305                     | \$ 749,956            |
| 2009 | 11,221,956                 | 1,001,182          | 1,706,450                 | 968,049                 | 423,373                      | 146,296                        | 501,975               |
| 2008 | 10,770,152                 | 1,051,353          | 1,659,057                 | 960,556                 | 414,220                      | (22,140)                       | 286,193               |
| 2007 | 10,354,708                 | 922,102            | 1,543,285                 | 1,022,471               | 443,624                      | 26,763                         | 391,059               |
| 2006 | 9,855,513                  | 813,966            | 1,489,492                 | 1,259,153               | 381,479                      | (135,062)                      | 190,037               |

At year-end 2010, there were 2,995 policies in-force.

### REINSURANCE

#### General

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

|         | <u>2006</u>         | <u>2007</u>         | <u>2008</u>         | <u>2009</u>         | <u>2010</u>         |
|---------|---------------------|---------------------|---------------------|---------------------|---------------------|
| Direct  | \$ 1,489,492        | \$ 1,543,285        | \$ 1,659,057        | \$ 1,706,450        | \$ 1,782,919        |
| Assumed | 0                   | 0                   | 0                   | 0                   | 0                   |
| Ceded   | (129,327)           | (150,269)           | (168,083)           | (203,665)           | (212,554)           |
| Net     | <u>\$ 1,360,165</u> | <u>\$ 1,393,016</u> | <u>\$ 1,490,974</u> | <u>\$ 1,502,785</u> | <u>\$ 1,570,365</u> |

#### Assumed

The Company does not assume any reinsurance.

### Ceded

The Company has an aggregate excess of loss reinsurance agreement with Grinnell Mutual Reinsurance Company. This agreement provides coverage for fire and wind losses above an attachment point that is calculated yearly. The attachment point for the 2010 contract year was \$1,417,497. The premium for this coverage is charged at a monthly rate based on the adjusted gross fire risk in force per \$1,000 at the end of each month during the contract year. The premium is also subject to an experience rating adjustment based on the loss ratio for the most recent five-year period.

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 Annual Statement was prepared using the accrual basis method of accounting. Accounting records for premiums, claims and financial reporting consist of paper files and are either processed manually or are transferred to a personal computer and processed electronically using a software package developed by Rural Computer Consultants. MHC Certified Public Accountants, LLC performed a compilation and prepared the Company's tax return.

### **FINANCIAL STATEMENTS**

The following financial statements, with supporting exhibits, present the financial condition of the Company for the period ending December 31, 2010, 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, 2010**

|  |               |
|--|---------------|
| Bonds  | \$ 9,230,508  |
| Stocks   | 1,020,889     |
| Real Estate                                      | 238,648       |
| Cash on Deposit                                  | 1,400,333     |
| Premium/Assessments/Agent's Balances Uncollected | 126,293       |
| Computer Equipment                               | 11,520        |
|  | -----         |
| Total Assets                                     | \$ 12,028,191 |
|  | =====         |

**LIABILITIES, SURPLUS AND OTHER FUNDS**  
**December 31, 2010**

|                                    |               |
|------------------------------------|---------------|
| Unpaid Losses                      | \$ 52,752     |
| Ceded Reinsurance Premiums Payable | 18,136        |
| Unearned Premiums                  | 908,723       |
| Federal Income Tax Payable         | 41,983        |
| Other Liabilities                  | 35,867        |
|                                    | -----         |
| Total Liabilities                  | \$ 1,057,461  |
|                                    | -----         |
| Guaranty Fund                      | \$ 150,000    |
| Other Surplus                      | 10,820,730    |
|                                    | -----         |
| Total Surplus                      | 10,970,730    |
|                                    | -----         |
| Total Liabilities and Surplus      | \$ 12,028,191 |
|                                    | =====         |

**STATEMENT OF INCOME**  
**For the Year Ending December 31, 2010**

|  |              |
|--|--------------|
| Net Premiums Earned                            | \$ 1,544,523 |
| Other Insurance Income                         | 43,898       |
| Net Losses & Loss Adjustment Expenses Incurred | (828,180)    |
| Other Underwriting Expenses Incurred           | (465,936)    |
|  | -----        |
| Net Underwriting Income (Loss)                 | \$ 294,305   |
|  | -----        |
| Investment Income                              | \$ 565,354   |
| Other Income                                   | 0            |
|  | -----        |
| Gross Profit (Loss)                            | \$ 859,659   |
| Federal Income Tax                             | (109,703)    |
|  | -----        |
| Net Income (Loss)                              | \$ 749,956   |
|  | =====        |

**CAPITAL AND SURPLUS ACCOUNT**  
**December 31, 2010**

|   |               |
|---|---------------|
| Policyholders' Surplus, December 31, 2009 | \$ 10,220,774 |
| Net Income (Loss)                         | 749,956       |
|   | -----         |
| Policyholders' Surplus, December 31, 2010 | \$ 10,970,730 |
|   | =====         |

## NOTES TO THE FINANCIAL STATEMENTS

None.

## EXAMINATION CHANGES

None.

## SUMMARY OF RECOMMENDATIONS

### **Management (Page 3)**

The Company should formalize in writing its agreement with its Manager/Secretary-Treasurer. The agreement must be filed with the DIFP as required by Section 380.611 RSMo.

### **Management (Page 3)**

The Board of Directors should set forth the Company's policies in written form by developing a comprehensive policies and procedures manual. Policies and procedures should be made available to management, employees, and agents, as deemed applicable.

### **Conflict of Interest (Page 5)**

The directors and officers of the Company should submit conflict of interest statements on an annual basis.

### **Corporate Records (Page 5)**

The Company should review, update, and restate its Bylaws, following the procedures set forth in RSMo 380.241 and its Articles of Incorporation, to reflect the Company's current operations.

### **Fidelity Bond and Other Insurance (Page 5)**

The Company should increase its fidelity bond coverage to at least \$125,000 to meet the minimum amount recommended by the NAIC.

**Policy Forms and Underwriting Practices (Page 6)**

The Company should require that all of its agents sign a written contract. The agent's contract should include a provision requiring applications be fully completed, and submitted to the Company within a specified time frame.

**SUBSEQUENT EVENTS**

There were no significant subsequent events.

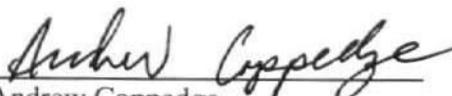
### ACKNOWLEDGMENT

The assistance and cooperation extended by the directors, officers and employees of Farmers and Laborers Cooperative Insurance Association of Audrain County during the course of this examination is hereby acknowledged and appreciated.

### VERIFICATION

State of Missouri )  
                          ) ss  
County of Cole    )

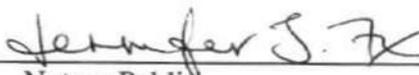
I, Andrew Coppedge, on my oath swear that to the best of my knowledge and belief the above examination report is true and accurate and is comprised of only the facts appearing upon the books, records or other documents of the company, its agents or other persons examined or as ascertained from the testimony of its officers or agents or other persons examined concerning its affairs and such conclusions and recommendations as the examiner finds reasonably warranted from the facts.

  
\_\_\_\_\_  
Andrew Coppedge  
Financial Examiner  
Missouri DIFP

Sworn to and subscribed before me this 15th day of December, 2011

My commission expires:

May 13, 2012

  
\_\_\_\_\_  
Notary Public

JENNIFER L. FOX  
Notary Public - Notary Seal  
State of Missouri  
Commissioned for St. Louis County  
My Commission Expires: May 13, 2012  
Commission Number: 08396820

### SUPERVISION

The examination process has been monitored and supervised by the undersigned. The examination report and supporting workpapers have been reviewed and approved. Compliance with NAIC procedures and guidelines as contained in the Financial Condition Examiners Handbook has been confirmed.

  
\_\_\_\_\_  
Michael Shadowens, CFE  
Audit Manager-St. Louis  
Missouri DIFP