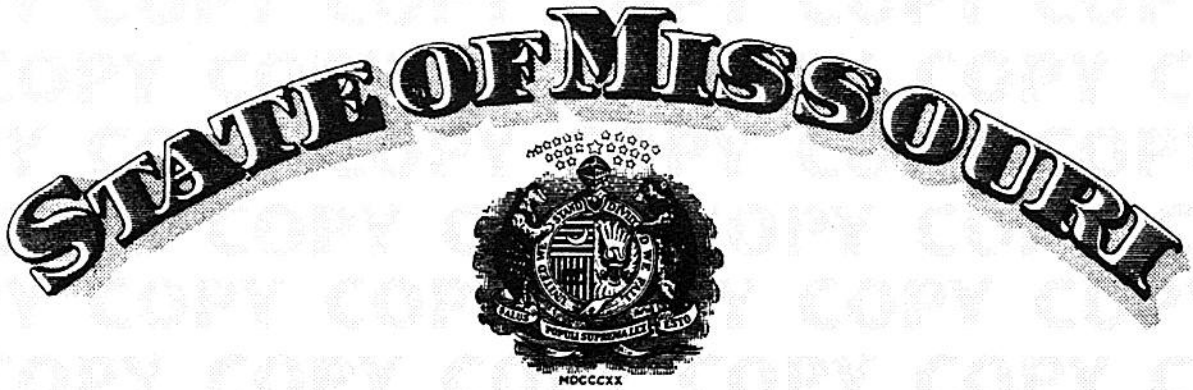


DEPARTMENT OF INSURANCE, FINANCIAL INSTITUTIONS AND PROFESSIONAL REGISTRATION

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

RE: Examination Report of Highland Mutual Insurance Company for the period ended December 31, 2012

ORDER

After full consideration and review of the report of the financial examination of Highland Mutual Insurance Company for the period ended December 31, 2012, 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 Highland Mutual Insurance Company 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 15th day of August 2013.

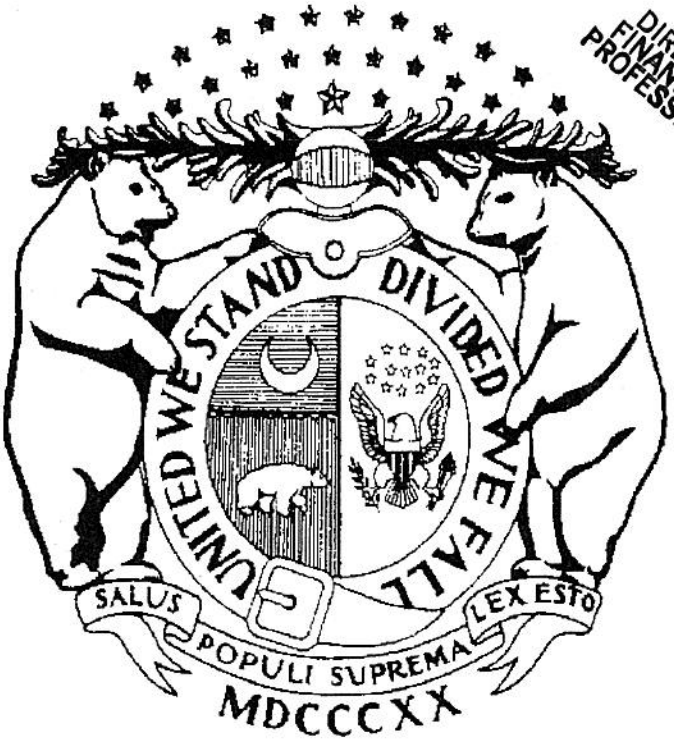
John M. Huff, Director
Department of Insurance, Financial Institutions and Professional Registration

REPORT OF THE
FINANCIAL EXAMINATION OF

HIGHLAND MUTUAL INSURANCE COMPANY

AS OF
DECEMBER 31, 2012

FILED
AUG 16 2013
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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May 6, 2013
California, 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

HIGHLAND MUTUAL INSURANCE COMPANY

hereinafter referred to as such, or as the "Company" or "Highland Mutual." The Company's administrative office is located at 104 East Third Street (P.O. Box 47), California, Missouri 65018, telephone number (573) 796-3614. This examination began and was completed on May 6, 2013, and is respectfully submitted.

SCOPE OF EXAMINATION

Period Covered

The prior full-scope examination of the Company was made as of December 31, 2007, and was conducted by examiners from the State of Missouri. The current full-scope examination covers the period from January 1, 2008, through December 31, 2012, 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 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

The comments, recommendations, and notes of the previous examination report dated December 31, 2007, are listed below followed by the Company's response and the current examination findings regarding such comments, recommendations and notes.

Accounts and Records

Comment: It was recommended the Company perform formal bank reconciliations on a monthly basis. The reconciliations should clearly present the bank balance, any outstanding and reconciling amounts and reconciled balance.

Company Response: Effective November 2008, a written report reflecting outstanding checks and deposits thereby reconciling amounts and balances is prepared and filed with the monthly bank statements.

Current Findings: As recommended, the Company currently performs bank reconciliations on a monthly basis.

Comment: It was recommended the Company properly complete future Annual Statement filings.

Company Response: The Company has obtained a copy of the Annual Statement Instructions, which has been reviewed by the Company Secretary and Treasurer in order to ensure proper reporting in future filings.

Current Findings: The issues in Annual Statement reporting noted in the prior examination have been adequately addressed by the Company.

Comment: It was recommended the Company report interest income on a consistent basis in future Annual Statement filings and retain detail of any resulting surplus adjustments.

Company Response: The Company will report interest income as noted on the 1099 tax statements and other reports as provided by the Company's financial institutions and investment managers.

Current Findings: There were no current issues noted regarding the accuracy and consistency of the Company's interest income reporting.

HISTORY

General

The Company was originally organized and incorporated on May 29, 1895, as Highland Farmer's Fire and Lightning Insurance Association, and subsequently changed its name to Highland Mutual Insurance Company. The Company has been party to several mergers since this time, and in all instances Highland Mutual remained as the surviving entity. These include mergers with Jamestown Fire Insurance Company in 2002, and Hazel Dell Mutual Insurance Company and German Salem Aid Association of Missouri in 2006.

The Company has a Certificate of Authority dated June 17, 1993, and is covered by Sections 380.201 through 380.611 RSMo. (Extended Missouri Mutual Insurance 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 last Saturday in February at the home office of the Company. 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. Quorum requirements and proxy voting are not addressed in the Articles of Incorporation.

The management of the Company is vested in the Board of Directors, who are elected from the general membership. The Articles of Incorporation require the Board of Directors to consist of nine members, serving staggered three-year terms. At December 31, 2012, the Company's Board of Directors consisted of eight members, with one vacant position (See the "Subsequent Events" section of this report). All directors must be policyholders of the Company. The Board of Directors meets approximately six times per year, and each director is compensated $75 per meeting attended.

Members serving on the Board of Directors as of December 31, 2012, were as follows:

Name and Address	Occupation	Term
Larry Rohrbach California, Missouri	Lobbyist	2012-2015
Wayne Dummermuth California, Missouri	Farmer	2011-2014
Danny Haldiman Jamestown, Missouri	Surveyor/Farmer	2011-2014

Kenneth Howard California, Missouri	Farmer	2010-2013
Robert Denker, Sr California, Missouri	Farmer/Retired Teacher	2012-2015
Fred Snyder High Point, Missouri	Farmer	2010-2013
Jerry Gerlt Barnett, Missouri	Farmer/Mail Carrier	2011-2014
Donald Wyss Russellville, Missouri	Retired School Administrator	2010-2013

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, 2012, were as follows:

Larry Rohrbach	President
Wayne Dummermuth	Vice-President
Joyce Rohrbach	Secretary
Patricia English	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. A review of the completed conflict of interest statements noted no material potential conflicts.

Corporate Records

A review was made of the Articles of Incorporation and the Bylaws of the Company. The Articles were amended on February 27, 2010, to reduce the required number of directors from ten to nine. The Bylaws were not amended during the examination period. 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.

FIDELITY BOND AND OTHER INSURANCE

The Company is a named insured on a fidelity bond providing a limit of liability of $100,000. The fidelity bond coverage of the Company meets the minimum amount suggested in the guidelines promulgated by the NAIC, which is $75,000.

The Company carries liability coverage for its directors and officers and errors and omissions coverage for its agents. The Company also carries general liability coverage for its leased home office.

The insurance coverage appears adequate.

EMPLOYEE BENEFITS

The Company has three part-time employees. The Company does not provide any employee benefits over and above employee salaries.

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 writes fire, wind, and liability coverages. The Company's policies are marketed by three agents. Agents receive a commission rate of 13% and $12.50 for each new member policy written. In addition, the agents are required to perform a coverage review of each policy every three years. The agent receives $20 for each policy review performed.

Policy Forms and Underwriting Practices

The Company utilizes primarily AAIS, MAMIC, Grinnell Mutual Reinsurance Company and custom policy forms. Policies are renewed annually. Renewal billings are mailed directly to the insured. Property inspections are performed by the agents. Property claims adjusting is performed by the agents, while liability claims adjusting is performed by the reinsurer. Rates are determined by the Board of Directors.

GROWTH AND LOSS EXPERIENCE OF THE COMPANY

Year	Admitted Assets	Liabilities	Gross Premiums	Gross Losses	Investment Income	Underwriting Income	Net Income
2012	$4,157,705	$ 496,010	$782,239	$307,103	$ 158,395	$ (27,316)	$ 105,284
2011	3,927,503	371,092	721,120	444,760	168,505	(107,311)	57,005
2010	3,892,838	393,432	612,205	174,701	164,416	73,128	164,651
2009	3,664,054	329,299	545,122	322,854	168,742	(111,296)	48,459
2008	3,542,810	250,214	439,283	457,509	170,655	(171,572)	(842)

At year-end 2012, 1,350 policies were 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:

	2008	2009	2010	2011	2012
Direct	$ 439,283	$ 545,122	$ 612,205	$ 721,120	$ 782,239
Assumed	0	0	0	0	0
Ceded	(158,768)	(158,453)	(173,219)	(194,262)	(224,580)
Net	$ 280,515	$ 386,669	$ 438,986	$ 526,858	$ 557,659

Assumed

The Company does not reinsure other companies.

Ceded

The Company has all of its reinsurance through Grinnell Mutual Reinsurance Company (the reinsurer) under an individual occurrence of loss with aggregate excess plan reinsurance agreement for property risks.

Under the individual occurrence of loss excess portion of the agreement, the Company retains $150,000 for each loss occurrence and the reinsurer's limits are $1 million per exposure, with the exception of farm machinery and equipment storage buildings, which are limited to $2 million per exposure.

Under the aggregate excess portion of the agreement, the Company's annual aggregate net retention, or attachment point, is based upon the Company's five-year average fire loss ratio plus a load, which is mutually agreed upon. The reinsurer is liable for 100% of losses in excess of this retention. The attachment point for 2012 was $416,477.

Under the facultative reinsurance portion of the agreement the Company may cede to the reinsurer risks that exceed the individual risk limits outlined in the agreement. Rates are determined by the reinsurer on an individual basis.

The agreement also provides reinsurance for liability coverages. The Company cedes 100% of liability premiums and losses to the reinsurer and receives a 20% ceding commission.

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 a modified cash basis. The Company utilizes the Automated Policy Processing System (APPS) by IMT Computer Servicing Company as its policy maintenance and accounting system. The CPA firm of Evers and Company, LLC, prepares the Company's tax filings.

FINANCIAL STATEMENTS

The following financial statements, with supporting exhibits, present the financial condition of the Company for the period ending December 31, 2012, 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.

ASSETS
December 31, 2012

Bonds (Note 1)	$ 1,133,792
Mutual Funds	200,000
Cash on Deposit	2,823,913
Other Investments (Note 1)	0
Total Assets	$ 4,157,705

LIABILITIES, SURPLUS AND OTHER FUNDS
December 31, 2012

Net Unpaid Losses	$ 59,500
Net Unpaid Loss Adjusting Expense	800
Ceded Reinsurance Premium Payable	20,558
Unearned Premiums	396,309
Federal Income Tax Payable	18,295
Accounts Payable	548
Total Liabilities	$ 496,010
Guaranty Fund	$ 150,000
Other Surplus	3,511,695
Total Surplus	3,661,695
Total Liabilities and Surplus	$ 4,157,705

STATEMENT OF INCOME
For the Year Ending December 31, 2012

Net Premiums Earned	$ 513,258
Other Insurance Income	2,905
Net Losses & Loss Adjusting Expenses Incurred	(326,834)
Other Underwriting Expenses Incurred	(216,645)
Net Underwriting Income (Loss)	$ (27,316)
Net Investment Income	158,395
Gross Profit (Loss)	$ 131,079
Federal Income Tax	(25,795)
Net Income (Loss)	$ 105,284

CAPITAL AND SURPLUS ACCOUNT
December 31, 2012

Policyholders' Surplus, December 31, 2011	$ 3,556,411
Net Income (Loss)	105,284
Policyholders' Surplus, December 31, 2012	$ 3,661,695

NOTES TO THE FINANCIAL STATEMENTS

Note 1 – Bonds/Other Investments

The Company reported a balance of $774,543 as "Other Investments." This balance consisted entirely of municipal bonds, which are more properly classified as "Bonds." The balance of $774,543 was therefore reclassified from "Other Investments" to "Bonds."

EXAMINATION CHANGES

The only examination change consisted of the reclassification of the municipal bond balance from "Other Investments" to "Bonds," as disclosed in the "Notes to the Financial Statements" above. The reclassification had a zero net effect on total policyholder surplus.

SUMMARY OF RECOMMENDATIONS

None.

SUBSEQUENT EVENTS

At the February 23, 2013 annual membership meeting, the membership approved an amendment to the Articles of Incorporation to reduce the required number of directors from nine to eight. This brought the number of director positions currently held by the Company into compliance with its Articles of Incorporation.

ACKNOWLEDGMENT

The assistance and cooperation extended by the employees of Highland Mutual Insurance Company during the course of this examination is hereby acknowledged and appreciated.

VERIFICATION

State of Missouri)
)
County of Cole)

I, Shannon W. Schmoeger 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 examiners find reasonably warranted from the facts.

Shannon W. Schmoeger, CFE
Financial Examiner
Missouri DIFP

Sworn to and subscribed before me this 22nd day of May, 2013.

My commission expires:

March 5, 2017

Tammy S Rodieck
Notary Public

TAMMY S. RODIECK
Notary Public - Notary Seal
State of Missouri
Commissioned for Cole County
My Commission Expires: March 05, 2017
Commission Number: 13751697

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.

Mark Nance, CFE, CPA
Audit Manager – Kansas City
Missouri DIFP