REPORT OF THE
FINANCIAL EXAMINATION OF

MARTINSBURG MUTUAL INSURANCE COMPANY

AS OF
DECEMBER 31, 2011

FILED
NOV 27 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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August 23, 2012
Martinsburg, 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

MARTINSBURG MUTUAL INSURANCE COMPANY

hereinafter referred to as such, or as the "Company". The Company's administrative office is located at 104 Jefferson Street (P.O. Box 171), Martinsburg, Missouri 65264, telephone number (573) 492-6168. This examination began on August 20, 2012, and concluded on August 23, 2012, and is respectfully submitted.

SCOPE OF EXAMINATION

Period Covered

The prior full-scope examination of the Company 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, 2011, 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, 2005, are listed below followed by the Company's response and the current examination findings regarding such comments, recommendations and notes.

Management and Control

Comment: The Company should develop a policy manual to ensure the Board's policies and directions are clearly communicated to all personnel. In particular, the Board should adopt an investment policy that ensures only approved investments are acquired.

Company Response: The Company does not have a written policy manual.

Current Findings: The Company is directed to develop a policies and procedures manual and file a copy of the manual with the DIFP. Areas addressed in the manual should include at a minimum, the following: investment policy, underwriting and inspection process, claims payment process, check signing procedure, employee manual, conflict of interest policy and agent payment process.

HISTORY

General

The Company was originally organized in 1905, and was incorporated on December 31, 1984, as Martinsburg Mutual Insurance Company.

The Company has a Certificate of Authority dated March 9, 2001, 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 second Saturday in January 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 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 seven members, serving staggered, three-year terms. All directors must be policyholders of the Company. The Board of Directors meets

about twice a year, and each director is compensated $200 per year.

Members serving on the Board of Directors as of December 31, 2011, were as follows:

Name and Address	Occupation	Term
Martin Bertels Laddonia, Missouri	Farmer/Crop Adjuster	2010-2013
Jim Hale Martinsburg, Missouri	Farmer	2009-2012
Martin Aulbur Martinsburg, Missouri	Farmer	2011-2014
Mike Fennewald Martinsburg, Missouri	Farmer	2011-2014
Jim Gastler Martinsburg, Missouri	Farmer/Insurance Agent	2011-2014
Rodney Willingham Martinsburg, Missouri	Farmer	2010-2013
Robert Dubbert Laddonia, Missouri	Farmer	2009-2012

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, 2011, were as follows:

Martin Bertels	President
Jim Hale	Vice-President
Linda Gastler	Secretary/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 statements noted the statement completed by Director Jim Gastler disclosed that he is the Company's agent and his spouse is the Company's sole employee and Secretary/Treasurer. No other significant disclosures were noted.

Corporate Records

A review was made of the Articles of Incorporation and the Bylaws of the Company, and this review did not indicate any amendments during the examination period. According to the minutes to the special membership meeting on April 26, 2008, the membership approved an amendment to the Articles of Incorporation. The Company indicated the amendment was to allow for the Company to transact the liability line of business. However, there is no evidence that the amendment was filed with the DIFP in accordance with Section 380.241 RSMo (Amendment to articles and bylaws, procedures –fee).

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 $25,000. The fidelity bond coverage of the Company meets the minimum amount suggested in the guidelines promulgated by the NAIC.

The Company carries liability coverage for its directors and officers and errors and omissions insurance for its agent, as well as business property and liability insurance on the home office.

The insurance coverage appears adequate.

EMPLOYEE BENEFITS

The Company has one part-time employee, who is also the Company Secretary/Treasurer. The employee received no additional benefits outside of normal wages.

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 became a direct writer of liability coverages during the examination period, whereas prior to that time, it only marketed liability products on behalf of its reinsurer under an organizational agreement. However, the Company is only authorized for the lines of fire and wind according to its certificate of authority.

The Company's policies are marketed by a single agent/director, who receives a fifteen percent commission on premiums written.

Policy Forms and Underwriting Practices

The Company utilizes various policy forms including, MAMIC, Grinnell Mutual Reinsurance Company, ACORD and AAIS forms. The policies are written on a continuous period. Renewal billings are mailed directly to the insured. Property inspections and claims adjusting are performed by the Company's agent/director. Adjusting for larger claims is coordinated with the reinsurer's adjusters. 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
2011	$1,051,437	$2,383	$206,265	$87,645	$27,713	$(5,381)	$22,332
2010	1,028,205	1,483	186,564	51,652	32,336	(3,816)	28,770
2009	999,393	1,441	158,640	15,273	33,533	41,746	75,279
2008	923,929	1,411	143,497	38,058	34,356	1,101	35,457
2007	887,867	1,258	131,343	29,762	35,831	12,147	48,478
2006	839,275	1,258	116,227	56,957	30,685	(4,823)	25,862

At year-end 2011, 152 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:

	2006	2007	2008	2009	2010	2011
Direct	$116,227	$131,343	$143,497	$158,640	$186,564	$206,265
Assumed	0	0	0	0	0	0
Ceded	(49,237)	(54,257)	(61,572)	(55,778)	(66,331)	(64,510)
Net	$ 66,990	$ 77,085	$ 81,924	$ 102,862	$ 120,234	$ 141,755

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 reinsurance agreement.

Under the individual occurrence of loss excess portion of the agreement, the Company retains $50,000 for each loss occurrence and the reinsurer's limits are $1,000,000 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 2011 was $77,944.

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 manually by the Company on a cash basis. The Martinsburg Bank and Trust provides a record keeping and reporting service that generates a general ledger and financial reports on a monthly basis, and prepares the Annual Statement. Tax filings are prepared by H&R Block.

FINANCIAL STATEMENTS

The following financial statements, with supporting exhibits, present the financial condition of the Company for the period ending December 31, 2011, 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, 2011

Bonds	$ 100,555
Mutual Funds	58,711
Real Estate	17,500
Cash and Short-Term Investments (Note 1)	873,272
Interest Due and Accrued	1,399
Total Assets	$ 1,051,437

LIABILITIES, SURPLUS AND OTHER FUNDS
December 31, 2011

Payroll Tax Payable	$ 2,383
Total Liabilities	$ 2,383
Guaranty Fund (Note 2)	$ 150,000
Other Surplus	899,054
Total Surplus	1,049,054
Total Liabilities and Surplus	$ 1,051,437

STATEMENT OF INCOME
For the Year Ending December 31, 2011

Net Premiums Earned	$ 141,755
Net Losses & Loss Adjusting Expenses Incurred	(91,570)
Other Underwriting Expenses Incurred	(55,566)
Net Underwriting Income (Loss)	$ (5,381)
Net Investment Income	27,713
Gross Profit (Loss)	$ 22,332
Federal Income Tax	(0)
Net Income (Loss)	$ 22,332

CAPITAL AND SURPLUS ACCOUNT
December 31, 2011

Policyholders' Surplus, December 31, 2010	$ 1,026,722
Net Income (Loss)	22,332
Policyholders' Surplus, December 31, 2011	$ 1,049,054

NOTES TO THE FINANCIAL STATEMENTS

Note 1 – Cash and Short-Term Investments

The Company reported a balance of $802,520 as "Other Investments." This balance consisted entirely of certificates of deposit, which are more properly classified as "Cash and Short-Term Investments." The balance of $802,520 was therefore reclassified from "Other Investments" to "Cash and Short-Term Investments."

Note 2 – Guaranty Fund

The Company began writing the liability line of business directly during the examination period. Section 380.271 RSMO (Financial reinsurance requirements) requires an additional guaranty fund balance for companies that write liability insurance. Per examination, the additional balance required for the Company is $50,000. An examination change was made to increase the guaranty fund balance by $50,000, to a total of $150,000.

EXAMINATION CHANGES

Total Policyholder Surplus Per Company, December 31, 2011			$ 1,049,054
	Increase in Surplus	Decrease in Surplus	
Cash & Short-Term Investments	$ 802,520	$ 0	
Other Investments	0	(802,520)	
Guaranty Fund	50,000		
Other Surplus		(50,000)	
Total Change	$ 852,520	$ (852,520)	(0)
Total Policyholder Surplus Per Examination, December 31, 2011			$ 1,049,054

SUMMARY OF RECOMMENDATIONS

Comments – Previous Examination Report (Page 2)

The Company is directed to develop a policies and procedures manual and file a copy of the manual with the DIFP. Areas addressed in the manual should include at a minimum, the following: investment policy, underwriting and inspection process, claims payment process, check signing procedure, employee manual, conflict of interest policy and agent payment process.

Corporate Records (Page 4)

The Company is directed to ensure the amendments to the Articles of Incorporation are filed with the DIFP in accordance with Section 380.241 RSMo (Amendment to articles and bylaws, procedures –fee).

Territory and Plan of Operations (Page 5)

The Company is directed to apply for an amended certificate of authority which includes authority for the liability line of business.

Notes to the Financial Statements (Page 10)

The Company should classify certificates of deposit as "Cash and Short-Term Investments" in future Annual Statement filings. The Company should ensure an adequate guaranty fund balance is reported on future Annual Statement filings.

SUBSEQUENT EVENTS

None.

ACKNOWLEDGMENT

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

VERIFICATION

State of Missouri)
) ss
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 27th day of August, 2012.

My commission expires:

February 10, 2013

Tammy S. Rodieck
Notary Public

TAMMY S. RODIECK
NOTARY PUBLIC STATE OF MISSOURI
COLE COUNTY
#07551697
MY COMMISSION EXPIRES
February 10, 2013
NOTARY SEAL

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