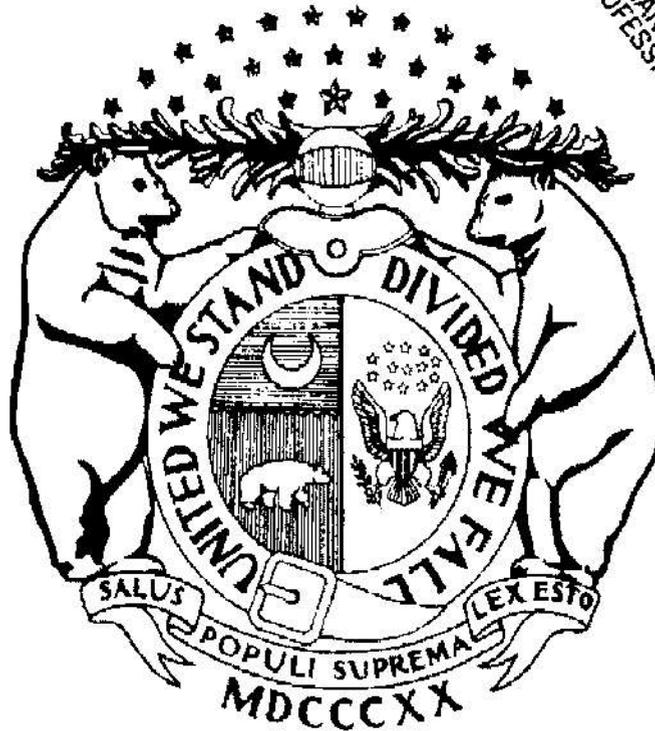


REPORT OF THE
FINANCIAL EXAMINATION OF
PATRONS AND FARMERS MUTUAL OF MISSOURI

AS OF
DECEMBER 31, 2008

FILED
JUL 24 2009
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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March 25, 2009
Harrisonville, 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

PATRONS AND FARMERS MUTUAL OF MISSOURI

hereinafter referred to as such, or as the "Company". The Company's administrative office is located at 1003 W. Mechanic, PO Box 236, Harrisonville, Missouri 64701, telephone number (816) 380-4241. This examination began on March 16, 2009, and concluded on March 20, 2009, and is respectfully submitted.

SCOPE OF EXAMINATION

Period Covered

The prior full-scope examination of the Company was made as of December 31, 2003 and was conducted by examiners from the State of Missouri. The current full-scope examination covers the period from January 1, 2004, through December 31, 2008, 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

There were no comments, recommendations or notes from the previous examination report dated December 31, 2003.

HISTORY

General

The Company was originally organized in 1877 and incorporated on January 30, 1896 as Patrons and Farmers Mutual Fire Insurance Company of Cass County. Effective August 21, 2006, the Company merged with Farmer's Mutual Insurance Company of Lee's Summit. The surviving Company's name was changed to Patrons and Farmers Mutual of Missouri. The Company operates under Sections 380.201 through 380.611 RSMo (Extended Missouri Mutual Insurance Companies).

Management

In accordance with the Articles of Incorporation, the annual meeting of the Company's members is held on the first Wednesday in April, at the home office of the Company or at such other place as may be designated by the Board of Directors. Eight members shall constitute a quorum at any membership meeting. Proxy voting is not 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 every month, and the directors are compensated \$225 per each meeting attended.

Members serving on the Board of Directors as of December 31, 2008, were as follows:

| <u>Name and Address</u> | <u>Occupation</u> | <u>Term</u> |
|---------------------------------------|-----------------------------|-------------|
| Ronald J. Dean Peculiar, Missouri | Insurance Agent | 2007-2010 |
| Victor A. Shipley Drexel, Missouri | Insurance/Real Estate Agent | 2007-2010 |
| Gary Kerby Raymore, Missouri | Tax Preparer | 2006-2009 |

| | | |
|--|-----------------------------|-----------|
| Larry W. Duncan Freeman, Missouri | Insurance Agent/Farmer | 2008-2011 |
| Everett L. Helms Garden City, Missouri | Insurance Agent/Farmer | 2008-2011 |
| Phillip Kelley Harrisonville, Missouri | Farmer | 2006-2009 |
| Gerald E. Land, Jr. Pleasant Hill, Missouri | Insurance/Real Estate Agent | 2008-2011 |
| Michael N. Kohler Harrisonville, Missouri | Insurance Agent/Farmer | 2006-2009 |
| John T. Southard Harrisonville, Missouri | Insurance Agent | 2007-2010 |

The Board of Directors elects for a term of one year the officers of the Company. The officers of the Company serving at December 31, 2008, were as follows:

| | |
|--------------------|----------------|
| Ronald J. Dean | President |
| Gerald E. Land Jr. | Vice-President |
| Vickie Francy | Secretary |
| Larry W. Duncan | 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. Conflict of interest statements were reviewed for the period under examination and no potential material conflicts were disclosed.

Corporate Records

A review was made of the Articles of Incorporation and the Bylaws of the Company. The Articles of Incorporation were not amended during the examination period. On February 11, 2009, the membership approved amended and restated Bylaws. The amendment removed the requirement that a director be a resident of the territory for which a directorship shall become vacant and provided for the election of two directors at large.

The minutes of the membership and the Board of Directors' meetings were reviewed for the period under examination. In addition, the Company's policies for investments and underwriting were reviewed. 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.

The Company carries directors' and officers' liability coverage with an annual aggregate limit of \$3,000,000 and a \$2,500 per loss deductible.

The Company requires its agents to purchase a minimum of \$500,000 in errors and omissions insurance coverage at their own expense.

Other insurance coverages carried by the Company include home office and contents, business liability and workers compensation.

The insurance coverage appears adequate.

EMPLOYEE BENEFITS

The Company has 4 full-time employees. The benefits package offered to employees includes an allowance for the purchase of private health insurance and paid time off.

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, 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 twelve licensed agents and agencies. Agents receive a 17.5%

commission on fire and wind policies and a 6% commission on commercial liability and inland marine policies. The agent commission rate is reduced by 1% for the following year if the loss ratio is over 75% at the end of the calendar year. The agent agreements provide for the compensation of an agent in such amounts as approved by the Board of Directors and as specified in a separate schedule of the agent's commission. However, the agent agreements did not have a separate commission schedule attached. It is recommended that the Company comply with the provisions of the agent agreements by attaching the required commission schedules to these agreements.

Policy Forms and Underwriting Practices

The Company utilizes AAIS policy forms. The policies are written on a continuous period. Rates are determined by the Board of Directors. Renewal billings are mailed directly to the insured. During the examination period, an independent inspector/adjuster performed inspections and adjusting services on large claims, and the agents performed adjusting services on small claims. Effective January 1, 2009, each agent is performing their own inspections and adjusting, as well as re-inspecting all insured properties over the next two years.

GROWTH AND LOSS EXPERIENCE OF THE COMPANY

| | <u>Admitted Assets</u> | <u>Liabilities</u> | <u>Gross Assessments</u> | <u>Gross Losses</u> | <u>Investment Income</u> | <u>Underwriting Income</u> | <u>Net Income</u> |
|------|----------------------------|--------------------|------------------------------|-------------------------|------------------------------|--------------------------------|-----------------------|
| 2008 | \$2,851,670 | \$1,211,457 | \$2,455,387 | \$1,904,828 | \$ 70,485 | \$(169,222) | \$ (70,471) |
| 2007 | 2,999,873 | 1,289,193 | 2,434,107 | 3,248,376 | 109,464 | (275,051) | (169,262) |
| 2006 | 3,279,497 | 1,399,566 | 2,688,322 | 3,243,596 | 96,794 | (569,498) | (307,939) |
| 2005 | 3,229,470 | 1,102,058 | 2,260,413 | 821,904 | 99,749 | 90,628 | 171,690 |
| 2004 | 3,028,477 | 1,076,673 | 2,032,623 | 1,198,492 | 99,015 | 116,509 | 147,702 |

At year-end 2008, 3,589 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:

| | <u>2004</u> | <u>2005</u> | <u>2006</u> | <u>2007</u> | <u>2008</u> |
|---------|---------------------|--------------------|--------------------|--------------------|--------------------|
| Direct | \$2,032,623 | \$2,260,413 | \$2,688,322 | \$2,434,107 | \$2,455,387 |
| Assumed | 0 | 0 | 0 | 0 | 0 |
| Ceded | <u>(522,274)</u> | <u>(631,669)</u> | <u>(817,743)</u> | <u>(1,416,823)</u> | <u>(1,389,649)</u> |
| Net | <u>\$ 1,510,349</u> | <u>\$1,628,744</u> | <u>\$1,870,579</u> | <u>\$1,017,284</u> | <u>\$1,065,738</u> |

Assumed

The Company does not reinsure other companies.

Ceded

The Company has all of its reinsurance through Rockford Mutual Insurance Company (the reinsurer) under separate reinsurance contracts for fire, wind and liability coverages.

The reinsurance agreements for the peril of fire provide per risk and aggregate excess of loss coverages. Under the per risk excess of loss coverage, the Company retains \$75,000 each risk and the reinsurer's limit is \$925,000 per risk. The aggregate excess contract consists of two layers. Under layer one, the Company retention is equal to 70% of subject net premium. The reinsurer is liable for 85% of losses in excess of the retention, limited to 85% of 70% of subject net premium. Under layer two, the reinsurer is responsible for 100% of losses in excess of 140% of subject net premium.

The Company has a quota share reinsurance agreement for the perils of wind and hail. The reinsurer assumes 100% of the premiums and risks associated with these perils, with the exception of the loss ratio corridor. Under the loss ratio corridor provisions, the Company must reimburse the reinsurer the same percentage of subject net premium that the loss ratio exceeds 65%, limited to a reimbursement of 15% of subject net premium. The Company receives a 26% ceding commission and is eligible for a 4% provisional commission if the loss ratio is below 65%. Risks ceded under the contract are limited to \$1,000,000 per risk. Individual risks in excess of this limit may be ceded to the reinsurer on a facultative basis per the agreement provisions.

The Company is eligible for a 10% profit sharing program associated with the property reinsurance agreements described above.

The Company has a liability excess of loss reinsurance agreement for liability risks. The Company retains \$5,000 per loss occurrence and the reinsurer is liable for all losses in excess of the retention.

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 Company maintains its records on an accrual basis. The CPA firm of DSWA Certified Public Accountants, P.C. prepares the Annual Statement and tax filings. Annual audits of the Company's financial statements had been performed prior to 2008. An annual financial audit was not performed for 2008.

The Company failed to properly report per-risk and pro-rata premium ceded on Page 2 Section 1 "Direct Assessments/Premiums" of the Annual Statement. The Company combined per-risk and pro-rata reinsurance premium with aggregate excess reinsurance premium and reported the total on Page 2 Section 3 "Catastrophe/Aggregate Excess of Loss Premiums Ceded." The Company is directed to properly report per risk and pro-rata reinsurance premium ceded by line of business on Page 2 Section 1 "Direct Assessments/Premiums" of future Annual Statement filings.

FINANCIAL STATEMENTS

The following financial statements, with supporting exhibits, present the financial condition of the Company for the period ending December 31, 2008, 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, 2008

| | |
|--|----------------------------|
| Bonds | \$ 909,046 |
| Real Estate | 80,798 |
| Cash on Deposit | 1,718,838 |
| Reinsurance Recoverable on Paid Losses | 9,804 |
| Computer Equipment | 2,643 |
| FTT Recoverable | 16,730 |
| Interest Due and Accrued | 16,896 |
| Other Assets | 96,915 |
| Total Assets | <u><u>\$ 2,851,671</u></u> |

LIABILITIES, SURPLUS AND OTHER FUNDS
December 31, 2008

| | |
|-----------------------------------|--------------|
| Losses Unpaid | \$ 270,628 |
| Ceded Reinsurance Premium Payable | 267,543 |
| Unearned Premium | 655,557 |
| Premium Tax Liability | 15,444 |
| Accounts Payable | 1,556 |
| Accrued Expenses | 728 |
| | ----- |
| Total Liabilities | \$ 1,211,456 |
| | ----- |
| Guaranty Fund (Note 1) | \$ 369,175 |
| Other Surplus | 1,271,040 |
| | ----- |
| Total Surplus | 1,640,215 |
| | ----- |
| Total Liabilities and Surplus | \$ 2,851,671 |
| | ===== |

STATEMENT OF INCOME
For the Year Ending December 31, 2008

| | |
|--|--------------|
| Net Assessments Earned | \$ 1,108,527 |
| Other insurance Income | 88,996 |
| Net Losses & Loss Adjustment Expenses Incurred | (601,506) |
| Other Underwriting Expenses Incurred | (765,239) |
| | ----- |
| Net Underwriting Income (Loss) | \$ (169,222) |
| | ----- |
| Investment Income | \$ 70,485 |
| Other Income | 11,536 |
| | ----- |
| Gross Profit (Loss) | \$ (87,202) |
| Federal Income Tax | 16,730 |
| | ----- |
| Net Income (Loss) | \$ (70,472) |
| | ===== |

CAPITAL AND SURPLUS ACCOUNT
December 31, 2008

| | |
|---|--------------|
| Policyholders' Surplus, December 31, 2007 | \$ 1,710,680 |
| Net Income (Loss) | (70,472) |
| Rounding | 7 |
| | ----- |
| Policyholders' Surplus, December 31, 2008 | \$ 1,640,215 |
| | ===== |

NOTES TO THE FINANCIAL STATEMENTS

Note 1 – Guaranty Fund

The Company understated the guaranty fund required by Section 380.271 RSMo. (Financial Reinsurance Requirements). The minimum aggregate guaranty fund required by the statute is \$369,175, while the amount reported on the 2008 Annual Statement was \$150,000. An examination change was made to increase the guaranty fund by \$219,175, with a corresponding decrease of \$219,175 to other surplus. The examination change had no affect on the total policyholder surplus balance. It is recommended the Company report an adequate guaranty fund balance in future Annual Statement filings in order to comply with the provisions of Section 380.271 RSMo (Financial Reinsurance Requirements).

EXAMINATION CHANGES

As disclosed in Note 1 above, the only examination change was related to the guaranty fund and resulted in no change to total policyholder surplus.

GENERAL COMMENTS AND RECOMMENDATIONS

Territory and Plan of Operations (Page 5)

It is recommended that the Company comply with the provisions of the agent agreements by attaching the required commission schedules to these agreements.

Accounts and Records (Page 6)

The Company is directed to properly report per-risk and pro-rata reinsurance premium ceded by line of business on Page 2 Section 1 "Direct Assessments/Premiums" of future Annual Statement filings.

Guaranty Fund (Page 11)

It is recommended the Company report an adequate guaranty fund balance in future Annual Statement filings in order to comply with the provisions of Section 380.271 RSMo (Financial Reinsurance Requirements).

SUBSEQUENT EVENTS

None.

PATRONS and FARMERS MUTUAL of MISSOURI
P. O. Box 236
HARRISONVILLE, MO 64701
(816) 380-4241
Fax # (816) 884-5205

JULY 14, 2009

Frederick G. Heese, CFE, CPA
Chief Financial Examiner & Acting Division Director

RE: Examination Report

Dear Mr. Heese:

The following is our response to the changes as stated in the report submitted to our company.

Under General Comments and Recommendations

Territory and Plan of Operations: We have attached the required commission schedules to the agreements.

Accounts and Record: We will correct this in the future Annual Statement filings.

Guaranty Fund: We will correct this in the future Annual Statement filings.

Please include this response to the report as part of the public document.

If I can be of any further assistance, please let me know.

Sincerely,



Ron J. Dean
President, Patrons & Farmers Mutual of Missouri