

**REPORT ON EXAMINATION**  
**OF**  
**FARMERS ALLIANCE MUTUAL INSURANCE COMPANY**  
**1122 NORTH MAIN STREET**  
**MCPHERSON, KANSAS 67460**  
**AS OF**  
**DECEMBER 31, 2017**

**FILED**  
**MAY 15 2019**  
**VICKI SCHMIDT**  
**Commissioner of Insurance**

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McPherson, Kansas  
March 1, 2019

Honorable Vicki Schmidt  
Commissioner of Insurance  
Kansas Insurance Department  
420 SW 9th Street  
Topeka, Kansas 66612-1678

Dear Commissioner:

In accordance with your authorization and pursuant to K.S.A. 40-222 – *Examination of condition of company*, an examination has been conducted of the financial condition and business affairs of:

**FARMERS ALLIANCE MUTUAL INSURANCE COMPANY**

with its statutory home office and main office at:

**1122 NORTH MAIN STREET  
MCPHERSON, KANSAS 67460**

hereinafter referred to as “the Company” or “FAMI”. The following report on such examination is respectfully submitted.

**SCOPE OF EXAMINATION**

The examiners have performed a multi-state financial examination of Farmers Alliance Mutual Insurance Company, a Kansas domiciled mutual property and casualty insurance company. The last examination covered the four-year period from January 1, 2010, through December 31, 2013. This examination covers the four-year period from January 1, 2014, through December 31, 2017.

The examination was conducted in accordance with the rules, regulations and directives of the Kansas Insurance Department (“KID”) and the observed guidelines and procedures contained in the National Association of Insurance Commissioners (“NAIC”)

*Financial Condition Examiners Handbook* ("Handbook"). The Handbook requires the examiners plan and perform the examination to evaluate the financial condition, assess corporate governance, identify current and prospective risks of the Company and evaluate system controls and procedures used to mitigate those risks. An examination also includes identifying and evaluating significant risks that could cause an insurer's surplus to be materially misstated both currently and prospectively.

All accounts and activities of the Company were considered in accordance with the risk-focused examination process. This may include assessing significant estimates made by management and evaluating management's compliance with Statutory Accounting Principles. The examination does not attest to the fair presentation of the financial statements included herein. If, during the course of the examination an adjustment is identified, the impact of such adjustment will be documented separately following the Company's financial statements.

This examination report includes significant findings of fact, as mentioned in K.S.A. 40-222, *Examination of condition of company*, and general information about the insurer and its financial condition. There may be other items identified during the examination that, due to their nature (e.g., subjective conclusions, proprietary information, etc.), are not included within the examination report but separately communicated to other regulators and/or the Company.

### **Independent Audit Reports**

The consolidated financial statements of the Farmers Alliance Insurance Companies, which are Farmers Alliance Mutual Insurance Company, Alliance Insurance Company, Inc. and Alliance Indemnity Company were audited by Strohm Ballweg, LLP. for the years ending December 31, 2014, through December 31, 2017. In each of the

years under examination, the auditors concluded that the financial statements of the Companies, present fairly, in all material respects, the admitted assets, liabilities and policyholders' surplus of the Companies and the results of their operations and their cash flows for the years then ended in accordance with the accounting practices prescribed or permitted by the KID.

The independent auditor's work papers were reviewed and analyzed by the examiners; whereby significant reliance was placed on select work papers during the course of this examination.

#### **SUMMARY OF SIGNIFICANT FINDINGS**

No significant findings were noted during the course of the examination.

#### **COMPANY HISTORY**

The McPherson County Farmers Fire Relief Association was incorporated on July 20, 1888, under K.S.A. 40-1201 et seq. – *Mutual Insurance Companies Other Than Life*. The name of the Company was changed to Kansas Farmers Alliance Insurance Company on December 31, 1889; Farmers Alliance Insurance Company of Kansas on October 3, 1893; Farmers Alliance Insurance Company on January 23, 1906; and to Farmers Alliance Mutual Insurance Company on April 9, 1954. On April 9, 1954, the charter powers were expanded to permit multiple line underwriting. In 1969, FAMI was merged with Alliance Mutual Casualty Company, with FAMI being the surviving entity. Effective April 1, 1993, Consolidated Farmers Mutual Insurance Company, Inc. of Colwich, Kansas, was merged with and into the Company with FAMI being the surviving entity.

The Company's charter provides for a perpetual existence.

## **MANAGEMENT AND CONTROL**

FAMI's bylaws consist of nineteen articles that provide the framework for the operation, management and control of the Company. As a mutual insurance company, FAMI is controlled by its policyholders and managed by a Board of Directors ("Board"). The Board consists of no less than nine persons and no more than thirteen persons. A minimum of three directors are elected by the policyholders at each annual meeting to serve for a term of three years, or until their successors are elected and qualified. Should a vacancy occur on the Board, the remaining directors select a replacement to serve until the next annual meeting, at which time a successor will be elected by a vote of the policyholders to fill the unexpired term.

Board meetings are to be held no less than quarterly. Special meetings of the Board will be called by the Company President when, in his judgment, the interests of the Company require it; or upon written application from three members of the Board.

The exhibit on the following page contains a listing of directors, their principal occupations, and elected terms as of December 31, 2017.

<u>Name</u>	<u>Principal Occupation</u>	<u>Term Expires</u>
L. Keith Birkhead McPherson, Kansas	President, Chief Executive Officer and Chairman of the Board Farmers Alliance Mutual Ins. Co.	2020
Robert M. Alexander Calhan, Colorado	Chief Executive Officer and Chairman of the Board Stockmens Bank	2020
Sheila G. Frahm Colby, Kansas	Retired	2018
Joseph W. Jeter Hays, Kansas	Attorney Jeter Law Firm, LLP	2018
Eric J. Larson Wichita, Kansas	Attorney & CPA Bever Dye, LC	2018
Brett A. Reber McPherson, Kansas	Attorney Wise & Reber, LC	2018
Robert J. Breidenthal, Jr. Bonner Springs, Kansas	President Security Bank	2019
Joe F. Jenkins, II Tonganoxie, Kansas	Retired	2019
Marilyn B. Pauly Wichita, Kansas	Vice Chairman Commerce Bank Wichita	2019
Vincent R. Amanor-Boadu, PhD. Manhattan, Kansas	Associate Professor Dept. of Agricultural Economics Kansas State University	2019
<b>Advisory Director:</b> I. John Cholnoky Big Sky, Montana	Retired	2018

The bylaws provide for the Board to have exclusive power and authority to manage the affairs of the Company and may appoint various committees as it deems necessary. As of December 31, 2017, the Company had established an executive committee, an audit committee, a finance committee, a corporate governance committee, and a compensation committee. The members of these committees are as follows:

Name	Executive	Audit	Finance	Corporate Governance	Compensation
L. Keith Birkhead	Member			Chair	Member
Robert M. Alexander		Member	Chair	Member	
Sheila G. Frahm		Member	Member		Member
Joseph W. Jeter		Member	Member		Member
Eric J. Larson	Member	Chair		Member	
Brett A. Reber		Member		Member	Chair
Robert J. Breidenthal, Jr.	Chair		Member	Member	
Joe F. Jenkins, II	Member		Member		Member
Marilyn B. Pauly	Member		Member		Member
Vincent R. Amanor-Boadu		Member		Member	Member
I. John Cholnoky		Member		Member	

The officers of the Company are a Chairman of the Board, a President, a Secretary and a Treasurer. Various Vice Presidents may be elected as well as other officers that are deemed necessary and expedient. The officers listed below were duly elected as of December 31, 2017.

<u>Name</u>	<u>Position</u>
L. Keith Birkhead	President, CEO and Chairman of the Board
W. Paul Taliaferro	CFO, Secretary and Treasurer
John M. Rader	Vice President, Marketing and Reinsurance
Andrew L. Edwardson	Vice President, Information Technology
Ryan P. Hicks	Vice President, Human Resources
Tonya K. Schafer	Vice President, Product and Compliance
Randall L. Lutgen	Vice President, Underwriting

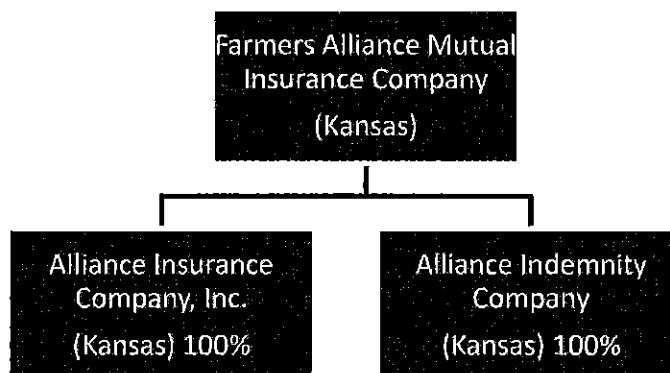
### INSURANCE COMPANY HOLDING SYSTEM

K.S.A. 40-3301, et seq. - *Insurance Holding Companies*, requires a domestic insurer that is part of an insurance holding company system to file appropriate registration statements with the Commissioner of Insurance. The Company has submitted Form "B" and "C" registration statements to the KID for each of the years



under examination. A review of the registration statements indicated that the Company is properly reporting items and events as required by statute.

The organizational chart below illustrates the identities and intercompany relationships among insurance the Farmers Alliance Insurance Companies and the controlling entities thereof, as of December 31, 2017.



### **Intercompany/Cost Sharing Agreements**

In 1979, FAMI and its subsidiaries have an intercompany pooling agreement, which is detailed in the “Reinsurance” section of this report.

FAMI files a consolidated tax return with its subsidiary companies in accordance with a tax allocation agreement, which was last reaffirmed in 2004.

In 2015, FAMI and its subsidiary companies entered into an Administrative Services Agreement to share all costs allocated among each company based upon the percentages in the intercompany pooling agreement.

### **TERRITORY AND PLAN OF OPERATION**

As of December 31, 2017, the Company is authorized to transact business in the following states; Colorado, Idaho, Iowa, Kansas, Minnesota, Missouri, Montana, Nebraska, New Mexico, North Dakota, Oklahoma, Oregon, South Dakota, Washington,

Wyoming. The NAIC Schedule T Exceptions Report was reviewed for each of the states where the Company is licensed. No exceptions were noted.

As of December 31, 2017, the Company's largest lines of business were farm owners multiple peril at 49% of direct premiums written, home owners multiple peril at 10%, other private passenger auto liability at 8% and private passenger auto physical damage at 8%. The remaining 25% represented fire, allied lines, inland marine, commercial auto and other liability business.

### GROWTH OF COMPANY

The exhibit below shows the Company's financial growth (in thousands) for the period of December 31, 2013, through December 31, 2017. The financial growth amounts were obtained from annual statements filed by the Company.

	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>	<u>2017</u>
<i>(in thousands)</i>					
Admitted Assets	277,144	288,872	304,753	309,641	319,154
Liabilities	133,158	141,544	139,112	140,613	143,448
Capital and Surplus	143,986	147,328	165,641	169,028	175,706
Net Underwriting Gain/(Loss)	(1,593)	3,285	7,192	(2,132)	(280)
Net Income	3,959	8,466	11,318	2,562	5,305
Net Premiums Written	123,706	129,480	132,213	133,587	139,207

### REINSURANCE

FAMI is the lead company in an intercompany quota share reinsurance agreement with its subsidiary companies, Alliance Insurance Company, Inc. ("AIC") and Alliance Indemnity Company ("AInC"). Under the provisions of the agreement, both subsidiary companies cede 100% of their premiums to FAMI. Of the business remaining after cessions to non-affiliated insurance companies, FAMI retains 87.5% of

the pooled business and then retro-cedes 10% to AIC and 2.5% to AInC. All expenses directly attributable to the business ceded by AIC and AInC are divided in the same proportions as indicated above. The current agreement has been in place since 1979.

FAMI limits the maximum net loss that can arise from large risks or risks in concentrated areas of exposure by reinsuring certain levels of risk with other insurers or reinsurers, either on an automatic basis under general reinsurance contracts, or by negotiation on individual risks. There is a comprehensive reinsurance program in place that includes property and casualty excess of loss, fidelity and surety bond excess of loss, commercial catastrophe excess of loss, three layers of property catastrophe excess of loss, and aggregate catastrophe excess of loss coverage.

All reinsurance agreements reviewed during the course of the examination contained insolvency and cancellation clauses as required by paragraph (c) of K.S.A. 40-221a—*Reinsurance of risks of and by Kansas companies*. All reinsurance agreements reviewed provided for the transfer of risk.

## **FINANCIAL STATEMENTS**

The following financial statements are based on the statutory financial statements filed by the Company with the Kansas Insurance Department and present the financial condition of the Company for the period ending December 31, 2017. The accompanying comments on financial statements reflect any examination adjustments to the amounts reported in the annual statement and should be considered an integral part of the financial statements.

**FARMERS ALLIANCE MUTUAL INSURANCE COMPANY**  
**ANALYSIS OF ASSETS**  
**AS OF DECEMBER 31, 2017**

	<u>Assets</u>	<u>Assets Nonadmitted</u>	<u>Net Admitted Assets</u>
Bonds	\$ 239,291,779		\$ 239,291,779
Common stocks	27,920,338		27,920,338
Properties occupied by the Company	5,672,764		5,672,764
Cash and short-term investments	5,370,121		5,370,121
Other invested assets	7,000		7,000
Investment income due & accrued	1,565,206		1,565,206
Uncollected premiums and agents' balances in the course of collection	29,530,601	\$ 113,795	29,416,806
Amounts recoverable from reinsurers	367,156		367,156
Funds held by or deposited with reinsured companies	100,000		100,000
Current federal and foreign income tax recoverable	1,168,216		1,168,216
Net deferred tax asset	7,994,830	943,939	7,050,891
Guaranty funds receivable or on deposit	84,596		84,596
EDP equipment and software	5,381,054	4,940,821	440,233
Furniture and equipment	360,678	360,678	-
Aggregate write-ins for other than invested assets	1,627,501	928,148	699,353
<b>Totals</b>	<u>\$ 326,441,840</u>	<u>\$ 7,287,381</u>	<u>\$ 319,154,459</u>

**FARMERS ALLIANCE MUTUAL INSURANCE COMPANY  
LIABILITIES, SURPLUS AND OTHER FUNDS  
AS OF DECEMBER 31, 2017**

Losses	\$ 37,826,220
Reinsurance payable on paid losses and loss adjustment expenses	2,009,173
Loss adjustment expenses	6,806,972
Commissions payable, contingent commissions and other similar charges	4,241,227
Other expenses	248,869
Taxes, licenses and fees	1,053,233
Unearned premiums	71,361,460
Advance premiums	2,054,365
Ceded reinsurance premiums payable	1,694,559
Amounts withheld or retained by company for others	16,103,175
Remittances and items not allocated	49,396
Total liabilities	<u>143,448,650</u>
Aggregate write-ins for special surplus funds	500,000
Unassigned funds	<u>175,205,809</u>
Surplus as regards policyholders	<u>175,705,809</u>
Totals	<u>\$ 319,154,459</u>

**FARMERS ALLIANCE MUTUAL INSURANCE COMPANY  
STATEMENT OF INCOME  
CAPITAL AND SURPLUS ACCOUNT  
FOR THE YEAR ENDED DECEMBER 31, 2017**

<u>Underwriting Income:</u>	
Premiums earned	\$ 135,237,702
<u>Deduct:</u>	
Losses incurred	80,096,125
Loss adjustment expenses incurred	12,808,520
Other underwriting expenses incurred	42,613,284
Total underwriting deductions	<u>135,517,929</u>
Net underwriting gain or (loss)	(280,227)
<u>Investment Income:</u>	
Net investment income earned	5,216,680
Net realized capital gains or (losses)	801,600
Net investment gain or (loss)	<u>6,018,280</u>
<u>Other Income:</u>	
Net gain (loss) from agents' or premium balances charged off	(18,658)
Finance and service charges not included in premiums	381,765
Aggregate write-ins for miscellaneous income	(45,388)
Total other income	<u>317,719</u>
Net income after dividends to policyholders and before federal income taxes	6,055,772
Federal income taxes incurred	751,269
Net income	<u>\$ 5,304,503</u>

**CAPITAL AND SURPLUS ACCOUNT**

Surplus as regards policyholders, December 31, 2016	\$ 169,027,546
Net income	5,304,503
Change in net unrealized capital gains (losses)	1,243,517
Change in net deferred income tax	(3,785,574)
Change in nonadmitted assets	6,311,900
Change in provision for reinsurance	8,424
Aggregate write-ins for gains and losses in surplus	(2,404,507)
Change in surplus as regards policyholders for the year	<u>6,678,263</u>
Surplus as regards policyholders, December 31, 2017	<u>\$ 175,705,809</u>

**FARMERS ALLIANCE MUTUAL INSURANCE COMPANY  
CAPITAL AND SURPLUS ACCOUNT  
RECONCILIATION OF CAPITAL AND SURPLUS SINCE LAST EXAMINATION**

Surplus as regards policyholders, December 31, 2013			<u>\$ 143,985,649</u>
Net income	2014	8,466,273	
	2015	11,317,939	
	2016	2,562,241	
	2017	<u>5,304,503</u>	27,650,956
Change in net unrealized capital gains or (losses)	2014	1,048,365	
	2015	333,749	
	2016	1,900,077	
	2017	<u>1,243,518</u>	4,525,709
Change in net deferred income tax	2014	(488,122)	
	2015	(3,646,195)	
	2016	(1,272,075)	
	2017	<u>(3,785,574)</u>	(9,191,967)
Change in nonadmitted assets	2014	863,594	
	2015	4,858,167	
	2016	2,196,040	
	2017	<u>6,311,900</u>	14,229,701
Change in provision for reinsurance	2014	-	
	2015	-	
	2016	(8,424)	
	2017	<u>8,424</u>	-
Aggregate write-ins for gains and losses in surplus	2014	(6,547,262)	
	2015	5,448,444	
	2016	(1,990,913)	
	2017	<u>(2,404,507)</u>	<u>(5,494,239)</u>
Surplus as regards policyholders, December 31, 2017			<u><u>\$ 175,705,809</u></u>



### **ANALYSIS OF CHANGES IN FINANCIAL STATEMENTS**

No adjustments were made to surplus as a result of this examination. The capital and surplus of the Company, as of December 31, 2017, was \$175,705,809, which was the same amount, reported by the Company in its 2017 filed Annual Statement.

### **COMMENTS ON FINANCIAL STATEMENTS**

There were no significant or material findings resulting from the examination that warranted inclusion in the Report on Examination.

### **SUBSEQUENT EVENTS**

There were no significant or material subsequent events resulting from the examination that warranted inclusion in the Report on Examination.

### **SUMMARY OF RECOMMENDATIONS**

There were no significant or material recommendations resulting from the examination that warranted inclusion in the Report on Examination.

### **MANAGEMENT LETTER**

There were several immaterial findings resulting from the examination that didn't warrant inclusion in this report. However, concerns were noted in a management letter that was issued to the Company's Board of Directors for review, resolution and response back to the KID.

## CONCLUSION

The assistance and cooperation by the officers of the Company during the course of this examination is hereby acknowledged and appreciated. In addition to the undersigned, Ms. Tamara House, CFE, a financial examiner representing the Kansas Insurance Department and Mr. Shane Mead, CISA, CISM, CRISC, an information technology examiner representing the Kansas Insurance Department, participated in this examination.

Respectfully submitted,



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Christopher W. Buchanan, CPA, CFE  
Senior Insurance Examiner  
Examiner-in-Charge

**EXHIBIT 5**  
**EXAMINER'S AFFIDAVIT AS TO STANDARDS AND**  
**PROCEDURES USED IN AN EXAMINATION**

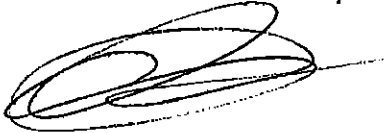
State of Kansas,

County of Shawnee,

Christopher W. Buchanan, being duly sworn, states as follows:

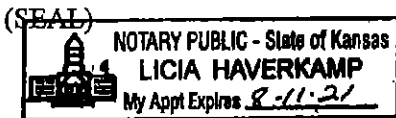
1. I have authority to represent the Kansas Insurance Department in the examination of Farmers Alliance Mutual Insurance Company.
2. The Kansas Insurance Department is accredited under the National Association of Insurance Commissioners Financial Regulation Standards and Accreditation.
3. I have reviewed the examination work papers and examination report, and the examination of Farmers Alliance Mutual Insurance Company was performed in a manner consistent with the standards and procedures required by K.S.A. 40-222.

The affiant says nothing further.



Examiner's Signature

Subscribed and sworn before me by Christopher W. Buchanan on this  
25<sup>th</sup> day of March, 20 19.



Notary Public

My commission expires 8-11-21

(date)