

REPORT ON EXAMINATION
OF
FARMERS MUTUAL INSURANCE COMPANY
16 NORTH MAIN
ELLINWOOD, KANSAS 67526
AS OF
DECEMBER 31, 2018

FILED

SEP 10 2020

VICKI SCHMIDT
Commissioner of Insurance

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Ellinwood, Kansas
July 2, 2020

Honorable Vicki Schmidt
Commissioner of Insurance
Kansas Insurance Department
1300 SW Arrowhead Road
Topeka, Kansas 66604

Dear Commissioner:

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

FARMERS MUTUAL INSURANCE COMPANY

with its statutory home and main administrative office at:

**16 NORTH MAIN
ELLINWOOD, KANSAS 67526**

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

SCOPE OF EXAMINATION

The examiners performed a single-state financial examination of FMIC, a Kansas domiciled property and casualty insurance company. The last examination covered the four-year period from January 1, 2011, through December 31, 2014. This examination covers the four-year period from January 1, 2015, through December 31, 2018.

The examination was conducted in accordance with the rules, regulations, and directives of the Kansas Insurance Department (“Department”) and the observed guidelines and procedures contained in the National Association of Insurance Commissioners (“NAIC”) *Financial Condition Examiners Handbook* (“Handbook”). The Handbook requires that 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, and general information about the insurer and its financial condition. The Department may have identified other items during the examination that, due to their nature (e.g., subjective conclusions, proprietary information, etc.), are not included within the examination report but are separately communicated to other regulators and/or the Company.

Independent Audit Reports

Financial statements of the Company were audited by Summers, Spencer & Company, P.A., for the years ending December 31, 2015, through December 31, 2018. In each of the years under examination, the auditors concluded that the financial statements present fairly, in all material respects, the admitted assets, liabilities, and policyholders' surplus of the Company, the results of its operations, and its cash flows in accordance with the accounting practices prescribed or permitted by the Department.

The independent auditor's work papers were reviewed and analyzed by the examiners. 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 Company was originally organized in Kansas on April 12, 1895, as the German American Farmers Association of Barton County. In 1904, the Company was admitted in Kansas, and in 1916 became a chartered corporation under the name, The German Mutual Fire Insurance Company of Barton County, Kansas. In 1918, the Company changed its name to The Farmers Mutual Insurance Company of Barton County, Kansas. In 1987, the articles of incorporation were amended providing perpetual existence and a change in the name to Farmers Mutual insurance Company.

CORPORATE RECORDS

The Company's articles of incorporation and bylaws were reviewed during the examination. During the period under review, the Company's articles of incorporation were amended on March 27, 2017, and the bylaws were amended on April 27, 2018. The amendments to both documents were properly filed with the Department.

MANAGEMENT AND CONTROL

Policyholders

Bylaw III of the Company's bylaws provides that: "Every named policyholder of this company shall be a member of this Company so long as his or her policy is in full force. Every member shall be entitled to one vote for each item voted on in Annual or Special Member Meetings."

Bylaw IV of the Company's bylaws provides that: "The Annual Meeting of the members shall be held at Ellinwood, Kansas on the third Thursday in the month of February of each year at the principal office of the Company at 1:00 p.m."

Bylaw V of the Company's bylaws provides that: "Votes by members at any Membership Meeting may only be cast in person, except as described here; Proxy votes may be used only at the Annual Meeting and only for the election Directors, providing that: a) No member shall hold and use the proxies of more than twenty (20) policyholders; b) All proxies must be received and recorded by the Secretary thirty (30) days prior to the date of the meeting; c) All proxies shall be in writing and signed by the person giving the proxy; and d) Proxies may be revoked at any time prior to the meeting by so notifying in writing the intention to the Secretary of the Company or by appearing in person at the meeting.

Board of Directors

Bylaw VI of the Company's bylaws provides that: "The Board of Directors of this Company shall consist of no less than five (5) and no more than fifteen (15) members. A Director will serve for a three (3) year term to be replaced by election at the Annual Meeting. Once elected he or she may serve on the Board as long as he or she is re-elected to his or her position at the Annual Meeting concluding their existing term."

Bylaw VI further provides that: "The Board shall hold four (4) regular meetings every year. The meetings shall be held the third Thursday of February (immediately prior to the Annual Meeting, and within 30 days following the close of each of the 1st, 2nd, & 3rd Quarters (March 31st, June 30th, and September 30th) each year, at a scheduled date/time set prior to or at the Reorganizational Meeting each year."

The following is a listing of directors and their position(s) held as of December 31, 2018:

<u>Director</u>	<u>Position(s) Held</u>
Herman D. Hartig, Jr.	Partner/Manager Harper Construction Company
Richard F. Kimple	President & CEO Kimple, Inc.
Ronald G. Rugan	Farmer
Melvin D. Waite	Manager National Billing, LLC
Ruth A. Teichman	Former Kansas Legislator
Mark A. Rondeau	Attorney Watkins Calcara, Chtd.
Edward J. Schloctermeier	Farmer

Committees

Bylaw XI of the Company's bylaws provides that: "The Executive Committee shall consist of the President, Vice President, Secretary-Treasurer, Assistant Secretary-Treasurer (if named), and the Chief Executive Officer. The Executive Committee shall meet between regular meetings of the Board of Directors for planning and advisory purposes as needed or assigned."

Bylaw XII of the Company's bylaws provides that: "The President or Board of Directors may appoint temporary or perpetual committees for specific tasks at the direction of the Board of Directors." As of December 31, 2018, the Company's active committees consisted of an Audit Committee and an Investment and Finance Committee.

Officers

Bylaw VIII of the Company's bylaws provides that: "Immediately after the close of the Annual Meeting, the Directors shall assemble for a brief session, and shall choose from their midst a President, a Vice-President, and a Secretary-Treasurer who shall serve for one year or until their successors have qualified." The duties of the Officers and the duties of the Chief Executive Officer are specifically outlined in Bylaw IX and Bylaw X of the Company's bylaws, respectively.

The following is a listing of officers and their position(s) held as of December 31, 2018:

<u>Officer</u>	<u>Position(s) Held</u>
Herman D. Hartig, Jr.	President
Ronald G. Rugan	Secretary & Treasurer
Melvin D. Waite	Vice President
Justin L. Lear	Chief Executive Officer

INSURANCE HOLDING COMPANY SYSTEM

K.S.A. 40-3305 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 and non-insurance companies and the controlling entities thereof, as of December 31, 2018.



Intercompany/Cost Sharing Agreements

The Company entered into a Principal Lease and Management Agreement with Jensen Associates, Inc. (“JAI”), effective December 6, 2016. The agreement covers the rental of office space, staffing services, and includes an overhead charge provided to the Company by JAI.

TERRITORY AND PLAN OF OPERATION

As of December 31, 2018, the Company is authorized to transact business in the state of Kansas. Products are distributed by independent agents throughout Kansas. In 2018, the Company’s largest lines of business by percentage of direct written premium are as follows: allied lines (49.0%), fire (35.6%), homeowners multiple peril (11.7%), and other liability-occurrence (3.7%).

SELECT FINANCIAL INFORMATION

The exhibit below shows the Company’s financial results for the period of December 31, 2015, through December 31, 2018. The financial results were obtained from annual statements filed by the Company.

	<u>2014</u>	<u>2015</u>	<u>2016</u>	<u>2017</u>	<u>2018</u>
<i>(in thousands)</i>					
Admitted Assets	3,268	3,638	4,696	5,157	5,317
Liabilities	2,124	2,274	2,363	2,004	1,947
Capital and Surplus	1,144	1,364	2,333	3,153	3,370
Net Underwriting Gain/(Loss)	(158)	104	829	326	219
Net Income	53	216	782	367	323
Net Premiums Written	2,709	2,899	2,718	2,697	2,632

REINSURANCE

As of December 31, 2018, the Company's reinsurance program includes the following types of coverage: multi-line excess of loss, property coded per risk excess of loss, and property catastrophe excess of loss.

The Company maintains a multi-line excess of loss agreement which covers both property and casualty lines. The Company's retention under the property portion of the agreement is \$50,000, with excess coverage totaling \$550,000 above the retention. The Company's retention under the casualty portion of the agreement is \$25,000, with excess coverage totaling \$675,000 above the retention.

The Company also maintains a property coded per risk excess of loss agreement which applies to the portion of any policy which the Company retains net for its own account. The Company's retention is a \$500,000 ultimate net loss on risks applicable to the contract. Additional levels of coverage apply based on the size of the ultimate net loss exceeding \$500,000. The excess coverage levels range from \$500,000 to \$7,500,000 based on the size of the ultimate net loss to the Company.

The Company also maintains a property catastrophe excess of loss treaty agreement, which consists of two layers and covers up to \$4,750,000 in excess of the Company's retention of \$260,000.

FINANCIAL STATEMENTS

The following financial statements are based on the statutory financial statements filed by the Company with the Department and present the financial condition of the Company for the period ending December 31, 2018. Any accompanying comments on the 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 MUTUAL INSURANCE COMPANY
ASSETS
AS OF DECEMBER 31, 2018

	<u>Assets</u>	<u>Nonadmitted Assets</u>	<u>Net Admitted Assets</u>
Bonds	\$ 1,649,443	\$ -	\$ 1,649,443
Common stocks	1,167,764	-	1,167,764
Properties occupied by the company	279,532	-	279,532
Cash, cash equivalents and short-term investments	1,435,350	-	1,435,350
Investment income due & accrued	9,994	-	9,994
Deferred premiums and agents' balances and installments booked but deferred and not yet due	561,270	-	561,270
Amounts recoverable from reinsurers	(270)	-	(270)
Other receivables relating to under reinsurance contracts	130,700	-	130,700
Net deferred tax asset	65,819	-	65,819
EDP equipment and software	252,751	252,751	-
Furniture and equipment	126,433	126,433	-
Aggregate write-ins for other than invested assets	22,047	4,779	17,268
Totals	<u>\$ 5,700,833</u>	<u>\$ 383,963</u>	<u>\$ 5,316,870</u>

**FARMERS MUTUAL INSURANCE COMPANY
LIABILITIES, SURPLUS AND OTHER FUNDS
AS OF DECEMBER 31, 2018**

Losses	\$ 95,460
Loss adjustment expense	10,092
Commissions payable, contingent commissions and other similar charges	41,378
Other expenses	15,998
Taxes, licenses and fees	104,511
Unearned premiums	1,556,770
Advance premiums	123,047
Ceded reinsurance premiums payable	(130,000)
Amounts withheld or retained by company for others	<u>130,000</u>
Total liabilities	<u>\$ 1,947,256</u>
Unassigned funds	<u>\$ 3,369,614</u>
Surplus as regards policyholders	<u>\$ 3,369,614</u>
Total liabilities, capital and surplus	<u><u>\$ 5,316,870</u></u>

**FARMERS MUTUAL INSURANCE COMPANY
STATEMENT OF INCOME
FOR THE YEAR ENDED DECEMBER 31, 2018**

UNDERWRITING INCOME

Premiums earned	\$	2,653,336
DEDUCTIONS		
Losses incurred		1,073,786
Loss expenses incurred		148,094
Other underwriting expenses incurred		1,212,301
Total underwriting deductions	\$	2,434,181
Net underwriting gain	\$	219,155

INVESTMENT INCOME

Net investment income earned	\$	45,779
Net realized capital losses		(27,184)
Net investment gain	\$	18,595

OTHER INCOME

Finance and service charges not included in premiums	\$	92,341
Aggregate write-ins for miscellaneous income		73,161
Total other income	\$	165,502

Net income after dividends to policyholders and before federal income taxes	\$	403,252
Federal income taxes incurred		80,332
Net income	\$	322,920

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

Surplus as regards policyholders, December 31, 2014			<u>\$ 1,144,719</u>
Net income	2015	216,295	
	2016	782,224	
	2017	367,203	
	2018	<u>322,920</u>	1,688,642
Change in net unrealized capital gains or (losses)	2015	(29,347)	
	2016	(123,273)	
	2017	85,325	
	2018	<u>(76,250)</u>	(143,545)
Change in net deferred income tax	2015		
	2016		
	2017	(66,852)	
	2018	<u>(611)</u>	(67,463)
Change in nonadmitted assets	2015	32,601	
	2016	309,375	
	2017	434,373	
	2018	<u>(29,088)</u>	747,261
Surplus as regards policyholders, December 31, 2018			<u>\$ 3,369,614</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, 2018, was \$3,369,614, which was the same amount, reported by the Company in its 2018 filed Annual Statement.

COMMENTS ON FINANCIAL STATEMENTS

No comments on the financial statements were identified that warranted inclusion in this Report on Examination.

SUBSEQUENT EVENTS

No significant or material subsequent events were identified that warranted inclusion in this Report on Examination.

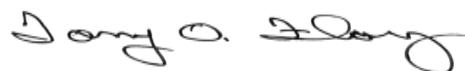
SUMMARY OF RECOMMENDATIONS

No recommendations for the Company were identified that warranted inclusion in this Report on Examination.

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, Mr. Shane Mead, CISA, CRISC, CISM, an Information Systems Examiner, Mr. Chris Buchanan, CFE, CPA, a Senior Insurance Examiner, and Ms. Tamara House, CFE, a Senior Insurance Examiner, all representing the Department, participated in this examination.

Respectfully submitted,



Tony O. Florez, CFE
Examiner-in-Charge
Kansas Insurance Department

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

State of Kansas

County of Shawnee

Tony O. Florez being duly sworn, states as follows:

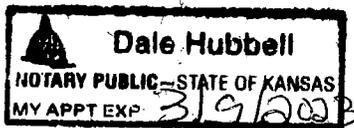
1. I have authority to represent the Kansas Insurance Department in the examination of Farmers Mutual Insurance Company.
2. The Kansas Insurance Department is accredited under the National Association of Insurance Commissioners Financial Regulation Accreditation Standards.
3. I have reviewed the examination work papers and examination report, and the examination of Farmers 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.

Tony O. Florez
Examiner's Signature

Subscribed and sworn before me by Tony Florez on this
24 day of August, 2020

(SEAL)



Dale Hubbell
Notary Public

My commission expires 3/9/2023
(date)