

REPORT ON EXAMINATION

OF THE

FARM FAMILY CASUALTY INSURANCE COMPANY

AS OF

DECEMBER 31, 2006

DATE OF REPORT

NOVEMBER 15, 2007

EXAMINER

FE ROSALES, CFE

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STATE OF NEW YORK
INSURANCE DEPARTMENT
25 BEAVER STREET
NEW YORK, NEW YORK 10004

November 15, 2007

Honorable Eric R. Dinallo
Superintendent of Insurance
Albany, New York 12257

Sir:

Pursuant to the requirements of the New York Insurance Law, and in compliance with the instructions contained in Appointment Number 22595 dated February 16, 2007 attached hereto, I have made an examination into the condition and affairs of Farm Family Casualty Insurance Company as of December 31, 2006, and submit the following report thereon.

Wherever the designations "the Company" or "FFCIC" appear herein without qualification, they should be understood to indicate Farm Family Casualty Insurance Company.

Wherever the term "Department" appears herein without qualification, it should be understood to mean the New York Insurance Department.

The examination was conducted at the Company's home office located at 344 Route 9W, Glenmont, New York 12077.

1. SCOPE OF EXAMINATION

The previous examination was conducted as of December 31, 2000. This examination covered the six-year period from January 1, 2001 through December 31, 2006. Transactions occurring subsequent to this period were reviewed where deemed appropriate by the examiner.

This examination was conducted in accordance with the National Association of Insurance Commissioners (“NAIC”) Financial Condition Examiners Handbook, which requires that we plan and perform the examination to evaluate the financial condition and identify prospective risks of the Company by obtaining information about the company including corporate governance, identifying and assessing inherent risks within the Company and evaluating system controls and procedures used to mitigate those risks. An examination also includes assessing the principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation, management’s compliance with the NAIC Accounting Practices and Procedures Manual, Statements of Statutory Accounting Principles (“SSAP”) and annual statement instructions when applicable to domestic state regulations.

All accounts and activities of the company were considered in accordance with the risk-focused examination process. This examination also included a review and evaluation of the Company’s own control environment assessment and evaluation based upon the Company’s Sarbanes Oxley documentation and testing. The examiners also relied upon audit work performed by the Company’s independent certified public accountants (“CPA”) when appropriate.

This examination report includes a summary of significant findings for the following items as called for in the Financial Condition Examiners Handbook of the NAIC:

- Significant subsequent events
- Company history
- Corporate records
- Management and control
- Fidelity bonds and other insurance
- Pensions, stock ownership and insurance plans
- Territory and plan of operation
- Growth of Company
- Loss experience
- Reinsurance
- Accounts and records
- Statutory deposits
- Financial statements

A review was also made to ascertain what action was taken by the Company with regard to comments and recommendations contained in the prior report on examination.

This report on examination is confined to financial statements and comments on those matters, which involve departures from laws, regulations or rules, or which are deemed to require explanation or description.

2. DESCRIPTION OF COMPANY

The Company was incorporated on April 21, 1955 under the laws of New York as Farm Family Mutual Insurance Company and was licensed by the Department on November 14, 1956. On July 26, 1996, the Company converted from a mutual property and casualty insurance company to a stock company and became a wholly-owned subsidiary of Farm Family Holdings, Inc. ("FFH"). The present name, Farm Family Casualty Insurance Company ("FFCIC") was then adopted.

On April 10, 2001, FFH was acquired by American National Insurance Company ("ANICO") of Galveston, Texas. Operations of the Company are closely related with those of the affiliated property/casualty carrier, United Farm Family Insurance Company ("UFFIC") and another affiliated company, Farm Family Life Insurance Company ("FFLIC"). The three companies share administrative offices.

The Company is a multiple line carrier that provides personal and commercial coverages throughout the Northeast to agri-businesses, and other related commercial and residential establishments in rural and suburban communities. Membership in a state or county Farm Bureau organization is no longer a prerequisite for insurance coverage for renewal business. However, membership in a Farm Bureau is still required for new business in certain states. FFCIC operates in the New England states, New York, New Jersey, Delaware and West Virginia.

The Company and UFFIC (collectively called "the Pool Companies") operate under an inter-company pooling agreement whereby all premium and losses are shared at a participation rate of 98% and 2% for FFCIC and UFFIC, respectively. (Refer to the Reinsurance section for further discussion on the pooling arrangement.)

At December 31, 2006, capital paid in was \$3,606,205 consisting of 2,253,878 shares of common stock at \$1.60 par value per share. Gross paid in and contributed surplus was \$71,776,893. This balance has not changed since the prior examination.

A. Management

Pursuant to the Company's charter and by-laws, management of the Company is vested in a board of directors consisting of not less than thirteen or more than twenty-five members. The board met at least four times during each calendar year. At December 31, 2006, the board of directors was comprised of the following thirteen members:

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
G. Richard Ferdinandtsen Galveston, TX	Director, President and Chief Operating Officer, American National Insurance Company
Stephen J. George Gladstone, NJ	Retired self-employed farmer
Irwin M. Herz, Jr. Galveston, TX	Partner/Attorney, Greer, Herz & Adams, LLP (ANICO's General Counsel)
Clark W. Hinsdale III Charlotte, VT	Owner/Operator, Charlotte Berry Farm
John W. Lincoln Bloomfield, NY	Owner/Operator, Lincoln Dairy Farm
A. Ingrid Moody Kemah, TX	Volunteer worker and board member of various educational and nonprofit organizations
Ross R. Moody Austin, TX	President & Director, National Western Life Insurance Company
Edward J. Muhl Bonita Springs, FL	Retired Partner, PricewaterhouseCoopers, LLP
Gregory V. Ostergren Springfield, MO	Director, Chairman, President and Chief Executive Officer, American National Property and Casualty Company
James E. Pozzi Galveston, TX	Senior Executive Vice President, Corporate Planning, Systems and Life Administration, American National Insurance Company

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Victoria M. Stanton Glenmont, NY	Executive Vice President, General Counsel & Secretary, Farm Family Holdings Inc. and its insurance subsidiaries
Timothy A. Walsh Slingerlands, NY	President & Chief Executive Officer, Farm Family Holdings Inc. and its insurance subsidiaries
Ronald J. Welch Galveston, TX	Senior Executive Vice President, Chief Actuary & Chief Corporate Risk Management Officer, American National Insurance Company

A review of the minutes of the board of directors' meetings held during the examination period indicated that the meetings were generally well attended and each board member has an acceptable record of attendance.

As of December 31, 2006, the principal officers of the Company were as follows:

<u>Name</u>	<u>Title</u>
Timothy A. Walsh	President & Chief Executive Officer
Victoria M. Stanton	Executive Vice President, General Counsel & Secretary
James J. Bettini	Executive Vice President – Operations
Michele M. Bartkowski	Senior Vice President, Chief Financial Officer & Treasurer

B. Territory and Plan of Operation

As of December 31, 2006, the Company was licensed to write business in the following eleven states:

Connecticut	Delaware
Maine	Massachusetts
Missouri	New Hampshire
New Jersey	New York
Rhode Island	Vermont
West Virginia	

As of the examination date, the Company was authorized to transact the kinds of insurance as defined in the following numbered paragraphs of Section 1113(a) of the New York Insurance Law:

<u>Paragraph</u>	<u>Line of Business</u>
4	Fire
5	Miscellaneous property
6	Water damage
7	Burglary and theft
8	Glass
9	Boiler and machinery
10	Elevator
11	Animal
12	Collision
13	Personal injury liability
14	Property damage liability
15	Workers' compensation and employers' liability
16	Fidelity and surety
19	Motor vehicle and aircraft physical damage
20	Marine and inland marine
21	Marine protection and indemnity

The Company is also authorized to transact such workers' compensation insurance as may be incident to coverages contemplated under paragraphs 20 and 21 of Section 1113(a) of the New York Insurance Law, including insurances described in the Longshoremen's and Harbor Workers' Compensation Act (Public Law No. 803, 69th Congress as amended).

Based on the lines of business for which the Company is licensed and the Company's current capital structure, and pursuant to the requirements of Articles 13 and 41 of the New York Insurance Law, the Company is required to maintain a minimum surplus to policyholders in the amount of \$3,800,000.

The following schedule shows the direct premiums written by the Company both in total and in New York for the period under examination:

<u>Calendar Year</u>	<u>New York State</u>	<u>Total United States</u>	<u>Premiums Written in New York State as a Percentage of United States Premium</u>
2001	\$91,093,489	\$236,943,044	38.45%
2002	\$111,663,007	\$279,411,495	39.96%
2003	\$132,827,466	\$329,949,731	40.26%
2004	\$145,879,021	\$374,882,153	38.91%
2005	\$147,844,851	\$386,860,192	38.22%
2006	\$147,558,522	\$392,045,830	37.64%

The largest line of business is personal auto, which comprises approximately 34% of the Pool Companies' total business and is generally marketed in conjunction with other lines. The "Special Farm Package 10" (SFP-10) policy is the second largest line of business and is considered the Pool Companies' flagship product. This policy is a flexible, multi-line insurance contract that combines personal, farm and business property and liability coverages for farm owners and a wide array of other agricultural businesses such as horse breeding and training facilities, nurseries, wineries and greenhouses. The Pool Companies also offer business-owners, artisan contractors, commercial automobile and workers' compensation products. Rounding out the primary product portfolio are commercial and personal umbrella policies, commercial general liability and a small number of claims-made pollution policies for farm risks.

The Company distributes its products through a system of career agents. Approximately two hundred and sixty agents are served by twenty-five general agents and two regional directors throughout the states where Farm Family is licensed. The relationship between the Company and these agents is noted to be one of the Company's key strategies. The Company provides training and technical support for its agents.

C. Reinsurance

Assumed Reinsurance

Assumed reinsurance accounted for 7.5% of the Company's gross premium written at December 31, 2006. Fifty-two percent of assumed premium written is attributable to pooling with the Company's affiliate, United Farm Family Insurance Company ("UFFIC"). The remainder of the Company's assumed premiums are from certain mandated reinsurance pools and associations. All other previously assumed business is in run-off. During the period covered by this examination, the Company's assumed reinsurance business has increased since the last examination. The Company utilizes reinsurance accounting as defined in SSAP No. 62 for all of its assumed reinsurance business.

Effective January 1, 2004, the Company entered into a pooling agreement with UFFIC. Under the terms of the agreement, UFFIC cedes 100% quota share of its assumed and direct business to the Company, net of external reinsurance. The Company then retrocedes 2% quota share of its net direct and assumed business to UFFIC. Concurrently, with the establishment of the pooling arrangement, an excess multiple line reinsurance contract between the Company and UFFIC, which was effective April 13, 2003, was terminated. The pooling agreement and the termination of the

excess agreement were non-objected to by the Department on June 29, 2004, pursuant to the provisions of Section 1505(d)(2) of the New York Insurance Law.

Additionally, all inter-company reinsurance between the Company and UFFIC was commuted on October 1, 2005, with no effect on the net income or surplus of either company. The commutation agreements were non-objected to by the Department on September 7, 2005.

The Company has structured its ceded reinsurance program to limit its maximum exposure to any one risk as follows:

Ceded Reinsurance

The Company, its pool affiliate, UFFIC, along with affiliates American National Property and Casualty Company (“ANPAC”), American National General Insurance Company (“ANGIC”), American National Lloyds Insurance Company (“ANLIC”), Pacific Property and Casualty Company (“PPCC”) and ANPAC Louisiana Insurance Company (“ALIC”), collectively referred to as “the Companies”, are cedants in a multiple line excess reinsurance agreement. The reinsurers of this agreement are all authorized in the State of New York. Coverage A of the agreement includes property lines with a retention of \$1 million per risk and reinsurance of \$5 million per risk, with an occurrence limit of \$10 million all risks any one occurrence. Coverage B of the agreement covers casualty lines, including workers’ compensation with a retention of \$1 million of ultimate net loss, each occurrence, and reinsurance of \$5 million each occurrence. There is an additional \$20 million aggregate limit for all workers’ compensation losses during the term of the contract (one year) and the run-off period, if any. Coverage C of the agreement covers pollution liability with a retention of \$1 million each policy, each loss, with a reinsurance limit of \$5 million each policy, each loss, along with an overall aggregate limit of \$5 million for all pollution liability policies involved in all incidents during the term of the contract. Coverage D has a retention of \$1 million as respects any one occurrence involving a combination of two or more classes of business under coverages A, B, and/or C. When this occurs, the reinsurers are liable for \$2 million excess over retention for any one occurrence per class. This coverage allows the Companies to limit their risk to \$1 million per occurrence when a combination of classes are involved in one loss occurrence.

The Company, UFFIC and ANPAC are party to a property facultative excess of loss binding agreement wherein the Companies can apply for facultative reinsurance of up to two times their net and treaty retention each risk, each occurrence subject to a maximum reinsurer limit of \$10 million each risk, each occurrence. The agreement is with an authorized company.

Property Catastrophe Excess of Loss

The Company and its pool affiliate, UFFIC, are party to a property catastrophe excess of loss agreement with two layers. The Pool Companies' retention is \$5 million each occurrence with the reinsurers liable for \$20 million above retention. The Pool Companies also have a 2.5% participation in each of the layers. Cessions to unauthorized companies were 22.1% on the first layer and 29.4% on the second layer.

The Company, UFFIC, ANPAC, ANGIC, ANLIC, PPCC and ALIC are party to a corporate property catastrophe excess of loss agreement with five layers. The Companies' retention is \$25 million each loss occurrence with the reinsurers liable for \$310 million above retention. The Companies also have a 2.5% participation in each of the five layers. Cessions to unauthorized companies ranged from 18.25% on the first layer to 31% on the fifth layer. A top and drop agreement adds an additional \$15 million to the top of the reinsurers' liability, but also allows the Companies to replace a lower layer that has been exhausted with this \$15 million. A reinstatement premium agreement indemnifies the Companies for 100% of any premium that the Companies pay or become liable for as a result of loss occurrences in the fourth or fifth excess layers of the preceding agreement. The agreement is 80% co-insured by the cedants and the remaining 20% is with an unauthorized company.

Excess Casualty Clash

The Company, UFFIC, ANPAC, ANGIC, ANLIC, PPCC and ALIC are party to a corporate casualty clash excess of loss agreement with three layers. The Companies' retentions are \$6 million of ultimate net loss per occurrence whether involving one or any combination of classes covered under this agreement. The reinsurers have a liability limit of \$44 million per occurrence above retention. The first layer is 100% reinsured with authorized companies. The second and third layers are 95% reinsured with authorized companies.

The Company, UFFIC, ANPAC, PPCC and ALIC are party to a casualty facultative master certificate wherein the Companies retain the first \$5 million coverage on each occurrence and the reinsurers will cover an additional \$5 million above retention. The agreement covers personal, farm and commercial umbrella policies written by the company. The agreement is with an authorized company.

Boiler and Machinery

The Company, UFFIC, ANPAC, ANGIC, ANLIC, PPCC, ALIC (along with American National County Mutual Insurance Company on the personal lines agreement) are party to two reinsurance agreements that cede 100% quota share of the equipment breakdown liability written on its business owners policies and on its homeowners policies. The Companies have no retention and cede to the reinsurer up to \$50,000 liability for any one accident under the personal policies, and \$25 million liability for any one accident for commercial policies. The reinsurer on both agreements is authorized in the State of New York. These two agreements did not include language specified by the New York Department of Insurance when an agreement has multiple cedants. During the course of the examination, the Company amended its homeowners agreement to include the multiple cedant language specified by the New York Department of Insurance. The business owners reinsurance agreement was cancelled and re-written on January 1, 2007 with the multiple cedant language included.

Aviation

The Company cedes 95% quota share general aviation risks underwritten by an aviation general agency to an affiliate of the general agent. The reinsurance agreement was effective July 1, 2006, and the reinsurer is an authorized insurer in the State of New York.

All of the above ceded agreements where the Company is a co-cedant with UFFIC and companies in the ANPAC Group are subject to a multiple cedant reinsurance allocation agreement. The agreement was effective on January 1, 2004, and applies to reinsurance agreements having a term on or after that date. Under the allocation agreement if policies of more than one reinsured company are involved in the same loss, the recovery and retention will be allocated based on the percentage each reinsured company's covered loss bears to the total combined covered loss. For treaty years after 2004, a separate premium rate for the Farm Family Group and a separate premium rate for the ANPAC Group will be established by the unaffiliated reinsurers or, in the event that the lead reinsurer does not provide a separate premium rate, the appointed reinsurance intermediary will set the rate. The separate premium rate reflects the fact that the Farm Family Group and the ANPAC Group have different exposure profiles. The allocation agreement was non-objected to by the Department on March 10, 2005.

Reinsurance agreements with affiliates were reviewed for compliance with Article 15 of the New York Insurance Law. It was noted that all affiliated reinsurance agreements were filed with the Department pursuant to the provisions of Section 1505(d)(2) of the New York Insurance Law.

All ceded reinsurance agreements in effect as of the examination date were reviewed and found to contain the required clauses, including an insolvency clause meeting the requirements of Section 1308 of the New York Insurance Law.

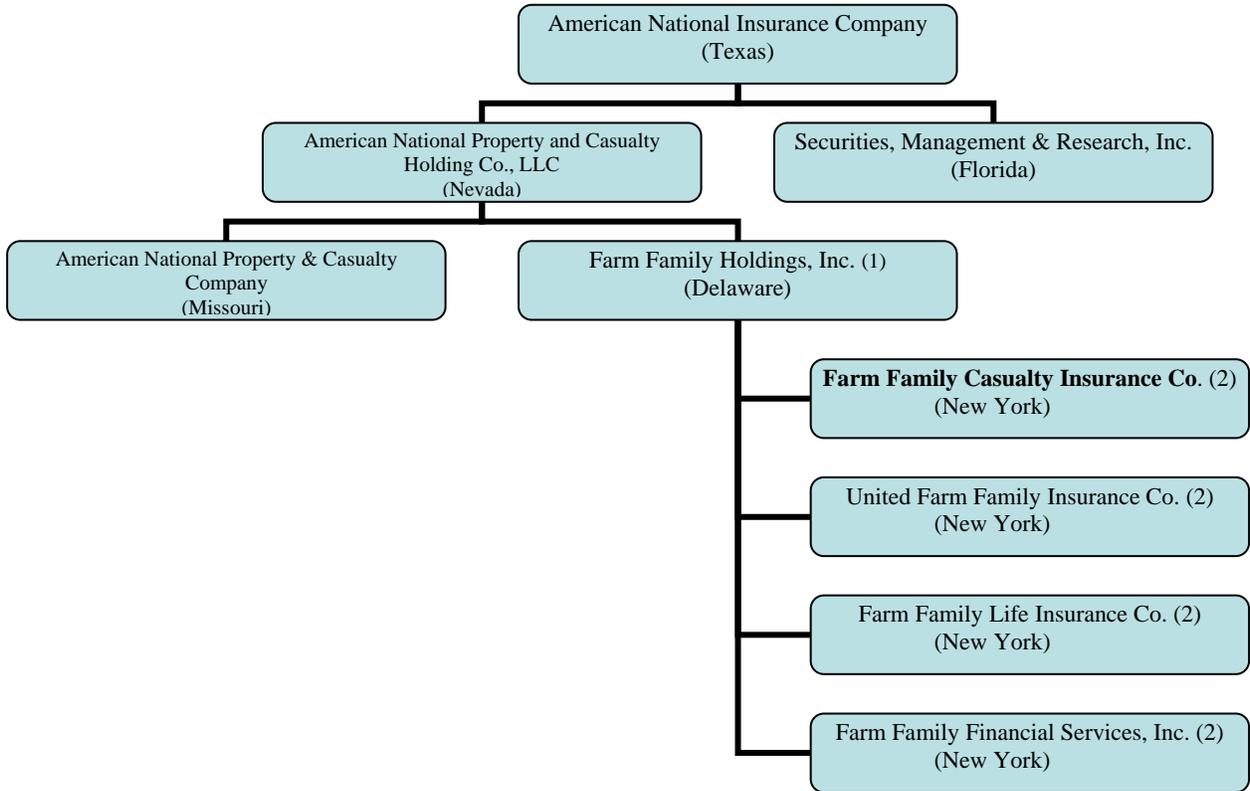
Examination review of the Schedule F data reported by the Company in its filed annual statement was found to accurately reflect its reinsurance transactions. Additionally, management has represented that all material ceded reinsurance agreements transfer both underwriting and timing risk as set forth in SSAP No. 62. Representations were supported by appropriate risk transfer analyses and an attestation from the Company's chief executive officer pursuant to Department Circular Letter No. 8 (2005). Additionally, examination review indicated that the Company was not a party to any finite reinsurance agreements. All ceded reinsurance agreements were accounted for utilizing reinsurance accounting as set forth in paragraphs 17 to 23 of SSAP No. 62.

D. Holding Company System

The Company is a member of the Farm Family Holdings Group. The Company is a wholly-owned subsidiary of Farm Family Holdings, Inc. ("FFH"), its immediate parent. FFH is a Delaware corporation which is ultimately controlled by American National Insurance Company ("ANICO"), a Texas domiciled insurance company.

A review of the holding company registration statements filed with this Department indicated that such filings were complete and were filed in a timely manner pursuant to Article 15 of the New York Insurance Law and Department Regulation 52.

The following is an abridged chart of the holding company system at December 31, 2006:



(1) 94.3% owned by American National Property and Casualty Holding Co., LLC; 5% owned by TMNY Investments, LLC; and 0.7% owned by Comprehensive Investments Services, Inc. All of these entities are owned by ANICO as follows: 94%, 100% and 100% ownership, respectively.

(2) 100% owned by Farm Family Holdings, Inc.

At December 31, 2006, the Company was party to the following agreements with other members of its holding company system:

1. Service Agreement with United Farm Family Insurance Company

Effective July 25, 1988, the Company entered into a service agreement with UFFIC. The agreement provides that the Company will perform certain administrative and special services for UFFIC and allows UFFIC to make use of its facilities. UFFIC reimburses the Company for all direct allocable expenses, reasonably and equitably determined to be attributable to UFFIC, plus direct overhead cost determined periodically by the parties. The review of the allocation of expenses between the parties revealed that the charges are reasonable and in accordance with the requirements of Department Regulation No. 30.

This agreement predates April 6, 1999, the date Farm Family Life Insurance Company and UFFIC were acquired by Farm Family Holdings, Inc. and as such the agreement was not subject to the filing requirements of Section 1505 of the New York Insurance Law. The agreement was subsequently filed with this Department in July 2001.

2. Mortgage Loan and Real Estate Investment Services Agreement

The Company entered into this mortgage loan and real estate investment services agreement among UFFIC and ANICO effective June 1, 2001, pursuant to which ANICO shall solicit and underwrite proposed mortgage loans deemed to be suitable mortgage loan investments for the Company and UFFIC. This agreement was filed with the Department pursuant to Section 1505(d) of the New York Insurance Law and was non-objected to by the Department.

3. Service Agreement with ANICO

The Company entered into this administrative services agreement with ANICO effective April 10, 2001, pursuant to which FFCIC and ANICO shall perform for each other as each company may request, certain services necessary in the conduct of their insurance operations. This agreement was filed with the Department pursuant to Section 1505(d) of the New York Insurance Law and was non-objected to by the Department.

4. Amended and Restated Service Agreement with ANPAC

The Company first entered into this administrative services agreement with American National Property and Casualty Company on April 10, 2001 which was amended effective December 1, 2005. Pursuant to the terms of the agreement, FFCIC and ANPAC shall perform for each other as each company may request, certain services necessary in the conduct of their insurance operations. This agreement was filed with the Department pursuant to Section 1505(d) of the New York Insurance Law and was non-objected to by the Department.

5. Amended and Restated Investment Advisory Agreement

The Company and UFFIC first entered into this investment advisory agreement with ANICO on August 1, 2001 and amended effective November 7, 2006, pursuant to which ANICO shall act as the investment advisor and shall manage their investment portfolio in compliance with the laws and regulations of the State of New York, and subject at all times to the direction, control and approval of the their board of directors or designated committee thereof. This agreement was filed with the Department pursuant to Section 1505(d) of the New York Insurance Law and was non-objected to by the Department.

6. Amended and Restated Tax Payment Allocation Agreement

The Company participates in a tax allocation agreement with ANICO (“Parent”), ANPAC Holding Company and FFH for taxable years commencing January 1, 2002. This agreement provides for the Company to pay the lesser of the amount of tax the Company would have paid if filing a separate return or the amount the Parent actually pays to the Internal Revenue Service (“IRS”) until such time as the carry-back period expires. This provision eliminates the need for the Parent to maintain an escrow account for any taxes remitted by the Company that are not paid to the IRS by the Parent. Effective December 1, 2004, this agreement was amended and restated to include UFFIC as a party to this agreement as a result of the purchase on this date of all its outstanding capital stock by FFH. The review of both the original and amended agreements revealed that it is in compliance with Department Circular Letter No. 33 (1979). The agreements were filed with the Department pursuant to Section 1505(d) of the New York Insurance Law and the Department did not object to their implementation.

7. Service Agreement with FFFS

The Company entered into an administrative services agreement with Farm Family Financial Services Inc. (“FFFS”) effective October 1, 1997, whereby the Company performs certain administrative and special services for FFFS and makes available its facilities to FFFS as FFFS determines to be reasonably necessary in the conduct of its operations. This agreement was revised per Amendment No. 1, effective January 1, 1999, to change the fees to be charged by the Company to FFFS. This agreement and its amendment were filed with the Department pursuant to Section 1505(d) of the New York Insurance Law and were non-objected to by the Department.

8. Lease Agreement

The Company is a party to a lease agreement with Farm Family Life Insurance Company (“FFLIC”) as lessor effective January 1, 1999 with an exercised option effective January 1, 2001 through December 31, 2002. During the examination period, this agreement was amended three times with the most recent amendment effective January 1, 2005, to extend the end date of the lease to December 31, 2009. The lease stipulates that the Company rents both office and storage spaces in the Glenmont, New York location of the home office building of the lessor. This agreement including all amendments thereto were filed with the Department pursuant to Section 1505(d) of the New York Insurance Law and were non-objected to by the Department.

9. Expense Sharing Agreement

The Company is a party to an amended and restated expense sharing agreement with an affiliate, Farm Family Life Insurance Company and its parent, FFH, effective February 14, 1996. The agreement provides for the sharing of certain expenses among the parties and defines the methods to be used for allocating such expenses. The review of the allocation of expenses among the parties revealed that the charges are reasonable and in accordance with the requirements of Department Regulation No. 30. This agreement was filed with the Department pursuant to Section 1505(d) of the New York Insurance Law and was non-objected to by the Department.

10. Renewal Note with Farm Family Holdings, Inc.

Effective December 31, 2006, the Company entered into a renewal note (“Note”) with its immediate parent, FFH for a \$10 million (face amount), 5-year, revolving line of credit. Under the terms of the Note, the Company has agreed to pay FFH: (i) an annual fee of 0.125% of the face amount; and (ii)

a fee calculated and accrued monthly, and paid at the end of each calendar quarter, equal to an annualized 0.25% of the difference between the face amount and the amount of principal outstanding. This translates to an annualized fee of \$25,000 if the Company makes no borrowings. The renewal note was filed with the Department pursuant to Section 1505(d) of the New York Insurance Law and was non-objected to by the Department.

E. Significant Operating Ratios

The following ratios have been computed as of December 31, 2006, based upon the results of this examination:

Net premiums written to surplus as regards policyholders	160%
Liabilities to liquid assets (cash and invested assets less investments in affiliates)	78%
Premiums in course of collection to surplus as regards policyholders	15%

All of the above ratios fall within the benchmark ranges set forth in the Insurance Regulatory Information System of the National Association of Insurance Commissioners.

The underwriting ratios presented below are on an earned/incurred basis and encompass the six-year period covered by this examination:

	<u>Amounts</u>	<u>Ratios</u>
Losses and loss adjustment expenses incurred	\$1,477,467,505	75.26%
Other underwriting expenses incurred	482,186,718	24.56
Net underwriting gain	<u>3,496,265</u>	<u>0.18</u>
Premiums earned	<u>\$1,963,150,488</u>	<u>100.00%</u>

F. Accounts and Records

i. Contract with KPMG, LLP

The examiner's review of the engagement letter ("Contract") between its independent auditor, KPMG, LLP ("KPMG") and the Companies' parent, ANICO, revealed that the Contract did not fully comply with the requirements of Part 89.2 of Department Regulation No. 118.

Specifically, the Contract does not require the CPA to:

- “(a) Provide an audited financial statement (with opinion) on or before May 31st, OR
- (b) Report to the Department in writing if the CPA has determined that the insurer has materially misstated its financial condition or that the insurer does not meet minimum capital or surplus requirements.”

In addition, the Contract does not require the CPA to retain their work papers for the period required (basically the longer of six years or date of report filing) pursuant to Part 243.2(b)(7) and (c) of Department Regulation No. 152.

It is therefore recommended that the Company ensure that the contract with its CPA firm comply with the requirements of Department Regulations 118 and 152.

ii. Custodian Agreement with Bank of New York

The review of the Company’s custodian agreement with Bank of New York revealed that the agreement lacks six of the twelve NAIC custodian agreement provisions. The provisions missing are as follows:

- a) The custodian is obligated to indemnify the insurance company for any insurance company's loss of securities in the custodian's custody, except that, unless domiciliary state law, regulation, or administrative action otherwise require a stricter standard, the bank or trust company shall not be so obligated to the extent that such loss was caused by other than the negligence or dishonesty of the custodian. (The wording in the current agreement states that the custodian shall be held liable, but not that the Custodian “is obligated to indemnify”.)
- b) If domiciliary state law, regulation, or administrative action requires a stricter standard of liability for custodians of insurance company securities than that set forth in a) above, then such stricter standard shall apply. An example of a stricter standard that may be used is that the custodian is obligated to indemnify the insurance company for any loss of securities of the insurance company in the custodian's custody occasioned by the negligence or dishonesty of the custodian's officers or employees, or burglary, robbery, holdup, theft, or mysterious disappearance, including loss by damage or destruction. (The Companies’ custodial agreements do not have any mention of such stricter standard).
- c) In the event of a loss of the securities for which the custodian is obligated to indemnify the insurance company, the securities shall be promptly replaced or the value of the securities and the value of any loss of rights or privileges resulting from said loss of securities shall be promptly replaced.

- d) In the event that the custodian gains entry in a clearing corporation through an agent, there should be a written agreement between the custodian and the agent that the agent shall be subjected to the same liability for loss of securities as the custodian. If the agent is governed by laws that differ from the regulation of the custodian, the Commissioner of Insurance of the state of domicile may accept a standard of liability applicable to the agent that is different from the standard liability. (The possibility of this event is not mentioned in the custodial agreements.)
- e) If the custodial agreement has been terminated or if 100% of the account assets in any one custody account have been withdrawn, the custodian shall provide written notification, within three business days of termination or withdrawal, to the insurer's domiciliary commissioner.
- f) The custodian and its agents, upon reasonable request, shall be required to send all reports which they receive from a clearing corporation or the Federal Reserve book-entry system which the clearing corporation or the Federal Reserve permits to be redistributed and reports prepared by the custodian's outside auditors, to the insurance company on their respective systems of internal control.

It is recommended that the Company amend its custodian agreement to include all the protective covenants and provisions in order to comply with the requirements set forth in the NAIC Financial Condition Examiners Handbook and to Department guidelines.

Subsequent to the examination date, the Company amended its custodian agreement with Bank of New York to include the missing provisions.

iii. Advance Premiums

It was noted during the review of "Advance premiums" that although the Company routinely bills policyholders for policy renewals and new business as much as 30 days in advance, the Company reported a \$0 liability for "Advance premiums" collected as of the examination date. Advance premiums are posted as credits to the "Premiums receivable" when received.

SSAP No 53 states:

"Advance premiums result when the policies have been processed, and the premium has been paid prior to the effective date. These advance premiums are reported as a liability in the statutory financial statement and not considered income until due. Such amounts are not included in written premium or the unearned premium reserve."

Information to quantify the amount that had been collected in advance as of December 31, 2006 was not readily available. Hence, no reclassification will be made.

It is recommended that the Company develop the reporting capability to accurately identify “Advance premiums” and report the amount as a liability in the Annual Statement in accordance with SSAP No. 53.

iv. Uncollected Premiums Aging Report

The prior examination report contained a recommendation that the Company develop reports that will clearly show the aging status of all uncollected premium balances. The Company has developed a new aging report which shows that the report total agrees with the Uncollected premiums. However, the sum total of all of the aging buckets does not agree with the report total. It was also noted that the financial reporting process still relies on the system-generated “short form” report for reporting of non-admitted premiums receivable with no periodic review of the report for accuracy. The Company has not effectively complied with the prior examination report recommendation.

In addition, the examiner’s review of the “short form” aging report used by financial reporting noted numerous account balances that were improperly included in the non-admitted amount due to a one cent balance. Our research indicates that these one cent balances are the result of dividing an odd dollar balance due by an even number of installments. Apparently, the Combined Bill system leaves a penny on the account and as that one cent ages past 90 days, the entire account balance is identified as non-admitted.

It is again recommended that the Company develop reports that will clearly show the aging status of all uncollected premium balances. It is further recommended that the Company periodically review system generated reports for accuracy.

v. Uncollected Premiums – Deferred Billing Report

The prior examination report recommended that the Company maintain a detailed deferred billing report in order that correct balances for each of the Uncollected premium lines may be reported. The examiners noted that the Company is still making an estimate to determine the Uncollected premium amounts to be allocated between “Premiums in course of collection and deferred premiums receivable.”

Furthermore, it was noted that the Company reports no non-admitted “Deferred premiums receivable”, when actually a portion of the non-admitted Premiums in course of collection are deferred premiums.

It is again recommended that the Company develop reports to accurately identify the uncollected premiums as either Premiums in course of collection or deferred premiums, including the non-admitted amounts.

vi. Bank Signatories

The examiners noted that the Company’s records regarding signatories did not match the bank records. Specifically, certain bank records still gave check signing privileges to persons who were no longer employees of the Company. Further verification from the branch showed that the signature card in place was not updated and still has the signature of a former employee.

The bank provided a letter confirming that the named former employee was removed as a signatory from its system as of May 2, 2006 when the bank received a letter from the Company instructing the bank to update the signature cards on file. However, the removal was not noted with the signature cards the bank has on file. It is important to note that the former employee resigned in April 2004 but the Company only requested the bank to update its records two years later, in May 2006.

It is therefore recommended that in the future the Company updates in a timely manner and maintains all signatory cards for all of its bank accounts in order that check signing authority is given only to the signatories approved by the board of directors.

viii. Fidelity Bond

Fidelity bonds provide coverage to the insured business or individual for money or other property lost because of dishonest acts of its bonded employees. While the need for fidelity bond coverage can vary from company to company, it is recommended that those who have access to cash and investments be bonded. This includes the people who have the ability to authorize wire transfers, write checks and those who can buy, sell, or transfer investments. The terms of each policy may vary. However, it is recommended that the policy be written to cover material acts of theft or dishonesty by bonded employees.

The examiner reviewed Exhibit R of the NAIC Financial Condition Examiners Handbook to ascertain the minimum suggested fidelity bond amount for the Company as of December 31, 2006. The review indicated that the minimum suggested amounts for fidelity insurance for FFCIC was \$1,500,000.

The Company had a fidelity bond in effect as of December 31, 2006 with Chubb Group of Insurance Companies of \$1.5 million for single loss limit and \$3 million aggregate limit. This bond, however, was issued to the Company's ultimate parent ANICO and includes coverage for a number of ANICO's subsidiaries (12 insurance companies and 35 non-insurance entities).

As indicated in Exhibit R, the exposure index is calculated using all insured companies named on the fidelity bond. The Company has indicated that because some of the companies under the ANICO Group do not sell insurance, it is difficult to apply the formula in Exhibit R for determining suggested minimum amounts of fidelity insurance.

It is important to note, however, that FFCIC's suggested minimum amount as a single entity is already \$1.5 million and the fidelity bond coverage for the entire ANICO Group of Companies is only \$1.5 million. This means that FFCIC's coverage under the fidelity bond is determined to fall short of the suggested minimum amount.

While it is noted that Exhibit R is not an absolute guide, it has been the Department's position to apply such guidance on examinations. Accordingly, it is recommended that the Company maintain fidelity bond coverage that meets the minimum suggested amounts as set forth in the NAIC Financial Condition Examiners Handbook.

ix. Directors' & Officers' ("D & O") Indemnification Policy

Department Regulation 110, Section 72.1(c) states in part that:

"Retention amounts and co-insurance are both required, in accordance with this Part, for D&O indemnification policies issued to corporations formed under the Insurance Law, Religious Corporations Law, Cooperative Corporations Law, Transportation Corporations Law, or any other law of this state, where provisions of such laws make such corporations subject to B.C.L. section 727 or N-PCL section 727."

The review of the Company's D&O Policy which was issued to its ultimate parent ANICO revealed that it is not in compliance with Department Regulation No. 110, which requires an individual retention of \$5,000 and an aggregate retention of \$50,000, as well as a coinsurance percentage of 0.50% be included in any D&O policy.

It is therefore recommended that the Company comply with the required retention and coinsurance percentages stipulated in Department Regulation 110.

G. Information Systems Controls Evaluation

A review of the Company's responses to the Controls in Information Systems Questionnaire (Exhibit C of the NAIC Financial Condition Examiners Handbook) was performed in connection with the examination as of December 31, 2006.

The review included procedures to obtain reasonable assurance about whether:

- The Company's responses to Exhibit C present fairly, in all material respects, the aspects of the Company's policies and procedures that may be relevant to its information technology ("IT") internal control structure;
- The control structure policies and procedures were suitably designed to achieve the control objectives implicit in the questionnaire, if those policies and procedures were complied with; and,
- Such policies and procedures had been placed in operation from January 1, 2006 to December 31, 2006, until the date of the IT report.

i. Contingency Planning Controls

The results of the review and testing do not provide reasonable assurance that policies and procedures have been developed to address contingency planning control objectives.

The Company lacks a business continuity plan ("BCP"), and a formal disaster recovery plan ("DRP") for recovering data, hardware and software necessary to resume critical business operations after a natural or human-caused disaster.

Presently, as part of its Sarbanes-Oxley initiative, in a joint project with other American National Companies, the Company has begun developing its BCP/DRP. Maji Systems, Inc. provides consulting help in developing the plans, and the Company purchased Mitigator software, developed by EverGreen, to use in building a complete business continuity/disaster recovery plan based upon a business impact analysis ("BIA") and information technology risk assessments.

It is recommended that the Company place a high priority on the implementation of a comprehensive corporate business contingency plan that is kept current, based on a business impact analysis, tested, and that addresses all significant business activities.

This plan should address critical business functions, their priorities, and recovery time objectives, and clearly describe senior management roles and responsibilities associated with the declaration of an

emergency, and implementation of the business continuity and disaster recovery plans. Plans should be tested regularly; weaknesses noted during the testing should be addressed promptly; and, testing documentation should be maintained. In addition, copies of the plan should be maintained at off-site locations.

The BCP should detail manual processing procedures to be used while computer systems are not available; and, list specific supplies required in the event of a disaster and corresponding vendor contact information. The plan should also reflect procedures for communications with stakeholders and significant entities outside the Company.

The DRP should list all critical data files, operating systems, applications and hardware including telecommunications.

The IT group should not be the sole provider and sponsor of the Company's business continuity program. Managers of each business unit should assume ownership of the plan and should have ultimate responsibility for the successful execution of the plan. The Plan should be centrally coordinated to ensure that all business units and the DRP are in tandem, and allow for an efficient resumption of business services.

3. FINANCIAL STATEMENTS

A Balance Sheet

The following shows the assets, liabilities and surplus as regards policyholders as of December 31, 2006 as determined by this examination and as reported by the Company:

<u>Assets</u>	<u>Assets</u>	<u>Assets Not Admitted</u>	<u>Net Admitted Assets</u>
Bonds	\$686,397,235	\$0	\$686,397,235
Preferred stocks	27,903,790	0	27,903,790
Common stocks	14,589,757	0	14,589,757
Cash, cash equivalents and short-term investments	57,421,671	0	57,421,671
Contract loans	0	0	0
Other invested assets	4,334,524	0	4,334,524
Receivable for securities	611,645	0	611,645
Aggregate write-ins for invested assets	0	0	0
Title Plants	0	0	0
Investment income due and accrued	9,415,724	0	9,415,724
Uncollected premiums and agents' balances in the course of collection	39,434,847	2,182,065	37,252,782
Deferred premiums, agents' balances and installments booked but deferred and not yet due	52,408,330	0	52,408,330
Accrued retrospective premiums	0	0	0
Amounts recoverable from reinsurers	1,793,529	0	1,793,529
Funds held by or deposited with reinsured companies	(13,326)	0	(13,326)
Net deferred tax asset	28,315,554	9,705,921	18,609,633
Aggregate write-ins for other than invested assets	<u>3,812,996</u>	<u>1,370,697</u>	<u>2,442,299</u>
Total assets	<u>\$926,426,276</u>	<u>\$13,258,683</u>	<u>\$913,167,593</u>

Liabilities, surplus and other fundsLiabilities

Losses		\$358,627,602
Reinsurance payable on paid losses and loss adjustment expenses		1,445,178
Loss adjustment expenses		58,914,949
Commissions payable, contingent commissions and other similar charges		3,655,948
Other expenses (excluding taxes, licenses and fees)		13,634,499
Taxes, licenses and fees (excluding federal and foreign income taxes)		5,288,552
Current federal and foreign income taxes		8,853,729
Unearned premiums		183,162,509
Ceded reinsurance premiums payable (net of ceding commissions)		(275,097)
Funds held by company under reinsurance treaties		2,680,630
Amounts withheld or retained by company for account of others		1,148,982
Remittances and items not allocated		(159,241)
Provision for reinsurance		33,000
Payable to parent, subsidiaries and affiliates		33,123,892
Aggregate write-ins for liabilities		<u>(136,771)</u>
Total liabilities		\$669,998,361

Surplus and other funds

Common capital stock	\$3,606,205	
Gross paid in and contributed surplus	71,776,893	
Unassigned funds (surplus)	<u>167,786,134</u>	
Surplus as regards policyholders		<u>243,169,232</u>
Total liabilities, surplus and other funds		<u>\$913,167,593</u>

NOTE: The Internal Revenue Service (“IRS”) has completed its audits of the Company’s consolidated Federal Income Tax returns for tax year 2001. However, this particular tax year is still considered open and eligible for appeal as IRS has not sent the parent company (ANICO) the required notice of claim disallowance. Audits covering tax years 2002 and 2003 are still pending before IRS Office of Appeals. In August 2007, the Company consented to extending the statute of limitations to December 31, 2008. The Internal Revenue Service has not yet audited tax returns covering tax years 2004 through 2006. The examiner is unaware of any potential exposure of the Company to any tax assessment and no liability has been established herein relative to such contingency.

B. Underwriting and Investment Exhibit

Surplus as regards policyholders increased \$116,611,620 during the six-year examination period January 1, 2001 through December 31, 2006, detailed as follows:

Underwriting Income

Premiums earned		\$1,963,150,488
Deductions:		
Losses incurred	\$1,294,522,687	
Loss adjustment expenses incurred	182,944,818	
Other underwriting expenses incurred	<u>482,186,718</u>	
Total underwriting deductions		<u>1,959,654,223</u>
Net underwriting gain or (loss)		\$3,496,265

Investment Income

Net investment income earned	\$174,390,226	
Net realized capital gain	<u>(1,354,142)</u>	
Net investment gain or (loss)		173,036,084

Other Income

Net gain or (loss) from agents' or premium balances charged off	\$ (7,133,185)	
Finance and service charges not included in premiums	15,170,185	
Aggregate write-ins for miscellaneous income	<u>(2,558,029)</u>	
Total other income		<u>5,478,971</u>
Net income before dividends to policyholders and before federal and foreign income taxes		\$182,011,320
Dividends to policyholders		<u>203,413</u>
Net income after dividends to policyholders but before federal and foreign income taxes		\$181,807,907
Federal and foreign income taxes incurred		<u>61,714,277</u>
Net income		<u>\$120,093,630</u>

- A. Sales and advertising
- B. Underwriting
- C. Rating
- D. Claims and complaint handling

No problem areas were encountered.

6. COMPLIANCE WITH PRIOR REPORT ON EXAMINATION

The prior report on examination contained four recommendations as follows (page numbers refer to the prior report):

<u>ITEM</u>	<u>PAGE NO.</u>
<p>A. <u>Holding Company System</u></p> <p>It was recommended that the Company comply with the prior notification requirements of Section 1505(d)(2) of the New York Insurance Law.</p> <p>The Company has complied with this recommendation.</p>	<p>17</p>
<p>B. <u>Accounts and Records</u></p> <p><u>Uncollected Premium Reports</u></p> <p>It was recommended that the Company develop reports that will clearly show the aging status of all uncollected premium balances.</p> <p>The Company has not complied with this recommendation. A similar comment is included in this report.</p> <p>It was recommended that the Company maintain a detailed deferred billing report that can be provided upon examination in order that correct balances for each of the Uncollected Premium lines in all future statements filed with the Department can be easily ascertainable.</p> <p>The Company has not complied with this recommendation. A similar comment is included in this report.</p>	<p>18</p> <p>18</p>
<p>C. <u>Losses and Loss Adjustment Expenses</u></p> <p>It was recommended that the Company provide accurate claims count data in all future statements filed with this Department.</p> <p>The Company has complied with this recommendation.</p>	<p>23</p>

7. SUMMARY OF COMMENTS AND RECOMMENDATIONS

<u>ITEM</u>	<u>PAGE NO.</u>
A. <u>Accounts and Records</u>	
i. <u>Contract with KPMG, LLP</u>	
It is recommended that the Company ensure that the contract with its CPA firm comply with the requirements of Department Regulations 118 and 152.	17
ii. <u>Custodian Agreement</u>	
It is recommended that the Company amend its custodian agreement to include all the protective covenants and provisions in order to comply with the requirements set forth in the NAIC Financial Condition Examiners Handbook and to Department guidelines.	18
iii. <u>Advance Premiums</u>	
It is recommended that the Company develop the reporting capability to accurately identify “Advance premiums” and report the amount as a liability in the Annual Statement in accordance with SSAP No. 53.	19
iv. <u>Uncollected Premiums Aging Report</u>	
It is again recommended that the Company develop reports that will clearly show the aging status of all uncollected premium balances.	19
It is further recommended that the Company periodically review system generated reports for accuracy.	19
v. <u>Uncollected Premiums – Deferred Premiums Report</u>	
It is again recommended that the Company develop reports to accurately identify the uncollected premiums as either Premiums in course of collection or deferred premiums, including the non-admitted amounts.	20
vi. <u>Bank Signatories</u>	
It is recommended that in the future the Company update in a timely manner and maintain all signatory cards for all of its bank accounts in order that check signing authority is given only to the signatories approved by the board of directors.	20
vii. <u>Fidelity Bond</u>	
It is recommended that the Company maintain fidelity bond coverage	21

ITEMPAGE NO.

that meets the minimum suggested amounts as set forth in the NAIC Financial Condition Examiners Handbook.

viii. Directors' & Officers' Indemnification Policy

It is recommended that the Company comply with the required retention and coinsurance percentages stipulated in Department Regulation 110. 21

i. Information System Controls Evaluation

Contingency Planning

It is recommended that the Company place a high priority on the implementation of a comprehensive corporate business contingency plan that is kept current, based on a business impact analysis, tested, and that addresses all significant business activities. 22

Respectfully submitted,

_____/S/
Fe Rosales, CFE
Associate Insurance Examiner

STATE OF NEW YORK)
)SS:
)
COUNTY OF ULSTER)

FE ROSALES, being duly sworn, deposes and says that the foregoing report, subscribed by her,
is true to the best of her knowledge and belief.

_____/S/
Fe Rosales, CFE

Subscribed and sworn to before me

this _____ day of _____, 2008.

Appointment No. 22595

STATE OF NEW YORK
INSURANCE DEPARTMENT

I, Eric R. Dinallo, Acting Superintendent of Insurance of the State of New York, pursuant to the provisions of the Insurance Law, do hereby appoint:

Fe Rosales

as proper person to examine into the affairs of the

FARM FAMILY CASUALTY INSURANCE COMPANY

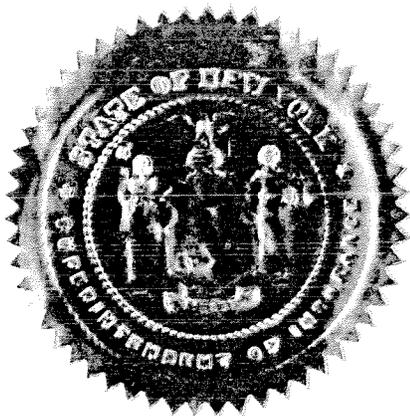
and to make a report to me in writing of the condition of the said

Company

with such other information as he shall deem requisite.

In Witness Whereof, I have hereunto subscribed by the name and affixed the official Seal of this Department, at the City of New York,

this 16th day of February, 2007



A handwritten signature in cursive script, appearing to read "Eric R. Dinallo", written over a horizontal line.

ERIC R. DINALLO

Acting Superintendent of Insurance