

REPORT ON EXAMINATION
OF THE
DRYDEN MUTUAL INSURANCE COMPANY
AS OF
DECEMBER 31, 2003

DATE OF REPORT

AUGUST 24, 2004

EXAMINER

GERARD L. FRANCO



STATE OF NEW YORK
INSURANCE DEPARTMENT
ONE COMMERCE PLAZA
ALBANY, NEW YORK 12257

George E. Pataki
Governor

Gregory V. Serio
Superintendent

Honorable Gregory V. Serio
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 22122 dated January 12, 2004 attached hereto, I have made an examination into the condition and affairs of Dryden Mutual Insurance Company as of December 31, 2003, and submit the following report thereon.

The examination was conducted at the Company's administrative offices located at 12 Ellis Drive, PO Box 635, Dryden, New York 13053-0635.

Wherever the designations " the Company" or "DMIC" appear herein without qualification, they should be understood to indicate Dryden Mutual Insurance Company.

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

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1. SCOPE OF EXAMINATION

The previous examination was conducted as of December 31, 1998. This examination covered the five year period from January 1, 1999 through December 31, 2003, and was limited in scope to those balance sheet items considered by this Department to require analysis, verification or description, including: invested assets, loss and loss adjustment expenses reserves and the provision for reinsurance. The examination included a review of income, disbursements, and company records deemed necessary to accomplish such analysis and verification and utilized, to the extent considered appropriate, work performed by the Company's independent certified public accountants. Transactions occurring subsequent to this period were reviewed where deemed appropriate by the examiner.

A review was 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 departure from laws, regulations or rules, or which are deemed to require explanation or description.

2. DESCRIPTION OF COMPANY

The Company was organized on May 7, 1860 as the Dryden and Groton Mutual Fire Insurance Company, for the purpose of transacting business as an assessment cooperative fire insurance association in the Towns of Dryden and Groton, Tompkins County, New York.

On April 1, 1984, the Company converted to an advance premium corporation, changing its corporate title to Dryden Mutual Insurance Company.

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 nine or more than fifteen members. As of the examination date, the board was comprised of nine members, divided into three equal groups, with one group being elected at each annual policyholder's meeting for a term of three years.

Every member insured by the Company is entitled to one vote at any meeting of the members. The annual meeting of the board of directors is held immediately after the annual meeting of the Company. The board meets 10 times during each calendar year, thereby complying with Section 6624(b) of the New York Insurance Law. At December 31, 2003, the board of directors was comprised of the following nine members:

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Lawrence L. Brown Marathon, NY	Self-Employed Transportation Horse Raising & Trading, Retired farmer
John J. Carlin Binghamton, NY	Attorney, Partner at Levene, Gouldin & Thompson, LLP
Richard J. Clark Dryden, NY	Owner, Dryden Shur-Fine Grocery Supermarket, Secretary- Treasurer of DMIC
Jerome F. Denton Elmira, NY	Retired Bank Executive Vice President, Chemung Canal Trust Co.
William J. Kaminski Romulus, NY	Human Resources Manager, Waterloo-Seneca ARC
Frank J. Lamphier Locke, NY	Retired Farm Implement Manufacturer, Vice President of DMIC

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Verl Rankin, Jr. Groton, NY	Retired Farm Operator
Donald P. Reed Cortland, NY	Owner of Reed's Seeds, President of DMIC
Gary L. Wood Dryden, NY	Self Employed, Owner Consulting Engineering Firm

A review of the minutes of the board of directors' meeting held during the examination period indicated that the meetings were generally well attended and each board member has an acceptable record of attendance, with average attendance of the board of directors for the examination period being approximately 94%.

As of December 31, 2003, the principal officers of the Company were as follows:

<u>Name</u>	<u>Title</u>
Donald P. Reed	President
Richard J. Clark	Secretary-Treasurer
Frank J. Lamphier	Vice President
Robert B. Baxter	Chief Executive Officer
Dana J. Abbey	Chief Operating Officer
Peter A. Thorp	Vice President-Marketing Manager
Samuel J. Crisalli	Vice President-Claims Manager

B. Territory and Plan of Operation

At December 31, 2003, the Company was licensed to write business in New York only.

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 damage
6	Water damage
7	Burglary and theft
8	Glass
12	Collision
13	Personal injury liability
14	Property damage liability
19	Motor vehicle and aircraft physical damage(excluding aircraft physical damage)
20	Marine and inland marine(inland marine only)

The following schedule shows the direct premiums written by the Company for the period under examination.

<u>Calendar Year</u>	<u>Direct Premiums Written</u>
1999	\$15,114,724
2000	16,513,165
2001	19,672,604
2002	25,439,756
2003	31,910,494

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, 41, and 66 of the New York Insurance Law, the Company is required to maintain a minimum surplus to policyholders in the amount of \$650,000.

The Company underwrites predominantly commercial multiple peril, fire and other liability lines of business, which accounted for 53%, 16% and 13%, respectively, of the 2003 net premium writings. Ninety-nine percent (99%) of the Company's business is on a direct bill basis, with insurance being written by approximately 140 independent agents located throughout the Company's territory. All policies presently being issued and those in force are non-assessable

and DMIC has met the requirements of Section 6620 of the New York Insurance Law for the issuance of same.

C. Reinsurance

Assumed

The Company assumes a very minor volume of business as compared to its direct writings. The assumptions reflect the Company's participation in a casualty pool.

Ceded

The Schedule F data as contained in the Company's filed annual statement was found to accurately reflect its reinsurance transactions.

The examiner reviewed all ceded reinsurance contracts in effect at December 31, 2003. The contracts all contained the required standard clauses, including insolvency clauses, meeting the requirements of Section 1308 of the New York Insurance Law.

The Company had the following general property per risk and casualty excess of loss reinsurance program in effect at December 31, 2003:

Property(2 layers)	\$1,750,000 x/s \$250,000 each risk any one loss occurrence, reinsurer's liability from all risks in each loss occurrence shall not exceed \$750,000 and \$4,500,000 for 1 st and 2 nd excess layers, respectively; as well as reinsurer's liability as respects acts of terrorism shall be further limited to \$750,000 and \$4,500,000 in all, each agreement year for 1 st and 2 nd layers excess layers, respectively
Casualty(3 layers)	\$1,750,000 x/s \$250,000 with respect to any one loss occurrence

The Company had the following catastrophe excess of loss reinsurance program in effect at December 31, 2003:

Property catastrophe 100% of \$24,250,000 in excess of the Company's ultimate net loss of \$750,000 in any one loss occurrence, reinsurer's liability for loss arising out of terrorism shall be further limited to an annual aggregate of \$750,000; \$3,500,000; \$5,000,000 and \$10,000,000, respectively of 1st through 5th excess of loss layers

All the reinsurance contracts in effect throughout the examination period were reinsured by an authorized reinsurer. The Company's ultimate net retention for both the property and casualty lines of business was increased from \$75,000 to \$250,000.

D. Holding Company System

The Company was not a member of any holding company system as of December 31, 2003. Furthermore, the Company had no affiliations or pooling agreements, except for that stated in Section C of this report, in force at December 31, 2003.

E. Abandoned Property Law

Section 1316 of the New York State Abandoned Property Law provides that amounts payable to a resident of this state from a policy of insurance, if unclaimed for three years, shall be deemed to be abandoned property. Such abandoned property shall be reported to the comptroller on or before the first day of April each year. Such filing is required of all insurers regardless of whether or not they have any abandoned property to report.

The Company's abandoned property reports for the period of this examination were all filed on a timely basis pursuant to the provisions of Section 1316 of the New York State Abandoned Property Law.

F. Significant Operating Ratios

The following ratios have been computed as of December 31, 2003, based upon the results of this examination:

Net premiums written to surplus as regards policyholders	172%
Liabilities to liquid assets (cash and invested assets less investments in affiliates)	69%
Premiums in course of collection to surplus as regards policyholders	8%

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 five-year period covered by this examination:

	<u>Amounts</u>	<u>Ratios</u>
Losses and loss adjustment expenses incurred	\$48,282,732	54.01%
Other underwriting expenses incurred	39,335,322	44.00%
Net underwriting gain	<u>1,768,510</u>	<u>1.99%</u>
Premiums earned	<u>\$89,386,564</u>	<u>100.00%</u>

G. Accounts and Records

i. Custodial Agreement

As indicated in the National Association of Insurance Commissioners (NAIC) Financial Condition Examiners Handbook there are specific guidelines that should be followed in the maintenance of a custodial or safekeeping agreement. After a review of the Company's current custodial agreement several provisions and safeguards required by the NAIC, reinforced by the Department's Circular Letter No. 2 of 1977 were not included in the agreement. Therefore, it is recommended that the Company comply with NAIC requirements, reinforced by Circular Letter No. 2 of 1977 and obtain a custodial agreement that includes the requirements specified by the NAIC and New York Insurance Department.

It is noted that the Company is in the process of executing a new custodial agreement that will be in compliance with the NAIC guidelines.

ii. Approval of Investments

A review of the Board Minutes relating to investment buys and sells reported on the filed annual statements for the examination period shows that the board of directors reviews and discusses the Company's investments both before and sometimes after the transaction has been completed. However, the board of directors after having reviewed the investment transactions and reports made no formal motion approving the investment transactions and reports. Section 1411(a) of the New York Insurance Law, which states, in part that "No domestic insurer shall make any loan or investment unless authorized or approved by its board of directors or a committee thereof responsible for supervising or making such investment or loan. The committee's minutes shall be recorded and a report submitted to the board of directors at its next meeting." Therefore, it is recommended that the Company be in full compliance with the requirements of Section 1411(a) of the New York Insurance Law by having the approval of all purchases and sales of investments entered into the board minutes through a written statement, thus ensuring that all investments are authorized or approved by its board of directors or a committee thereof responsible for supervising or making such investments.

iii. Rent Charged for Office Space

Recalculation of the examination rent coverage/shortage worksheet resulted in the determination that the Company did not charge itself enough in rent for the period under examination to cover real estate related repairs, expenses, taxes, depreciation incurred, plus interest added at an average fair rate on the carrying value of the reporting entity's investment in its home office building.

SSAP 40 paragraph 15 states that the amount of rent recorded by the Company shall be comparable to rent received from others and or rental rates of like property in the same area. Per a discussion with the Company management it was determined the amount of rent is based upon the Company's best estimate of the value per square foot for real estate in the area and this method is not in compliance with the requirements of SSAP 40 paragraph 15. Therefore, it is recommended that the Company comply with SSAP 40 paragraph 15 henceforth and charge itself an amount in rent that is comparable to rent received from others and or rental rates of like property in the same area, if this is not available, the rent amount should be derived from a consideration of the repairs, expense, taxes, and depreciation incurred, plus interest added at an average fair rate on the carrying value of the reporting entity's investment in its home office building.

iv. Check Signing of Miscellaneous Expenses

The review of sampled checks drawn on the Company's operating account found the Company uses a printer to place signatures on miscellaneous expense checks. Section 6611(a)(4)(C) of the New York State Insurance Law requires that all checks be signed either by two officers or by one officer upon the written order of another officer, except as otherwise provided by resolution of the corporation's board of directors or in its by-laws for the handling of miscellaneous expenses. The Company was not able to provide a resolution of the corporation's board of directors nor is there a provision in its by-laws for the handling of miscellaneous expenses. The Company's usage of a check-signing machine does not satisfy the requirements of Section 6611(a)(4)(C) of the NYIL. Therefore, it is recommended that the Company comply with Section 6611(a)(4)(C) of the New York Insurance Law.

3. FINANCIAL STATEMENTS

A. Balance Sheet

The following shows the assets, liabilities and surplus as regards policyholders as determined by this examination as of December 31, 2003. This statement is the same as the balance sheet filed by the Company.

	<u>Assets</u>	<u>Assets Not Admitted</u>	<u>Net Admitted Assets</u>
Bonds	\$35,295,737	-0-	\$35,295,737
Common stocks	2,088	-0-	2,088
Real estate occupied by company	921,371	-0-	921,371
Cash and short-term investments	5,243,794	-0-	5,243,794
Other invested assets	8,625	-0-	8,625
Aggregate write-ins for invested assets	370,906	370,906	-0-
Investment income due and accrued	552,931	-0-	552,931
Premiums, agents' balances and installments booked but deferred and not yet due	5,167,766	144,139	5,023,627
Reinsurance: Funds held by or deposited with reinsured companies	80,765	-0-	80,765
Net deferred tax asset	1,353,274		1,353,274
Other assets nonadmitted	718,833	718,833	
Aggregate write-ins for other than invested assets	<u>416,241</u>	<u>-0-</u>	<u>416,241</u>
Total Assets	<u>\$50,132,331</u>	<u>\$1,233,878</u>	<u>\$48,898,453</u>

Liabilities, surplus and other funds

Losses and Loss adjustment expenses		\$11,992,821
Commissions payable, contingent commissions and other similar charges		2,060,351
Other expenses(excluding taxes, licenses and fees)		213,891
Taxes, licenses and fees(excluding federal and foreign income taxes)		30,356
Federal and foreign income taxes		259,400
Unearned premiums		16,635,445
Ceded reinsurance premiums payable(net of ceding commissions)		632,548
Amounts withheld or retained by company for account of others		<u>27,176</u>
Total liabilities		\$31,851,988
Aggregate write-ins for special surplus funds	\$ 650,000	
Unassigned funds(surplus)		<u>16,396,465</u>
Surplus as regards policyholders		<u>17,046,465</u>
Total liabilities, surplus and other funds		<u>\$48,898,453</u>

B. Underwriting and Investment Exhibit

Surplus as regards policyholders increased \$6,251,459 during the five-year examination period January 1, 1999 through December 31, 2003, detailed as follows:

Underwriting Income

Premiums earned		\$89,386,564
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Deductions:

Losses and loss adjustment expenses incurred	\$48,282,732	
Other underwriting expenses incurred	<u>39,335,322</u>	

Total underwriting deductions		<u>87,618,054</u>
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Net underwriting gain or (loss)		\$ 1,768,510
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Investment Income

Net investment income earned	\$ 6,726,802	
Net realized capital gain	<u>102,085</u>	

Net investment gain or (loss)		\$ 6,828,887
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Other Income

Net gain or (loss) from agents' or premium balances	(\$94,893)	
Finance and service charges not included in premiums	1,348,788	
Aggregate write-ins for miscellaneous income	<u>4,781</u>	

Total other income		<u>\$ 1,258,676</u>
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Net income before dividends to policyholders and before federal and foreign income taxes		\$ 9,856,073
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Federal and foreign income taxes incurred		<u>4,032,376</u>
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Net Income		<u>\$5,823,697</u>
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Capital and Surplus Account

Surplus as regards policyholders per report on Examination as of December 31, 1998			\$10,795,006
	<u>Gains in Surplus</u>	<u>Losses in Surplus</u>	
Net income	\$5,823,697	\$ -0-	
Net realized capital gains or (loss)	-0-	56,085	
Change in net deferred income tax	493,236	-0-	
Change in nonadmitted assets	-0-	811,961	
Cumulative effect of changes in accounting principles	860,038	-0-	
Aggregate write-ins for gains and losses in surplus	<u>-0-</u>	<u>57,466</u>	
Net increase(decrease) in surplus			<u>\$ 6,251,459</u>
Surplus as regards policyholders per report on Examination as of December 31, 2003			<u>\$17,046,465</u>

4. LOSSES AND LOSS ADJUSTMENT EXPENSES

The examination liability for the captioned items of \$11,992,821 is the same as that reported by the Company as of December 31, 2003. The examination analysis was conducted in accordance with generally accepted actuarial principles and practices and was based on statistical information contained in the Companies internal records and in its filed annual statements.

The Company's actuarial opinion and report, as well as Company's CPA workpapers, were reviewed and utilized in the determination of an appropriate reserve for the Company's unpaid losses and loss adjustment expenses.

5. MARKET CONDUCT ACTIVITIES

In the course of this examination, a review was made of the manner in which the Company conducts its business and fulfills its contractual obligations to policyholders and claimants. The review was general in nature and is not to be construed to encompass the more precise scope of a market conduct investigation.

The general review was directed at practices of the Company in the following areas:

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

A review of the Company's two agent terminations during the examination period was performed to confirm compliance with the requirements of Regulation 90(NYCRR Parts 218.4(b) and 218.5). Upon completion of this review it was discovered that the Company did not give proper notice in accordance with Part 218.5 of Department Regulation 90, which ensures that the redlining notice is prominently set out in boldface type on the front of the termination letter sent to agents. Also, the Company did not give agents 30 days notice prior to contract termination as required by Part 218.4(b) of Regulation 90. Therefore, it is recommended that the Company comply with all the requirements of Regulation 90(NYCRR Parts 218.4(b) and 218.5) and make sure the redlining notice is prominently set out in boldface type on the front of the termination letter sent to agents as required by Part 218.5 and give at least 30 days notice prior to contract termination as required by Part 218.4(b).

The Company's complaint log for the period under examination was provided for review. The Company was able to produce a formal complaint log for those items that appeared to be

claims related complaints. However, those items that were not claims related were not being logged. The complaint log is required by Regulation 64-11 NYCRR 216.4(e), which states that "As part of its complaint handling function, an insurer's consumer services department shall maintain an ongoing central log to register and monitor all complaint activity." By not logging its non-claim related complaints the Company is not in full compliance with the requirements of Regulation 64-11 NYCRR 216.4(e).

Circular Letter No. 11 (1978) provides the format for the Company's log. During the review of the Company's 1999 through 2003 complaint log for compliance with the specific requirements of Circular Letter No. 11 (1978), a number of columns were found to be missing. Therefore, it is recommended that the Company comply with Part 216.4(e) of Regulation 64 and Circular Letter No. 11 (1978) and include all complaints filed with the Company in the complaint log, as well as maintain a complete complaint log by including all columns.

6. COMPLIANCE WITH PRIOR REPORT ON EXAMINATION

The prior report on examination contained the following recommendations (page numbers refer to the prior report):

<u>ITEM</u>	<u>PAGE NO.</u>
A. It is recommended that the Company report its operating expenses in accordance with the uniform accounting instructions of this Department's Regulation No. 30 in future financial statements submitted to this Department.	8
The Company has complied with this recommendation.	
B. It is recommended that the Company record its liability for commissions payable in future financial statements submitted to this Department.	8
The Company has complied with this recommendation.	

<u>ITEM</u>	<u>PAGE NO.</u>
C. It is recommended that the Company report individually its liability for IBNR losses and its liability for IBNR loss adjustment expenses in future financial statements submitted to this Department.	9
<p>The Company has complied with this recommendation.</p>	
D. It is recommended that the Company comply with Section 1209(f) of the Insurance Law and cease compensating its officers based upon its profitability.	9

The Company has complied with this recommendation.

7. SUMMARY OF COMMENTS AND RECOMMENDATIONS

<u>ITEM</u>	<u>PAGE NO.</u>
A. <u>Accounts and Records</u>	8
<p>i. It is recommended that the Company comply with NAIC requirements, reinforced by Circular Letter No. 2 of 1977 and obtain a custodial agreement that includes the requirements specified by the NAIC and New York Insurance Department.</p>	
<p>ii. It is recommended that the Company be in full compliance with the requirements of Section 1411(a) of the New York Insurance Law by having the approval of all purchases and sales of investments entered into the board minutes through a written statement, thus ensuring that all investments are authorized or approved by its board of directors or a committee thereof responsible for supervising or making such investments.</p>	9
<p>iii. It is recommended that the Company comply with SSAP 40 Paragraph 15 henceforth and charge itself an amount in rent that is comparable to rent received from others and or rental rates of like property in the same area, if this is not available, the rent amount should be derived from a consideration of the repairs, expenses, taxes and depreciation incurred, plus interest added at an average fair rate on the carrying value of the reporting entity's investment in its home office building.</p>	10

<u>ITEM</u>	<u>PAGE NO.</u>
iv. It is recommended that the Company comply with Section 6611(a)(4)(C) of the New York Insurance Law, regarding check-signing authorization.	11
B. <u>Market Conduct Activities</u>	
i. It is recommended that the Company comply with all the requirements of Regulation 90 (NYCRR Part 218.4(b) and 218.5) and make sure the redlining notice is prominently set out in boldface type on the front of the termination letter sent to agents as required by Part 218.5 and give at least 30 days notice prior to contract termination as required by Part 218.4(b).	16
ii. It is recommended that they comply with Part 216.4(e) of Regulation 64 and Circular Letter No. 11(1978) and include all complaints filed with the Company in the complaint log, as well as maintain a complete complaint log by including all columns.	17

Appointment No 22122

STATE OF NEW YORK
INSURANCE DEPARTMENT

I, GREGORY V. SERIO , Superintendent of Insurance of the State of New York, pursuant to the provisions of the Insurance Law, do hereby appoint:

Gerard Franco

as proper person to examine into the affairs of the

Dryden Mutual 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 Albany,

*this 12th day of *January, 2004*



A handwritten signature in dark ink, appearing to read "Gregory V. Serio", written over a horizontal line.

GREGORY V. SERIO
Superintendent of Insurance