

REPORT ON EXAMINATION

OF THE

FRANKLIN FIRE INSURANCE COMPANY

AS OF

DECEMBER 31, 2008

DATE OF REPORT

OCTOBER 8, 2009

EXAMINER

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TABLE OF CONTENTS

<u>ITEM NO.</u>		<u>PAGE NO.</u>
1.	Scope of Examination	2
2.	Description of Company	3
	A. Management	3
	B. Territory and plan of operation	5
	C. Reinsurance	6
	D. Holding company system	7
	E. Significant operating ratios	7
	F. Accounts and records	7
3.	Financial Statements	9
	A. Balance sheet	9
	B. Underwriting and investment exhibit	10
4.	Losses and loss adjustment expenses	11
5.	Compliance with prior report on examination	11
6.	Summary of comments and recommendations	12



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

October 8, 2009

Honorable James J. Wrynn
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 30369 dated August 6, 2009 attached hereto, I have made an examination into the condition and affairs of the Franklin Fire Insurance Company as of December 31, 2008, and submit the following report thereon.

Wherever the designation “the Company” appears herein without qualification, it should be understood to indicate the Franklin Fire 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 13077 State Highway 357, Franklin, New York 13775.

1. SCOPE OF EXAMINATION

The Department has performed a single-state examination of the Franklin Fire Insurance Company. The previous examination was conducted as of December 31, 2003. This examination covered the five-year period from January 1, 2004 through December 31, 2008. 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 (“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. This 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 Statutory Accounting Principles and annual statement instructions when applicable to domestic state regulations.

All financially significant accounts and activities of the Company were considered in accordance with the risk-focused examination process.

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
- Territory and plan of operation
- Loss experience
- Reinsurance
- Accounts and records
- Financial statements
- Summary of recommendations

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 that involve departures from laws, regulations or rules, or that are deemed to require explanation or description.

2. DESCRIPTION OF COMPANY

Franklin Fire Insurance Company was organized in 1881 for the purpose of transacting business as an assessment co-operative fire insurance company in the Town of Franklin, Delaware County, New York.

As of December 31, 2008, the Company was licensed to operate in seven counties in New York State, namely: Broome, Chenango, Delaware, Greene, Otsego, Schoharie and Sullivan.

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 nor more than thirteen members, divided into three groups as nearly equal as possible, with one group being elected at each annual policyholders' meeting for a term of three years. The board meets six times during each calendar year. At December 31, 2008, the board of directors was comprised of the following eleven members:

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Burton George Barnes Treadwell, New York	Treasurer, Franklin Fire Insurance Company
Thomas William Barnes Treadwell, New York	Vice President, Franklin Fire Insurance Company
Richard Blackman Walton, New York	Farmer
James Robert Carey Franklin, New York	Vice President, National Bank of Delaware County
Herman Paul Herklotz Franklin, New York	President, Franklin Fire Insurance Company
Beverly Koopmann Treadwell, New York	Farmer & Bus Driver

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Heather Elizabeth Ross North Franklin, New York	Director of Human Resources, Countryside Care Center
Brian Scott Sickler Franklin, New York	Owner, Sickler Memorials
Ruth Mae Sickler Franklin, New York	Secretary, Franklin Fire Insurance Company
Donald Marvin Smith Franklin, New York	Farmer
Richard Charles Yarnes Downsville, New York	Retired Farmer

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.

Article II Section 1 of the Company's by-laws states that each member of the board of directors "...shall be a member and resident of the territory in which it is authorized to transact business." On examination, it was found that one of the directors sold his property, which was insured by the Company. Upon the sale of the property, the policy was cancelled; therefore, the director was no longer a member. Nevertheless, the said director attended and participated in board meetings and also received remuneration for his attendance.

It is recommended that the Company comply with its by-laws and allow only qualified members of the Company to serve on the board.

As of December 31, 2008, the principal officers of the Company were as follows:

<u>Name</u>	<u>Title</u>
Herman Paul Herklotz	President
Ruth Mae Sickler	Secretary
Burton George Barnes	Treasurer
Thomas William Barnes	Vice President

B. Territory and Plan of Operation

As of December 31, 2008, the Company was licensed as an assessment cooperative insurance company to transact business in the following counties of New York only: Broome, Chenango, Delaware, Greene, Otsego, Schoharie and Sullivan.

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

Paragraphs 5, 6, 7, and 8 can be written solely in conjunction with fire insurance written under the same policy and covering the same premises. The Company is also licensed to accept and cede reinsurance as provided in Section 6606 of the Insurance Law of the State of New York.

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>
2004	\$56,320
2005	\$55,256
2006	\$57,625
2007	\$57,534
2008	\$57,583

Based on the lines of business for which the Company is licensed, and pursuant to the requirements of Articles 13 and 66 of the New York Insurance Law, the Company is required to maintain a minimum surplus to policyholders in the amount of \$100,000.

The Company writes fire and allied lines through its director-agents. Policies are issued for a term of three years covering farms, residential and commercial risks, including contents, livestock, produce and machinery. Policies are issued against specified perils that include fire and windstorm. Applications for insurance are received by directors of the Company and all risks are inspected at least every three years, on or prior to the renewal dates of policies.

C. Reinsurance

The Company assumed no reinsurance during the period covered by this examination.

As of December 31, 2008, the Company had the following ceded reinsurance program in place:

Property	100% of \$75,000 each loss, each risk, for the ultimate net loss over and above an initial Ultimate Net Loss of \$15,000 each loss, each risk, subject to a limit of liability to the Reinsurer of \$75,000 each loss, each risk and further subject to a limit of liability to the Reinsurer of \$225,000 each loss occurrence.
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The Company had the following catastrophe excess of loss reinsurance program in effect at December 31, 2008:

Windstorm	100% of the ultimate net loss over and above an ultimate net loss equal to 10% of the Company's policyholder's surplus. However, no claim shall be made hereunder unless the loss occurrence involves three or more risks.
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All reinsurance contracts in effect throughout the examination period were with authorized reinsurers. Since the previous examination, the Company's net retention for the property line of business has increased from \$14,000 to \$15,000.

All significant 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 the NAIC Statement of Statutory Accounting Principles ("SSAP") No. 62. Representations were supported by an attestation from the Company's Executive Officers pursuant to the NAIC Annual Statement Instructions. 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 26 and 27 of SSAP No. 62.

D. Holding Company System

The Company is not a member of any holding company system. As of December 31, 2008, the Company was independent with no affiliations.

E. Significant Operating Ratios

The following ratios have been computed as of December 31, 2008, based upon the results of this examination:

Net premiums written to surplus as regards policyholders	.03:1
Liabilities to liquid assets (cash and invested assets less investments in affiliates)	2%

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	\$ 80,065	36.70%
Other underwriting expenses incurred	244,533	112.09
Net underwriting loss	<u>(106,439)</u>	<u>(48.79)</u>
Premiums earned	<u>\$ 218,159</u>	<u>100.00%</u>

F. Accounts and Records

i. Compliance with the annual statement instructions

The NAIC annual statement instructions provide a guide for completion of schedules and exhibits. Upon examination, it was found that the Company did not complete or accurately complete some of the columns in Schedule D. Some of the Company's bonds were callable, but that was not indicated in the column for bond characteristics. Other columns not completed included the NAIC designation, current amortization (or accretion), and due and accrued interest. The columns with inaccurate data included date (securities were) acquired, date of maturity, and month in which interest

was paid. It is recommended that the Company comply with the annual statement instructions and accurately complete Schedule D of the annual statement and all other schedules and exhibits.

ii. Recording of bond acquisition dates

SSAP No. 26 paragraph 4 states, in part, that “A bond acquisition or disposal shall be recorded on the trade date, not the settlement date...”

Examination review of broker’s advices and Schedule D - Part 1 of the annual statements filed during the examination indicated that the Company recorded the settlement date as the date of acquisition for some bonds. Accordingly, it is recommended that the Company comply with SSAP No. 26 and record the trade date as the acquisition date for each applicable bond reported in Schedule D of the annual statement.

iii. Approval of Investments

Section 1411(a) of the New York Insurance Law 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.”

Upon review of the annual statement General Interrogatories Part 1 No. 14, minutes of board meetings, communication with the Department, as well as an interview with the Treasurer, it was determined that the Treasurer has been making all investment decisions without the board’s approval. Therefore, it is recommended that the Company comply with the requirements of Section 1411(a) of the New York Insurance Law regarding its investment transactions.

3. FINANCIAL STATEMENTS

A. Balance Sheet

The following shows the assets, liabilities and surplus as regards policyholders as of December 31, 2008 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	\$1,230,395	\$0	\$1,230,395
Cash, cash equivalents and short-term investments	129,205	0	129,205
Investment income due and accrued	<u>150</u>	<u>0</u>	<u>150</u>
Total assets	<u>\$1,359,750</u>	<u>\$0</u>	<u>\$1,359,750</u>
 <u>Liabilities, surplus and other funds</u>			
Losses and loss adjustment expenses			\$ 1,100
Unearned premiums			<u>28,835</u>
Total liabilities			\$ 29,935
Required Surplus		\$ 100,000	
Unassigned funds (surplus)		<u>1,229,815</u>	
Surplus as regards policyholders			<u>1,329,815</u>
Total liabilities, surplus and other funds			<u>\$1,359,750</u>

Note: The Internal Revenue Service (“IRS”) has completed its audits to determine the Company’s eligibility for exemption from Federal income tax as of December 31, 2007. The Company was cited for non-compliance with Section 6033 of the Internal Revenue Code of 1986, which requires that income and expenses from all activities be stated separately on the appropriate line of IRS Form 990. The finding did not have an impact on the Company’s tax exempt status.

B. Underwriting and Investment Exhibit

Surplus as regards policyholders increased \$149,122 during the five-year examination period January 1, 2004 through December 31, 2008, detailed as follows:

Underwriting Income

Premiums earned		\$ 218,159
Deductions:		
Losses and loss adjustment expenses incurred	\$ 80,065	
Other underwriting expenses incurred	<u>244,533</u>	
Total underwriting deductions		<u>324,598</u>
Net underwriting gain or (loss)		\$(106,439)

Investment Income

Net investment income earned	\$254,723	
Net realized capital gains	<u>152</u>	
Net investment gain or (loss)		254,875
Net Income		<u>\$ 148,436</u>

Capital and Surplus Account

Surplus as regards policyholders per report on examination as of December 31, 2003		\$1,180,693
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	<u>Gains in Surplus</u>	<u>Losses in Surplus</u>
Net income	\$148,436	\$0
Net unrealized capital gains or losses	<u>686</u>	-
Total gains and losses	<u>\$149,122</u>	<u>\$0</u>
Net increase in surplus		<u>149,122</u>
Surplus as regards policyholders per report on examination as of December 31, 2008		<u>\$1,329,815</u>

4. LOSSES AND LOSS ADJUSTMENT EXPENSES

The examination liability for the captioned items of \$1,100 is the same as reported by the Company as of December 31, 2008. The examination analysis was based on a review of the Company's loss register to determine the existence of any outstanding claims and any trends in the reporting of incurred but not reported losses.

5. 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>
A.	<u>Custodial Agreement</u>	
	It was recommended that the Company comply with the NAIC requirements, reinforced by Circular Letter No. 2 of 1997 and obtain a custodial agreement that includes the requirements specified by the NAIC and the New York Insurance Department.	7
	The Company has complied with this recommendation.	
B.	<u>Checking Account and signature requirements</u>	
	It was recommended that the Company comply with Section 6611(a)(4)(C) of the New York Insurance Law and implement control procedures for its checking account.	8
	The Company has complied with this recommendation.	
C.	<u>Misclassification of Asset</u>	
	It was recommended that the Company comply with SSAP No. 26 paragraph 2 and report investments in certificates of deposit, with maturity term in excess of one year, as bonds in Schedule D of the annual statement.	8
	The Company has complied with this recommendation.	
D.	<u>Acknowledging Pertinent Communications</u>	
	It was recommended that the Company comply with 11NYCRR 216.4 and acknowledge receipt of claimant notices within 15 working days and maintain records of such communication in the claim files.	12
	The Company has complied with this recommendation.	

6. SUMMARY OF COMMENTS AND RECOMMENDATIONS

<u>ITEM</u>		<u>PAGE NO.</u>
A.	<u>Management</u> It is recommended that the Company comply with its by-laws and allow only qualified members of the Company to serve on the board.	4
B.	<u>Accounts and Records</u>	
i.	It is recommended that the Company comply with the annual statement instructions and accurately complete Schedule D of the annual statement and all other schedules and exhibits.	8
ii.	It is recommended that the Company comply with SSAP No. 26 and record the trade date as the acquisition date for each applicable bond reported in Schedule D of the annual statement.	8
iii.	It is recommended that the Company comply with the requirements of Section 1411(a) of the New York Insurance Law regarding its investment transactions.	8

STATE OF NEW YORK
INSURANCE DEPARTMENT

I, Kermitt J. Brooks Acting Superintendent of Insurance of the State of New York, pursuant to the provisions of the Insurance Law, do hereby appoint:

Nyantakyi Akuoko

as proper person to examine into the affairs of the

Franklin Fire Insurance Company

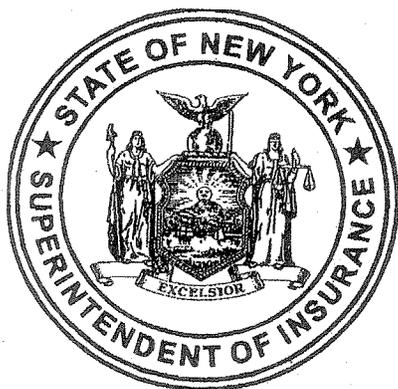
and to make a report to me in writing of the condition of the said

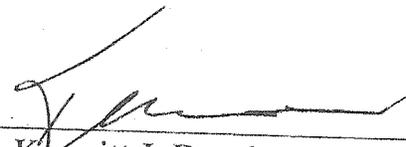
Company

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 6TH day of August 2009




Kermitt J. Brooks
Acting Superintendent of Insurance