

REPORT ON EXAMINATION

OF THE

UNITED FRONTIER MUTUAL INSURANCE COMPANY

AS OF

DECEMBER 31, 2004

DATE OF REPORT

JUNE 10, 2005

EXAMINER

GERARD L. FRANCO



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

George E. Pataki  
Governor

Howard Mills  
Superintendent

June 22, 2005

Honorable Howard Mills  
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 22332 dated February 14, 2005 attached hereto, I have made an examination into the condition and affairs of United Frontier Mutual Insurance Company as of December 31, 2004, and submit the following report thereon.

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

Wherever the "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 195 Davison Road Lockport, New York 14094-3333.

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## 1. SCOPE OF EXAMINATION

The previous examination was conducted as of December 31, 1999. This examination covered the five-year period from January 1, 2000 through December 31, 2004, and was limited in scope to these balance sheet items considered by this Department to require analysis, verification or description, including: invested assets, inter-company balances, loss and loss adjustment expense reserves and the provision for reinsurance. The examination included a review of income, disbursements and company records deemed necessary to accomplish such analysis or verification. 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.

A review or audit was also made of the following items as called for in the Examiners Handbook of the National Association of Insurance Commissioners.

- History of Company
- Management and control
- Corporate records
- Fidelity bond and other insurance
- Territory and plan of operation
- Growth of Company
- Loss experience
- Reinsurance
- Accounts and records
- Financial statements

## 2. DESCRIPTION OF COMPANY

The Company was organized in 1877 as The Farmers Mutual Insurance Company of Orleans and Niagara Counties, for the purpose of transacting business as an assessment cooperative fire insurance company.

In 1970, the Department permitted the Company to change its name to the Niagara Orleans Mutual Insurance Company.

This Department, on January 1, 1984, issued a certificate permitting the Company to do business as an advance premium cooperative insurance company and to issue non-assessable policies.

On July 1, 1986, the Niagara and Erie County Farmers' Protective Association merged into the Niagara Orleans Mutual Insurance Company. On January 1, 1987, the Frontier Cooperative Fire Insurance Company merged into the Niagara Orleans Mutual Insurance Company. The merged companies at this time petitioned the Superintendent for approval to change the Company's name to the United Frontier Mutual Insurance Company. Permission was granted for the use of the new name effective January 1, 1987.

On July 1, 1999, The Alliance Mutual Insurance Company merged into the United Frontier 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 nor more than twenty-five members. The board and executive committee each meet at least three times during each calendar year to comply with Section 6624(b) of the New York Insurance Law. At December 31, 2004, the board of directors was comprised of the following twelve members:

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
David W. Cloy Ransomville, NY	Business owner
Carolyn R. Flansburg Albion, NY	Treasurer, United Frontier Mutual Insurance Company
John Gavenda Albion, NY	Attorney
Lynn Hill Albion, NY	Retired
John W. Long Albion, NY	Farmer
Glenn D. Maxon Holley, NY	Farmer
Roger Millis Waterport, NY	Farmer
David H. Muck Williamsville, NY	Equipment Operator
Donald B. Noell Williamsville, NY	Chairperson, United Frontier Mutual Insurance Company
Leon A. Wendt North Tonawanda, NY	Accountant and Insurance Agent
Thomas S. Wronski Lockport, NY	President United Frontier Mutual Insurance Company
Lloyd V. Ziemendorf Niagara Falls, NY	Insurance agent and Secretary, United Frontier Mutual 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. The average attendance by the board of directors during the examination period was approximately 94%.

Each of the directors' qualifications, as set forth in Article VI of the Company's charter and Article II Section I of its by-laws, was reviewed and it appears that each director is duly qualified.

As of December 31, 2004, the principal officers of the Company were as follows:

<u>Name</u>	<u>Title</u>
Thomas S. Wronski	President
Carolyn R. Flansburg	Treasurer
Donald B. Noell	Chairperson of the Board
Lloyd V. Ziemendorf	Vice Chairperson of the Board & Secretary

B. Territory and Plan of Operation

As of December 31, 2004, 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
20	Marine and inland marine(inland marine only)

Section 6604(a)(3) of the New York Insurance Law states in part, "A licensed advance premium corporation may apply for an amended license to do any one or more of the kinds of

insurance specified in subsection(a) of section one thousand one hundred thirteen of this chapter..." The Company started writing boiler and machinery, as defined in Section 1113(a)(9) of the Insurance Law, in 2004. As of December 31, 2004, the Company was not licensed to write this line of business. In 2005 the Company requested approval from the Insurance Department to have Boiler and Machinery Insurance added to its license. An amended license was issued by the Department on May 5, 2005 adding Boiler and Machinery Insurance as defined in Section 1113(a)(9) of the Insurance Law. However, it is recommended that the Company comply with Section 6604(a)(3) of the Insurance Law and in the future obtain prior approval from the Insurance Department before writing a new line of business.

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

<u>Calendar Year</u>	<u>Direct Premiums Written</u>
2000	\$ 3,202,204
2001	3,091,438
2002	3,073,408
2003	3,305,682
2004	3,734,686

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.

At December 31, 2004, the Company wrote insurance through independent agents and several director-agents.

The Company's predominate lines of business are homeowners multiple peril, commercial multiple peril and fire which accounted for 42.8%, 36.6% and 7.6%, respectively, of the Company's 2004 direct written business.

C. Reinsurance

Assumed

The Company assumes a relatively minor volume of business as compared to its direct writings. The assumptions reflect the Company's participation in the NAMICO Reinsurance Facility. The Company is reporting Reinsurance assumed of \$18,008 in its 2004 filed Annual Statement. The pool provides reinsurance on Directors and Officers Liability and Insurance Company Professional Liability insurance policies.

Ceded

The Schedule F data as contained in the Company's filed annual statement was found to accurately reflect its reinsurance transactions. However, it should be noted that the Company did not list the respective reinsurers on Schedule F part 3 or part 4 as required by the annual statements instructions. Instead, the Company is showing Guy Carpenter & Co., Inc. Regional Account Program, which is comprised of a number of different reinsurers.

As of December 31, 2004, the Company had the following excess of loss reinsurance program in place:

Property(2 layers)	\$950,000 x/s \$50,000 each risk any one loss occurrence, reinsurer's liability from all risks in each loss occurrence shall not exceed \$900,000 and \$1,000,000 for 1 <sup>st</sup> and 2 <sup>nd</sup> excess layers respectively.
Casualty(2 layers)	\$950,000 x/s \$50,000 combined net loss any one-loss occurrence.

As of December 31, 2004, the Company had in force the following special casualty excess of loss reinsurance agreement in place:

Special Casualty Excess of Loss Reinsurance	\$500,000 x/s \$500,000 combined net loss, any one loss occurrence. It is warranted by the Company that in the event it issues a policy, contract or binder providing limits greater than \$1,000,000 Bodily Injury Liability and Property Damage Liability combined the excess thereof shall be deemed to have been reinsured elsewhere on an excess of loss basis.
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The Company had the following catastrophe excess of loss reinsurance program in effect at December 31, 2004:

Property catastrophe (1 layer)	95% of \$1,850,000 x/s \$150,000 each loss occurrence. Reinsurer's liability shall not exceed \$3,515,000 during each agreement year.
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As of December 31, 2004, the Company had in place an Equipment Breakdown Coverage 100 Percent Quota Share Reinsurance Treaty Effective January 1, 2004 with Factory Mutual Insurance Company for coverage of its boiler and machinery business. As of December 31, 2004, boiler and machinery insurance was not included on the Company's license. It is stated in the Company's charter that the Company can write boiler and machinery insurance if so licensed. See Section B. Territory and Plan of Operation of this report for approval of amended license.

As of December 31, 2004, the Company had the following Property Facultative

Reinsurance program in place:

Property            Submission under which are limited to two (2) times the net retained liability of the Company subject to a maximum cession of \$1,000,000 and a minimum retention of \$250,000 as respects any one risk covering business classified as: Fire and Allied Lines -- HO/FO (Sect 1 Only) Inland Marine-- Commercial Multi Peril (Section 1 Only). Coverage in respect of animals when written as insured property shall be subject to a maximum ceded amount of \$500,000 any one insured. It is further agreed that the ceded amount in respect of any one animal shall not exceed \$250,000. Specially agreed that the Company may request reinsurance for greater limits subject to acceptance.

All reinsurance contracts in effect at December 31, 2004 were reinsured by an authorized reinsurer.

As of the date of the prior examination December 31, 1999, the Company's net retention on its property and casualty business was \$30,000 and \$20,000, respectively.

As of December 31, 2004, the Company's net retention for both the property and casualty lines of business is \$50,000.

D.    Holding Company System

The Company was independent with no affiliations at December 31, 2004. It is not a member of any holding company system.

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 report for the period of this examination were all filed on a timely basis pursuant to the provisions of Section 1316 of the New York Abandoned Property Law.

F. Significant Operating Ratios

The following ratios have been computed as of December 31, 2004, based upon the results of this examination:

Net premiums written to surplus as regards policyholders	41%
Liabilities to liquid assets(cash and invested assets less investments in Affiliates	39%
Premiums in course of collection to Surplus as regards policyholders	1%

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	\$ 9,325,369	77.69%
Other underwriting expenses incurred	4,355,519	36.28%
Net underwriting loss	<u>(1,676,634)</u>	<u>(13.97%)</u>
Premiums earned	<u>\$12,004,254</u>	<u>100.00%</u>

G. Accounts and Records

i. Schedule D-Part 1 Preparation

The Company should use the NAIC annual statement instructions when completing Schedule D Part 1 of the 2004 annual statement. The Company is noted to have made several errors in completing Schedule D Part 1 of the 2004 annual statement. The noted errors include: 1) typing errors in the entry of the cost of bonds; 2) entering the incorrect designations of bonds that were filed with the SVO; and 3) not correctly recording how the bond interest is paid (monthly, quarterly, and semi-annually). Therefore, it is recommended that the Company comply with the annual statement instructions and properly record all information in Schedule D-Part 1 of the annual statement.

ii. Custodial Agreement

After a review of the Company's current custodial agreement several provisions and safeguards required by Department guidelines, as set forth in the National Association of Insurance Commissioners (NAIC) Financial Condition Examiners Handbook, 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 Department guidelines, as set forth by NAIC guidelines, 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.

Before the examination was completed the Company management had obtained an amendment to the custodial agreement from their custodian. The amended custodial agreement was found to be in substantial compliance of the requirements specified by the NAIC and the New York Insurance Department.

## 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, 2004 and as reported by the Company:

<u>Assets</u>	<u>Assets</u>	<u>Assets Not Admitted</u>	<u>Net Admitted Assets</u>
Bonds	\$ 6,912,746	\$ 0	\$ 6,912,746
Common Stocks	2,491,515	0	2,491,515
First lien-mortgage loans on real estate	76,670	0	76,670
Properties occupied by the Company	463,840	0	463,840
Cash, cash equivalents and short-term investments	418,570	0	418,570
Aggregate write-ins for invested assets	<u>1</u>	<u>0</u>	<u>1</u>
Subtotals, cash and invested assets	\$10,363,342	0	\$10,363,342
Investment income due and accrued	44,133	0	44,133
Uncollected premiums, agents' balances in the course of collection	38,128	0	38,128
Deferred premiums, agents' balances and installments booked but deferred and not yet due	501,254	0	501,254
Amounts recoverable from reinsurers	36,931	0	36,931
Funds held by or deposited with reinsured companies	23,155	0	23,155
Net deferred tax asset	186,677	81,867	104,810
Electronic data processing equipment and software	18,230	0	18,230
Aggregate write-ins for other than invested assets	<u>66,354</u>	<u>4</u>	<u>66,350</u>
Totals	<u>\$11,278,204</u>	<u>\$81,871</u>	<u>\$11,196,333</u>

Liabilities, surplus and other funds

Losses and loss adjustment expenses		\$ 2,237,942
Other expenses (excluding taxes, licenses and fees)		13,142
Unearned premiums		1,950,051
Advance premium		62,681
Ceded reinsurance premiums payable (net of ceding commissions)		43,041
Amounts withheld or retained by company for amount of others		<u>310</u>
Total liabilities		\$ 4,307,167
Aggregate write-ins for special surplus funds	\$ 650,000	
Unassigned funds (surplus)	<u>6,239,166</u>	
Surplus as regards policyholders		<u>6,889,166</u>
Totals		<u>\$11,196,333</u>

Note: The Internal Revenue Service has not yet begun to audit tax returns covering tax years 2000 through 2004. 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 \$1,173 during the five-year examination period January 1, 2000 through December 31, 2004, detailed as follows:

Underwriting Income

Premiums earned		\$ 12,004,254
Deductions:		
Losses and loss adjustment expenses incurred	\$9,325,369	
Other underwriting expenses incurred	<u>4,355,519</u>	
Total underwriting deductions		<u>\$ 13,680,888</u>
Net underwriting gain or (loss)		(\$ 1,676,634)

Investment Income

Net investment income earned	\$ 1,653,289	
Net realized capital gain	<u>272,858</u>	
Net investment gain or (loss)		1,926,147

Other Income

Net gain or (loss) from agents' or premium balances charged off	\$ 33,140	
Finance and service charges not included in premiums	230,933	
Aggregate write-ins for miscellaneous income	<u>2</u>	
Total other income		<u>264,075</u>
Net income before dividends to policyholders		\$ 513,588
Federal and foreign income taxes incurred		<u>167,151</u>
Net income		<u>\$ 346,437</u>

Surplus as regards policyholders per report on Examination as of December 31, 1999			\$ 6,887,993
	<u>Gains in Surplus</u>	<u>Losses in Surplus</u>	
Net income	\$ 346,437		
Net unrealized capital gains or (losses)	-0-	450,200	
Change in net deferred income tax	-0-	17,812	
Change in nonadmitted assets	4,273	-0-	
Cumulative effect of changes in accounting principles	118,491	-0-	
Aggregate write-ins for gains and losses in surplus	<u>-0-</u>	<u>16</u>	
Net increase(decrease) in surplus			<u>1,173</u>
Surplus as regards policyholders per report on Examination as of December 31, 2004			<u>\$ 6,889,166</u>

#### 4. LOSSES AND LOSS ADJUSTMENT EXPENSES

The examination liability for the captioned items of \$ 2,237,942 is the same as reported by the Company as of December 31, 2004. 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.

#### 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, which is the responsibility of the Market Conduct Unit of the Property Bureau of this Department.

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

No problem areas were encountered.

#### 6. COMPLIANCE WITH PRIOR REPORT ON EXAMINATION

The prior report on examination contained 5 recommendations as follows (page numbers refer to the prior report):

ITEM	PAGE NO.
<p>i. It is recommended that the Nominating Committee have formal meetings and that minutes of all Nominating Committee meetings be maintained, as required by Section 6611(a)(3) of the New York Insurance Law.</p> <p style="padding-left: 40px;">The Company has complied with this recommendation.</p>	6
<p>ii. It is recommended that the Company adhere to all the provision of its by-laws and of the New York Business Corporation Law in the future. It is noted that a similar recommendation was included in the previous report on examination.</p>	7

ITEM	PAGE NO.
<p>The Company has complied with this recommendation.</p>	
<p>iii. It is recommended that the Company charge itself a reasonable rental for the occupancy of its own building. This amount must be in excess of the expenses for operating the home office building (including taxes, depreciation and a return on its investment).</p>	12
<p>The Company has complied with this recommendation.</p>	
<p>iv. It is recommended that the Company maintain its books of account and records in such manner as will facilitate the verification of all its financial statements filed with this Department, as required by Section 6611(a)(1) of the New York Insurance Law. It is noted that a recommendation regarding compliance with Section 6611(a)(1) of the New York Insurance law was included in the prior report on examination</p>	13
<p>The Company has complied with this recommendation.</p>	
<p>v. It is recommended that the Company comply with all the provisions of Section 3425 and 3426 of the New York Insurance Law.</p>	19
<p>The Company has complied with this recommendation.</p>	

7. SUMMARY OF COMMENTS AND RECOMMENDATIONS

ITEM	PAGE NO.
<p>A. <u>Territory and plan of operation</u></p> <p style="padding-left: 40px;">i. It is recommended that the Company comply with Section 6604(a) (3) of the Insurance Law and in the future obtain prior approval from the Insurance Department before writing a new line of business.</p>	<p>6</p>
<p>B. <u>Accounts and Records</u></p> <p style="padding-left: 40px;">i. It is recommended that the Company comply with the annual statement instructions and properly record all information in Schedule D-Part 1 of the annual statement.</p> <p style="padding-left: 40px;">ii. It is recommended that the Company comply with Department guidelines as set forth by 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>11</p> <p>11</p>

Respectfully submitted,

LS/  
Gerard L. Franco, CIE  
Senior Insurance Examiner

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

Gerard L. Franco, being duly sworn, deposes and says that the foregoing report, subscribed by him, is true to the best of his knowledge and belief.

LS/  
Gerard L. Franco

Subscribed and sworn to before me  
this 23<sup>RD</sup> day of JUNE, 2005.

LS/  
**GERARD M. BUSTI**  
Notary Public, State of New York  
Qualified in Albany County  
No. 018U5076509  
Commission Expires April 21, 2007

Appointment No 22332

STATE OF NEW YORK  
INSURANCE DEPARTMENT

I, HOWARD MILLS , Acting 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*

**United Frontier 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 14th day of February, 2005*



A handwritten signature in cursive script, appearing to read "Howard Mills".

HOWARD MILLS

Acting Superintendent of Insurance