



STATE OF NEW YORK
INSURANCE DEPARTMENT
AGENCY BUILDING ONE
EMPIRE STATE PLAZA
ALBANY, NY 12257

REPORT ON EXAMINATION
OF THE
SECURITY MUTUAL INSURANCE COMPANY
AS OF
DECEMBER 31, 2000

DATE OF REPORT:

JUNE 3, 2002

EXAMINER:

GERARD L. FRANCO



STATE OF NEW YORK
INSURANCE DEPARTMENT
AGENCY BUILDING ONE
EMPIRE STATE PLAZA
ALBANY, NY 12257

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 No. 21678 dated January 10, 2001, attached hereto, I have made an examination into the condition and affairs of the Security Mutual Insurance Company as of December 31, 2000 and submit the following report thereon. The examination was conducted at the Company's home office, located at 2417 Triphammer Road, Ithaca, New York 14852.

Whenever the designations "the Company", or "SMIC" appear herein without qualification, they should be understood to indicate the Security Mutual Insurance Company.

TABLE OF CONTENTS

	<u>Page No.</u>
1. Scope of Examination	2
2. Description of Company	2
A. Management	3
B. Territory and plan of operation	5
C. Reinsurance	6
D. Holding Company System	7
E. Significant Operating Ratios	8
F. Abandoned Property Law	8
G. Accounts and Records	9
3. Financial Statements	10
A. Balance Sheets	10
B. Underwriting and Investment Exhibit	12
4. Losses and Loss Adjustment Expenses	13
5. Treatment of Policyholders and Claimants	14
6. Compliance with Prior Report on Examination	16
7. Summary of Comments	17

1. SCOPE OF EXAMINATION

The prior examination was conducted as of December 31,1995. This examination covered the five year period from January 1,1996 through December 31,2000 and was limited in its scope to a review or audit of only those 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 and verification and utilized, to the extent considered appropriate, work performed by the Company's independent 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 departures from laws, regulations or rules, or which are deemed to require explanation or description.

2. DESCRIPTION OF COMPANY

The Company was organized in 1887 as the "Tompkins County Co-operative Fire Insurance Company" for the purpose of transacting business as a co-operative fire insurance corporation in Tompkins County, New York.

Subsequently, the territorial limits of the Company were extended to include all of the Counties of this State, and wherever authorized by law, any other States of the United States of America and the District of Columbia.

In 1935, a certificate was issued by the Department authorizing the Company to change its name to the "Tompkins Co-operative Fire Insurance Company."

Under the terms of an agreement of merger, effective in June 1957, the Company merged with the West Seneca Mutual Fire Insurance Association under the title and charter of the Tompkins Co-operative Fire Insurance Company.

Concurrent with the approval of the merger of Security Mutual Fire Insurance Company of Delhi, New York into the Tompkins Co-operative Fire Insurance Company, the latter was authorized in 1964 to change its corporate title to the Security Mutual Fire Insurance Company.

Subsequently, in 1964 the Company also merged with the Canton Co-operative Fire Insurance Company, of Canton, New York. Furthermore, on February 18, 1975, this Department approved the Company's current name of Security 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 thirteen members. As of the examination date, the board was comprised of eleven members. The board meets four times during each calendar year.

The board of directors membership at December 31,2000 was as follows:

<u>Director</u>	<u>Principal Business Affiliation</u>
Frederick S. Brown(E) Ithaca, NY	Retired
Peter A. Carriero Mechanicville, NY	Insurance Agent
Robert J. Clune Ithaca, NY	Attorney
Delbert L. Hall(E) Dryden, NY	Secretary and Treasurer, Security Mutual Insurance Company
Joan M. Holden Lansing, NY	Retired
Stephen M. James Binghamton, NY	Insurance Agent
Thomas R. Ruane(E) Ithaca, NY	President, Security Mutual Insurance Company
Roy E. Staley Ithaca, NY	Contractor
Robert B. Tallman(E) Ithaca, NY	Architect
Eben D. Tisdale, MD Ithaca, NY	Retired
Frederick Wilder Canton, NY	Retired

(E) Denotes member of Executive Committee.

The minutes of all meetings of the Board of Directors' and committees there of held during the examination period were reviewed. The average attendance by the board of directors

during the examination period was approximately 95% with each individual director's attendance being adequate at these meetings, unless otherwise indicated.

At December 31,2000, the officers of the Company were as follows:

President	Thomas R. Ruane
Secretary and Treasurer	Delbert L. Hall
Vice President	Stephen M. James

B. Territory and Plan of Operation

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

<u>Calendar Year</u>	<u>Total Direct Premiums Written (000)</u>
1996	\$26,705
1997	28,982
1998	29,656
1999	29,176
2000	28,770

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>Kind of Business</u>
4	Fire
5	Miscellaneous property
6	Water damage
7	Burglary and theft
8	Glass
12	Collision
13	Personal injury liability
14	Property damage liability
15	Workers' Compensation and employers' liability
19	Motor vehicle and aircraft physical damage(excluding aircraft physical damage)
20	Marine and inland marine(inland marine only)

The Company was also licensed as of December 31,2000, to accept and cede reinsurance as provided in Section 6606 of the Insurance Law of the State of New York.

The Company underwrites predominantly package policies with homeowners multiple peril and commercial multiple peril comprising 60.6% and 31.4% respectively of 2000 net premium writings.

C. Reinsurance

The Company had no assumed reinsurance premiums written as of December 31,2000.

The Schedule F's as contained in the Company's annual statements filed for the years within the examination period were found to accurately reflect its reinsurance transactions.

The examiner reviewed all ceded reinsurance contracts effected during the examination period. These contracts all contained the required standard clauses, including insolvency clauses, meeting the requirements of Section 1308 of the New York Insurance Law.

As of the examination date, the Company has the following property and casualty excess of loss reinsurance program in place:

Property(2 layers)	\$50,000 x/s \$100,000 as respect any one risk, with the reinsurer liable to a maximum of \$150,000 by reason of any one loss occurrence \$100,000 x/s \$150,000 as respects any one risk, with the reinsurer liable to a maximum of \$300,000 by reason of any one loss occurrence
Casualty(3 layers)	\$2,410,000 x/s \$90,000 in respect to any one loss occurrence
Property catastrophe (5 layers)	95% of \$21,000,000 x/s \$1,000,000 net loss each occurrence
Aggregate catastrophe Property	95% of \$1,500,000 x/s \$700,000 net catastrophe losses

As of the examination date, the Company has the following multiple line facultative binding authority reinsurance program in place:

Property	Pro-rata as to participation in excess of \$5,000 minimum Company retention up to a \$225,000 maximum cession
Casualty	\$400,000 x/s \$600,000 each occurrence, any one risk

As of the examination date, the Company has the following obligatory first surplus reinsurance program in place:

Property	Pro-rata to participation in risk, limited to \$850,000 cession each risk, each occurrence
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As the examination date, the Company has the following umbrella reinsurance program in place:

Casualty(2 layers)	95% of \$1,000,000 for each policy
	100% of \$2,000,000 x/s \$1,000,000 each occurrence, each policy for commercial risks
	95% of \$1,000,000 for each policy
	100% of \$4,000,000 x/s \$1,000,000 each occurrence, each policy for other risks

All the reinsurance contracts reviewed during the examination period were reinsured by authorized and unauthorized reinsurers, as was the case in the previous examination. Since the previous examination, the Company's net retention has increased from \$75,000 to \$100,000 on property business, and from \$75,000 to \$90,000 on casualty business.

D. Holding Company System

The Company participates as a direct writer in any combination policy issued by New York Mutual Underwriters. As of November 1997 the Company shares, with one other advance premium corporation one-half of all New York Mutual Underwriters' premiums, losses and

expenses. The Combination's predominate lines of business are commercial/special multiple peril, commercial landlord, personal dwellings and allied lines of business.

In 1998, SMIC organized a subsidiary, to be known as Security Mutual Brokers Services, Inc.(SMBS) pursuant to Section 1603 of the New York Insurance Law and this Department's Regulation No. 53(NYCRR Part 81-1). SMBS was incorporated to act as a general insurance agency to accept applications for property/casualty insurance of all kinds.

E. Significant Operating Ratios

The following ratios have been computed as of December 31, 2000 based upon the results of this examination:

Net premiums written in 2000 to Surplus as regards policyholders at December 31,2000	.90:1
Uncollected premiums(net of Reinsurance balances payable) to Surplus as regards policyholders	6.3%
Liabilities to Cash and invested assets	84.12%

The underwriting ratios presented below are on an earned-incurred basis and encompass the five year December 31,1995 to December 31,2000:

	<u>Amounts</u>	<u>Ratios</u>
Losses and loss adjustment expenses incurred	\$ 70,888,415	70.0%
Other underwriting expenses	39,077,993	38.6%
Net underwriting gain (loss)	(8,741,229)	(8.6%)
Premiums earned	\$ 101,225,179	100.0%

F. Abandoned property law

During the period covered by this examination, the Company was in compliance with Section 1316 of the New York Abandoned Property Law. Attempts were made to locate payees and appropriate filings were delivered to the state comptroller.

G. Accounts and Records

It is noted that the Company failed to include all of the call option data in Columns 3b and 3c of Schedule D, Part 1 of the Annual Statements filed during the examination period, as directed by the annual statement instructions. At the examination date of December 31, 2000 the company held callable bonds. Therefore, it is recommended the Company follow the annual statement instructions by including all call option data in future financial statements submitted to this Department.

3. STATEMENTS

A. Balance Sheet

The following shows the Company's financial condition as of December 31, 2000 determined by this examination, and as reported by the Company:

	<u>Ledger Assets</u>	<u>Non-Ledger Assets</u>	<u>Assets Not Admitted</u>	<u>Net Assets Admitted</u>
Bonds	\$29,244,291	\$ -0-	\$162,152	\$29,082,139
Common Stocks	4,273,522	12,115,825	-0-	16,389,347
Real Estate	585,249	-0-	-0-	585,249
Cash and short term investments	3,073,989	-0-	-0-	3,073,989
Agents' balances or uncollected premiums	2,976,014	-0-	22,528	2,953,486
Reinsurance recoverable on loss payments	503,838	-0-	-0-	503,838
Federal income tax recoverable	-0-	109,335	-0-	109,335
Electronic data processing equipment	180,323	-0-	-0-	180,323
Interest and divided income due and accrued		530,210		530,210
Equities and deposits in pools and associations	583,422		1,483	581,939
Other assets nonadmitted	143,088		143,088	
Aggregate write-ins for other than invested assets	<u>26,840</u>			<u>26,840</u>
Total assets	<u>\$41,590,576</u>	<u>\$12,755,370</u>	<u>\$329,251</u>	<u>\$54,016,695</u>

Liabilities

Losses and loss adjustment expenses		\$14,058,628
Contingent commissions and other similar charges		338,696
Other expenses		143,080
Taxes, licenses and fees		8,168
Unearned premiums		13,715,156
Funds held by company under reinsurance treaties		7,877
Amounts withheld for account of others		91,686
Drafts		<u>24</u>
Total Liabilities		\$28,363,315
Special contingent surplus	\$ 772,859	
Unassigned funds(surplus)	<u>21,880,521</u>	
Surplus as regards policyholders		<u>25,653,380</u>
Total Liabilities and surplus		<u>\$54,016,695</u>

The Internal Revenue Service did audit the Company's federal income tax returns for 1994 and 1995 during the 1998 examination year. Audits covering subsequent tax years have yet to commence. Except for any impact that might result from the examination changes contained in this report, the examiner is unaware of any potential exposure of the Company to any further tax assessment and no liability has been established herein relative to such contingency.

B. Underwriting and Investment Exhibit

Surplus as regards policyholders increased \$9,943,833 during the five-year examination period,(January 1, 1995 to December 31, 2000) detailed as follows:

Statement of Income

	<u>Underwriting</u>	
Premiums earned		\$101,225,179
Losses and loss adjustment expenses incurred	\$70,888,415	
Other underwriting expenses incurred	<u>39,077,993</u>	
Total underwriting deductions		<u>(109,966,408)</u>
Net underwriting loss		(\$8,741,229)
<u>Investment Income</u>		
Net investment income earned	\$10,503,643	
Net realized capital gain or (loss)	<u>1,004,457</u>	
Net investment gain		11,508,100
<u>Other Income</u>		
Finance charges	\$ 1,233,980	
Agents' balances charged off	(64,971)	
Amounts withheld or retained for account of others	(135,075)	
Miscellaneous income	<u>(20,718)</u>	
Net other Income		<u>1,013,216</u>
Net income before federal income taxes		\$3,780,087
Federal income tax incurred		<u>(857,076)</u>
Net income		<u>\$2,923,011</u>

Capital and Surplus Account

Surplus as regards policyholders, December 31,2000,

per prior report on examination \$15,709,547

	Gains in	Losses in
Net income or loss	\$2,923,011	\$-0-
Net unrealized capital loss	7,023,350	-0-
Change in non-admitted assets	-0-	2,528
Totals	\$9,946,361	\$2,528

Net increase in Surplus as regards policyholders 9,943,833

Surplus as regards policyholders, December 31, 2000,

per report on examination \$25,653,380

4. LOSSES AND LOSS ADJUSTMENT EXPENSES

The loss and loss adjustment expense reserves for accident years 2000 and prior, evaluated at December 31, 2001, are estimated to be deficient by \$1,372,000. The examination analysis was conducted in accordance with generally accepted actuarial principles and practices and was based on statistical information contained in the Company's internal records and in its filed annual statements. As the above amount represents approximately 5% of the Company's surplus, such amount will not be considered material. Therefore, the examination liability of \$14,058,628 is the same amount reported by the Company in its filed 2000 annual statement.

The Company's actuarial opinion and report were reviewed and utilized in the determination of an appropriate reserve for the Company's unpaid losses and loss adjustment expenses. According to the Company's Schedule P, Part 2 of the 2001 annual statement, the Company's one-year run-off is deficient by \$2,030,000. Therefore, the deficiency as of

December 31, 2000 is estimated to be \$3,402,000. Through the analysis of calculated ratios it could be shown that reserve strengthening has been carried out by the Company. Thus, the increase in the loss and loss adjustment expense reserve has been estimated to be \$1,372,000 at December 31, 2001.

It is recommended that the Company take the appropriate steps necessary to report adequate reserves for losses and loss adjustment expenses in accordance with Section 1303 of the New York Insurance Law. It is noted that a similar recommendation was made in the previous report on examination.

5. TREATMENT OF POLICYHOLDERS AND CLAIMANTS

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

No unfair practices were encountered unless otherwise noted.

It is noted that claim files of the Company were reviewed for compliance with this Department's Regulation 64 (11NYCRR216). Section 216.11 of the aforementioned Regulation

provides that claim files must be so maintained that the Insurance Department examiners can reconstruct all events relating to a claim. Although claim files contained proper information, claim files were difficult to read and entries were difficult to follow. The Company does not have written procedures for establishing diaries for claim files. Therefore, it is recommended that the Company comply with Section 216.11 Regulation 64 by organizing their claim files in such a manner as to enable Insurance Department personnel to reconstruct all events relating to a claim.

Also, cancellations were reviewed for Company compliance with Section 3425(d)(1) and 3426(e)(2) of the New York Insurance Law. It was found in several instances that only general reasons, such as “poor physical condition” and “loss frequency”, were given for the cancellation. The above mentioned reasons are too broad in nature and do not comply with the specificity required by the above-cited laws. Therefore, it is recommended that the Company comply with Section 3425(d)(1) and 3426(e)(2) of the New York Insurance Law and give a more detailed description of the reason for the cancellation.

6. COMPLIANCE WITH PRIOR REPORT ON EXAMINATION

The prior report contained comments and recommendations as follows (page numbers refer to the prior report):

<u>Item</u>	<u>Page No.</u>
A. The Company should revise its reserving methods to adequately provide for unpaid losses on all lines of business when submitting financial statements to this Department	13
The Company has not complied with this recommendation. See item B of Section 7 of this report for further details.	
B. The Company should revise its procedure to adequately provide for the liability for unallocated loss adjustment expenses when submitting financial statements to this Department	14
The Company has not complied with this recommendation. See item B of Section 7 of this report for further details.	

7. SUMMARY OF COMMENTS

As indicated in the body of this report, the Company should be directed to comply with the following:

<u>Item</u>	<u>Page No.</u>
<u>A. Annual Statement Schedule D-Part</u>	
It is recommended the Company follow the annual statement instructions by including all call option data in future financial statements submitted to this Department	9
<u>B. Losses and Loss Adjustment Expenses</u>	
It is recommended that the Company take the appropriate steps necessary to report adequate reserves for losses and loss adjustment expenses in accordance with Section 1303 of the New York Insurance Law.	14
<u>C. Treatment of Policyholders and Claimants</u>	
i. It is recommended that the Company comply with Regulation 64 (NYCRR Part 16.11) by organizing their claim files in such a manner as to enable Insurance Department personnel to reconstruct all events relating to a claim.	15
ii. It is recommended that the Company comply with Section 3425(d)(1) and 3426(e)(2) of the New York Insurance Law and give a more detailed description of the reason for the cancellation.	15

Appointment No 21678

STATE OF NEW YORK
INSURANCE DEPARTMENT

I, Gregory V. Serio, First Deputy Superintendent of Insurance of the State of New York, pursuant to the provisions of the Insurance Law, do hereby appoint:

Gerard L. Franco

as proper person to examine into the affairs of the

Security Mutual Insurance Company

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

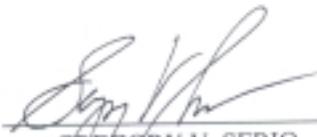
Company

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 New York,

this 10th day of January, 2001




GREGORY V. SERIO
First Deputy Superintendent of Insurance