

REPORT ON EXAMINATION

OF THE

FULMONT MUTUAL INSURANCE COMPANY

AS OF

DECEMBER 31, 2005

DATE OF REPORT

FEBRUARY 16, 2007

EXAMINER

WAYNE LONGMORE

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

February 16, 2007

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

Sir:

Pursuant to the requirements of the New York Insurance Law, and in compliance with the instructions contained in Appointment Number 22539 dated August 31, 2006, attached hereto, I have made an examination into the condition and affairs of the Fulmont Mutual Insurance Company as of December 31, 2005 and submit the following report thereon.

Wherever the designations “the Company” or “FMIC” appear herein without qualification, they should be understood to indicate Fulmont Mutual 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 2240 State Highway 29, Johnstown, New York 12095.

## **1. SCOPE OF EXAMINATION**

The prior examination was conducted as of December 31, 2000. This examination covered the five year period from January 1, 2001 through December 31, 2005, 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 or verification and utilized, to the extent considered appropriate, work performed by the Company's independent public accountants.

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 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 on August 9, 1853 for the purpose of transacting business as an assessment cooperative fire insurance association in Fulton and Montgomery Counties, New York.

A certificate was issued by this Department on December 27, 1910 which authorized the Company to continue the transaction of business in the above named counties.

On December 31, 1986, the Company converted to an advance premium cooperative insurance company and changed its name from "Fulton and Montgomery Counties Farmers Mutual Fire Insurance Association" to "Fulmont Mutual Insurance Company". At the same time, the Company became qualified to write non-assessable policies and was permitted to extend its territorial limits to include the entire state of New York.

Effective June 1, 1990, the license of FMIC was changed to require that the Company reinsure the whole risk for all perils specified in paragraphs seven, eight, thirteen, fourteen and fifteen of Section 1113(a) of the Insurance Law.

On May 1, 1998, The Mohawk Minden Insurance Company merged into the Fulmont Mutual Insurance Company.

On October 15, 2002, FMIC's license was amended to add paragraph 9 of Section 1113(a) of the New York Insurance Law, boiler and machinery insurance. That license also requires it to reinsure the whole risk for all perils specified in paragraphs seven, eight, nine, thirteen, fourteen and fifteen.

A. Management

Pursuant to the Company's charter, management of the Company is vested in a board of directors consisting of not less than nine nor more than fifteen members. As of the examination date, the board of directors was comprised of ten members.

At least four board meetings were held in each of the years during the period under examination, thereby complying with Section 6624(b) of the New York Insurance Law.

The Company reported that the directors as of December 31, 2005, were as follows:

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Burlin C. Argotsinger Gloversville, NY	Insurance Agent; Director Westport MLM Agency, Inc.; Director FM Scion Service Corporation
Marlene A. Benton Amsterdam, NY	President of FMIC; Director and Secretary-Treasurer Westport MLM Agency, Inc.; Director and Secretary-Treasurer FM Scion Service Corporation
Norbert E. Bicheler Sprakers, NY	Retired Farmer; Insurance Agent; Vice Chairman of the Board FMIC; Director Westport MLM Agency, Inc.; Director FM Scion Service Corporation
Warren A. Canary St. Johnsville, NY	Retired Farmer; Retired Insurance Agent; Director Westport MLM Agency, Inc.; Director and Vice President FM Scion Service Corporation
Raynor B. Duncombe Middleburgh, NY	Attorney; Chairman of the Board FMIC; Director Westport MLM Agency, Inc.; Director FM Scion Service Corporation

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Margaret M. Leackfeldt Pattersonville, NY	Director and President Westport MLM Agency, Inc.; Director FM Scion Service Corporation
Richard D. Rathbun Cooperstown, NY	Retired Insurance Agent; Farmer; Director Westport MLM Agency, Inc.; Director FM Scion Service Corporation
Deborah A. Sidney Herkimer, NY	Secretary and Treasurer of FMIC; Director and Assistant Secretary-Treasurer Westport MLM Agency, Inc.; Director and Assistant Secretary- Treasurer FM Scion Service Corporation
Michael W. Smrtic Johnstown, NY	Attorney
Isabella Ann VanDewerker Cherry Valley, NY	Homemaker; Director Westport MLM Agency, Inc.; Director and President FM Scion Service Corporation

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 prior Report on Examination as of December 31, 2000 contained a recommendation that the Company adhere to all the provisions of its charter and by-laws and Section 712(a) of the New York Business Corporation Law, henceforth. During this examination it was found that the Company was not fully complying with the provisions of Article IV Section 5 "Nominations" of its by-laws which states, in part, that:

"The directors to be elected at the annual meeting, and who qualify shall be nominated by Nominating Committee ... which shall be approved by the Executive Committee at a regular meeting held during the twelve months prior to the annual meeting."

Thus, it is recommended that the Company comply with all the provisions of its by-laws, henceforth or that it request Department approval to change its by-laws to reflect the way that the Company is currently operating.

As of December 31, 2005, the principal officers of the Company were as follows:

<u>Name</u>	<u>Title</u>
Raynor B. Duncombe	Chairman of the Board
Norbert E. Bicheler	Vice-Chairman of the Board
Marlene A. Benton	President
Deborah A. Sidney	Secretary and Treasurer
Joanne E. Gifford	Assistant Secretary
Brian Kingsley	Assistant Secretary
Anabel Kovarovic	Assistant Treasurer
Terry Dufel	Assistant Treasurer

B. Territory and Plan of Operation

As of December 31, 2005, 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
6	Water damage
7	Burglary and theft
8	Glass
9	Boiler and machinery
12	Collision
13	Personal injury liability
14	Property damage liability
15	Workers' compensation and employers' liability (excluding workers' compensation)
19	Motor vehicle and aircraft physical damage
20	Marine and inland marine (inland marine only)

On October 15, 2002, FMIC's license was amended to add paragraph 9 of Section 1113(a) of the New York Insurance Law, boiler and machinery insurance. That license also requires it to reinsure the whole risk for all perils specified in paragraphs 7, 8, 9, 13, 14 and 15. FMIC's license, effective June 1, 1990 through October 14, 2002, required it to reinsure the whole risk for all perils specified in paragraphs 7, 8, 13, 14 and 15.

The Company was also licensed as of December 31, 2005, to accept and cede reinsurance as provided in Section 6606 of the Insurance Law of the State of New York.

Based upon the lines of business for which the Company is licensed, and pursuant to the requirements of Articles 13, 41 and 66 of the New York Insurance Law, as of December 31, 2005, the Company is required to maintain a minimum surplus to policyholders in the amount of \$100,000.

FMIC was granted an amendment to its license effective January 1, 2007. Under the new license there is no change in the previously defined kinds of insurance the Company is authorized to transact, except paragraph 15 was removed. In addition, the Company is no longer required to reinsure the whole risk for all perils specified in paragraphs 7, 8, 9, 13, and 14.

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 (000's)</u>
2001	\$3,738
2002	\$4,180
2003	\$4,477
2004	\$4,127
2005	\$3,685

At December 31, 2005, the Company wrote insurance through independent agents, its two subsidiaries and director-agents. The Company maintained a branch office ("West") at 62 Erie Boulevard, Canajoharie, New York. As of December 31, 2005 the Westport operations (the former "North" branch office) were being handled out of the home office of the Company.

The Company's predominant lines of business are homeowners multiple peril and commercial multiple peril, which accounted for 39.73% and 41.81%, respectively, of the Company's 2005 direct written business.

C. Reinsurance

The Company had no assumed business at year-end 2005.

As of December 31, 2005, the Company had the following property and casualty excess of loss ceded reinsurance program in place:

Property 2 Layers	\$450,000 in excess of \$50,000 each loss, each risk. Per occurrence limit of \$150,000 on first layer and \$800,000 on the second.
Casualty 1 Layer	100% of \$1,000,000 per any loss occurrence.
Casualty Clash	\$1,000,000 in excess of \$1,000,000 each loss occurrence.

As of December 31, 2005, the Company had the following aggregate excess of loss reinsurance coverage in place:

Property	95% of \$750,000 in excess of 60% of net premiums earned.
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As of December 31, 2005, the Company also maintained a catastrophe cover on a per occurrence basis:

Property 3 layers	95% of \$1,900,000 in excess of \$100,000 each loss occurrence (layers 1 & 2). \$1,000,000 in excess of \$2,000,000 each loss occurrence (layer 3).
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As of December 31, 2005, the Company had a Machinery & Equipment Coverage Quota Share Treaty on Boiler and Machinery Insurance as follows:

Reinsurer obligates itself to accept as reinsurance of the Company and the Company obligates itself to cede to the reinsurer 100% of the Company's net retained liability as defined in the contract.

Cessions under the Contract shall not exceed \$5,000,000 on any one risk without prior written agreement of the reinsurer. One policy constitutes one risk.

In 1998, an \$80,000 annual corridor deductible was implemented on the first layer of the Company's property excess of loss coverage. That deductible was increased in 2005 to \$100,000.

However, this provision shall not apply to the extent that it would result in the Company violating Section 6610 of New York Insurance Law.

The Company also had in effect, as of the examination date, a "Property Facultative Pro Rata Reinsurance Agreement" that provides cessions to this contract shall be limited to an amount equal to three times the Company's net retention, subject to minimum retention of \$250,000 and to a maximum cession of \$500,000 on any one risk. However, if the cession is greater than \$250,000 the maximum cession as respects any one animal shall not exceed \$250,000. Business not within the scope of the contract maybe submitted for special acceptance by the lead reinsurer.

In addition, the Company had in effective at December 31, 2005, a "Special Casualty Excess of Loss Reinsurance" agreement that allows the Company to cede on a facultative basis \$500,000 in excess of \$500,000 per loss occurrence.

The Company's net retention on its property business was \$50,000 throughout the period under examination, which was an increase from the \$40,000 as of December 31, 2000. The Company continued to cede 100% of its casualty business.

All of the Company's cessions during the period under examination were to authorized reinsurers.

All addendums and reinsurance contracts that became effective during the period under examination were submitted to the Department for review in accordance with Section 1308(e) of the New York Insurance Law.

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

Examination review of the Schedule F data reported by the Company in its 2005 filed Annual Statement was found to accurately reflect its reinsurance transactions except as noted below.

The Company consistently reported throughout the filed Annual Statement that it ceded its reinsurance to affiliates. Based upon discussion with an officer of the Company and a review of the

reinsurance contracts this was found to be inaccurate. The Company is not affiliated with any of its reinsurers.

It is recommended that the Company comply with the Annual Statement Instructions and classify its reinsurers properly as affiliated or non-affiliated based upon the actual parties to the contracts.

Management has represented that all material ceded reinsurance agreements transfer both underwriting and timing risk as set forth in Statements of Statutory Accounting Principles (“SSAP”) No. 62. Representations were supported by an attestation from the Company's Chief Executive Officer and Chief Financial Officer pursuant to the NAIC Annual Statement Instructions. Additionally, examination review indicated that the Company was not a party to any finite reinsurance agreements.

D. Holding Company System

The Company had two subsidiaries in its holding company system at December 31, 2005. A description of the system is as follows:

FM Scion Service Corporation (“FM Scion”) was organized for the purpose of providing certain ancillary services to the Company. The initial funding of FM Scion was the Company’s purchase of five shares of \$1,000 par value common stock at \$1,000 per share for a total investment of \$5,000. Subsequent purchases of common stock by the Company increased its investment in FM Scion to 87 shares for a total investment of \$87,000.

In 1982, FM Scion expanded its scope to include the business of insurance broker, which provided a vehicle for those agents, who were also brokers, to write coverage that the Company does not write, through FM Scion. This brokerage activity was further expanded in 1985 when FM Scion purchased an independent agency, MLM Agency, Inc., which was later transferred to the Company, and became the second subsidiary, Westport MLM Agency, Inc. (“Westport MLM”).

Westport was organized in 1987 to conduct business as a general insurance agency and brokerage company, with the provision that neither Westport nor the Company would broker business for each other. The Company contributed capital to the subsidiary by purchasing forty shares of \$3,000 par value common stock at \$3,000 per share for a total investment of \$120,000.

A contract for the sale of the agency book of business and the real estate of the 100% wholly owned subsidiary of Fulmont Mutual Insurance Company, Westport MLM Agency, Inc., was executed on December 5, 2005 between seller Westport MLM and purchaser Wayne Shepard. Under the terms of what is described as an “installment sale contract” there is no money down and the purchaser agrees to pay the total purchase price of Five hundred seventy-five thousand two hundred fifty-three and no/100 Dollars (\$575,253) by making consecutive monthly payments of principal and interest of Five thousand one hundred seventy and 54/100 Dollars (\$5,170.54) commencing January 5, 2006 and continuing every month thereafter for fifteen (15) years at seven percent (7%) interest until entire unpaid balance of principal and accrued interest are paid in full. Upon the signing of the contract, seller is to execute to the Purchaser a Warranty Deed with lien covenant to the premises, conveying marketable title thereto, duly executed and acknowledged so as to convey to the Purchaser the fee simple to the premises, free of all liens and encumbrances. The deed is to be held in escrow by Seller’s attorney or other duly appointed agent of Seller and released to the Purchaser upon the payment in full of the agreed principal sum along with all accrued interest.

As part of the contract, the Seller agrees that the contract will be carried as a non-admitted asset on its balance sheet and that the value of the real estate being transferred will not be increased on its balance sheet.

E. Significant Operating Ratios

The following ratios have been computed as of December 31, 2005, based upon the results of this examination:

Net premiums written in 2005 to Surplus as regards policyholders	1.24 to 1
Liabilities to liquid assets (cash and invested assets less investments in affiliates)	61%
Premiums in course of collection to Surplus as regards policyholders	3%

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	\$8,314,372	62.80%
Other underwriting expenses incurred	5,694,610	43.02%
Net underwriting loss	<u>(770,603)</u>	<u>(5.82)%</u>
Premiums earned	<u>\$13,238,379</u>	<u>100.00%</u>

F. Accounts and Records

1. Superintendent's Account Transactions

The previous report on examination as of December 31, 2000 included the following recommendation:

“It is recommended that the Company ensure that matured security proceeds are not taken out of the Superintendent’s custodial account without the written approval of the New York Insurance Department as required by Section 1314 of the New York Insurance Law.”

During the previous examination, Company management provided correspondence, dated July 24, 2001, which stated that the Superintendent’s account will be monitored to ensure that approval by the New York State Insurance Department is obtained prior to funds being released from that account.

Comparison of the securities being held in the Superintendent’s Account as of the previous examination, December 31, 2000, with those being held at December 31, 2005, revealed that in 2003 the Company removed the proceeds from the redemption of a \$100,000 par value New York St PWR Auth & Gen P Rev 8/15/93 5.25% due 1/1/18 (CUSIP 649892C38) bond.

Company management was unable to provide documentation of the New York Insurance Department approval of the above transaction, as such; it appears that the Company did not comply with the previous report on examination recommendation.

Thus, it is recommended that the Company ensure that matured/redeemed security proceeds are not taken out of the Superintendent’s custodial account without the written approval of the New York Insurance Department as required by Section 1314 of the New York Insurance Law.

2. Allocation of Expenses

During the course of the previous examination Company management provided a memorandum dated July 26, 2001 to the examiners which stated that time studies will be completed on a yearly basis comprising two (2) separate weeks at different times during the year beginning in 2002. During the current examination Company management was asked for the basis for the allocation of salary expenses by department within the Company and the breakdown by expense groupings used in the Underwriting & Investment Exhibit Part 3 - Expenses of the 2005 filed Annual Statement. The examiners were informed in correspondence from the Company dated December 14, 2006 that management was not generating current time studies and the one in use at December 31, 2005 is estimated to date back to the year 2000.

It should be noted that inter-company agreements titled the "EXPENSE ALLOCATION AMONG CORPORATIONS" in effect during 2005, call for the use of time studies as the basis for the allocation of salaries. Said agreements also call for the employment of time usage studies for the "System 36" (computer system) in the allocation of data processing hardware time to FMIC. Company management was also asked for the 2005 time usage studies. In their response, dated December 14, 2006, Company management explained that no studies could be provided for 2005 since during that year the "System 36" was replaced by an "AS-400" computer system. Management explained that an average of the totals for the previous four years was used to arrive at the usage figure for 2005 since time usage studies, similar to that generated by the "System 36," cannot be generated by the new "AS-400" system.

Given the above observations, it is recommended that the Company comply with its established "EXPENSE ALLOCATION AMONG CORPORATIONS" agreement with respect to the use of allocation bases or amend its agreement to conform to how expenses are actually being allocated. In addition, it is recommended that the Company establish and maintain written documentation supporting the allocation of each expense category to the major expense groups as required by Department Regulation 30.

3. New York Insurance Law Section 1411(e)

The following observations were made during the review of expenses relative to the current examination of the Company.

During the review of payment documentation pertaining to the Company's investment in mortgage loans, a check for \$500 dated September 15, 2006 made payable to a director of the Company was noted.

The review of the Company's inter-company expenses revealed an additional \$1,000 payment made to the same director via check dated December 5, 2005. That payment pertained to services provided in relation to negotiating the terms of the contract on the Westport MLM sale previously discussed in the holding company section of this report.

New York Insurance Law Section 1411(e) states, in part, the following:

"No director or officer of an insurer doing business in this state shall receive, in addition to his fixed salary or compensation, any money or valuable thing, directly or indirectly, or through any substantial interest in any other corporation or business unit, for negotiating, procuring, recommending or aiding in any purchase or sale of property, or loan, made by such insurer or any affiliate or subsidiary thereof; nor shall he be pecuniarily interested, as principal, co-principal, agent or beneficiary, directly or indirectly, or through any substantial interest in any other corporation or business unit, in any such purchase, sale or loan..."

Company management is also noted to have provided a memorandum dated July 25, 2001 to the New York Insurance Examiners during the previous examination indicating that the Company will no longer pay such officer/director of the Company for representing it at mortgage closings.

The above transactions appear to be violations of Section 1411(e) of the New York Insurance Law; thus, Company management was directed to obtain reimbursement (evidence of which was provided to the examiners) for the aforementioned expenditures since this would be in keeping with its fiduciary responsibility to the Company and to the policyholders.

It is recommended that the Company comply with Section 1411(e) of the New York Insurance Law and ensure that no director or officer receive, in addition to their fixed salary or compensation, any money or valuable thing, directly or indirectly, for negotiating, procuring, recommending or aiding in any purchase or sale of property, made by such insurer or any affiliate or subsidiary thereof.

#### 4. Compliance with commitments made to this Department

The Company merged with The Mohawk Minden Insurance Company (“Mohawk Minden”) effective May 1, 1998.

In correspondence dated July 17, 2001 the Company agreed to make the necessary changes to incorporate Mohawk Minden’s loss data into FMIC's Schedule P for 2001. However, based upon the review of the 1997 filed Annual Statement for Mohawk Minden as well as the review of the 1998 and 2005 filed Annual Statements for FMIC (see Schedule P Part 2 Summary) it does not appear that the Company complied with its written commitment to this Department. This was confirmed in correspondence provided by Company management dated February 8, 2007.

In a number of instances it was observed that the Company provided letters of commitment to this Department during the course of the previous examination, agreeing to perform certain acts of compliance and for one reason or another said commitments were not adhered to. See as examples the preceding paragraphs regarding The Mohawk Minden Insurance Company’s loss data as well as matters included in Section F, “Accounts and Records” of this report under caption “Allocation of Expenses” and “New York Insurance Law Section 1411(e).”

Given the preceding observations, it is recommended that the Company comply with all written commitments made to this Department, henceforth.

#### 5. Custodial Agreement Requirements

Based upon a review of the Company's current custodial agreement, it was determined that some provisions and safeguards required by the New York Insurance Department and the National Association of Insurance Commissioners (“NAIC”) Financial Condition Examiners Handbook were not included in the agreement. It is noted that Company management was in the process of revising said agreement to allow compliance with the requirements at the conclusion of the field portion of the examination. Nonetheless, it is recommended that the Company continue to finalization the process of amending its custodial agreement to include all the provisions required by the New York Insurance Department and the NAIC Financial Condition Examiners Handbook.

6. Approval of short term investments

The Company was not having all of its short term investments authorized or approved in accordance with Section 1411(a) of the New York Insurance Law during the period under examination.

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.”

Thus, it is recommended that the Company comply with the investment authorization requirements of Section 1411(a) of the New York Insurance Law.

7. Misclassification of long term Certificates of Deposit

The Company is noted to have misclassified and listed two certificates of deposits with maturity dates in excess of one year on Schedule E - Part 1 - Cash in its 2005 filed Annual Statement.

It is recommended that the Company comply with SSAP No. 26 paragraph 2, SSAP No. 2 paragraph 3 as well as the Annual Statement Instructions and classify certificates of deposit that have a maturity date in excess of one year from the date of acquisition as bonds.

8. PAYTRUST, Inc. (“PayTrust”) check issuing service

Fulmont Mutual Insurance Company, an advance premium corporation subject to Article 66 of the New York Insurance Law, is using a check issuing service (“PayTrust”) to pay some of its expenses.

The checks issued by PayTrust have Fulmont Mutual Insurance Company’s name and bank account number on them. In the signature area of the checks is the notation “SIGNATURE ON FILE”. The checks issued are not "signed" by two officers of the Company although the Payment Authorization Form allowing PAYTRUST, Inc. to receive and pay bills is signed by two officers.

Apparently, the Company is using the service to pay bills below a threshold of \$10,000. This amount, based upon the financial size of the Company, does not seem prudent.

Section 6611(a)(4)(C) is specific in that it requires all checks to be signed either by two officers or by one officer upon the written order of another officer with an exception noted in the law for miscellaneous expenses. The Company should comply fully with Section 6611(a)(4)(C) of the New York State Insurance Law.

In addition, the Board resolution(s) authorizing the use of the aforementioned check issuing service should set a specific dollar limit over which no one check may be issued pursuant to such an arrangement.

The directors of the Company should remain mindful of their fiduciary responsibilities to the Company and its policyholders, as set forth in Section 717(a) of the New York Business Corporation Law, when determining the dollar threshold for the amount considered as miscellaneous expenses. The basis used when making the determination should be clearly documented in the resolution passed. The reasonableness of the amount determined based upon among other factors the financial condition of the Company will be reviewed upon examination;

The resolution should specify the expenses and/or types of expenses, which must be characterized as "miscellaneous", that may be paid using the check writing arrangement; and the resolution should specifically identify the expenses for which this arrangement may not be used.

Reference should be made to Department Regulation 30, Part 105 relative to what constitutes a miscellaneous expense.

In view of the above, it is recommended that the Company adopt a resolution which incorporates the specific Department guidance provided above relative to its arrangement with PayTrust. In addition, it is recommended that the board of directors ensure that the management of the Company has put into place adequate controls over this arrangement in order to adequately protect the assets of the Company. Evidence that the board has verified periodically, but no less frequently than annually, that the controls are operating properly must be maintained and provided for review upon examination.

### 3. FINANCIAL STATEMENTS

#### A. Balance Sheet

The following shows the assets, liabilities and surplus as regards policyholders as of December 31, 2005 as determined by this examination and as reported by the Company:

<u>Assets</u>	<u>Assets</u>	Assets Not <u>Admitted</u>	Net Admitted <u>Assets</u>
Bonds	\$2,460,495	\$ 0	\$2,460,495
Common stocks	300,684	0	300,684
Mortgage loans on real estate: First liens	65,497	0	65,497
Real Estate: Properties occupied by the company	142,807	0	142,807
Cash, cash equivalents and short-term investments	687,918	0	687,918
Investment income due and accrued	29,925	0	29,925
Uncollected premiums and agents' balances in the course of collection	57,552	6,301	51,251
Deferred premiums, agents' balances and installments booked but deferred and not yet due	315,385	18,902	296,483
Amounts recoverable from reinsurers	19,820	0	19,820
Current federal and foreign income tax recoverable and interest thereon	1,410	0	1,410
Net deferred tax asset	50,622	0	50,622
Furniture and equipment, including health care delivery assets	35,654	35,654	0
Receivables from parent, subsidiaries and affiliates	33,106	0	33,106
A/R Other	7,538	0	7,538
Fair Plan & Loans	104,364	10,700	93,664
Automobile	<u>12,671</u>	<u>12,671</u>	<u>0</u>
Total assets	<u>\$4,325,448</u>	<u>\$84,228</u>	<u>\$4,241,220</u>

Liabilities, surplus and other funds

Losses and loss adjustment expenses		\$ 153,084
Commissions payable, contingent commissions and other similar charges		68,092
Other expenses (excluding taxes, licenses and fees)		7,530
Unearned premiums		1,970,281
Advance premiums		60,304
Ceded reinsurance premiums payable (net of ceding commissions)		45,635
Amounts withheld or retained by company for account of others		10,185
Payable to parent, subsidiaries and affiliates		6,426
Aggregate write-ins for liabilities		<u>24,013</u>
Total liabilities		\$2,345,550
Aggregate write-ins for special surplus funds	\$ 100,000	
Unassigned funds (surplus)	<u>1,795,670</u>	
Surplus as regards policyholders		<u>1,895,670</u>
Total liabilities, surplus and other funds		<u>\$4,241,220</u>

Note: The Internal Revenue Service did not audit the Company's federal income tax returns for the period under examination. Audits covering subsequent tax years have yet to commence. 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 by \$504,481 during the five-year examination period, January 1, 2001 to December 31, 2005, detailed as follows:

Statement of Income

Underwriting Income

Premiums earned		\$13,238,379
Deductions:		
Losses and loss adjustment expenses incurred	\$8,314,372	
Other underwriting expenses incurred	<u>5,694,610</u>	
Total underwriting deductions		<u>14,008,982</u>
Net underwriting gain or (loss)		\$ (770,603)

Investment Income

Net investment income earned	\$ 882,272	
Net realized capital gain	<u>(5,156)</u>	
Net investment gain or (loss)		877,116

Other Income

Net gain or (loss) from agents' or premium balances charged off	\$ 31,975	
Finance and service charges not included in premiums	342,147	
Aggregate write-ins for miscellaneous income	<u>11,069</u>	
Total other income		<u>385,191</u>
Net income before federal and foreign income taxes		\$ 491,704
Federal and foreign income taxes incurred		<u>12,500</u>
Net Income		\$ <u>479,204</u>

Capital and Surplus Account

Surplus as regards policyholders per report on Examination as of December 31, 2000			\$1,391,189
	<u>Gains in Surplus</u>	<u>Losses in Surplus</u>	
Net income	\$479,204	\$ 0	
Net unrealized capital gains or losses	0	46,288	
Change in net deferred income tax	50,622	0	
Change in nonadmitted assets	22,059	0	
Aggregate write-ins for gains and losses in surplus	<u>0</u>	<u>1,116</u>	
Total gains or losses in surplus	<u>\$551,885</u>	<u>\$47,404</u>	
Net increase in surplus			<u>504,481</u>
Surplus as regards policyholders per report on Examination as of December 31, 2005			<u>\$1,895,670</u>

**4. LOSSES AND LOSS ADJUSTMENT EXPENSES**

The examination liability for the captioned items of \$153,084 is the same as reported by the Company as of December 31, 2005.

The examination analysis of the loss and loss adjustment expense reserves 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.

**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 eight recommendations as follows (page numbers refer to the prior report):

<u>ITEM</u>	<u>PAGE NO.</u>
A. <u>Management</u>	
i. It is recommended that the Company adhere to all the provisions of its charter and by-laws and Section 712(a) of the New York Business Corporation Law, henceforth.	5
The Company has not fully complied with this recommendation. A similar recommendation regarding the by-laws is made in this report.	
ii. It is recommended that the minutes of the annual policyholders meeting clearly state the names of the individuals being nominated including their length of term and the minutes definitively state that the policyholders elected such individuals as directors.	5
The Company has complied with this recommendation.	
B. <u>Holding Company System</u>	10
It is recommended that the Company report transactions with its two subsidiaries in accordance with Regulation 53, henceforth.	
The Company has complied with this recommendation.	
C. <u>Securities in the Superintendent's Custodial Account</u>	12
It is recommended that the Company ensure that matured security proceeds are not taken out of the Superintendent's custodial account without the written approval of the New York Insurance Department as required by Section 1314 of the New York Insurance Law.	
The Company has not complied with this recommendation. A similar recommendation is made in this report.	

<u>ITEM</u>	<u>PAGE NO.</u>
D. <u>Custodianship of Securities</u>	12
<p>It is recommended that the Company comply with Department Circular Letter No. 2 (1977) and only allow its investments to be held under custodial arrangements that meet the requirements put forth in the circular letter.</p> <p>The Company has complied with this recommendation.</p>	
E. <u>Market Conduct Activities</u>	
i. It is recommended that the Company comply with all the provisions of Section 3403 of the New York Insurance Law and Department Regulation No. 96, henceforth.	18
<p>The Company has complied with this recommendation.</p>	
ii. It is recommended that the Company comply with all the provisions of Sections 3425(d) and 3426(e) of the New York Insurance Law.	19
<p>The Company has substantively complied with this recommendation.</p>	
iii. It is recommended that the Company comply with all the provisions of Section 216.9(a) of Department Regulation 64, henceforth.	20
<p>The Company has complied with this recommendation.</p>	

## 7. SUMMARY OF COMMENTS AND RECOMMENDATIONS

<u>ITEM</u>	<u>PAGE NO.</u>
A. <u>Management</u>	
<p>It is recommended that the Company comply with all the provisions of its by-laws, henceforth or that it request Department approval to change its by-laws to reflect the way that the Company is currently operating. It is noted that a similar recommendation was included in the prior report on examination.</p>	
B. <u>Reinsurance</u>	
<p>It is recommended that the Company comply with the Annual Statement Instructions and classify its reinsurers properly as affiliated or non-affiliated based upon the actual parties to the contracts.</p>	
	9

<u>ITEM</u>		<u>PAGE NO.</u>
C.	<u>Accounts and Records</u>	
i.	It is recommended that the Company ensure that matured/redeemed security proceeds are not taken out of the Superintendent’s custodial account without the written approval of the New York Insurance Department as required by Section 1314 of the New York Insurance Law. It is noted that a similar recommendation was included in the prior report on examination.	11
ii.	It is recommended that the Company comply with its established “EXPENSE ALLOCATION AMONG CORPORATIONS” agreement with respect to the use of allocation bases or amend its agreement to conform to how expenses are actually being allocated. In addition, it is recommended that the Company establish and maintain written documentation supporting the allocation of each expense category to the major expense groups as required by Department Regulation 30.	12
iii.	It is recommended that the Company comply with Section 1411(e) of the New York Insurance Law and ensure that no director or officer receive, in addition to their fixed salary or compensation, any money or valuable thing, directly or indirectly, for negotiating, procuring, recommending or aiding in any purchase or sale of property, made by such insurer or any affiliate or subsidiary thereof.	13
iv.	It is recommended that the Company comply with all written commitments made to this Department, henceforth.	14
v.	It is recommended that the Company continue to finalization the process of amending its custodial agreement to include all the provisions required by the New York Insurance Department and the NAIC Financial Condition Examiners Handbook.	14
vi.	It is recommended that the Company comply with the investment authorization requirements of Section 1411(a) of the New York Insurance Law.	15
vii.	It is recommended that the Company comply with SSAP No. 26 paragraph 2, SSAP No. 2 paragraph 3 as well as the Annual Statement Instructions and classify certificates of deposit that have a maturity date in excess of one year from the date of acquisition as bonds.	15

ITEMPAGE NO.

- viii. It is recommended that the Company adopt a resolution which incorporates the specific Department guidance provided in the body of the report relative to its arrangement with PayTrust. In addition, it is recommended that the board of directors ensure that the management of the Company has put into place adequate controls over this arrangement in order to adequately protect the assets of the Company. Evidence that the board has verified periodically, but no less frequently than annually, that the controls are operating properly must be maintained and provided for review upon examination.

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Respectfully submitted,

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Wayne Longmore  
Senior Insurance Examiner

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

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

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Wayne Longmore

Subscribed and sworn to before me

this \_\_\_\_\_ day of \_\_\_\_\_, 2010.

Appointment No 22539

STATE OF NEW YORK  
INSURANCE DEPARTMENT

I, HOWARD MILLS, Superintendent of Insurance of the State of New York,  
pursuant to the provisions of the Insurance Law, do hereby appoint:

Wayne Longmore

as proper person to examine into the affairs of the

**Fulmont 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 31st day of August 2006



A handwritten signature in black ink, appearing to read "Howard Mills", written over a horizontal line.

HOWARD MILLS  
Superintendent of Insurance