

REPORT ON EXAMINATION

OF THE

CHERRY VALLEY COOPERATIVE INSURANCE COMPANY

AS OF

DECEMBER 31, 2013

DATE OF REPORT

JANUARY 13, 2015

EXAMINER

WAYNE LONGMORE

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NEW YORK STATE
DEPARTMENT *of*
FINANCIAL SERVICES

Andrew M. Cuomo
Governor

Benjamin M. Lawsky
Superintendent

January 13, 2015

Honorable Benjamin M. Lawsky
Superintendent of Financial Services
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 31129 dated March 6, 2014 attached hereto, I have made an examination into the condition and affairs of Erie and Niagara Insurance Association as of December 31, 2013, and submit the following report thereon.

Wherever the designation “the Company” or “Cherry Valley” appears herein without qualification, it should be understood to indicate Cherry Valley Cooperative Insurance Company.

Wherever the term “Department” appears herein without qualification, it should be understood to mean the New York State Department of Financial Services.

The examination was conducted at the Company’s home office located at 8800 Sheridan Drive, Williamsville, NY 14221.

1. SCOPE OF EXAMINATION

The Department has performed an individual examination of the Company, a single-state insurer. The previous examination was conducted as of December 31, 2008. This examination covered the five-year period from January 1, 2009 through December 31, 2013. 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.

This examination report includes a summary of significant findings for the following items as called for in the Handbook:

- Significant subsequent events
- Company history
- Corporate records
- Management and control
- Fidelity bonds and other insurance
- Territory and plan of operation
- Growth of Company
- 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

The Company was organized on April 17, 1880, for the purpose of transacting business as an assessment cooperative fire insurance company in the Towns of Cherry Valley, Roseboom, and Westfield in Otsego County of New York State. In 1915, this Department permitted the Company to extend its territory to include Montgomery, Otsego and Schoharie Counties of this State.

By means of a charter amendment dated May 3, 1983, the Company changed its name to the Cherry Valley Cooperative Insurance Company and increased its territory to include all the counties of this state, excluding the counties of New York, Kings, Queens, Bronx and Richmond.

This charter amendment also authorized the Company to write those kinds of insurance specified in subsections (a), (b) and (c) of Section 6605 of the New York Insurance Law.

On April 1, 1985, the Company converted to an advance premium corporation. At the time of conversion, the Company became qualified to write non-assessable policies, extended its territorial limits to include the entire State of New York and, wherever authorized by law, any other state and the District of Columbia.

A. Management

Pursuant to the Company's charter, management of the Company is vested in a board of directors consisting of not less than seven members.

The board and executive committee meetings numbered at least four during each calendar year, thereby complying with Section 6624(b) of the New York Insurance Law.

At December 31, 2013, the board of directors was comprised of the following nine members:

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Gordon Paul Assad East Aurora, NY	Chairman of the Board and Chief Executive Officer, Cherry Valley Cooperative Insurance Company Director and Chief Executive Officer, Erie and Niagara Insurance Association Director/President/Chief Executive Officer, E&N Financial Services, Inc.
Donald Raymond Crosby Williamsville, NY	Vice President, The Notable Corporation
James Walter Fulmer LeRoy, NY	Chairman/President/CEO, Tompkins Financial Corp. Director, Erie and Niagara Insurance Association
Robert Harmon Lowe Geneseo, NY	Director and Executive Vice President, Erie and Niagara Insurance Association Director/ Vice President/ Secretary, E&N Financial Services, Inc.
John Alan Noble LeRoy, NY	President, Noblehurst Farms Chairman of the Board, Erie and Niagara Insurance Association
Norman J. Orlowski, Jr.* East Amherst, NY	President, Erie and Niagara Insurance Association Director/ Vice President/ Treasurer E&N Financial Services, Inc.
Linwood Dean Poelma East Amherst, NY	Vice President, M&T Bank Director, Erie and Niagara Insurance Association
Philip Stanley Sandler Williamsville, NY	Financial Planner, DBA Philip Stanley Sandler
Everett Gordon Yerdon Roseboom, NY	Farmer (Self Employed)

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 member had an acceptable record of attendance.

As of December 31, 2013, the principal officers of the Company were as follows:

<u>Name</u>	<u>Title</u>
Gordon Paul Assad*	Chairman of the Board Chief Executive Officer
Norman John Orlowski, Jr.*	President
Maureen Ann Mulcahy	Vice President/Secretary
Gina Marie Cartenuto	Vice President, Finance/Treasurer

* Effective February 12, 2014, Gordon Paul Assad retired from the Company. Norman John Orlowski, Jr. was made Chairman of the Board of Cherry Valley.

B. Territory and Plan of Operation

As of December 31, 2013, the Company was licensed to write business in New York State 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
12	Collision
13	Personal injury liability
14	Property damage liability
19	Motor vehicle and aircraft physical damage
20	Marine and inland marine (inland only)

The Company was also licensed as of December 31, 2013, to accept and cede reinsurance as provided in Section 6606 of the Insurance Law of the State of New York.

Based on 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, the Company is required to maintain a minimum surplus to policyholders in the amount of \$380,526.

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 Written Premiums</u>
2009	\$258,996
2010	\$259,573
2011	\$248,117
2012	\$235,619
2013	\$218,258

At December 31, 2013, the Company wrote insurance through one primary independent agent and through E&N Financial Services, Inc. the wholly owned subsidiary of Erie and Niagara Insurance Association (“Erie and Niagara”), an affiliate company.

The Company’s predominant lines of business are homeowners multiple peril, commercial multiple peril and other liability, which accounted for 14.59%, 20.44% and 64.58%, respectively, of the Company’s 2013 direct written business.

C. Reinsurance

Assumed

The Company assumed business during the examination period from its affiliate the Erie and Niagara Insurance Association (“Erie and Niagara” or “ENIA”). As of December 31, 2013, the property per risk excess of loss contract provided for the assumption, on the part of Cherry Valley from Erie and Niagara, of \$50,000 in excess of \$350,000 per risk, per occurrence. The business assumed from Erie and Niagara during 2013 amounted to approximately \$184,833 in 2013. The business assumed from ENIA is not reinsured.

Ceded

The Company has structured its ceded reinsurance program as of December 31, 2013 as follows:

Property 3 layers	\$2,985,000 excess of \$15,000 each risk, each loss. The first, second and third layers have a maximum reinsurer liability limit for all risks involved in each loss occurrence as follows: First -- \$1,155,000, Second--\$1,800,000 and Third--\$5,000,000.
100% Authorized	
Casualty 3 layers	\$2,985,000 excess of \$15,000 each loss occurrence. As respects umbrella liability policies the 95% quota share component, of the umbrella facultative policy inures to the benefit of the third layer of casualty coverage
100% Authorized	
Combined Property and Casualty	In the event of a loss occurrence involving at least one casualty and one property policy subject the contract, the reinsurer shall be liable in respect of each loss occurrence for the ultimate net loss over and above an initial ultimate net loss of \$15,000 each loss occurrence, subject to a limit of liability to the reinsurer of \$15,000 each loss occurrence.
100% Authorized	
Property Catastrophe Excess	\$200,000 excess of \$100,000 each loss occurrence
100% Authorized	
Umbrella Facultative	The Company shall cede and the reinsurer shall accept 95% share of up to \$1,000,000 of ultimate net loss, each occurrence, each policy. The reinsurer shall also be liable in respect of each loss occurrence, each policy, for the ultimate net loss over and above an initial ultimate net loss of \$1,000,000 each loss occurrence, each policy, subject to an additional limit of liability to the reinsurer of up to 100% of \$4,000,000 each loss occurrence, each policy. The liability of the reinsurer shall not exceed an annual aggregate of \$10,000,000 inclusive of loss adjustment expense, during the term of the contract for all acts of terrorism, as defined in the contract. This contract covers policies classified by the Company as personal, farm, and umbrella liability.
100% Authorized or certified	

The Company's largest net amount of risk is \$50,000 which relates to the business assumed from affiliate Erie and Niagara under the property per risk excess of loss contract. The business assumed from Erie and Niagara is not reinsured. Based on the reinsurance program in effect, the Company's largest net amount at risk on its direct business is \$15,000.

Since the date of the prior examination, December 31, 2008, the Company's net retention has remained unchanged at \$15,000 for both property business and casualty business.

All significant ceded reinsurance agreements in effect as of the examination date were reviewed. These contracts were 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 material reinsurance transactions. Additionally, management has represented that all material ceded reinsurance agreements transfer both underwriting and timing risk as set forth in SSAP No. 62R. Representations were supported by appropriate risk transfer analyses and an attestation from the Company's Chief Executive Officer and Chief Financial Officer. 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 SSAP No. 62R.

D. Holding Company System

As of December 31, 2013, the Company was affiliated with the Erie and Niagara Insurance Association, of Williamsville, New York by virtue of common officers, directors and management.

The two insurers entered into a service agreement, effective January 1, 2010, whereby ENIA provides specified services to Cherry Valley.

The agreement provides that expenses incurred and paid for by the ENIA, in the course of providing services under this agreement, are to be allocated between the two companies in a manner consistent with Department Regulation 30. ENIA will forward an itemized bill to Cherry Valley for its share of such allocated expenses quarterly and Cherry Valley shall pay each such bill within 30 days of

receipt. This Department issued a letter of non-objection relative to the implementation of the agreement on January 27, 2010.

The Company assumed business during the examination period from its affiliate, Erie and Niagara. See section 2(C) Reinsurance of this report for additional information.

E. Significant Operating Ratios

The following ratios have been computed as of December 31, 2013, based upon the results of this examination:

Net premiums written to policyholders' surplus	17%
Adjusted liabilities to liquid assets	8%
Gross agents' balances (in collection) to policyholders' surplus	0%

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	\$ 335,742	24.20%
Other underwriting expenses incurred	600,030	43.26
Net underwriting gain	<u>451,425</u>	<u>32.54</u>
Premiums earned	<u>\$1,387,197</u>	<u>100.00%</u>

F. Accounts and Records

i. Non-compliance with New York Insurance Law (“NYIL”) Section 6613(a)

Section 6613 (a) of the NYIL states:

"The expenses of management of any co-operative property/casualty insurance company shall not exceed in any one calendar year forty-two and one-half percent of its net premiums written for such year."

Review of the expenses for the five-year period under examination revealed that the Company exceeded the management expense limits in 2013.

It is recommended that the Company implement and/or follow its established procedures to ensure compliance with the management expense limitations set forth in Section 6613(a) of the NYIL.

ii. Non-compliance with New York Insurance Law (“NYIL”) Section 1409(a)

NYIL Section 1409(a) states that “Except as more specifically provided in this chapter, no domestic insurer shall have more than ten percent of its admitted assets as shown by its last statement on file with the superintendent invested in, or loaned upon, the securities (including for this purpose certificates of deposit, partnership interests and other equity interests) of any one institution.”

At December 31, 2013 the Company reported a Certificate of Deposit investment that was in excess of the limit established by the above-mentioned section of law. Given the immateriality of the excess, no change was made to the financials included in this report.

It is recommended that the Company comply with the requirements of Section 1409(a) of the New York Insurance Law by limiting investments in any one institution to ten percent of admitted assets.

3. FINANCIAL STATEMENTS

A Balance Sheet

The following shows the assets, liabilities and surplus as regards policyholders as of December 31, 2013 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	\$ 319,992	\$ 0	\$ 319,992
Cash, cash equivalents and short-term investments	1,322,381	0	1,322,381
Investment income due and accrued	795	0	795
Uncollected premiums and agents' balances in the course of collection	6,277	15	6,262
Deferred premiums, agents' balances and installments booked but deferred and not yet due	2,638	0	2,638
Equities and deposits in pools and associations	975	0	975
Finance Charges Receivable	<u>70</u>	<u>70</u>	<u>0</u>
Total assets	<u>\$1,653,128</u>	<u>\$ 85</u>	<u>\$ 1,653,043</u>

Liabilities, surplus and other funds

Liabilities

Losses and Loss Adjustment Expenses		\$ 48,800
Commissions payable, contingent commissions and other similar charges		3,913
Other expenses (excluding taxes, licenses and fees)		263
Taxes, licenses and fees (excluding federal and foreign income taxes)		340
Unearned premiums		42,292
Advance premium		8,174
Ceded reinsurance premiums payable (net of ceding commissions)		9,611
Amounts withheld or retained by company for account of others		(125)
Payable to parent, subsidiaries and affiliates		<u>16,284</u>
Total liabilities		\$ 129,552
Aggregate write-ins for special surplus funds	\$ 380,526	
Unassigned funds (surplus)	<u>1,142,965</u>	
Surplus as regards policyholders		<u>1,523,491</u>
Totals liabilities, surplus and other funds		<u>\$1,653,043</u>

NOTE: The Internal Revenue Service has not performed an audit of the Company's federal income tax returns for any tax year during the examination period. 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. Statement of Income

Premiums earned		\$1,387,197
Deductions:		
Losses and loss adjustment expenses incurred	\$335,742	
Other underwriting expenses incurred	<u>600,030</u>	
Total underwriting deductions		<u>935,772</u>
Net underwriting gain		\$ 451,425
<u>Investment Income</u>		
Net investment income earned		\$ 32,123
<u>Other Income</u>		
Net gain or (loss) from agents' or premium balances charged off	\$ (1,321)	
Finance and service charges not included in premiums	<u>10,840</u>	
Total other income		<u>9,519</u>
Net income before federal and foreign income taxes		\$ 493,067
Federal and foreign income taxes incurred		<u>0</u>
Net Income		\$ <u>493,067</u>

C. Capital and Surplus Account

Surplus as regards policyholders increased \$492,982 during the five-year examination period January 1, 2009 through December 31, 2013, detailed as follows:

<u>Surplus as regards policyholders per report on examination as of December 31, 2008</u>				\$1,030,509
	<u>Gains in Surplus</u>	<u>Losses in Surplus</u>		
Net income	\$493,067	\$ 0		
Change in nonadmitted assets	<u>0</u>	<u>85</u>		
Net increase (decrease) in surplus	<u>\$493,067</u>	<u>\$85</u>		<u>\$492,982</u>
<u>Surplus as regards policyholders per report on examination as of December 31, 2013</u>				<u>\$1,523,491</u>

4. LOSSES AND LOSS ADJUSTMENT EXPENSES

The examination liability for the captioned items of \$48,800 is the same as reported by the Company as of December 31, 2013. 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.

5. COMPLIANCE WITH PRIOR REPORT ON EXAMINATION

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

<u>ITEM</u>	<u>PAGE NO.</u>
A. <u>Management</u> It is recommended that the Company exercise due care in obtaining, verifying for accuracy and completeness, and maintaining signed conflict of interest questionnaires from its board of directors, officers and key employees. The Company has complied with this recommendation.	5
B. <u>Market Conduct Activities</u>	
i. It is recommended that the Company comply with the requirements of Section 3425(e) of the New York Insurance Law and not non-renew personal lines policies midterm for other than the statutory reasons put forth in Section 3425(c)(2) of the New York Insurance Law. It is noted that a similar recommendation regarding compliance with Section 3425(e) of the New York Insurance Law was included in the two prior reports. The Company has complied with this recommendation.	15
ii. It is recommended that the Company comply with the requirements of Section 3425(d)(1) of the New York Insurance Law, henceforth. The Company has substantively complied with this recommendation.	17
iii. It is recommended that the Company comply fully with the review requirements of Department Regulation 129 Part 161.7(c) and thoroughly review the rates being charged for consistency with the rates in effect and make any necessary three (3) year update filings as opposed to just filing a statement that no updating is appropriate. The Company has complied with this recommendation.	17
iv. It is recommended that the Company comply with Section 2314 of the New York Insurance Law by charging rates that do not depart from the rates, rating plans, classifications, schedules, rules and standards it has in effect. It is noted that this is a repeat recommendation. The Company has complied with this recommendation.	17

- v. It is recommended that the Company comply with Department Regulation 57 Part 160.2(g) and implement additional periodic testing procedures to further minimize the occurrence of improperly charged rates as opposed to mainly testing at the inception of rate changes. 17

The Company has complied with this recommendation.

6. SUMMARY OF COMMENTS AND RECOMMENDATIONS

<u>ITEM</u>		<u>PAGE NO.</u>
A.	<u>Accounts and Records</u>	
i.	It is recommended that the Company implement and/ or follow its established procedures to ensure compliance with Section 6613(a) of the NYIL in the future.	10
ii.	It is recommended that the Company comply with the requirements of Section 1409(a) of the New York Insurance Law by limiting investments in any one institution to ten percent of admitted assets.	10

NEW YORK STATE

DEPARTMENT OF FINANCIAL SERVICES

I, **BENJAMIN M. LAWSKY**, Superintendent of Financial Services of the State of New York, pursuant to the provisions of the Financial Services Law and the Insurance Law, do hereby appoint:

Wayne Longmore

as a proper person to examine the affairs of the

Cherry Valley Cooperative Insurance Company

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

COMPANY

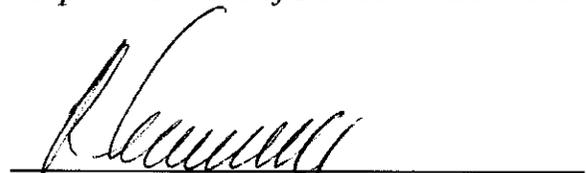
with such other information as he shall deem requisite.

In Witness Whereof, I have hereunto subscribed by name
and affixed the official Seal of the Department
at the City of New York

this 6th day of March, 2014

BENJAMIN M. LAWSKY
Superintendent of Financial Services

By:



Rolf Kaumann
Deputy Chief Examiner

