

REPORT ON EXAMINATION

OF

OTSEGO MUTUAL FIRE INSURANCE COMPANY

AS OF

DECEMBER 31, 2017

DATE OF REPORT

FEBRUARY 13, 2019

EXAMINER

WAYNE LONGMORE

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Department of Financial Services

ANDREW M. CUOMO
Governor

LINDA A. LACEWELL
Superintendent

August 2, 2019

Honorable Linda A. Lacewell
Superintendent
Department of Financial Services
Albany, New York 12257

Madam:

Pursuant to the requirements of the New York Insurance Law, and in compliance with the instructions contained in Appointment Number 31813 dated September 4, 2018, attached hereto, I have made an examination into the condition and affairs of Otsego Mutual Fire Insurance Company as of December 31, 2017, and submit the following report thereon.

Wherever the designation “the Company” appears herein, without qualification, it should be understood to indicate Otsego Mutual Fire 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 143 Arnold Road, Burlington Flats, New York 13315.

1. SCOPE OF EXAMINATION

The Department has performed an examination of the Company, a single-state insurer. The previous examination was conducted as of December 31, 2012. This examination covered the five-year period from January 1, 2013 through December 31, 2017. 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 current and 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 New York laws, statutory accounting principles and annual statement instructions.

This examination report includes, but is not limited to, the following:

- Company history
- Management and control
- Territory and plan of operation
- Holding company description
- Reinsurance
- Loss review and analysis
- Financial statement presentation
- Summary of recommendations

A review was also made to ascertain what action was taken by the Company regarding 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

Otsego Mutual Fire Insurance Company was incorporated on March 10, 1897, under the laws of the State of New York, and commenced business on April 1, 1897.

On December 29, 1942 the Company merged with Chemical Mutual Fire Insurance Company and Otsego Mutual Fire Insurance Company was the surviving company. On this date the corporate powers were amended to permit the Company to do business in the entire State of New York in accordance with the provisions of Section 367 of the New York Insurance Law, and wherever authorized by law, in any other state of the United States of America or the District of Columbia.

On June 12, 1943, the Company was authorized to issue non-assessable policies.

A. Corporate Governance

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 eleven members. Two board meetings and two executive committee meetings were held each year of the examination period, thereby complying with Section 6624(b) of the New York Insurance Law. At December 31, 2017, the board of directors was comprised of the following eleven members:

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Deanne Payne Burke New Hartford, NY	Retired
Denise Julianna Clark Slingerlands, NY	Associate Vice President for Research Administration, University of Maryland
Kelley Burke Cough Sauquoit, NY	President, Otsego Mutual Fire Insurance Company
Kevin Scott Cough New Hartford, NY	Vice President, Otsego Mutual Fire Insurance Company
Terry Michael Gras West Winfield, NY	Corporate Secretary, Otsego Mutual Fire Insurance Company
Judith Burke Hamilton New Hartford, NY	Assistant Secretary & Data Processing Manager, Otsego Mutual Fire Insurance Company

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
John Hyland Hemmel New Hartford, NY	Executive Director, Health Friends
Dion Alan Howard Edmeston, NY	Proprietor, Howard's Trailer Sales
Timothy Richard Johnson, Esq. Edmeston, NY	Chief Executive Officer, Otsego Electric Cooperative Inc.
Francis Kearn Peo West Winfield, NY	Retired
Cynthia Ann Woody Ilion, NY	Manager of Human Resources, Commercial Travelers Insurance Company

As of December 31, 2017, the principal officers of the Company were as follows:

<u>Name</u>	<u>Title</u>
Kelley Burke Cough	President
Terry Michael Gras	Corporate Secretary
Gregory Michael Gaeta	Treasurer
Kevin Scott Cough	Vice President
Judith Burke Hamilton	Assistant Secretary

B. Territory and Plan of Operation

As of December 31, 2017, 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
19	Motor vehicle and aircraft physical damage
20	Marine and inland marine (inland marine only)

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, the Company is required to maintain a minimum surplus to policyholders in the amount of \$559,386.

The following schedule shows the direct and assumed premiums written by the Company for the period under examination:

<u>Calendar Year</u>	<u>Direct Premiums</u>	<u>Assumed Premiums</u>	<u>Total Gross Premiums</u>
2013	\$16,613,872	\$170,815	\$16,784,687
2014	\$17,372,360	\$174,514	\$17,546,874
2015	\$17,608,967	\$174,531	\$17,783,498
2016	\$18,289,541	\$175,609	\$18,465,150
2017	\$18,781,557	\$184,793	\$18,966,350

The Company's predominant lines of business are homeowners multiple peril and fire, which accounted for 88% and 6%, respectively of the 2017 direct written premiums. The Company markets its business through approximately ninety agents throughout New York. Within the agency force, there are approximately twenty wholesalers that utilize a network of brokers mainly throughout the New York City metropolitan area.

Due to the large reinsurance program (described in Section 2C of this report) the net exposure of the Company is significantly different than its direct and assumed exposure.

The Company's assumed premiums represent the Company's participation in the voluntary Regional Reciprocal Catastrophe Pool.

C. Reinsurance Ceded

As of December 31, 2017, the Company had the following ceded reinsurance program in place:

<u>Type of Treaty</u>	<u>Cession</u>
<u>All lines Quota Share Property and Casualty</u> 60% Authorized	50% of the business covered by the agreement after deducting all other reinsurance inuring to the benefit of the agreement, subject to a maximum ultimate net loss of \$60,000 each loss and a per occurrence limit of \$10,000,000. Terrorism coverage is limited to \$5,000,000 in aggregate during any profit period.

Type of Treaty

Facultative First Surplus Property
60% Authorized

Cession

Net retention of at least \$5,000 (after 50% quota share) on each risk. The reinsurer will automatically be liable on a pro-rata basis subject to a maximum limit of \$500,000 any one risk and \$22,100,000 per occurrence. Terrorism coverage is limited to \$7,375,000 in aggregate during any profit period.

Property Per Risk Excess of Loss
60% Authorized

\$440,000 excess \$60,000 each risk (or any one location as respects Inland Marine), each loss occurrence subject to an occurrence limit of \$1,320,000.

The Company shall retain net and unreinsured, in addition to the above, an annual aggregate retention equal to 2% of the subject net premium as defined in the agreement each contract year.

Casualty Excess of Loss
60% Authorized

\$440,000 excess \$60,000 per occurrence.

Property Catastrophe Excess of Loss
(3 Layers) 60% Authorized

Layers 1 and 2

50% of \$12,000,000 excess \$3,500,000 ultimate net loss, each occurrence, not to exceed \$4,000,000 or \$8,000,000 for layers 1 and 2 respectively, with respect to all occurrences during the term of the agreement.

Layer 3

\$10,500,000 excess \$15,500,000 ultimate net loss, each occurrence, not to exceed \$21,000,000 with respect to all occurrences during the term of the agreement.

The Company ceded to authorized and unauthorized reinsurers during the period under examination. It is the Company's policy to obtain the appropriate collateral, where required, for its cessions to unauthorized reinsurers. Letters of credit obtained by the Company to take credit for cessions to unauthorized reinsurers were reviewed for compliance with Department Regulation 133 and no exceptions were noted.

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

Examination review found that the Schedule F data reported by the Company in its filed annual statement accurately reflected its 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 an attestation from the Company's President and Treasurer. 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 the NAIC Accounting Practices and Procedures Manual, Statement of Statutory Accounting Principle ("SSAP") No. 62R.

D. Holding Company System

As of December 31, 2017, the Company was not a member of any holding company system.

E. Significant Ratios

The Company's operating ratios, computed as of December 31, 2017, fall within the benchmark ranges set forth in the Insurance Regulatory Information System of the National Association of Insurance Commissioners.

<u>Operating ratios</u>	<u>Result</u>
Net premiums written to policyholders' surplus	4%
Adjusted liabilities to liquid assets	12%
Two-year overall operating	3%

Underwriting Ratios

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	\$ 9,952,013	44.42%
Other underwriting expenses incurred	1,735,244	7.75
Net underwriting gain	<u>10,716,378</u>	<u>47.83</u>
Premiums earned	<u>\$22,403,635</u>	<u>100.00%</u>

The Company's reported risk-based capital score ("RBC") was 1,499.6% as of December 31, 2017. The RBC is a measure of the minimum amount of capital appropriate for a reporting entity to support its overall business operations in consideration of its size and risk profile. An RBC of 200 or below can result in regulatory action. There were no financial adjustments in this report that impacted the Company's RBC score.

3. FINANCIAL STATEMENTS

A. Balance Sheet

The following shows the assets, liabilities and surplus as regards policyholders as of December 31, 2017 as reported by the Company.

<u>Assets</u>	<u>Assets</u>	<u>Assets Not Admitted</u>	<u>Net Admitted Assets</u>
Bonds	\$ 66,477,719		\$ 66,477,719
Preferred stocks (stocks)	1,085,568		1,085,568
Common stocks (stocks)	53,259,206		53,259,206
Properties occupied by the company	421,342		421,342
Cash, cash equivalents and short-term investments	4,886,283		4,886,283
Investment income due and accrued	538,499		538,499
Uncollected premiums and agents' balances in the course of collection	997,915	\$ 7,730	990,185
Deferred premiums, agents' balances and installments booked but deferred and not yet due	354,945		354,945
Accrued retrospective premiums	38,923		38,923
Amounts recoverable from reinsurers	130,128		130,128
Current federal and foreign income tax recoverable and interest thereon	180,834		180,834
Electronic data processing equipment and software	42,735		42,735
Furniture and equipment, including health care delivery assets	203,226	203,226	0
Cash value life insurance	3,344,832		3,344,832
Prepaid pension asset	3,289,248	3,289,248	
Overfunded plan asset	(3,289,248)	(3,289,248)	
Pools and associations	<u>45,017</u>	<u>0</u>	<u>45,017</u>
Total assets	<u>\$132,007,172</u>	<u>\$ 210,956</u>	<u>\$131,796,216</u>

Liabilities, surplus and other fundsLiabilities

Losses and loss adjustment expenses	\$ 2,310,647
Commissions payable, contingent commissions and other similar charges	(709,129)
Other expenses (excluding taxes, licenses and fees)	469,484
Taxes, licenses and fees (excluding federal and foreign income taxes)	121,363
Net deferred tax liability	5,561,514
Unearned premiums	2,970,024
Advance premium	208,705
Ceded reinsurance premiums payable (net of ceding commissions)	1,362,434
Amounts withheld or retained by company for account of others	2
Provision for supplemental executive retirement plan (SERP)	1,510,250
Liability for plan benefits	<u>1,172,033</u>
Total liabilities	\$ 14,977,327

Surplus and Other Funds

Special contingent surplus	\$ 559,386
Unassigned funds (surplus)	<u>116,259,503</u>
Surplus as regards policyholders	<u>116,818,889</u>
Total liabilities, surplus and other funds	<u>\$131,796,216</u>

NOTE: The Internal Revenue Service did not audit any of the Company's federal income tax returns during the period under examination. 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

The net income for the examination period as reported by the Company was \$26,264,803 as detailed below:

Underwriting Income

Premiums earned		\$22,403,635
Deductions:		
Losses and loss adjustment expenses incurred	\$ 9,952,013	
Other underwriting expenses incurred	<u>1,735,244</u>	
Total underwriting deductions		<u>11,687,257</u>
Net underwriting gain or (loss)		\$10,716,378

Investment Income

Net investment income earned	\$11,428,634	
Net realized capital gain	<u>7,671,476</u>	
Net investment gain or (loss)		19,100,110

Other Income

Net gain or (loss) from agents' or premium balances charged off	\$ (43,807)	
Finance and service charges not included in premiums	128,192	
Life insurance on employees	624,358	
NAMICO Reinsurance Pool	(3,412)	
NY FAIR Plan	(334,264)	
Income from other sources	5,513	
Gain on sale of equipment	<u>514</u>	
Total other income		<u>377,094</u>
Net income before federal income taxes		\$30,193,582
Federal income taxes incurred		<u>3,928,779</u>
Net income		<u>\$26,264,803</u>

C. Capital and Surplus Account

Surplus as regards policyholders increased \$37,851,024 during the five-year examination period January 1, 2013 through December 31, 2017 as reported by the Company, detailed as follows:

Surplus as regards policyholders as reported by the Company as of December 31, 2012				\$78,967,865
	<u>Gains in Surplus</u>	<u>Losses in Surplus</u>		
Net income	\$26,264,803			
Net unrealized capital gains or (losses)	11,908,004			
Change in net deferred income tax	2,548,477			
Change in non-admitted assets		\$ 18,267		
SSAP102 Transition Liability		976,695		
Provision for SERPS		212,475		
Change in non-admitted overfunded plan asset	<u>0</u>	<u>1,662,823</u>		
Net increase (decrease) in surplus	<u>\$40,721,284</u>	<u>\$2,870,260</u>		<u>37,851,024</u>
Surplus as regards policyholders as reported by the Company as of December 31, 2017				<u>\$116,818,889</u>

No adjustments were made to surplus as a result of this examination.

4. LOSSES AND LOSS ADJUSTMENT EXPENSES

The examination liability for the captioned items of \$2,310,647 is the same as reported by the Company as of December 31, 2017. The examination analysis of the loss and loss adjustment expense reserves was conducted in accordance with generally accepted actuarial principles and statutory accounting principles, including SSAP No. 55.

The reported reserves are concentrated in the homeowners' multiple peril line, which is consistent with the business written by the Company.

5. COMPLIANCE WITH PRIOR REPORT ON EXAMINATION

The prior report on examination contained the following five recommendations (page numbers refer to the prior report):

<u>ITEM</u>	<u>PAGE NO.</u>
A. <u>Management</u> It was recommended that board members who are unable or unwilling to attend meetings consistently should resign or be replaced.	4
The Company has complied with this recommendation.	
B. <u>Reinsurance</u> It was recommended that the Company review and update its letters of credit to ensure that all current and any future letters of credit are in compliance with the requirements of 11 NYCRR 79.2 (Department Regulation 133).	8
The Company has complied with this recommendation.	
C. <u>Accounts and Records</u>	
i. It was recommended that the Company ensure that future agreements with its CPA are in compliance with the requirements of Department Regulation 118.	10
The Company has complied with this recommendation.	
ii. It was recommended that the Company prepare an Actuarial Report underlying the Statement of Actuarial Opinion, on an annual basis, pursuant to the NAIC Annual Statement Instructions and ASOP #41.	11
The Company has complied with this recommendation.	
iii. It was again recommended that the Company strengthen its internal controls by segregating the functions of checking account reconciliation and check writing.	11
The Company has complied with this recommendation.	

6. **SUMMARY OF COMMENTS AND RECOMMENDATIONS**

This report on examination contains no comments or recommendations.

Respectfully submitted,

_____/S/
Wayne Longmore
Associate Insurance Examiner

STATE OF NEW YORK)
)ss:
COUNTY OF OTSEGO)

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.

_____/S/
Wayne Longmore

Subscribed and sworn to before me

this _____ day of _____, 2019.

APPOINTMENT NO. 31813

NEW YORK STATE
DEPARTMENT OF FINANCIAL SERVICES

I, Maria T. Vullo, 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

Otsego Mutual Fire 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 4th day of September, 2018

MARIA T. VULLO
Superintendent of Financial Services



By:

Joan P. Riddell

Joan Riddell
Deputy Bureau Chief