<u>REPORT ON EXAMINATION</u>

<u>OF THE</u>

<u>SAUQUOIT VALLEY INSURANCE COMPANY</u>

<u>AS OF</u>

<u>DECEMBER 31, 2006</u>

<u>DATE OF REPORT</u>	<u>JUNE 22, 2007</u>
<u>EXAMINER</u>	<u>FRANK P. SCHIRALDI</u>

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

June 22, 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 22598 dated February 23, 2007 attached hereto, I have made an examination into the condition and affairs of the Sauquoit Valley Insurance Company as of December 31, 2006, and submit the following report thereon.

The examination was conducted at the Company’s home office located at 10170 Roberts Road, Sauquoit, NY 13456.

Wherever the designations “the Company” or “SVIC” appear herein without qualification, they should be understood to indicate the Sauquoit Valley Insurance Company.

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

1. SCOPE OF EXAMINATION

The previous examination was conducted as of December 31, 2001. This examination covered the five-year period from January 1, 2002 through December 31, 2006. Transactions occurring subsequent to this period were reviewed where deemed appropriate by the examiner. The examination comprised a verification of assets and liabilities as of December 31, 2006, a review of income, disbursements and Company records deemed necessary to accomplish such analysis or verification and utilized, to the extent considered appropriate, the work of the Company's independent certified public accountants. A review or audit was also made of the following items as called for in the Examiners Handbook of the National Association of Insurance Commissioners:

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

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, which involve departures from laws, regulations or rules, or which are deemed to require explanation or description.

2. DESCRIPTION OF COMPANY

The Sauquoit Valley Insurance Company was incorporated under the laws of the State of New York on February 21, 1878 for the purpose of transacting business as an assessment co-operative fire insurance company in Herkimer and Oneida Counties of New York State. The territorial limits were extended on January 1, 1987 to cover all the counties in New York State excluding the counties of New York, Kings, Queens, Bronx and Richmond. The writing authority of the Company was also expanded from writing only fire coverage to the writing powers currently authorized and outlined under item 2(B), "Territory and Plan of Operation", in this report.

A. Management

Pursuant to the Company's charter and by-laws, management of the Company was vested in a board of directors consisting of not less than nine nor more than twelve members at December 31, 2006. The board met four times during each calendar year during the examination period. As of December 31, 2006, the board of directors was comprised of nine members, divided into three equal groups, with one group being elected at each annual policyholders' meeting for a term of three years.

At December 31, 2006, the board of directors was comprised of the following nine members:

Name and Residence	Principal Business Affiliation
Homer Casler West Winfield, NY	Vice-President, Sauquoit Valley Insurance Company
Dale Champion Deansboro, NY	Retired
Nicholas Crescenzo Utica, NY	Retired
Gordon Donahoe Frankfort, NY	Retired
Alfred Eisenhut Deansboro, NY	Retired
Scott T. Jeffers Oriskany Falls, NY	President Sauquoit Valley Insurance Company
Sharon K. Linder Sauquoit, NY	Secretary-Treasurer Sauquoit Valley Insurance Company
Melville Merry Frankfort, NY	Retired
Max Townsend Cassville, NY	Chairman of the Board Sauquoit Valley Insurance Company

A review of the minutes of the board of directors' meetings held during the examination period indicated that the meetings were generally well attended and each board member had an acceptable record of attendance.

As of December 31, 2006, the principal officers of the Company were as follows:

Name	Title
Max Townsend	Chairman of the Board
Scott T. Jeffers	President
Homer Casler	Vice-President
Sharon K. Linder	Secretary-Treasurer

B. Territory and Plan of Operation

As of December 31, 2006, the Company was only licensed to write business in New York State, in all counties except the counties of Kings, Queens, New York, Bronx and Richmond.

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:

Paragraph	Line of Business
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 employer's liability (excluding workers' compensation)
19	Motor vehicle and aircraft physical damage (excluding aircraft physical damage)
20	Marine and inland marine (inland marine only)

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

Calendar Year	Direct Premiums Written(000)
2002	$1,063
2003	1,087
2004	1,056
2005	1,060
2006	1,045

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

The Company underwrites predominantly farmowners' multiple peril and homeowners' multiple peril lines of business, which accounted for 35.7% and 42.2%, respectively, of the 2006 net premium writings.

C. Reinsurance

The Company did not assume any reinsurance during the examination period.

The Company has structured its ceded reinsurance program to limit its maximum exposure to any one risk as follows:

- Property Lines – First layer excess of loss reinsurance above $35,000 up to $100,000 is maintained on all lines with a property occurrence limit of $195,000. Second layer excess of loss reinsurance above $100,000 up to $500,000 is maintained for all lines with a property occurrence limit of $800,000. The Company also has an excess of loss catastrophe cover above $100,000 up to $1,000,000 (95% cover) and 100% cover for amounts over $1,000,000.

- Facultative property coverage is maintained for all limits in excess of $500,000. Cessions to this contract are limited to an amount equal to four times the Company's net retention, subject to a minimum net retention of $200,000 and to a maximum cession of $750,000 on any one risk covered. Risks where cession value exceeds $750,000 are underwritten on an offer and accept basis.

- Casualty Lines – Excess of loss reinsurance above $25,000 up to $500,000 is maintained on all casualty lines.

- Facultative casualty coverage is available for amounts over $500,000 up to $1,000,000.

- The Company also maintains aggregate excess of loss reinsurance for 95% of the ultimate net loss in excess of initial ultimate net loss equal to 94% of gross net earned premium income subject to a limit of liability to the reinsurer of $465,000 (95% of $500,000) aggregate net losses any one contract year.

With the exception of one unauthorized reinsurer that participated on the Company's Combination Excess of Loss reinsurance contract for the period of July 1, 2003 through June 30, 2004, the Company ceded reinsurance only to authorized/accredited reinsurers during the examination period. Pursuant to Section 6606(a)(2) of the New York Insurance Law ("NYIL"), "unless otherwise permitted by the superintendent, an assessment corporation may assume reinsurance only from other authorized assessment corporations but may cede reinsurance to any other licensed insurer if such insurer is authorized to reinsure such kind or kinds of insurance in this state or to an accredited reinsurer." Accordingly it is recommended that the Company comply with Section 6606(a)(2) of the NYIL and only cede reinsurance to an authorized/accredited reinsurer.

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 filed annual statement was found to accurately reflect the dollar amounts for its reinsurance transactions, however, it was noted that the Company did not report all reinsurers participating on its reinsurance program in the Schedule F, Part 3 of filed annual statement at December 31, 2006. It is recommended that the Company comply with the annual statement instructions and include all required information in the Schedule F, Part 3 in all future statements filed with this Department.

Additionally, management has represented that all material ceded reinsurance agreements transfer both underwriting and timing risk as set forth in SSAP No. 62. Representations were supported by appropriate risk transfer analyses and an attestation from the Company's President and Treasurer pursuant to the NAIC Annual Statement Instructions. 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 paragraphs 17 through 33 of SSAP No. 62.

D. Holding Company System

As of December 31, 2006, the Company was not a member of any holding company system. The Company was independent with no affiliation or pooling agreements in force at December 31, 2006.

E. Significant Operating Ratios

The following ratios have been computed as of December 31, 2006, based upon the results of this examination:

Net premiums written to surplus as regards policyholders	24%
Liabilities to liquid assets (cash and invested assets less investments in affiliates)	19%
Premiums in course of collection to surplus as regards policyholders	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:

	Amounts	Ratios
Losses and loss adjustment expenses incurred	$2,679,745	72.40%
Other underwriting expenses incurred	1,296,910	35.03%
Net underwriting loss	(275,187)	(7.43%)
Premiums earned	$3,701,468	100.00%

F. Accounts and Records

A review of the Company's accounts, records and annual statement reporting revealed the following:

1. Limitation of expenses

Pursuant to Section 6613 of the NYIL, "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..." The Company's management expenses for 2006 were 42.71% of its net premium written in 2006.

It is recommended that the Company comply with Section 6613 of the NYIL and bring its expenses of management in line with the statutory limit.

2. Allocation of expenses

The Company allocated expenses for each expense category in the Underwriting and Expense Exhibit, Part 3 – Expenses, lines 8 through 18 as follows: 30% to Loss Adjustment Expenses, 60% to Other Underwriting Expenses, and 10% to Investment Expenses. The percentages used by the Company did not change during the examination period. Further, the Company was unable to provide support for the basis of allocation using these percentages.

SSAP No. 70 requires that allocation to these categories "…should be based on a method that yields the most accurate results…where specific identification is not feasible allocation of expenses should be based upon pertinent factors or ratios as studies of employee activities, salary ratios or similar analysis."

It is recommended that management establish and maintain written documentation supporting the allocation of each expense category to the major expense groups as required by SSAP No. 70.

3. Complaint Log

Department Circular Letter No. 11 (1978) requires that companies maintain a log of all complaints received. The Company kept a complaint log during the examination period, but this log did not contain all of the information required by Circular Letter No. 11 (1978).

It is recommended that the Company maintain a complaint log that contains all of the information required by Circular Letter No. 11 (1978).

Subsequent to the examination date, but before completion of the field work, the Company revised its complaint log to comply with Circular Letter No. 11 (1978).

4. Limitation of Investments

Section 1409(a) of the NYIL states, in part, that "…no insurer shall have more than ten percent of its admitted assets…invested in, or loaned upon, the securities…of any one institution." As of the examination date, the Company held investments in certain institutions in excess of ten percent of its admitted assets at December 31, 2006; specifically, the investment in PIMCO NY Mutual Bond Fund, and the combined Vanguard investments.

It is recommended that the Company comply with Section 1409(a) of the NYIL and limit its investments in any one institution to ten percent of its admitted assets.

3. FINANCIAL STATEMENTS

A Balance Sheet

The following shows the assets, liabilities and surplus as regards policyholders as determined by this examination of December 31, 2006. This statement is the same as the balance sheet filed by the Company:

Assets	Assets	Assets Not Admitted	Net Admitted Assets
Bonds	$1,011,626	$ 0	$1,011,626
Common stocks	2,243,531	0	2,243,531
Properties occupied by the Company	59,117	0	59,117
Cash, cash equivalents and short-term investments	355,097	0	355,097
Other invested assets	12,000	12,000	0
Investment income due and accrued	20,973	0	20,973
Uncollected premiums and agents' balances in the course of collection	10,733	1,140	9,593
Deferred premiums, agents' balances and installments booked but deferred and not yet due	153,374	0	153,374
Amounts recoverable from reinsurers	23,645	0	23,645
Current federal and foreign income tax recoverable and interest thereon	15,560	0	15,560
Furniture and equipment	33,924	33,924	0
Totals	$3,939,580	$47,064	$3,892,516

Liabilities, surplus and other funds

Losses and Loss adjustment expenses	$ 223,372
Other expenses (excluding taxes, licenses and fees)	8,405
Net deferred tax liability	45,000
Unearned premiums	522,927
Advance premiums	21,258
Ceded reinsurance premiums payable (net of ceding commissions)	27,065
Total liabilities	$ 848,027
Required surplus	100,000
Unassigned funds (surplus)	2,944,489
Surplus as regards policyholders	$3,044,489
Totals	$3,892,516

Note: The Internal Revenue Service did not audit the Company's federal income tax returns during the period under examination. Audits covering subsequent tax years have yet to commence. Except for any impact that might result from any examination changes contained in this report, the examiner is unaware of any potential exposure to 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 $264,175 during the five-year examination period January 1, 2002 through December 31, 2006, detailed as follows:

Underwriting Income		
Premiums earned		$3,701,468
Deductions:		
Losses incurred	$1,930,759	
Loss adjustment expenses incurred	748,986	
Other underwriting expenses incurred	1,296,910	
Total underwriting deductions		3,976,655
Net underwriting gain or (loss)		$ (275,187)
Investment Income		
Net investment income earned	$351,203	
Net realized capital gain	68,507	
Net investment gain or (loss)		419,710
Other Income		
Net gain or (loss) from agents' or premium balances charged off	$(6,561)	
Finance and service charges not included in premiums	34,335	
Aggregate write-ins for miscellaneous income	11,007	
Total other income		38,781
Net income before dividends to policyholders and before federal and foreign income taxes		$ 183,304
Dividends to policyholders		0
Net income after dividends to policyholders but before federal and foreign income taxes		$ 183,304
Federal and foreign income taxes incurred		66,942
Net Income		$ 116,362

	Gains in Surplus	Losses in Surplus	
Surplus as regards policyholders per report on examination as of December 31, 2001			$2,780,314
Net income	$116,362	$ 0	
Change in net unrealized capital gains	161,943	0	
Change in net deferred income tax	0	5,000	
Change in nonadmitted assets	0	9,130	
Net increase (decrease) in surplus	$278,305	$14,130	264,175
Surplus as regards policyholders per report on examination as of December 31, 2006			$3,044,489

4. LOSSES AND LOSS ADJUSTMENT EXPENSES

The examination liability for the captioned items of $223,372 is the same as reported by the Company as of December 31, 2006. 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. 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.

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

ITEM		PAGE NO.
A	It was recommended that the Company comply with Section 1212(a) of the Insurance Law and file a new Certificate of Designation by Insurer naming a current employee as the proper contact person. The Company has complied with this recommendation.	8
B	It was recommended that the Company follow the annual statement instructions and fill out Schedule P – Part 5 completely, so that accurate claim count numbers may be used in the calculation of loss and loss adjustment reserves. The Company has complied with this recommendation.	8
C	It was recommended that the Company comply with both the minimum retention and coinsurance percentage required by Regulation 110 (NYCRR Part 72.4) The Company has complied with this recommendation.	8
D	It was recommended that the Company comply with the provisions of the New York Standard Mortgagee Clause, henceforth, when cancelling such policies containing same. The Company has complied with this recommendation.	12
E	It was recommended that the Company comply with Regulation 64 (NYCRR Part 216.11) by organizing claim files in a manner that will enable Department personnel to reconstruct the reserving events in a more efficient way. The Company has complied with this recommendation.	12

7. SUMMARY OF COMMENTS AND RECOMMENDATIONS

ITEM			PAGE NO.
A.	Reinsurance		
	i.	It is recommended that the Company comply with Section 6606(a)(2) of the NYIL and only cede reinsurance to an authorized/accredited reinsurer.	6
	ii.	It is recommended that the Company comply with the annual statement instructions and include all required information in the Schedule F, Part 3 in all future statements filed with this Department.	6
B.	Accounts and Records		
	i.	It is recommended that the Company comply with Section 6613 of the NYIL and bring its expenses of management in line with the statutory limit.	8
	ii.	It is recommended that management establish and maintain written documentation supporting the allocation of each expense category to the major expense groups as required by SSAP No. 70.	8
	iii.	It is recommended that the Company maintain a complaint log that contains all of the information required by Department Circular Letter No. 11 (1978). Subsequent to the examination date, but before completion of the field work, the Company revised its complaint log to comply with Circular Letter No. 11 (1978).	9
	iv.	It is recommended that the Company comply with Section 1409(a) of the NYIL and limit its investments in any one institution to ten percent of its admitted assets.	9

Respectfully submitted,

____________/S/____________
Frank P. Schiraldi
Senior Insurance Examiner

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

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

____________/S/____________
Frank P. Schiraldi

Subscribed and sworn to before me

this__________ day of ____________________, 2008.

Appointment No 22598

STATE OF NEW YORK
INSURANCE DEPARTMENT

I, **Eric R. Dinallo,** *Acting Superintendent of Insurance of the State of New York, pursuant to the provisions of the Insurance Law, do hereby appoint:*

Frank Schiraldi

as proper person to examine into the affairs of the

Sauquoit Valley 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 23rd *day of February 2007*

Eric R. Dinallo
Acting Superintendent of Insurance