

REPORT ON EXAMINATION

OF THE

LEATHERSTOCKING COOPERATIVE INSURANCE COMPANY

AS OF

DECEMBER 31, 2011

DATE OF REPORT
EXAMINER

MAY 24, 2013
SUSAN K. WEIJOLA

TABLE OF CONTENTS

<u>ITEM NO.</u>		<u>PAGE NO.</u>
1	Scope of examination	2
2.	Description of Company	3
	A. Management	3
	B. Territory and plan of operation	4
	C. Reinsurance	5
	D. Holding company system	7
	E. Significant operating ratios	7
	F. Risk management and internal controls	7
3.	Financial Statements	9
	A. Balance sheet	9
	B. Statement of income	10
4.	Losses and loss adjustment expenses	11
5.	Compliance with prior report on examination	12
6.	Summary of comments and recommendations	13



NEW YORK STATE
DEPARTMENT *of*
FINANCIAL SERVICES

Andrew M. Cuomo
Governor

Benjamin M. Lawsky
Superintendent

May 24, 2013

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 30882 dated September 17, 2012, attached hereto, I have made an examination into the condition and affairs of Leatherstocking Cooperative Insurance Company as of December 31, 2011, and submit the following report thereon.

Wherever the designation “the Company” appears herein without qualification, it should be understood to indicate Leatherstocking 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 4313 County Highway 11, Cooperstown, New York 13326.

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, 2006. This examination covered the five-year period from January 1, 2007 through December 31, 2011. 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.

All financially significant accounts and activities of the Company were considered in accordance with the risk-focused examination process. The examiners also relied upon audit work performed by the Company’s independent public accountants when appropriate.

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 incorporated under the laws of the State of New York on June 27, 1887 as the Otsego County Farmers' Cooperative Fire Insurance Company. The current name, Leatherstocking Cooperative Insurance Company, was adopted on October 1, 1990.

A. Management

Pursuant to the Company's charter and by-laws, management of the Company is vested in a board of directors consisting of not less than nine nor more than twenty-five members. The board meets at least four times during each calendar year. At December 31, 2011, the board of directors was comprised of the following eleven members:

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Wayne D. Benjamin Morris, NY	Vice President, Leatherstocking Cooperative Ins. Company
Jeffrey T. Coffin Maryland, NY	Consultant
Peter L. Craig Hartwick, NY	Retired President, Leatherstocking Cooperative Ins. Company
Nathan R. Fenno Cooperstown, NY	President, Delaware Otsego Corp.
James S. Foote Oneonta, NY	Director, Otsego Electric Corp.
Carl Johansen Edmeston, NY	Secretary, Leatherstocking Cooperative Ins. Company
Philip A. Lewis Cooperstown, NY	President, Leatherstocking Cooperative Ins. Company

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Margaret Maguire Oneonta, NY	Retired, State University of NY College at Oneonta
Kim K. Muller Oneonta, NY	Grant Writer, State University of NY College at Oneonta
Carol B. Ronovech Oneonta, NY	Independent CPA
Lynn J. Woodard New Berlin, NY	Retired Vice President, Preferred Mutual Insurance Company

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

As of December 31, 2011, the principal officers of the Company were as follows:

<u>Name</u>	<u>Title</u>
Philip A. Lewis	President
Carl Johansen	Secretary
Amy Lyon	Treasurer
Wayne D. Benjamin	Vice President

B. Territory and Plan of Operation

As of December 31, 2011, 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
19	Motor vehicle and aircraft physical damage
20	Marine and inland marine

The Company was also licensed as of December 31, 2011, 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 \$100,000.

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>
2007	\$5,764,088
2008	\$5,631,919
2009	\$5,904,959
2010	\$6,343,689
2011	\$6,946,921

The Company's major lines of business are commercial multiple peril, homeowners multiple peril and fire which accounted for 46.5%, 38.4% and 8.8% respectively. The Company writes mainly through approximately 65 separate agencies concentrated in the eastern central part of New York State in close proximity to the Company's home office.

C. Reinsurance

The Company did not assume any reinsurance as of December 31, 2011.

The Company has structured its ceded reinsurance program as follows:

<u>Type of Treaty</u>	<u>Cession</u>
Property Excess of Loss 100% Authorized	\$480,000 in excess of \$120,000 ultimate net loss, each loss, each risk, subject to a limit of liability of \$960,000 each loss occurrence. This coverage is subject to an annual aggregate deductible of \$225,000.

<u>Type of Treaty</u>	<u>Cession</u>
Casualty Excess of Loss 100% Authorized	\$920,000 in excess of \$80,000 ultimate net loss each loss occurrence.
Casualty Clash Excess of Loss 100% Authorized	\$1,000,000 in excess of \$1,000,000 ultimate net loss each loss occurrence.
Property Catastrophe Excess (2 Layers) Layer 1 100% Authorized	95% of \$800,000 excess of \$200,000 ultimate net loss each loss occurrence, which involves three or more risks.
Layer 2 100% Authorized	100% ultimate net loss in excess of \$1,000,000 each loss occurrence, which involves three or more risks.
Equipment Breakdown 100% Quota Share 100% Authorized	100% Company's Net Retained Liability subject to a limit of \$5,000,000.

In addition to its treaty reinsurance program, the Company obtained property facultative reinsurance program coverage. The maximum cession for the program is four times the Company's net retention, subject to a minimum retention of \$200,000, and a maximum cession of \$750,000 on any one risk. If the cession is greater than \$250,000, the maximum cession as respects any one animal shall not exceed \$250,000. The Company also obtained a casualty excess of loss facultative treaty covering casualty risks in excess of \$1,000,000.

Since the previous examination, the Company's retention has increased from \$60,000 to \$120,000 on property business and from \$30,000 to \$80,000 on casualty business. All business was ceded to authorized/accredited reinsurers.

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 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 appropriate risk transfer analyses and 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. 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, 2011, the Company was independent with no affiliation or pooling agreements in place.

E. Significant Operating Ratios

The following ratios have been computed as of December 31, 2011, based upon the results of this examination:

Net premiums written to surplus as regards policyholders	69%
Liabilities to liquid assets (cash and invested assets less investments in affiliates)	41%
Premiums in course of collection to surplus as regards policyholders	2%

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	\$12,959,361	49.85%
Other underwriting expenses incurred	8,753,577	33.67
Net underwriting gain	<u>4,285,102</u>	<u>16.48</u>
Premiums earned	<u>\$25,998,040</u>	<u>100.00%</u>

F. Risk Management and Internal Controls

A risk-focused assessment and review of the Company's controls was performed in accordance with NAIC requirements as outlined in the Examiners' Handbook. As a result of the review, it was noted that a few controls identified by the Company were not fully documented.

It is recommended that the Company fully document each risk mitigation strategy in order for examiners to evaluate the existence of controls in place at the Company and to determine whether the control procedures are operating as expected, applied throughout the entire period of reliance, and performed on a timely basis.

A risk-focused assessment and review of the Company's Information Technology ("IT") general controls was performed in accordance with NAIC requirements as outlined in the Examiners' Handbook. As a result of the review, numerous deficiencies were noted.

It is recommended that the Company strengthen its IT controls.

3. FINANCIAL STATEMENTS

A Balance Sheet

The following shows the assets, liabilities and surplus as regards policyholders as of December 31, 2011 as determined by this examination and as reported by the Company:

Assets

	<u>Assets</u>	Assets Not <u>Admitted</u>	Net Admitted <u>Assets</u>
Bonds	\$ 9,824,310	\$ 0	\$ 9,824,310
Common stocks (stocks)	2,732,834	0	2,732,834
Properties occupied by the company	291,546	0	291,546
Cash, cash equivalents and short-term investments	1,305,133	0	1,305,133
Other invested assets	100,262	100,262	0
Investment income due and accrued	113,364	0	113,364
Uncollected premiums and agents' balances in the course of collection	190,237	0	190,237
Deferred premiums, agents' balances and installments booked but deferred and not yet due	767,423	0	767,423
Accrued retrospective premiums	0	0	0
Amounts recoverable from reinsurers	10,557	0	10,557
Other amounts receivable under reinsurance contracts	5,580	0	5,580
Current federal and foreign income tax recoverable and interest thereon	142,715	0	142,715
Net deferred tax asset	70,400	0	70,400
Electronic data processing equipment and software	266,498	266,498	0
Furniture and equipment, including health care delivery assets	<u>30,485</u>	<u>30,485</u>	<u>0</u>
Total Assets	<u>\$15,851,344</u>	<u>\$397,245</u>	<u>\$15,454,099</u>

Liabilities, surplus and other funds

Losses and loss adjustment expenses	\$ 2,396,468
Commissions payable, contingent commissions and other similar charges	211,707
Other expenses (excluding taxes, licenses and fees)	123,452
Borrowed money and interest thereon	23,032
Unearned premiums	3,637,592
Advance premium	75,836
Amounts withheld or retained by company for account of others	<u>7,318</u>
Total liabilities	\$ <u>6,475,405</u>
Unassigned funds (surplus)	\$ <u>8,978,694</u>
Surplus as regards policyholders	\$ <u>8,978,694</u>
Total liabilities and surplus	<u>\$15,454,099</u>

Note: The Internal Revenue Service has not yet begun its audit of the Company's Federal Income Tax returns through tax year 2011. The examiner is unaware of any potential exposure to a tax assessment and no liability has been established relative to such contingency.

B. Statement of Income

Surplus as regards policyholders increased \$4,413,438 during the five-year examination period January 1, 2007 through December 31, 2011, detailed as follows:

Underwriting Income

Premiums earned		\$25,998,040
Deductions:		
Losses and loss adjustment expenses incurred	\$12,959,361	
Other underwriting expenses incurred	<u>8,753,577</u>	
Total underwriting deductions		<u>21,712,938</u>
Net underwriting gain or (loss)		\$ 4,285,102

Investment Income

Net investment income earned	\$ 2,040,544	
Net realized capital gain	<u>530</u>	
Net investment gain or (loss)		2,041,074

Other Income

Net gain or (loss) from agents' or premium balances charged off	\$ (38,986)	
Finance and service charges not included in premiums	509,247	
Aggregate write-ins for miscellaneous income	<u>44,993</u>	
Total other income		<u>515,254</u>
Net income before dividends to policyholders and before federal and foreign income taxes		\$ 6,841,430
Dividends to policyholders		<u>0</u>
Net income after dividends to policyholders but before federal and foreign income taxes		\$ 6,841,430
Federal and foreign income taxes incurred		<u>2,277,881</u>
Net Income		\$ <u>4,563,549</u>

Surplus as regards policyholders per report on examination as of December 31, 2006				\$ 4,565,256
	<u>Gains in</u>	<u>Losses in</u>		
	<u>Surplus</u>	<u>Surplus</u>		
Net income	\$4,563,549	\$ 0		
Net unrealized capital gains or (losses)	153,662			
Change in net deferred income tax	63,112			
Change in nonadmitted assets	<u>0</u>	<u>366,885</u>		
Net increase (decrease) in surplus	<u>\$4,780,323</u>	<u>\$366,885</u>	<u>4,413,438</u>	
Surplus as regards policyholders per report on examination as of December 31, 2011				\$ <u>8,978,694</u>

4. LOSSES AND LOSS ADJUSTMENT EXPENSES

The examination liability for the captioned items of \$2,396,468 is the same as reported by the Company as of December 31, 2011. 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 six recommendations as follows (page numbers refer to the prior report):

<u>ITEM</u>	<u>PAGE NO.</u>
A. <u>Accounts and Records</u>	
i. It was recommended that the Company ensures that its custodial agreement contains satisfactory safeguards and controls including the provisions as set forth in the NAIC Financial Examiners Handbook.	17
The Company has complied with this recommendation.	
ii. It was recommended that the Company, when applying the annual aggregate deductible, be mindful of the limitations set forth in Section 6610(c) of the NYIL and limit its net insurance on a single property risk accordingly.	17
The Company has complied with this recommendation.	
B. <u>Market Conduct Activities</u>	
i. It is recommended that the Company maintain claim files in a manner that will facilitate compliance with the requirements of Part 216.11 of Department Regulation 64.	17
The Company has complied with this recommendation.	
It is also recommended that the Company implement proper internal controls that will ensure that both the claim files and the electronic database reflect all data adjustments.	
The Company has complied with this recommendation.	
ii. It is recommended that the Company maintain records to support compliance with Department Circular letter 17 of 1976 when canceling policies with mortgagees' interests.	17
The Company has complied with this recommendation.	
iii. It is recommended that the Company fully comply with Section 6615(a)(1) of the NYIL and rate policies in accordance with the specific rating rules approved by its board of directors.	17
The Company has complied with this recommendation.	

6. SUMMARY OF COMMENTS AND RECOMMENDATIONS

<u>ITEM</u>	<u>PAGE NO.</u>
A. <u>Risk Management and Internal Controls</u>	
i. It is recommended that the Company strengthen its IT controls.	8
ii. It is recommended that the Company fully document each risk mitigation control in order for examiners to document and test the existence of controls in place at the Company.	8

Respectfully submitted,

_____/s/
Susan Weijola
Senior Insurance Examiner

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

Susan Weijola, being duly sworn, deposes and says that the foregoing report, subscribed by her, is true to the best of her knowledge and belief.

_____/s/
Susan Weijola

Subscribed and sworn to before me
this _____ day of _____, 2013.

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:*

Susan Weijola

as a proper person to examine the affairs of the

LEATHERSTOCKING COOPERATIVE INSURANCE COMPANY

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

COMPANY

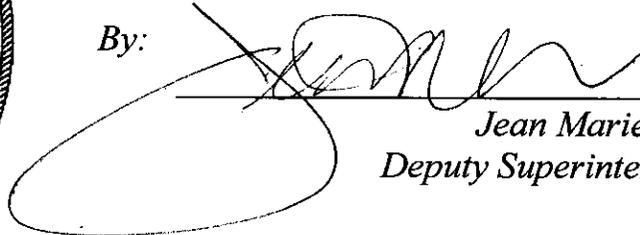
with such other information as she shall deem requisite.

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

this 17th day of September, 2012

BENJAMIN M. LAWSKY
Superintendent of Financial Services

By:



Jean Marie Cho
Deputy Superintendent

