

REPORT ON EXAMINATION

OF THE

FDM PREFERRED INSURANCE COMPANY, INC.

AS OF

DECEMBER 31, 2010

DATE OF REPORT

AUGUST 16, 2011

EXAMINER

KAREN GARD, AFE

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NEW YORK STATE
DEPARTMENT *of*
FINANCIAL SERVICES

Andrew M. Cuomo
Governor

Benjamin M. Lawsky
Superintendent

August 16, 2011

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 30637 dated January 7, 2011, attached hereto, I have made an examination into the condition and affairs of FDM Preferred Insurance Company, Inc. as of December 31, 2010, and submit the following report thereon.

Wherever the designation “the Company” appears herein without qualification, it should be understood to indicate FDM Preferred Insurance Company, Inc.

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

The examination was conducted at the Company’s home office located at 777 Chestnut Ridge Road, Chestnut Ridge, New York 10977.

1. SCOPE OF EXAMINATION

The Department has performed a single-state examination of FDM Preferred Insurance Company, Inc. This is the first financial examination of the Company after the report on organization, which was conducted as of February 9, 2009. This examination covered the period from February 10, 2009 through December 31, 2010. 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. An 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 accounts and activities of the Company were considered in accordance with the risk-focused examination process. This examination also included a review and evaluation of the Company’s own control environment assessment. 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
- Statutory deposits
- Financial statements
- Summary of recommendations

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

FDM Preferred Insurance Company, Inc. is a not-for-profit stock company, which writes workers' compensation insurance and employer's liability insurance, primarily for volunteer firefighters, in New York State. It was established by Fire Districts of New York Mutual Insurance Company, Inc. ("FDM") as a discounted company for policyholders who exhibited better than average loss ratios and exposures to losses. The Company received a determination from the State of New York Department of Taxation and Finance that it is entitled to the exemption provided in Section 1512(a)(1) of the New York State Tax Law.

The Company was incorporated under the laws of the State of New York on December 21, 2007. It became licensed on March 16, 2009 and commenced business on the same date.

At December 31, 2010, capital paid in was \$600,000 consisting of 60,000 shares of \$10 par value per share common stock. Gross paid-in and contributed surplus was \$670,020 and has not changed during the examination period.

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 thirteen members. The board meets four times during each calendar year. At December 31, 2010, the board of directors was comprised of the following thirteen members:

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
Joseph L. Cruger Poughkeepsie, NY	Roosevelt Fire District, Dutchess County
Craig P. DeBaun Oceanside, NY	Oceanside Fire District
Michael H. Geoghan Bayport, NY	Bayport Fire District

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>
D. Donald Greene Newburgh, NY	Cronomer Valley Fire District
Thomas E. Herlihy, Jr. Apulia Station, NY	Fabius Fire District
Kenneth Hoffarth Valhalla, NY	Valhalla Fire District
John LoScalzo Huntington, NY	Eaton's Neck Fire District
James J. McCormick East Northport, NY	Retired
Daniel F. McNeil, III Cortland, NY	President, McNeil and Company
Frank A. Nocerino North Massapequa, NY	North Massapequa Fire District
George J. Paul West Seneca, NY	West Seneca Fire District #3
Lawrence Pierce Mendon, NY	Mendon Fire District
Michael L. White Clay, NY	Insurance Marketing, McNeil and 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 has an acceptable record of attendance.

As of December 31, 2010, the principal officers of the Company were as follows:

<u>Name</u>	<u>Title</u>
Daniel F. McNeil III	President
Lanny D. Strain*	Chief Operating Officer and Executive Vice President
Frank A. Nocerino	Vice President
Michael H. Geoghan	Treasurer
Kenneth E. Hoffarth	Secretary

*Effective June 1, 2011, Mr. Strain resigned; the position is currently vacant.

B. Territory and Plan of Operation

As of December 31, 2010, the Company was licensed to write business in New York only. The license covers workers' compensation and employers' liability insurance as defined in paragraph 15 of Section 1113(a) of the New York Insurance Law, including volunteer firefighters' benefit insurance provided pursuant to the Volunteer Firefighters' Benefit Law.

Based on the lines of business for which the Company is licensed and the Company's current capital structure, and pursuant to the requirements of Articles 13 and 41 of the New York Insurance Law, the Company is required to maintain a minimum surplus to policyholders in the amount of \$600,000.

The following schedule shows the direct premiums written by the Company in the State of New York for the period under examination:

<u>Calendar Year</u>	<u>Direct Premiums Written</u>
2009	\$2,020,005
2010	\$5,614,251

Given that the New York Compensation Insurance Rating Board sets the rates, FDM, in order to achieve more equitable pricing for its insureds, created a 3-tier pricing format by forming two wholly-owned subsidiaries: the Company and Fire Districts Insurance Company, Inc. ("FDI"). Standard risks are written by FDM, preferred risks are written by the Company, and substandard risks are written by FDI.

The Company is a direct writer and its business is produced through approximately eighty-seven agents.

C. Reinsurance

Assumed reinsurance accounted for 20% of the Company's gross premium written at December 31, 2010, primarily due to its participation in the pooling agreement discussed below. The Company utilizes reinsurance accounting as defined in Statement of Statutory Accounting Principle ("SSAP") No. 62 for all of its assumed reinsurance business.

Effective April 1, 2009, the Company entered into an Inter-company Pooling Agreement with FDM and FDI. The companies pool all insurance risks and participate therein on a fixed percentage basis, as follows:

FDM	75%
FDI	15%
The Company	10%

The Company has structured its ceded reinsurance program as follows:

<u>Type of treaty</u>	<u>Cession</u>
<u>Casualty</u>	
First layer 100% authorized	\$500,000 excess of \$500,000 ultimate net loss, each loss occurrence; further subject to an aggregate limit of \$5,000,000 each agreement year as respects losses arising from an Act of Terrorism.
Second layer 100% authorized	\$1,000,000 excess of \$1,000,000 ultimate net loss, each loss occurrence; further subject to an aggregate limit of \$1,000,000 each agreement year as respects losses arising from an Act of Terrorism.
Third layer 100% authorized	\$3,000,000 excess of \$2,000,000 ultimate net loss, each loss occurrence, limit of \$6,000,000 ultimate net loss in the aggregate each agreement year; further subject to an aggregate limit of \$3,000,000 each agreement year as respects losses arising from an Act of Terrorism.
Fourth layer 100% authorized	\$5,000,000 excess of \$5,000,000 ultimate net loss, each loss occurrence, limit of \$10,000,000 ultimate net loss in the aggregate each agreement year; further subject to an aggregate limit of \$5,000,000 each agreement year as respects losses arising from an Act of Terrorism.
Fifth layer 100% authorized	\$5,000,000 excess of \$10,000,000 ultimate net loss, each loss occurrence, limit \$10,000,000 ultimate net loss in the aggregate each agreement year; further subject to an aggregate limit of \$5,000,000 each agreement year as respects losses arising from an Act of Terrorism.

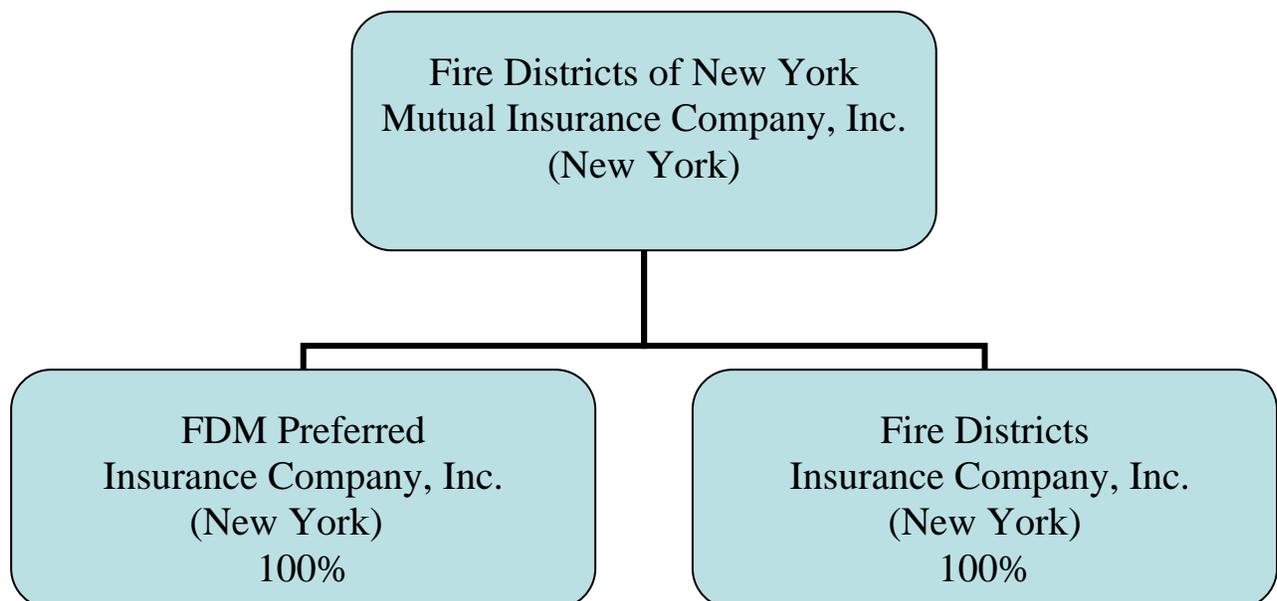
All significant ceded reinsurance agreements in effect as of the examination date were reviewed and found to contain the required clauses, including an insolvency clause meeting the requirements of Section 1308 of the New York Insurance Law.

Examination review 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 NAIC Accounting Practices and Procedures Manual, Statements of Statutory Accounting Principles (“SSAP”) No. 62. Representations were supported by appropriate risk transfer analyses and an attestation from the Company's chief executive 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. 62.

D. Affiliated group

The Company is wholly owned by FDM. Since the ultimate controlling party of the affiliated group is an authorized insurer, it is exempt from the requirements of Article 15 of the New York Insurance Law and Department Regulation 52. The Company is subject to the requirements of Article 16 of the New York Insurance Law; however, it received a waiver for the filing requirements of Department Regulation 53, since all affiliates are insurance companies subject to Articles 3 and 16 of the New York Insurance Law.

The following is a chart of the affiliated group at December 31, 2010:



In addition to the Inter-company Pooling Agreement with FDM and FDI, the Company was party to the following agreement with the other members of the affiliated group at December 31, 2010:

Inter-company Cost Allocation Agreement

Effective January 30, 2009, the Company entered into a service and cost allocation agreement with FDM and FDI, whereby FDM agrees to provide personnel services and to make available its property, equipment and facilities. Pursuant to the agreement, the Company and FDI agree to reimburse FDM in accordance with the requirements of Department Regulation No. 30. This agreement was filed with the Department as part of its license application and was non-disapproved.

E. Significant Operating Ratios

The following ratios have been computed as of December 31, 2010, based upon the results of this examination:

Net premiums written to surplus as regards policyholders	122%
Liabilities to liquid assets (cash and invested assets less investments in affiliates)	75%
Premiums in course of collection to surplus as regards policyholders	19%

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 examination period February 10, 2009 through December 31, 2010:

	<u>Amounts</u>	<u>Ratios</u>
Losses and loss adjustment expenses incurred	\$2,044,890	86.70%
Other underwriting expenses incurred	442,459	18.76
Net underwriting loss	<u>(128,899)</u>	<u>(5.46)</u>
Premiums earned	<u>\$2,358,450</u>	<u>100.00%</u>

3. FINANCIAL STATEMENTS

A. Balance Sheet

The following shows the assets, liabilities and surplus as regards policyholders as of December 31, 2010 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	\$1,177,001	\$ 0	\$1,177,001
Cash, cash equivalents and short-term investments	2,260,151		2,260,151
Investment income due and accrued	6,112		6,112
Uncollected premiums and agents' balances in the course of collection	228,171		228,171
Deferred premiums, agents' balances and installments booked but deferred and not yet due	214,263		214,263
Amounts recoverable from reinsurers	<u>85,605</u>	<u>\$ 0</u>	<u>85,605</u>
Total assets	<u>\$3,971,303</u>	<u>\$ 0</u>	<u>\$3,971,303</u>

Liabilities, Surplus and Other Funds

Losses and loss adjustment expenses	\$1,505,579
Reinsurance payable on paid losses and loss adjustment expenses	39,519
Commissions payable, contingent commissions and other similar charges	(191,075)
Other expenses (excluding taxes, licenses and fees)	497
Taxes, licenses and fees (excluding federal and foreign income taxes)	448,396
Unearned premiums	434,471
Advance premium	184,091
Ceded reinsurance premiums payable (net of ceding commissions)	269,058
Payable to parent, subsidiaries and affiliates	<u>100,870</u>
Total liabilities	\$2,791,406

Surplus and Other Funds

Common capital stock	\$600,000
Gross paid in and contributed surplus	670,020
Unassigned funds (surplus)	<u>(90,124)</u>
Surplus as regards policyholders	<u>1,179,894</u>
Total liabilities, surplus and other funds	<u>\$3,971,301</u>

B. Statement of Income

Surplus as regards policyholders decreased \$90,126 during the examination period February 10, 2009 through December 31, 2010, detailed as follows:

Underwriting Income

Premiums earned		\$2,358,450
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Deductions:

Losses and loss adjustment expenses incurred	\$2,044,890	
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Other underwriting expenses incurred	<u>442,459</u>	
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Total underwriting deductions		<u>2,487,349</u>
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Net underwriting gain or (loss)		\$ (128,899)
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Investment Income

Net investment income earned	\$ <u>36,105</u>	
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Net investment gain or (loss)		\$ <u>36,105</u>
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Other Income

Net gain or (loss) from agents' or premium balances charged off	\$ <u>2,668</u>	
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Total other income		\$ <u>2,668</u>
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Net income before dividends to policyholders and before federal and foreign income taxes		\$ <u>(90,126)</u>
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Net income after dividends to policyholders but before federal and foreign income taxes		\$ <u>(90,126)</u>
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Net income		\$ <u>(90,126)</u>
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Surplus as regards policyholders per report on organization as of February 9, 2009			\$1,270,021
	<u>Gains in Surplus</u>	<u>Losses in Surplus</u>	
Net income (loss)		<u>\$90,125</u>	
Total gains and losses		<u>\$90,125</u>	
Net increase (decrease) in surplus			<u>(90,125)</u>
Surplus as regards policyholders per report on examination as of December 31, 2010			<u>\$1,179,896</u>

4. LOSSES AND LOSS ADJUSTMENT EXPENSES

The examination liability for the captioned items of \$1,505,579 is the same as reported by the Company as of December 31, 2010. 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 REPORT ON ORGANIZATION

The report on organization did not contain any comments or recommendations.

6. SUMMARY OF COMMENTS AND RECOMMENDATIONS

This report contains no comments or recommendations.

Respectfully submitted,

/s/
Karen Gard, AFE,
Senior Insurance Examiner

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

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

/s/
Karen Gard

Subscribed and sworn to before me

this _____ day of _____, 2012.

Appointment No. 30637

*STATE OF NEW YORK
INSURANCE DEPARTMENT*

*I, James J. Wrynn Superintendent of Insurance of the State of New York,
pursuant to the provisions of the Insurance Law, do hereby appoint:*

Karen Gard

as proper person to examine into the affairs of the

FDM PREFERRED INSURANCE COMPANY, INC.

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

Company

with such other information as she 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 7th day of January, 2011



James J. Wrynn

JAMES J. WRINN

Superintendent of Insurance