

REPORT ON EXAMINATION  
OF THE  
BROOME CO-OPERATIVE INSURANCE COMPANY  
AS OF  
DECEMBER 31, 2002

DATE OF REPORT:

APRIL 21, 2003

EXAMINER:

GERARD L. FRANCO



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

George E. Pataki  
Governor

Gregory V. Serio  
Superintendent

April 21, 2003

Honorable Gregory V. Serio  
Superintendent of Insurance  
Albany, New York 12257

Pursuant to the requirements of the New York Insurance Law, and in compliance with the instructions contained in Appointment Number 22003 dated February 5, 2003, attached hereto, I have made an examination into the condition and affairs of the Broome Co-operative Insurance Company as of December 31, 2002 and submit the following report thereon.

The examination was conducted at the Company's home office located at 51 Chapel Street, Windsor, New York 13865

Wherever the designations "the Company", or "BCIC" appear herein without qualification, they should be understood to indicate the Broome Co-operative Insurance Company.

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## 1. SCOPE OF EXAMINATION

The prior examination was conducted as of December 31, 1997. This examination covered the five year period from January 1, 1998 through December 31, 2002 and was limited in its scope to a review or audit of only those balance sheet items considered by this Department to require analysis, verification or description, including: invested assets, loss and loss adjustment expense reserves and the provision for reinsurance. The examination included a review of income, disbursements and company records deemed necessary to accomplish such analysis or verification and utilized, to the extent considered appropriate, work performed by the Company's independent certified public accountants. Transactions occurring subsequent to this period were reviewed where deemed appropriate by the examiner.

A review was 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 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 Company was organized on January 20, 1887 as the Broome County Farmers' Fire Relief Association, for the purpose of transacting business as an assessment cooperative fire insurance association in Broome County of this State.

In 1951 the Association merged with the Broome County Patrons Fire Relief Association, of Whitney Point, New York and the surviving corporation resulting from said merger became the "Broome County Co-operative Fire Insurance Company."

On March 27, 2002 approval was given by the Insurance Department for the Company to change its name from the "Broome County Co-operative Fire Insurance Company" to the "Broome Co-operative Insurance Company."

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 or more than fourteen directors. As of the examination date, the board of directors was comprised of nine members, divided into three equal groups, with one group being elected at each annual policyholder's meeting for a term of three years.

Each person insured by the Company is entitled to one vote in person at each of its annual meetings and no one may vote by proxy. The annual meeting of the board of directors is held immediately after the annual meeting of the Company. The full board met at least four times each year for the period under examination, thereby complying with Section 6624(b) of the New York Insurance Law.

The directors as of December 31, 2002 were as follows:

<u>Director</u>	<u>Principal Business Affiliation</u>
Clifford W. Crouch Bainbridge, NY	New York State Assemblyman
Robert M. Dean Whitney Point, NY	Retired
Peter A. Ellis Owego, NY	Chairman of the Board, BCIC
Ralph E. Kelsey Spencer, NY	Bank Vice-President
Steven P. Krna Whitney Point, NY	Attorney
Oscar C. Lerwick Coventry, NY	President-Treasurer, Broome Co-operative Insurance Company
John W. Salt Windsor, NY	Vice President, BCIC and Funeral director
Ruth A. Smith Windsor, NY	Secretary-Asst. Treasurer, Broome Co-operative Insurance Company
Antoinette Weller Afton, NY	Retired

The minutes of all meetings of the Board of Directors' held during the examination period were reviewed. Section 6611(a)(3) of the New York Insurance Law states that, "The secretary shall maintain a minute book recording the proceedings of all meetings of the corporation, its board of directors and the principal committees thereof." However, upon examination of the minutes it was discovered that no written minutes were kept of the Company's finance and nominating committee meetings. Therefore, it is recommended that the Company comply with Section 6611(a)(3) of the Insurance Law and record in written form all minutes of the finance and nominating committee meetings.

Article II Section II of the Company's by-laws states that the names of all qualified persons for the office of director should be submitted to the Secretary of the Company at least thirty days before the annual meeting. After a review of the board of director minutes it was learned that the nominating committee met just before the annual meeting of the policyholders each year of the examination period. It is recommended that the Company comply with Article II Section II of its by-laws and have the names of all qualified persons for the office of director submitted to the Secretary of the Company at least thirty days before the annual meeting.

The average attendance by the board of directors during the examination period was approximately 96%, with each individual director's attendance being adequate at these meetings.

Each of the director's qualifications, as set forth in Article II Section I of the Company' by-laws, was reviewed and it appears that each director is duly qualified.

At December 31, 2002 the officers of the Company were as follows:

Chairman of the Board	Peter A. Ellis
President and Treasurer	Oscar C. Lerwick
Vice President	John W. Salt
Secretary and Asst. Treasurer	Ruth A. Smith

B. Territory and Plan of Operation

At December 31, 2002, the Company was given authority to write insurance in all the Counties of the State of New York excluding the Counties of New York, Kings, Queens, Bronx and Richmond. The following schedule represents the Company's direct premiums written by year:

<u>Calendar Year</u>	<u>Direct Premiums Written(000)s</u>
1998	\$ 3,416
1999	3,520
2000	3,675
2001	3,874
2002	4,180

The Company was licensed, as of December 31, 2002, to transact the kinds of businesses defined in the following numbered paragraphs of Section 1113(a) of the New York Insurance Law:

<u>Paragraph</u>	<u>Kind 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
15	Workers' compensation and employers' 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 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 homeowners multiple peril and commercial multiple peril lines of business, which accounted for 53% and 31%, respectively, of the 2002 net premium writings.

### C. Reinsurance

The Company had no assumed reinsurance premiums written as of December 31, 2002.

The Schedule F's as contained in the Company's annual statements filed for the years within the examination period were found to accurately reflect its reinsurance transactions.

The examiner reviewed all ceded reinsurance contracts effected during the examination period. These contracts, as endorsed during the examination, all contained the required standard clauses, including insolvency clauses, meeting the requirements of Section 1308 of the New York Insurance Law.

As of December 31, 2002, the Company had the following property and casualty excess of loss reinsurance program in place:

Property 2 layers	\$100,000 x/s \$50,000 ultimate net loss each loss occurrence, each risk; subject to a further limit of \$330,000 any one loss occurrence
	\$350,000 x/s \$150,000 ultimate net loss each loss occurrence, each risk; subject to a further limit of \$1,200,000 any one loss occurrence
Casualty 2 layers	\$510,000 x/s \$40,000 ultimate net loss each loss occurrence
Casualty clash	\$500,000 x/s \$500,000 ultimate net loss in respect to any one loss occurrence
Property catastrophe 2 layers	95% of \$1,300,000 x/s \$200,000 ultimate net loss each and every loss occurrence
100% quota share(windstorm)	\$500,000 x/s \$1,500,000 net loss, per occurrence

As of December 31, 2002, the Company had the following non-obligatory surplus reinsurance program in place:

Property	10(ten) times the Company's net retention per risk, subject to a maximum cession of \$500,000 per risk, subject to limited liability as respect all losses arising from any one occurrence, to an amount not to exceed \$1,000,000
Casualty	\$500,000 x/s \$500,000 per occurrence

Section 1308(e)(1)(A) of the New York Insurance Law states, that “During any period of twelve consecutive months, without the superintendent’s permission: no domestic insurer, except life, shall by any reinsurance agreement or agreements cede an amount of its insurance on which total gross reinsurance premiums are more than fifty percent of the unearned premiums on the net amount of its insurance in force at the beginning of such period...”

The Department had previously granted approval for the Company to cede an amount in excess of the 50% limitation prescribed by Section 1308(e)(1)(A) of the New York Insurance Law. However, during the period covered by this examination, the Company failed to submit to the Department for review, various reinsurance agreements, and subsequent amendments to the reinsurance agreements as required by Section 1308(e)(1)(A) of the Insurance Law.

It is recommended that the Company comply with the requirements of Section 1308(e)(1)(A) of the New York Insurance Law.

Since the previous examination as of December 31, 1997, the Company’s reinsurance program is being underwritten by another authorized reinsurer as was the case in the previous examination. It is noted the Company has increased its retention from \$25,000 to \$50,000 on its property business and from \$15,000 to \$40,000 on its casualty business.

#### D. Holding Company System

The Company was not a member of any holding company system as of December 31, 2002. Furthermore, the Company had no affiliations or pooling agreements in force at December 31, 2002.

#### E. Significant Operating Ratios

The following ratios have been computed as of December 31, 2002 based upon the results of this examination:

Net premiums written in 2002 to Surplus as regards policyholders	0.35 to 1
Premiums in course of collection to Surplus as regards policyholder	0.23%
Liabilities to cash and invested assets	26.9%

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 January 1, 1998 to December 31, 2002:

	<u>Amounts</u>	<u>Ratios</u>
Losses and loss adjustment expenses	\$ 6,873,943	50.9%
Other underwriting expenses	4,751,172	35.2%
Net underwriting gain	<u>1,878,146</u>	<u>13.9%</u>
Premiums	<u>\$13,503,261</u>	<u>100.0%</u>

#### F. Abandoned Property

During the period covered by this examination, the Company maintained appropriate records of unclaimed funds as required by Section 1316 of the New York Abandoned Property Law. Those reports that were required to be filed with the State Comptroller were done so in a timely manner.

#### G. Accounts and Records

The annual statement instructions state that the balance reported on Page 2 Lines 10.1 and 10.2 of the annual statement should be receivable amounts due and receivable amounts not yet due, respectively. The Company recorded only the over ninety-day balance due on Line 10.1 of page 2. It is recommended that the Company adheres to the annual statement instructions and includes all receivable amounts due, not just over ninety-day balances, on Line 10.1 of page 2 in all future annual statements filed with the Insurance Department.

It is the Department's position, reinforced by Circular Letter No. 2 of 1977, that a security broker may not be a custodian of insurer owned securities, even if such securities are then re-deposited by the broker in a "book entry only" program. As of the examination date, two of the Company's callable certificates of deposit in the amount of \$200,000 and one of its common stocks valued at \$159,007 were being held by two brokerage firms. Therefore, it is recommended that the Company comply with

Department directives, reinforced by Circular Letter No. 2 of 1977, and move any investments held by a broker to a proper banking institution in a timely fashion with a suitable written custodial agreement.

It is noted that no examination change will be made as the total of the securities involved is less than 5% of the Company's surplus.

#### H. Fidelity Bond

At December 31, 2002 BCIC had in effect blanket employee dishonesty insurance coverage of \$100,000, which is included with their commercial account policy. The Examiner's Handbook of the National Association of Insurance Commissioners (NAIC) suggested fidelity insurance for a Company of this size is between \$150,000 and \$175,000. The Company had direct premiums written of over \$4,000,000 for the 2002 examination year and the fidelity coverage carried by BCIC for this amount of writings is not adequate enough to be a sound business practice. Therefore, it is recommended that the Company increase its fidelity coverage to a level at least equal to the minimum suggested by the NAIC.

### 3. FINANCIAL STATEMENTS

#### A. Balance sheet

The following shows the assets, liabilities and surplus as regards policyholder as determined by this examination as of December 31, 2002. This statement is the same as the balance sheet filed by the Company.

<u>Assets</u>	Ledger <u>Assets</u>	Not Admitted <u>Assets</u>	Net Admitted <u>Assets</u>
Bonds	\$ 4,604,114	\$ -0-	\$ 4,604,114
Common Stocks	164,124	-0-	164,124
Real Estate	15,702	-0-	15,702
Cash and short term investments	5,260,808	-0-	5,260,808
Agents' balances or Uncollected premiums	295,569	19,029	276,540
Reinsurance recoverables on loss and loss adjustment expense	17,518	-0-	17,518
Federal and foreign income tax recoverable	232,800	-0-	232,800
Interest, dividends and real estate income	526,842	-0-	526,842
Other assets nonadmitted	<u>112,249</u>	<u>112,249</u>	<u>-0-</u>
Total	<u>\$ 11,229,726</u>	<u>\$ 131,248</u>	<u>\$ 11,098,448</u>

#### Liabilities and Surplus

Losses and loss adjustment expenses		\$ 564,836
Commissions payable		37,916
Other expenses		36,141
Unearned premiums		2,110,803
Advance premiums		87,887
Ceded reinsurance premiums payable		<u>3,377</u>
Total liabilities		\$ 2,840,960
Unassigned funds(surplus)	\$ 100,000	
Special contingent surplus	<u>8,157,488</u>	
Surplus as regards policyholders		<u>8,257,488</u>
Total		<u>\$ 11,098,448</u>

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 the examination changes contained in this report, the examiner is unaware of any potential exposure of 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 regard policyholders increased \$ 2,932,019 during the five-year examination period (January 1, 1998 through December 31, 2002) detailed as follows:

Statement of IncomeUnderwriting Income

Premiums earned		\$ 13,503,261
Losses and loss adjustment expenses incurred	\$ 6,873,943	
Other underwriting expenses incurred	<u>4,751,172</u>	
Total underwriting deductions		<u>11,625,115</u>
Net underwriting gain		\$ 1,878,146

Investment Income

Net investment income earned	\$2,095,073	
Net realized capital gain	<u>110,309</u>	
Net investment gain		2,205,382

Other Income

Agents balances charged off	\$ (99,786)	
Premiums received in advance	37,729	
Finance and service charge	194,819	
Cumulative effect of changes in accounting principles	<u>130,872</u>	
Net other income		<u>263,634</u>
Net income before federal income taxes		\$ 4,347,162
Federal income taxes incurred		<u>1,459,815</u>
Net income		<u>\$2,887,347</u>

Capital and Surplus Account

Surplus as regards policyholders, December 31, 1997, per prior report on examination		\$ 5,325,469
	<u>Gains in Surplus</u>	<u>Losses in Surplus</u>
Net income or loss	\$ 2,887,347	\$ -0-
Net unrealized capital gain	21,654	-0-
Change in non-admitted assets		47,982
Excess of statutory reserves	<u>71,000</u>	<u>-0-</u>
Totals	<u>\$ 2,980,001</u>	<u>\$47,982</u>
Net increase in Surplus as regards policyholders		<u>2,932,019</u>
Surplus as regards policyholders, December 31, 1997, per report on examination		<u>\$8,257,488</u>

4. LOSSES AND LOSS ADJUSTMENT EXPENSES

The examination liability of \$564,836 is the same as the \$564,836 reported by the Company on its filed 2002 annual statement.

The Department's 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.

The Company's actuarial opinion and report were reviewed and utilized in the determination of an appropriate reserve for the Company's unpaid losses and loss adjustment expenses.

5. MARKET CONDUCT ACTIVITIES

In the course of this examination, a review was made of the manner in which the Company conducts its business practices and fulfills its contractual obligations to policyholders and claimants. The review was general in nature and is not to be construed to encompass the generally 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

A review of loss checks was undertaken during the course of the examination. Regulation 64(NYCRR Part 216.6(g) states, in part, that “No insurer shall issue a check or draft in payment of a first-party claim... that contains any language or provision that expressly or impliedly states that acceptance of such check or draft shall constitute a final settlement or release of any or all future obligations arising out of the loss...” After a review of the Company’s cancelled loss checks it was revealed that the wording “final payment” appears on these checks. Therefore, it is recommended that the Company comply with Regulation 64(NYCRR Part 216.6(g) and discontinue using the phrase “final payment” or any other expression that would imply that such check represents a final settlement of the loss on all loss checks.

#### 6. COMPLIANCE WITH PRIOR REPORT ON EXAMINATION

The prior report contained comments and recommendations as follows (page numbers refer to the prior report):

<u>Item</u>	<u>Page No.</u>
A. It is recommended that the Company include its call option data in future annual statements submitted to this Department	8

The Company has complied with this recommendation.

<u>Item</u>	<u>Page No.</u>
B. It is recommended that the Company correctly report it's callable certificates of deposit in all future financial statements submitted to this Department	8
The Company has complied with this recommendation	
C. It is recommended that the Company properly report its contingent commissions as a separate liability in all future financial statements submitted to this Department	9
The Company has complied with this recommendation.	

## 7. SUMMARY OF COMMENTS AND RECOMMENDATIONS

As indicated in the body of this report, the Company should be directed to comply with the following:

<u>Item</u>	<u>Page No.</u>
<u>A. Management</u>	4
i. It is recommended that the Company comply with Section 6611(a)(3) of the Insurance Law and record in written form all minutes of the finance and nominating committee meetings.	
ii. It is recommended that the Company comply with Article II Section II of its by-laws and have the names of all qualified persons for the office of director submitted to the Secretary of the Company at least thirty days before the annual meeting.	4

<u>Item</u>	<u>Page No.</u>
<u>B. Reinsurance</u>	7
<p>It is recommended that the Company comply with the requirements of Section 1308(e)(1)(A) of the New York Insurance Law.</p>	
<u>C. Accounts and Records</u>	8
<p>i. It is recommended that the Company adhere to the annual statement instructions and include all receivable amounts due, not just over ninety-day balances on Line 10.1 of page 2 in all future annual statements filed with the Insurance Department.</p>	
<p>ii. It is recommended that the Company comply with Department directives, reinforced by Circular Letter No. 2 of 1977, and move any investments held by a broker to a proper banking institution in a timely fashion with a suitable written custodial agreement.</p>	
<u>D. Fidelity Bond</u>	8-9
<p>It is recommended that the Company increase its fidelity coverage to a level at least equal to the minimum suggested by the NAIC.</p>	
<u>E. Market Conduct Activities</u>	9
<p>It is recommended that the Company comply with Regulation 64 (NYCRR Part 216.6 (g)) and discontinue using the phrase “final payment” or any other expression that would imply that such check represents a final settlement of the loss on all loss checks.</p>	
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Respectfully submitted,

*[Signature]*  
Gerard L. Franco  
Senior Insurance Examiner

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

Gerard L. Franco, being duly sworn, deposes and says that the foregoing report, subscribed by him, is true to the best of his knowledge, information and belief.

*[Signature]*  
Gerard L. Franco  
Senior Insurance Examiner

Sworn to before me this

3rd day of June, 2003

*[Signature]*  
Notary Public

ANDREA M. CLARE  
Notary Public, State of New York  
Qualified in Montgomery County  
No. 4638585  
Commission Expires July 31, 2006

Appointment No 22003

STATE OF NEW YORK  
INSURANCE DEPARTMENT

I, GREGORY V. SERIO, Superintendent of Insurance of the State of New York, pursuant to the provisions of the Insurance Law, do hereby appoint:

**Gerard Franco**

*as proper person to examine into the affairs of the*

**Broome Co-operative Insurance Company**

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

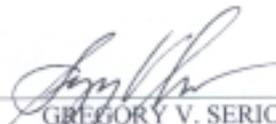
**Company**

*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 Albany,*

this 5<sup>th</sup> day of February, 2003



  
\_\_\_\_\_  
GREGORY V. SERIO  
Superintendent of Insurance