

**STATE OF NORTH DAKOTA
BISMARCK, NORTH DAKOTA**

REPORT OF EXAMINATION

OF

**DAKOTA MUTUAL INSURANCE COMPANY
GWINNER, NORTH DAKOTA**

**AS OF
DECEMBER 31, 2002**

STATE OF NORTH DAKOTA
DEPARTMENT OF INSURANCE

I, the undersigned, Commissioner of Insurance of the State of North Dakota do hereby certify that I have compared the annexed copy of the Report of Examination of the

Dakota Mutual Insurance Company

Gwinner, North Dakota

as of December 31, 2002, with the original on file in this Department and that the same is a correct transcript therefrom and of the whole of said original.

IN WITNESS WHEREOF, I have hereunto
set my hand and affixed my official seal at my
office in the City of Bismarck, this _____ day of
_____, 2004.

Jim Poolman
Commissioner of Insurance

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Gwinner, North Dakota
December 23, 2003

Honorable Jim Poolman
Commissioner of Insurance
North Dakota Department of Insurance
600 East Boulevard
Bismarck, ND 58505-0320

Dear Sir:

Pursuant to your instructions and in accordance with the North Dakota Insurance Code and resolutions adopted by the National Association of Insurance Commissioners, an examination was made of the books, records, and financial condition of

Dakota Mutual Insurance Company

Gwinner, North Dakota

as of December 31, 2002.

INTRODUCTION

Dakota Mutual Insurance Company, Gwinner, North Dakota, hereinafter referred to as the "Company," was last examined as of December 31, 1996, by a representative of the State of North Dakota.

SCOPE OF EXAMINATION

The current examination covers the period January 1, 1997, through December 31, 2002, including any material transactions and events occurring subsequent to the examination date and noted during the course of this examination.

This examination was made in accordance with the practices and procedures promulgated by the National Association of Insurance Commissioners with due regard to the statutory requirements of the insurance laws, rules, and regulations of the State of North Dakota.

Examination procedures included a verification and evaluation of assets, a determination of liabilities, and reviews of corporate records, claim files, and other records relating to Company operational practices.

The Company was not in compliance with one recommendation contained in the previous examination report relating to the accrual of general expenses that are incurred before year end but paid in the following year.

HISTORY

The Company was incorporated on March 4, 1904, as "The Farmers Mutual Fire and Lightning Insurance Company of Sargent and Ransom Counties" with its home office and principal place of business at Gwinner, North Dakota.

The Company's term of existence is perpetual as provided in N.D. Cent. Code § 26.1-13-03.

The Company was organized for the specific purpose of mutually insuring the property of its members against any risk of hazard by fire, lightning, and limited extended coverage.

At the annual meeting held on June 28, 1993, the policyholders voted to change the Company's name to "Dakota Mutual Insurance Company" and to expand its territory to consist of Sargent, Ransom, LaMoure, Dickey, Logan, McIntosh, Richland and Emmons Counties. Article 1 of the Articles of Incorporation was amended to reflect these changes. The Bylaws were also amended to change the name of the Company.

MANAGEMENT AND CONTROL

The Company is controlled by its membership. Any person owning property within the limits of the territory within which the Company is authorized to transact business may become a member of the Company and be entitled to all the rights and privileges accorded each member. No person who does not reside within such territorial limits shall become a director of the Company.

Directors

The management of the Company's affairs, business, and property is vested in a Board of Directors composed of seven members elected for staggered terms of three years each at the annual meeting of the membership. A majority of the entire Board of Directors constitutes a quorum for the transaction of business.

Directors duly elected and serving the Company at December 31, 2002, were as follows:

<u>Name and Residence</u>	<u>Term Expires</u>
William Holmstrom Gwinner, ND	2003
Donald Colby Milnor, ND	2005
Dale Asche Gwinner, ND	2004
Dennis Howey Gwinner, ND	2003
Elwood Enge Milnor, ND	2005
John Totenhagen Stirum, ND	2004
Position is vacant due to death	2005

Officers

Officers are elected annually by the Board of Directors at the first meeting of the Board of Directors held after each annual meeting. Officers serving at December 31, 2002, were as follows:

<u>Name</u>	<u>Office</u>
William Holmstrom	President
Donald Colby	Vice President
Linda Hanson	Secretary-Treasurer

Executive Committee

The following Executive Committee members were elected by the Board of Directors and were serving as of December 31, 2002:

William Holmstrom
Donald Colby
Dale Asche
Linda Hanson

CORPORATE RECORDS

The minutes of the meetings held by the membership and directors during the years under examination were reviewed for compliance with the Articles of Incorporation, Bylaws, and statutory requirements.

Articles of Incorporation

- Article 8 was amended to provide that the fiscal year of the company shall commence on the 1st day of January and end on the 31st day of December in each year.

Bylaws

- Article II, Section 1 was amended to provide that the Annual Meeting of the Company shall be held on the fourth Monday in June of each year.
- Article III, Section 1 was amended to provide that the directors shall receive \$20 per diem and expenses for the time necessarily employed in attending to the business of the Company.
- Article IV, Section 1 was amended to provide that the Company's policies shall be written for a term not to exceed three years.

Members

During the period under examination the annual meetings of the policyholders were held on the following dates: June 23, 1997; June 22, 1998; June 28, 1999; June 26, 2000; June 25, 2001; and June 25, 2002.

Directors

During the period under examination, the Board of Directors held four regular meetings in 1997, two in 1998, three in 1999, one in 2000, six in 2001, and one in 2002.

FIDELITY BOND AND OTHER INSURANCE

At December 31, 2002, there was in force a continuous position schedule fidelity bond covering the Secretary-Treasurer and the President for the faithful performance of duty in the amount of \$15,000 each. The coverage meets the minimum amount of fidelity insurance recommended in the NAIC's *Financial Examiners Handbook*.

TERRITORY AND PLAN OF OPERATION

At December 31, 2002, the Company had 10 licensed agents and was authorized to transact business within the following counties:

Sargent
Logan

Ransom
McIntosh

LaMoure
Richland

Dickey
Emmons

SIGNIFICANT OPERATING RESULTS

Growth

The following exhibit reflects the growth of the Company over a seven-year period. Data with respect to the years 1997 through 2001 is as compiled from home office copies of the filed Annual Statements. Data for the years 1996 and 2002 reflects the results of examination. The operational results are presented on a cash basis.

<u>Year</u>	<u>Admitted Assets</u>	<u>Total Liabilities</u>	<u>Surplus as Regards Policyholders</u>	<u>Net Premiums Written</u>	<u>Underwriting Deductions</u>	<u>Investment and Other Income</u>	<u>Net Income (Loss)</u>
1996	\$120,829	\$62,330	\$58,499	\$59,443	\$74,322	\$ 20,233	\$ 5,354
1997	110,234	65,507	44,728	76,122	109,010	22,468	(10,420)
1998	126,538	59,554	66,984	67,853	71,841	19,510	15,522
1999	129,363	47,819	81,544	53,841	66,542	16,443	3,742
2000	146,977	96,604	50,373	50,189	78,149	15,381	(12,579)
2001	111,885	50,841	61,045	48,194	68,344	15,003	(5,147)
2002	150,451	68,314	82,137	87,719	65,796	17,153	39,075

Operating Ratios

The underwriting ratios presented below are on a cash basis and encompass the six-year period ending December 31, 2002:

	<u>2002</u>	<u>2001</u>	<u>2000</u>	<u>1999</u>	<u>1998</u>	<u>1997</u>
Premiums	100%	100%	100%	100%	100%	100%
Deductions:						
Losses and Loss Adjustment	27.5%	68.9%	86.2%	53.5%	50.5%	89.1%
Underwriting Expenses	47.5%	72.9%	69.5%	70.1%	55.3%	54.1%
Total Deductions	75.0%	141.8%	155.7%	123.6%	105.8%	143.2%
Net Underwriting Gain (Loss)	25.0%	(41.8%)	(55.7%)	(23.6%)	(5.8%)	(43.2%)

MARKET CONDUCT ACTIVITY

Treatment of Policyholders

- Claims From an examination of claim files, the Company appears to pay claims fairly within policy provisions upon receipt of satisfactory proof of loss or damage.
- Advertising Written advertising material was not available for review. The Company uses primarily name announcements during radio programs for advertising purposes.

REINSURANCE

The Company ceded reinsurance under a reinsurance treaty with Grinnell Mutual Reinsurance Company during the years under examination. This nonaffiliated ceding contract consists of individual occurrence of loss and aggregate excess as summarized below. The contract contained the insolvency clause required by N.D. Cent. Code § 26.1-02-21.

- Type: Excess
- Reinsurer: Grinnell Mutual Reinsurance Company
- Scope: Fire, Lightning and Extended Coverage:
- (A) Individual Occurrence of Loss Excess - covers all risks written by the Company in excess of \$30,000 retention subject to the following limits:
- | | |
|--------------------------------|-----------|
| Dwellings | \$750,000 |
| Farm Outbuildings | 750,000 |
| Livestock Confinements | 500,000 |
| Commercial and Public Property | 500,000 |
- (B) Aggregate Excess - provides coverage for 100 percent of the Company's aggregate net loss in excess of a defined retention limit. The retention limit for 2002 was \$53,735.
- Premium:
- (A) Individual Occurrence of Loss Excess - The 2002 annual premium was \$.0442 per \$1,000 of adjusted gross fire risks in force at the end of each month during the contract year.
- (B) Aggregate Excess - The 2002 annual premium was \$.0323 per \$1,000 of gross fire risks in force at the end of each month during the contract year.
- Commissions: None
- Termination Date: The agreement may be terminated only as of the last day of any calendar year by either party upon 90 days notice in writing.

ACCOUNTS AND RECORDS

The accounts and records of the Company are on a cash basis and consist of a cash receipts journal, a cash disbursement journal, a claims register, a policy register, a check register, and a corporate record book.

A trial balance was prepared as of December 31, 2002, for the purpose of tracing it to the Annual Statement. No exceptions were noted.

The following exceptions related to Accounts and Records were noted:

- The Company is not recording denied claims on its claims register. **It is recommended that all claims submitted by policyholders be entered into the claims register and assigned a claims number, with the subsequent disposition of the claim noted in the register.**
- The Company is incorrectly including liability premiums in the amount reported on line 1c, page 2 of its Annual Statement. The net liability premiums attributable to the reinsurer's direct business should be reported as write-in income (amount collected from insureds less the amount remitted to the reinsurer) on line 10, page 2, of the Annual Statement. The Company did not correctly compute the amount reported on line 10. The net effect of these reporting errors results in an understatement of net premium income, which is offset by a balancing overstatement of write-in income on line 10. **It is recommended that the Company report liability premiums collected for and remitted to the reinsurer in compliance with *Annual Statement Instructions*.**

FINANCIAL STATEMENTS

The following statements reflect the financial condition of the Company as of December 31, 2002, as determined by this examination and its operating results for the year then ended.

Dakota Mutual Insurance Company
Statement of Assets, Liabilities, and Surplus
December 31, 2002

ASSETS

LEDGER ASSETS:

Cash on Hand and Checking Account	\$83,015.14	
Cash on Deposit	67,031.46	

TOTAL LEDGER ASSETS		\$150,046.60
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NONLEDGER ASSETS:

Interest Due and Accrued on Cash on Deposit	\$ 404.30	

TOTAL NONLEDGER ASSETS		404.30
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DEDUCT: ASSETS NOT ADMITTED	0	

TOTAL NONADMITTED ASSETS		0
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TOTAL NET ADMITTED ASSETS		<u>\$150,450.90</u>
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LIABILITIES

Unpaid Losses	\$ 0	
Unpaid Loss Adjustment Expenses	0	
Unearned Premium Reserve	64,285.68	
Unpaid Taxes	677.00	
Unpaid General Expenses	80.00	
Reinsurance Premiums Due and Payable	3,271.19	

TOTAL LIABILITIES		\$68,313.87
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SURPLUS TO POLICYHOLDERS		82,137.03

TOTAL LIABILITIES AND SURPLUS		<u>\$150,450.90</u>
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Dakota Mutual Insurance Company
Statement of Cash Receipts and Cash Disbursements
For the Year 2002

INCOME:

Gross Premium Income	\$126,080.49
Less: Return Premiums	2,299.44
Premiums for Reinsurance Ceded	<u>36,062.30</u>

NET PREMIUM INCOME \$87,718.75

Interest on Cash on Deposit	2,241.18
Commissions and Fees Received on Liability Business	2,269.25
Liability Premiums Collected	11,974.31
Miscellaneous Income	<u>668.01</u>

TOTAL INCOME RECEIPTS \$104,871.50

DISBURSEMENTS:

Gross Losses Paid and Incurred in 2002	\$ 16,122.47
Gross Losses Paid in 2002 But Incurred in Prior Years	5,577.74
Deduct: Subrogation	0
Salvage	0
Reinsurance	<u>0</u>

NET LOSSES PAID \$21,700.21

Claim Adjustment Expenses	2,462.96
Commissions Paid to Agents	20,173.72
Directors Fees and Expenses	140.00
Salaries to Employees	12,000.00
Printing, Stationary, and Office Supplies	660.91
Rent and Rent Items	600.00
State and Local Insurance Taxes	1,932.00
Insurance Department Licenses and Fees	200.00
Payroll Taxes	1,886.40
Legal Fees and Auditing	44.46
Travel and Travel Items	177.14
Advertising	1,716.02
Dues and Donations	418.00
Insurance and Bonds	133.25
Postage, Telephone, and Bank Charges	1,198.98
Employee Relations and Welfare	125.00
Miscellaneous Expenses	<u>227.00</u>

TOTAL FUNDS DISBURSED 65,796.05

NET GAIN (LOSS) \$ 39,075.45

COMMENTS TO THE FINANCIAL STATEMENTS

Financial statement balances at December 31, 2002, are commented upon only if financial changes, recommendations, or special explanations are considered necessary.

Unpaid General Expenses

The Company did not accrue for an advertising expense that was invoiced in December 2002 but paid in the following year. No adjustment was made to the financial statements because the amount was immaterial. **It is again recommended that the Company accrue for all general expenses which are incurred before year end but paid in the following year.**

CONCLUSION

The financial condition of Dakota Mutual Insurance Company, Gwinner, North Dakota, as determined by this examination is summarized as follows:

TOTAL ADMITTED ASSETS		<u>\$150,451</u>
Liabilities	\$68,314	
Surplus to Policyholders	<u>82,137</u>	
TOTAL LIABILITIES AND SURPLUS		<u>\$150,451</u>

During the six-year period under examination, admitted assets increased by \$29,622, liabilities increased by \$5,984, and surplus to policyholders increased by \$23,638.

The Examiner expresses her appreciation for the courteous cooperation extended her during the course of this examination.

Respectfully submitted,

Rhoda M. Sautner, CPA, ACS
Examiner
N.D. Insurance Department

COMMENTS AND RECOMMENDATIONS

- Page 7 It is recommended that all claims submitted by policyholders be entered into the claims register and assigned a claims number, with the subsequent disposition of the claim noted in the register.
- Page 7 It is recommended that the Company report liability premiums collected for and remitted to the reinsurer in compliance with *Annual Statement Instructions*.
- Page 10 It is again recommended that the Company accrue for all general expenses which are incurred before year end but paid in the following year.