

**REPORT ON EXAMINATION**  
**OF THE**  
**DELAWARE GRANGE MUTUAL INSURANCE COMPANY**  
**AS OF**  
**DECEMBER 31, 2008**



REPORT ON EXAMINATION  
OF THE  
DELAWARE GRANGE MUTUAL INSURANCE COMPANY  
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The above-captioned Report was completed by examiners of the Delaware Department of Insurance.

Consideration has been duly given to the comments, conclusions and recommendations of the examiners regarding the status of the Company as reflected in the Report.

This Report is hereby accepted, adopted and filed as an official record of this Department.

A handwritten signature in black ink, appearing to read "Karen Weldin Stewart".

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Karen Weldin Stewart, CIR-ML  
Insurance Commissioner

Dated this 10th day of December, 2010



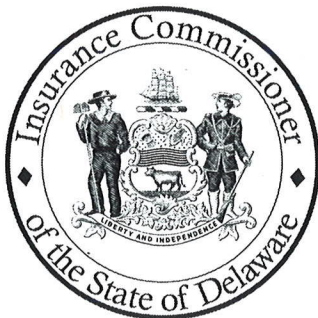
I, Karen Weldin Stewart, Insurance Commissioner of the State of Delaware, do hereby certify that the attached REPORT ON EXAMINATION, made as of December 31, 2008 of the

**DELAWARE GRANGE MUTUAL INSURANCE COMPANY**

is a true and correct copy of the document filed with this Department.

Attest By:           *Sonia C. Harris*          

Date: 10 December 2010



In Witness Whereof, I have hereunto set my hand and affixed the official seal of this Department at the City of Dover, this 10th day of December 2010.

\_\_\_\_\_  
Karen Weldin Stewart, CIR-ML  
Insurance Commissioner

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January 10, 2010

Honorable Karen Weldin Stewart CIR-ML  
Insurance Commissioner  
State of Delaware  
Rodney Building  
841 Silver Lake Boulevard  
Dover, Delaware 19901

Dear Commissioner:

In compliance with instructions contained in Certificate of Authority No. 9.026,  
an examination has been made of the affairs, financial condition and management of the

**DELAWARE GRANGE MUTUAL INSURANCE COMPANY**

hereinafter referred to as “DGMIC” or “Company”, incorporated under the laws of the  
state of Delaware. The examination was conducted at 9 E. Loockerman Street, Dover,  
Delaware.

The report of such examination is respectfully submitted herewith.

## **SCOPE OF EXAMINATION**

The last examination was conducted as of December 31, 2003. This examination covered the five year period of January 1, 2004 to December 31, 2008, and consisted of a general survey of the Company's business policies and practices; management, any corporate matters incident thereto; a verification and evaluation of assets; and a determination of liabilities. Transactions subsequent to the latter date were reviewed where deemed necessary.

The format of this report is designed to explain the procedures employed on examination and the text will explain changes wherever made. If necessary, comments and recommendations have been made in those areas in need of correction or improvement. In such cases, these matters were thoroughly discussed with responsible officials during the course of the examination.

The general procedures of the examination followed the rules established by the National Association of Insurance Commissioners' (NAIC) Committee on Financial Condition Examiners Handbook, and generally accepted statutory insurance examination standards.

In addition to items hereinafter incorporated as part of the written report, the following were checked and made a part of the workpapers of this examination:

All asset and liability items not mentioned

## **HISTORY**

DGMIC was chartered by the Delaware Legislature in 1877 and commenced business in 1880. In 1924, a new charter provided for the Company's perpetual existence.

Prior to 1999, the Company's corporate title was the Delaware State Grange Mutual Fire Insurance Company. Effective August 6, 1999, the present corporate title was adopted.

## **MEMBERSHIP**

Each person to whom a policy of insurance has been issued is a member of the Company and shall be entitled to one vote for each policy issued at all meetings of the members.

The Company amended the bylaws in 2006 to change the number of members needed for a quorum at annual membership meetings. As per an additional amendment to the bylaws, the Company no longer mails notices of the annual meeting to the members; rather it advertises the meeting in 2 newspapers, 3 times a week, 2 weeks before the annual meeting.

The Company did not submit the amended bylaws to the Delaware Insurance Department in accordance with Section 4912 of the Insurance Code.

**It is recommended the Company submit its bylaws to the Delaware Insurance Department in accordance with Section 4912 of the Insurance Code.**

**MANAGEMENT AND CONTROL**

The control and management of the Company is vested in the Board of Directors.

The persons elected and serving as Directors of the Company at December 31, 2008 were:

<u>Director</u>	<u>Principal Occupation</u>
Edward Williams	Retired/Agriculture
William Lehnert	Retired/ Former Marketing Representative, Lititz Mutual
Harvey Thomas	Agriculture
Gary Evans	Retired/Former Director, Delaware Insurance Department
Mervin Richard	Retired/Agriculture
Francis O’Neill, Jr.	Insurance Agent, Lobbyist
Ronald Martin	Maintenance Staff, City of Newark
Mel Warren	Insurance Agent
Richard Harper, Jr.	Retired/U.S. Air Force
William O’Day	Agriculture
Robin Blendt	Secretary, Town of Smyrna
Albert Holmes, Jr.	Insurance Agent
Warner J. Clark	Insurance Agent
Elva Burrows	Retired

The officers of DGMIC are elected by the Board of Directors annually. Those persons serving as of December 31, 2008 were:

<u>Name</u>	<u>Title</u>
Warner J. Clark	President
William O’Day	Vice President
Ronald Martin	Treasurer
Diana Price	Secretary

At December 31, 2008, the Board had appointed the following members to the Executive Committee:

Warner J. Clark	William O’Day
William Holmes	Edward Williams

The Board of Directors also has appointed Underwriting, Personnel and Nominating committees.

In 2002, the Company amended its bylaws to include a provision that members of the Board of Directors who are also insurance agents are required to sign a conflict of interest acknowledgement. The examination noted that the three agents on the Board in 2002 signed the acknowledgement; however, there has been no conflict of interest acknowledgements signed since 2002. The examination also noted that an additional insurance agent has become a Board member since 2002 and no conflict of interest acknowledgement was signed.

**It is recommended that all members of the Board of Directors who are insurance agents sign conflict of interest acknowledgements, and that conflict of interest acknowledgements be executed by all insurance agents on a regular basis.**

### GROWTH OF COMPANY

The following information was obtained from the Company's filed Annual Statements and covers the five preceding years (all amounts in US dollars):

	<u>2008</u>	<u>2007</u>	<u>2006</u>	<u>2005</u>	<u>2004</u>
Assets	\$1,201,076	\$1,140,827	\$1,046,981	\$976,478	\$1,021,066
Policyholder Surplus	1,009,984	971,378	867,115	818,538	763,470
Underwriting gain (loss)	41,384	72,107	8,089	2,395	(54,002)
Net Income	69,638	99,220	31,453	36,947	(35,846)
Premiums written					
Direct	909,049	867,720	756,075	689,996	694,391
Assumed					
Ceded	<u>(661,817)</u>	<u>(626,840)</u>	<u>(524,244)</u>	<u>(466,549)</u>	<u>(450,096)</u>
Net Premiums Written	<u>\$247,232</u>	<u>\$240,880</u>	<u>\$231,831</u>	<u>\$223,447</u>	<u>\$244,295</u>

At December 31, 2003 (the date of the previous examination), the Company reported \$760,936 in Surplus as Regards Policyholders (Policyholders Surplus). During

the previous examination period, the Company's Policyholders Surplus decreased to a level below the minimum surplus level of \$750,000 required by the Delaware Insurance Code. To alleviate this deficiency, DGMIC obtained a surplus note in the amount of \$100,000. From October, 2003 to September, 2006, the Company's writing of new business was restricted.

During the present examination period, the Company's Policyholders Surplus increased by \$249,048. As noted above, the Company reported Net Income of \$201,412 during the examination period. DGMIC also obtained an additional \$50,000 surplus note funding in 2004.

As indicated, the Company cedes a significant portion of its direct premiums written. At the time of the 2003 examination, DGMIC ceded 62.7% of its direct premiums. That percentage increased steadily over the examination period, and for 2008, the Company ceded 72.8% of its direct premiums written.

The Company reported the following operating ratios for the years under examination:

	<u>2008</u>	Ratio	<u>2007</u>	Ratio	<u>2006</u>	Ratio
Losses Incurred	\$71,140	29.60%	\$52,926	21.90%	\$74,472	34.20%
Losses Adjustment Exp Incurred	31,034	12.90%	32,163	13.30%	38,888	17.80%
Underwriting Exp. Incurred	96,563	40.20%	84,481	35.00%	96,432	44.30%
Underwriting Gain/(Loss)	<u>41,384</u>	<u>17.30%</u>	<u>72,107</u>	<u>29.80%</u>	<u>8,089</u>	<u>3.70%</u>
Premiums Earned	<u>\$240,121</u>	<u>100.00%</u>	<u>\$241,677</u>	<u>100.00%</u>	<u>\$217,881</u>	<u>100.00%</u>

Delaware Grange Mutual Insurance Company

	<u>2005</u>	Ratio	<u>2004</u>	Ratio
Losses Incurred	\$76,835	31.50%	\$47,397	17.50%
Loss Adjustment Exp Incurred	38,175	15.60%	48,281	17.80%
Underwriting Exp. Incurred	126,644	51.90%	229,503	84.60%
Underwriting Gain/(Loss)	<u>2,395</u>	<u>1%</u>	<u>(54,002)</u>	<u>(19.90)%</u>
Premiums Earned	<u>\$244,049</u>	<u>100.00%</u>	<u>\$271,179</u>	<u>100.00%</u>

As a small insurer, DGMIC's results are heavily impacted by fixed costs. As indicated by the data above, the Company has controlled its loss adjusting and underwriting expenses. The Company does receive a large commission from its ceded reinsurance program; at year end 2008, DGMIC reported a commission receivable of \$91,197 for its reinsurance program. (This amount is netted against Ceded Reinsurance Premiums Payable in the financial statements of this report).

The number of the Company's policyholders at the respective year end was as follows:

2005	1,484
2006	1,515
2007	1,564
2008	1,587

### **TERRITORY AND PLAN OF OPERATION**

The Company is licensed to transact business only in the State of Delaware. The Company is authorized to write the following lines of business: property; casualty, including liability; burglary & theft; personal property floater; and glass.

A breakdown by the Company's direct premiums written for 2008 by line of business noted the following:

Delaware Grange Mutual Insurance Company

Fire	\$553,175
Homeowners multiple peril	345,617
Inland marine	2,439
Other liability	<u>7,818</u>
Total Direct Premiums Written	<u>\$909,049</u>

The Company's business is produced by independent agents who do have binding authority. Presently, DGMIC has appointed 62 agents representing 26 agencies. Most of the Company's business is written in Kent and Sussex Counties of Delaware.

**REINSURANCE**

For the year ended December 31, 2008, the Company reported the following distribution of premiums written:

Direct	\$ 909,049
Assumed	
Ceded	<u>(661,817)</u>
Net	<u>\$ 247,232</u>

As indicated, DGMIC ceded 72.8% of its direct premiums in 2008. At the 2003 examination date, the Company ceded 62.7% of its direct premium.

As of December 31, 2008, the Company's ceded reinsurance program was as follows:

**Property**

**Obligatory First Surplus Treaty**

Coverage: 10 times the Company's net retention, with a maximum cession of \$400,000. The Company's minimum retention on all risks is \$20,000.

**Commission:** The provisional commission is 35%, however, the Company is eligible to receive up to a 50% commission based on claims experience. Similarly, the Company's commission can be reduced to 32.5% based on claims experience.

Aggregate Excess of Loss Reinsurance

**Coverage:** The reinsurer is liable for 95% of 320% of subject net premiums earned, or 95% of \$1,286,400, whichever is lesser in excess of 70% of gross net premiums earned, or \$187,600, whichever is greater.

Supplemental Excess of Loss Reinsurance

**Coverage:** The reinsurer will provide coverage of 100% of 610% of the Company's gross net premiums earned or \$2,043,500 whichever is lesser, in excess of an amount equal to the sum of the Company's net retention plus coverage provided by the Aggregate Excess of Loss Reinsurance coverage.

**Casualty**

Excess of Loss First Layer: Coverage is 100% of \$580,000 in excess of \$20,000 net loss per occurrence, covering bodily injury and property damage, including medical payments.

Second Layer: \$500,000 excess \$500,000 combined net loss, per occurrence.

The Company's ceded reinsurance program did not change significantly in 2009.

**ACCOUNTS AND RECORDS**

For the 2008 Annual Statement, the Company's financial statements were prepared by the accounting firm of Buffamante Whipple Buttafaro, P.C. (BWB). The workpapers of BWB were reviewed.

At this time, the Company is exempt from having an annual audit performed.

The examination noted the following instance where the Company did not report annual statement items in accordance with SSAP and the NAIC Annual Statement Instructions:

- Employee withholding taxes were reported as Taxes, Licenses and Fees. These taxes should have been reported as Amounts Withheld for the Account of Others.

**It is recommended the Company prepare its financial statements and report individual line items in accordance with SSAP and the NAIC Annual Statement Instructions.**

The examination noted that DGMIC does not have contracts with its accounting firm, its actuarial firm, or the adjusting firm that handles all the Company's claims activity.

**For the Company's protection: it is recommended the Company execute contracts with its accounting, actuarial and claims adjusting firms. Said contracts should detail each party's obligations and responsibilities, and include a listing of fees and services.**

**FINANCIAL STATEMENTS**

The Company's financial position on December 31, 2008 and the results of operations for 2008 are presented in the following statements:

**ASSETS**

	<u>Assets</u>	Nonadmitted <u>Assets</u>	Net Admitted <u>Assets</u>	Notes
Bonds	\$446,020		\$446,020	1
Preferred Stock	220,239		220,239	
Cash, Cash Equivalents, Short-Term Investments	487,416		487,416	
Investment Income Due and Accrued	4,149		4,149	
Uncollected Premiums:				
In Course of Collection	10,064	\$686	9,378	
Deferred Premiums	1,982		1,982	
Amts Recoverable from Reinsurers	2,161		2,161	
Net Deferred Tax Asset	25,499	282	25,217	
Electronic Data Processing Equip.	504		504	
Furniture and Equipment	14,793	14,793		
Aggregate Write-In Items	<u>4,010</u>	<u>0</u>	<u>4,010</u>	
Totals	<u>\$1,216,837</u>	<u>\$15,761</u>	<u>\$1,201,076</u>	

**LIABILITIES, SURPLUS AND  
OTHER FUNDS**

		Notes
Losses	\$30,499	2
Loss Adjustment Expenses	13,000	
Commissions Payable	11,593	
Other Expenses	11,000	
Taxes, Licenses and Fees	4,962	
Advance Premium	18,518	
Unearned Premiums	160,108	
Ceded Reinsurance Premiums Payable	<u>(58,588)</u>	
Total Liabilities	<u>\$191,092</u>	
Surplus Notes	\$ 150,000	3
Unassigned Funds	<u>859,984</u>	
Surplus as Regards Policyholders	<u>\$1,009,984</u>	
Total Liabilities and Surplus as Regards Policyholders	<u>\$1,201,076</u>	

**STATEMENT OF INCOME**

Premiums Earned	\$240,121
Losses Incurred	71,140
Loss Adjustment Expenses Incurred	31,034
Other Underwriting Expenses Incurred	<u>96,563</u>
Total Underwriting Deductions	<u>\$198,737</u>
Net Underwriting Gain	\$ 41,384
Net Investment Income Earned	24,200
Finance and Service Charges	<u>4,054</u>
Net Income	\$69,638
Surplus as Regards Policyholders- Previous Year	\$971,379
Net Income	69,638
Change in net deferred income tax	(22,335)
Change in nonadmitted assets	(2,688)
Change in Net Unrealized Capital Gains/-Losses	<u>(6,010)</u>
Change in Surplus as Regards Policyholders	<u>\$38,605</u>
Surplus as Regards Policyholders- Current year	<u>\$1,009,984</u>

**SCHEDULE OF EXAMINATION ADJUSTMENTS**

The examination will propose no adjustments.

**NOTES TO FINANCIAL STATEMENTS**

**Note #1**  
**Investments**

Most of DGMIC's investment securities are held at US Bank without the benefit of a custodian agreement.

**It is recommended the Company enter into a custodian agreement for its investment securities. The custodian agreement should contain the safeguard language recommended in the NAIC Examiners Handbook.**

**Note #2**

Losses	\$30,499
<u>Loss Adjustment Expenses(LAE)</u>	<u>\$13,000</u>

The Company's reported Loss reserves amounts at December 31, 2008 were comprised of the following

Case - Direct	\$ 102,200
Assumed	
Ceded	<u>( 72,701)</u>
Net	\$ 29,499
IBNR - Direct	\$ 2,000
Assumed	
Ceded	<u>(1,000)</u>
Net	\$ 1,000
Total	<u>\$ 30,499</u>

The Company's Loss and LAE reserves were tested through a review of open claim files at December 31, 2008, and through a review of Loss and LAE activity in 2009.

The examination noted that due to the small size of the Company, adverse development on a single claim can impact the Company. That situation occurred in 2009 when payments on one claim exceeded the reserve at year end 2008 by 100%. Much of the negative development was absorbed by ceded reinsurance.

The examination noted that DGMIC's reserve for Incurred But Not Reported Losses (IBNR) at year end 2008 was just \$2,000 on a direct basis and \$1,000 as a net reserve. Through June 30, 2009, DGMIC reported three claims with incurred dates prior

to December 31, 2008. The net incurred on the IBNR claims was \$7,545 through June 30, 2009. The examination review of the Company's quarterly statements ( see next paragraph) noted an exception as per the reporting of the Company's IBNR claims in 2009.

Subsequent Event:

The Company's quarterly financial statements filed with the Delaware Insurance Department in 2009 were reviewed. As per June 30, 2009, DGMIC reported the following amounts that were compared to financial statements as of December 31, 2008:

	<u>6/30/2009</u>	<u>12/31/2008</u>
Assets	\$1,101,782	\$1,201,076
Liabilities	171,692	191,092
Policyholders Surplus	930,090	1,009,984
Net Income	(64,086)	69,638

The negative Net Income and decrease in Policyholders Surplus was caused by loss activity, primarily adverse development of the Loss and LAE reserves as of December 31, 2008.

As part of the Subsequent Events review, the Loss and Loss Adjustment Expense Reserves Schedule as of June 30, 2009 was reviewed. This schedule provides a run-off development of the Company's Loss and LAE reserves as of 12/31/2008. It was noted that the Company did not prepare the Schedule correctly. All amounts reported in Column 5, Losses and LAE paid in 2009 on claims not reported as of December 31, 2008 are reported by the Company to be losses with incurred dates in 2009. The examination noted that three IBNR claims with incurred dates in December 2008 were reported and paid in 2009.

**It is recommended the Company properly prepare the Loss and Loss Adjustment Expense Reserve Schedule in the quarterly financial statements filed with the Delaware Insurance Department. Specifically, the Company should report losses in the correct incurred year.**

**Note #3**

**Surplus Notes**

During 2003, the Company's Surplus as Regards Policyholders fell below the minimum amount of \$750,000 as required by the Delaware Insurance Code. To bring its Policyholder Surplus into compliance with the Code, the Company issued a Surplus Note in the amount of \$100,000 to First National Bank of Wyoming. In 2004, the Company cancelled the first surplus note and issued a second note in the amount of \$150,000, also to First National Bank of Wyoming. The Surplus Note contains the usual statutory requirements as per the payment of principal and interest, and was approved by the Delaware Insurance Department.

**STATUS OF PREVIOUS EXAMINATION RECOMMENDATIONS**

The prior examination report as of December 31, 2003, contained three recommendations. Two of the recommendations related to the Company's bylaws. See the Membership section of this report for a review of the change in the Company's bylaws. The third recommendation noted that the Company did not report annual statement items in accordance with the NAIC Annual Statement instructions. That recommendation is repeated in this report.

## **RECOMMENDATIONS**

The Company's attention is directed to the following examination recommendations:

It is recommended the Company submit its bylaws to the Delaware Insurance Department in accordance with Section 4912 of the Insurance Code. (p.3)

It is recommended that all members of the Board of Directors who are insurance agents sign conflict of interest acknowledgements, and that conflict of interest acknowledgements be executed by all insurance agents on a regular basis.(p.5)

It is recommended the Company prepare its financial statements and report individual line items in accordance with SSAP and the NAIC Annual Statement Instructions. (p.10)

For the Company's protection: it is recommended the Company execute contracts with its accounting, actuarial and claims adjusting firms. Said contracts should detail each parties' obligations and responsibilities, and include a listing of fees and services. (p.10)

It is recommended the Company enter into a custodian agreement for its investment securities. The custodian agreement should contain the safeguard language recommended in the NAIC Examiners Handbook. (p.14)

It is recommended the Company properly prepare the Loss and Loss Adjustment Expense Reserve Schedule in the quarterly financial statements filed with the Delaware Insurance Department. Specifically, the Company should report losses in the correct incurred year. (p.16)

**SUMMARY COMMENTS**

The following items of significance were noted during the examination:

- The Company's Policyholders Surplus increased by \$249,048 or 32.7% during the period under examination.
- DGMIC reported positive Net Income in each year of the four year period from January 1, 2005 to December 31, 2008.
- The Company's direct premiums increased each year under examination, though it is noted that from October, 2003 to September, 2006, DGMIC's writing of new business was restricted.
- DGMIC cedes a significant portion of its direct premiums. For 2008, the Company ceded 72.8% of its direct premiums, and reported a ceded commission receivable amount of \$91,197 at year end 2008.

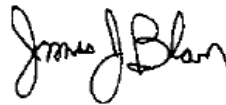
**CONCLUSION**

The following schedule shows the results of this examination and the results of the prior examination with changes between the examination periods:

<u>Description</u>	<u>Current Examination</u>	<u>12/31/03 Examination</u>	<u>Changes Increases (Decreases)</u>
Assets	\$1,201,076	\$1,028,903	\$172,173
Liabilities	191,092	267,967	(76,875)
Policyholders Surplus	1,009,984	760,936	249,048

The examination was conducted by the undersigned.

Respectfully submitted,



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James J. Blair Jr., CFE, CPA  
Examination Supervisor  
Insurance Department  
State of Delaware