

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

REPORT OF EXAMINATION

OF

**FLAXTON FARMERS MUTUAL FIRE
INSURANCE COMPANY**

BOWBELLS, NORTH DAKOTA

**AS OF
DECEMBER 31, 2017**

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


Flaxton Farmers Mutual Fire Insurance Company

Bowbells, North Dakota

as of December 31, 2017, 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 6th day of
December, 2018.





Jon Godfread
Commissioner of Insurance

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October 5, 2018
Bowbells, North Dakota

Honorable Jon Godfred
Commissioner of Insurance
North Dakota Insurance Department
600 East Boulevard Avenue
Bismarck, ND 58505

Dear Commissioner:

Pursuant to your instructions and statutory requirements, an examination was made of the books, records and financial condition of

Flaxton Farmers Mutual Fire Insurance Company

Bowbells, North Dakota

Flaxton Farmers Mutual Fire Insurance Company, hereinafter referred to as "the Company", was last examined as of December 31, 2012, by representatives of the State of North Dakota.

SCOPE OF STATUTORY EXAMINATION

This examination was a financial condition examination conducted in accordance with North Dakota Century Code (N.D.C.C.) § 26.1-03-19.3 and the guidelines and procedures contained in the NAIC Financial Condition Examiners Handbook. The examination was conducted to determine the Company's financial condition, its compliance with statutes, and to review the corporate affairs and insurance operations. This statutory examination covers the period from January 1, 2013, to December 31, 2017, including any material transactions and/or events occurring subsequent to the examination date and noted during the course of this statutory examination.

STATUS OF PRIOR EXAM FINDINGS

Our examination included a review to determine the current status of the twelve exception conditions commented upon in our preceding Report on Examination which covered the period from January 1, 2013 to December 31, 2017. We determined that the Company had satisfactorily addressed all of these items, except the following:

Recommendation

It is recommended that the Board of Directors or a Board-appointed Investment Committee thereof approve investment transactions and review the Company's investment guidelines pursuant to N.D. Admin Code § 45-03-12-05(3-4).

Response

The Company did not completely comply. Two quarters during the examination period noted no approval of investment transactions. **It is again recommended that the Board of Directors or a Board-appointed Investment Committee thereof**

Recommendation

Response

approve investment transactions and review the Company's investment guidelines pursuant to N.D. Admin Code § 45-03-12-05 (3-4).

Findings and recommendations related to the above areas are addressed under various captions below for the current period under examination.

SUBSEQUENT EVENTS

The meeting minutes and general ledger were reviewed through June 2018. On June 6 2018, Courtney Seime succeeded James Anderson as the Secretary-Manager of the Company.

HISTORY

The Company was incorporated on February 6, 1906, as "The Flaxton Farmers Mutual Fire Insurance Company of Ward County", and commenced business on June 10, 1906.

At the annual meeting of policyholders, held on July 19, 1975, the Articles of Incorporation were officially amended, changing the name of the Company to "Flaxton Farmers Mutual Fire Insurance Company".

The Company's term of existence is perpetual as provided by N.D.C.C. § 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 and lightning. During 1963, the Company extended its coverage to include the perils of windstorm, hail, explosion, aircraft or vehicles, smoke, riot, theft of personal property, injury or death of livestock, overturn or collision of farm machinery, vandalism or malicious mischief and additional living expenses.

MANAGEMENT AND CONTROL

Membership

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 the Board of Directors who are elected for staggered terms of three years by the membership at the annual meeting. 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, 2017, were as follows:

Director	Term Expires	Occupation
Nathan Jepsen Bowbells, ND	2020	CPA, Farmer
Ted Hawbaker Portal, ND	2020	Farmer
Douglas Winzenburg Bowbells, ND	2019	Farmer
Arlan Espeseth Portal, ND	2019	Custom's Broker
Jerol Staael Stanley, ND	2018	Retired Farmer
Tom Dhuyvetter Noonan, ND	2018	Farmer

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, 2017, were as follows:

<u>Name</u>	<u>Office</u>
Nathan Jepsen	President
Jerol Staael	Vice President
James Anderson	Secretary-Treasurer

Committees

The Board annually appoints three members to the Finance Committee to meet on an as-needed basis. The committee did not meet during the exam period. Membership at December 31, 2017 was:

Jerol Staael, President
 Douglas Winzenburg, Director
 James Anderson, Secretary-Treasurer

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.

There were no amendments to the Bylaws or Articles of Incorporation during the period under examination.

Members

During the period under examination the annual meetings of the policyholders were held in accordance with the Company's Bylaws on the following dates: June 5, 2013; June 4, 2014; June 3, 2015; June 1, 2016; and June 7, 2017.

Directors

During the period under examination, the Board of Directors held the following number of meetings annually:

2013	2014	2015	2016	2017
4	4	4	5	8

Approval of Investments

For two quarters in 2017, the minutes of the Board of Directors did not reflect approval of investment transactions as required by N.D. Admin. Code § 45-03-12-05 which states:

3. Investments shall be acquired and held under the supervision and direction of the board of directors and the board shall evidence by formal resolution, at least annually, that it has determined whether all investments have been made in accordance with delegations, standards, limitations, and investment objectives prescribed by the board or a committee of the board charged with the responsibility to direct its investments.
4. On no less than a quarterly basis, the board of directors or committee of the board of directors shall:
 - a. Receive and review a summary report on the insurer's investment portfolio, its investment activities, and investment practices engaged in under delegated authority, in order to determine whether the investment activity of the insurer is consistent with its written plan; and
 - b. Review and revise, as appropriate, the written plan.

It is again recommended that the Board of Directors or a Board-appointed Investment Committee thereof approve investment transactions and review the Company's investment guidelines pursuant to N.D. Admin. Code § 45-03-12-05 (3-4).

CONFLICT OF INTEREST

The Company's conflict of interest policy and annual conflict disclosures were reviewed for the period under examination. No material conflicts were noted.

EMPLOYEES WELFARE AND PENSION PLANS

At December 31, 2017, the Company offered no employee welfare or pension plans.

FIDELITY BOND AND OTHER INSURANCE

The Company has a fidelity bond in force which provides \$75,000 coverage for losses associated with employee dishonesty. The coverage meets the minimum recommended amount of fidelity insurance suggested in the NAIC's *Financial Examiners Handbook*.

The Company is covered by a professional liability and directors and officers liability policy with a \$2 million dollars per occurrence and a \$2 million dollar aggregate limit each policy year, subject to a \$5,000 deductible per claim. The policy provides coverage for errors or omissions in the performance of professional services and wrongful acts of a director or officer while acting solely in their individual or collective capacities as directors and officers.

The Company also is covered under a commercial general liability policy. Limits under this policy include a \$2 million dollar general aggregate limit, \$1 million dollar per occurrence, \$1 million dollar personal and advertising injury, \$100,000 fire damage liability, \$5,000 medical expenses.

The Company does not carry insurance on its furniture, fixtures, records, and files against insurable hazards.

TERRITORY AND PLAN OF OPERATION

At December 31, 2017, the Company had 37 licensed agents and was authorized to transact business within the following counties:

Bottineau	Burke	Divide	McHenry	McKenzie
McLean	Mercer	Mountrail	Nelson	Renville
Sheridan	Ward	Williams		

The Company paid commissions to these 37 agents through nine agencies. None of these agencies were appointed to produce business for the Company. Per N.D.C.C. § 26.1-26-06:

An insurance producer may not act as an agent of an insurer unless the insurance producer becomes an appointed insurance producer of that insurer.

Because the Company paid commissions to these agencies, rather than to its appointed agents directly, the Company is required to appoint these agencies as licensed producers.

It is recommended that the Company only produce business through appointed agents and agencies in accordance with N.D.C.C. § 26.1-26-06.

At December 31, 2017, the Company insured a nonresidential risk that was used by the general public within the platted limits of an incorporated city. Per N.D.C.C. § 26.1-13-15(3):

A policy may not be issued covering property located within the platted limits of an incorporated city in this state, except the policy may provide coverage as specified under sections 26.1-13-14 and 26.1-13-16 within the platted limits of the incorporated city on:

- a. The place of residence;
- b. A rental property that is no larger than a four residential rental unit;
- c. A nonresidential property that is not used by the general public; or
- d. A nonresidential property that is part of an existing policy.

It is recommended that the Company non-renew the identified publically accessible nonresidential risk located within the platted limits of an incorporated city and discontinue the practice of insuring risks that do not comply with N.D.C.C. § 26.1-13-15.

SIGNIFICANT OPERATING RESULTS

Growth

The following exhibit reflects the growth of the Company for the 10-year period ended December 31, 2017. Data from 2008 through 2012 is compiled from the prior statutory examination. Data with respect to the years 2013 through 2017 is as compiled from home office copies of the filed Annual Statements. The operational results are presented on a modified cash basis.

Year	Admitted Assets	Total Liabilities	Surplus as Regards Policyholders	Net Premiums Written	Underwriting Deductions	Investment And Other Income	Net Income (Loss)
2008	1,950,696	514,734	1,435,962	711,797	733,107	98,247	36,937
2009	2,155,789	534,750	1,621,039	752,007	669,820	68,044	150,231
2010	2,149,017	550,380	1,598,637	838,467	948,125	95,842	(13,816)
2011	2,278,998	647,819	1,631,179	896,155	814,658	81,802	163,299
2012	2,577,081	928,012	1,649,069	1,031,113	872,680	79,189	237,622
2013	2,813,291	1,007,342	1,805,949	1,208,368	1,006,020	75,602	277,950

2014	3,083,707	1,012,233	2,071,474	1,303,808	1,258,913	81,274	126,169
2015	3,275,803	1,033,966	2,241,837	1,291,045	1,230,055	134,198	195,188
2016	2,957,041	960,921	1,996,120	1,280,803	1,630,815	70,936	(279,076)
2017	2,997,142	1,050,616	1,946,526	1,350,794	1,527,194	90,106	(86,294)

Operating Ratios

The underwriting ratios presented below are on a cash basis and encompass the five-year period ending December 31, 2017:

	2017	2016	2015	2014	2013
Premiums	100%	100%	100%	100%	100%
Deductions:					
Losses and Loss Adjustment	69.5	79.3	46.2	41.1	35.4
Underwriting Expenses	43.6	48.1	49.1	55.4	47.9
Total (Operating Ratio)	113.1	127.3	95.3	96.6	83.3
Net Underwriting Gain (Loss)	(13.1)	(27.3)	4.7	3.4	16.7

MARKET CONDUCT ACTIVITY

Treatment of Policyholders

Claims Based on a limited review of claim files, the Company pays claims fairly within policy provisions upon receipt of satisfactory proof of loss or damage.

Advertising The Company's advertising consists primarily of newspaper, radio, and miscellaneous ads (i.e. county fair). The advertising material was reviewed and did not appear to be deceptive.

OPERATING AGREEMENTS

Investment Advisor Services

On May 11, 2015, the Company entered into an agreement with Stonebridge Capital Advisors, LLC (Stonebridge), a Registered Investment Advisor (RIA), to manage its invested assets. The agreement grants Stonebridge discretionary authority, subject to written investment objectives and restrictions that are approved by the Board of Directors. As compensation for these services, Stonebridge charges the Company an annual fee (billed quarterly) of 65 basis points or 0.65 percent of the market value of the Company's assets under its management.

Custodial Agreements

The Company executed an agreement with Fidelity Brokerage Services, LLC and National Financial Services, LLC (Fidelity) on April 19, 2017 to hold its securities. This agreement was reviewed and found to be in compliance with N.D. Admin. Code § 45-03-23-02.

Office Rental Agreement

The Company has an office lease agreement with Bowbells Development Corporation which began on July 1, 2003 and renews annually or until either party gives written notice of termination. At December 31, 2017, the Company's monthly rent was \$600.

Loss Adjusting/ Inspection Services

During the examination period, the Company contracted with Hartland Mutual Insurance Company (Hartland) to perform claims adjusting and inspection services. The Agreement sets the fees for inspection and/or adjustment at \$45 per hour, plus any direct fees incurred.

Agency Agreements

At December 31, 2017, the Company had written agency agreements with each of the agents that it paid commissions to during the year. The Agreement outlines the commission rates for new and renewal business, the Company's contingent bonus commission criteria, and the renewal ownership details.

OPERATIONS REVIEW

No operations reviews were completed by Grinnell Mutual Reinsurance Company during the examination period.

REINSURANCE

The following is a summary of the Company's most significant reinsurance contracts in force at December 31, 2017:

Grinnell Mutual Reinsurance Company

Nonaffiliated Ceding Contract:

Type:	Excess of Loss
Reinsurer:	Grinnell Mutual Reinsurance Company
Scope:	All policy forms and endorsements issued by the Company
	(A) Property Per Risk Excess of Loss – Covers up to \$20 million in losses from fire and windstorm risks written by the Company in excess of a \$175,000 retention.

- (B) Property Catastrophe Excess of Loss – Covers 100 percent of the Company's net losses incurred from windstorm, hail, or tornado loss occurrences within a period of 96 consecutive hours, in excess of a \$500,000 retention.
- (C) Property Aggregate Excess of Loss - Provides coverage for 100 percent of the Company's aggregate net losses in excess of a defined annual retention limit. The retention limit for 2017 was \$1,000,000.

Premium:

- (A) Property Per Risk Excess of Loss - The 2017 annual premium was \$66,200.
- (B) Property Catastrophe Excess of Loss – The 2017 annual premium was \$182,800.
- (C) Aggregate Excess - The 2017 annual premium was \$122,000.

Termination Date: The agreement may be terminated by either party with a written 90 day notice.

The contract contained all of the clauses required by the NAIC's *Accounting Practices and Procedures Manual*.

ACCOUNTS AND RECORDS

The Company's accounting procedures, internal controls, and transaction cycles were reviewed during the course of the examination and a trial balance as of December 31, 2017, was traced to the appropriate schedules of the Company's 2017 Annual Statement. Revenues and expenses were test checked to the extent deemed necessary.

FINANCIAL STATEMENTS

The following pages present a Statement of Assets, Liabilities, and Surplus as of December 31, 2017, and an Statement of Income for 2017.

These financial statements are based on the statutory financial statements filed by the Company with the North Dakota Insurance Department and present the financial condition of the Company for the period ending December 31, 2017. The accompanying comments on financial statements reflect any examination adjustments to the amounts reported in the annual statement and should be considered an integral part of the financial statements.

Flaxton Farmers Mutual Fire Insurance Company
Statement of Assets, Liabilities, and Surplus
December 31, 2017

ASSETS:

LEDGER ASSETS:

Bonds	\$ 808,837	
Stocks	362,384	
Cash on Hand and Checking Accounts	23,253	
Cash on Deposit (Banks and Savings & Loans)	1,567,590	
TOTAL LEDGER ASSETS		\$2,762,064

NONLEDGER ASSETS:

Interest Due and Accrued on Bonds	\$ 6,625	
Interest Due and Accrued on Certificates of Deposit and Passbook Savings	2,171	
Assessments or Premiums in Course of Collection	51,535	
Market Value of Stocks over Book Value	83,770	
Reinsurance Recoverable on Paid Losses	6,421	
Federal Income Tax Recoverable	84,610	
TOTAL NONLEDGER ASSETS		235,132

DEDUCT: ASSETS NOT ADMITTED

Book Value Over Market Value	\$ 54	
TOTAL NONADMITTED ASSETS		54

TOTAL NET ASSETS ADMITTED		\$2,997,142
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LIABILITIES:

Unpaid Losses	\$ 79,994	
Incurred But Not Reported Claims	6,000	
Unpaid Loss Adjustment Expense	1,354	
Advanced Premiums	22,107	
Unearned Premium Reserve	863,747	
Commissions Due and Payable to Agents	20,433	
Unpaid Taxes	11,926	
Unpaid General Expenses	2,524	
Reinsurance Premiums Due and Payable	32,412	
Premiums Written for Others	6,762	
Amounts Withheld for Others	3,357	
TOTAL LIABILITIES		\$ 1,050,616

SURPLUS TO POLICYHOLDERS		\$ 1,946,526
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TOTAL LIABILITIES AND SURPLUS		\$ 2,997,142
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Flaxton Farmers Mutual Fire Insurance Company
Statement of Income
For the Year 2017

INCOME:

Gross Premium Income	\$1,767,706	
Less: Returned Premiums	26,211	
Premiums for Reinsurance Ceded	390,701	
NET PREMIUM INCOME		\$1,350,794
Interest on Bonds		\$ 15,146
Dividends on Stocks		10,140
Interest on Cash on Deposit		10,090
Profit on Sale or Maturity of Ledger Assets		2,356
Commissions and Service Fees Received		29,677
Federal Tax Refund		22,684
Miscellaneous Income		14
TOTAL INCOME RECEIPTS		<u>\$1,440,901</u>

DISBURSEMENTS:

Gross Losses Paid that Occurred During Current Year	\$ 1,059,183	
Gross Losses Paid Current Year but Occurred in Previous Years	286,355	
Deduct: Salvage	18,600	
Reinsurance Recovered	411,707	
NET LOSSES PAID		\$915,231
Claim Adjustment Expenses		22,921
Commissions Paid to Agents		280,500
Directors' Fees and Expenses		6,351
Salaries to Employees		184,252
Printing, Stationery, and Office Supplies		942
Rent and Rent Items Including Self Rent for Company's Occupancy		7,200
State and Local Insurance Taxes		30,021
Insurance Department Licenses and Fees		525
Payroll Taxes		14,266
Legal Fees and Auditing		1,833
Travel and Travel Items		3,614
Advertising		1,864
Dues and Donations		9,380
Insurance and Bonds		4,718
Postage, Telephone, Internet, and Bank Charges		10,491
Employee Relations and Welfare		1,678
Data Processing Expenses		21,181
Custodial and Investment Management Fees		9,723
Annual Meeting Expense		1,222
Change in Liabilities for Payroll Withholdings/Suspense Account		(1,145)
Miscellaneous Expenses		426
TOTAL FUNDS DISBURSED		<u>\$ 1,527,194</u>
NET GAIN (LOSS)		<u><u>\$(86,293)</u></u>

COMMENTS ON FINANCIAL STATEMENTS

Financial statement balances at December 31, 2017, are commented upon only if financial changes, recommendations, or special explanations are considered necessary.

Assets

Reinsurance Recoverable on Paid Losses

At December 31, 2017, the Company had unreported reinsurance recoverables on paid losses totaling \$6,421 as shown below:

<u>Description</u>	<u>Company</u>	<u>Examination</u>
Reinsurance Recoverable on Paid Losses	\$ 0	\$ 6,421
Total	<u>\$ 0</u>	<u>\$ 6,421</u>

It is recommended that the Company complete a monthly reconciliation from the Claims Log to the reinsurance treaties in force to ensure the proper submission of all potential reinsurance recoverables.

Liabilities

Advance Premiums

The report used by the Company to determine its Advance Premium Liability was automatically cut-off on January 2, 2018 instead of December 31, 2017, which caused seven policies to be incorrectly excluded from the listing of Advance Premiums. This error caused an understatement of \$4,565.

Also, the Company incorrectly included commissions payable in its advance premium calculation which caused an overstatement of \$3,033. The net effect of these two errors was an understatement of the liability by \$1,532 as shown below:

<u>Description</u>	<u>Company</u>	<u>Examination</u>
Advance Premiums	\$ 20,575	\$ 22,107
Total	<u>\$ 20,575</u>	<u>\$ 22,107</u>

Commissions Due and Payable to Agents

As addressed within the Advance Premiums section above, the Company incorrectly included commissions payable to Agents in its Advance Premium Liability entry which caused an understatement in the Commissions Due and Payable to Agents in the amount of \$3,033.

<u>Description</u>	<u>Company</u>	<u>Examination</u>
Commissions Due and Payable to Agents	\$17,400	\$20,433
Total	<u>\$ 17,400</u>	<u>\$ 20,433</u>

It is recommended that the Company report its advance premiums net of commissions.

Surplus to Policyholders

Surplus to policyholders was determined by this examination to be \$1,946,526 or \$1,856 more than the amount reported by the Company. Adjustments to surplus are shown in the following schedule:

Description	Company	Examination	Increase (Decrease) to Surplus
<u>Non-Ledger Assets:</u>			
Reinsurance Recoverable on Paid Losses	\$ 0	6,421	6,421
<u>Liabilities:</u>			
Advance Premiums	20,575	22,107	(1,532)
Commissions Due and Payable to Agents	17,400	20,433	(3,033)
Net Increase			<u>\$ 1,856</u>
Surplus to Policyholders as reported by Company	\$ 1,944,670		
Increase(Decrease) to Surplus from above			<u>1,856</u>
Surplus to Policyholders per Examination	\$ 1,946,526		

CONCLUSION

The financial condition of Flaxton Farmers Mutual Fire Insurance Company, Bowbells, North Dakota, as determined by this examination is summarized as follows:

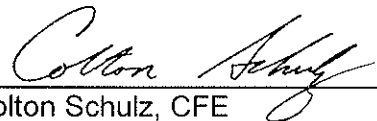
TOTAL ADMITTED ASSETS		<u>\$2,997,142</u>
Liabilities	\$ 1,050,616	
Surplus to Policyholders	<u>1,946,526</u>	
TOTAL LIABILITIES AND SURPLUS		<u>\$2,997,142</u>

Since the last examination conducted as of December 31, 2012, the Company's admitted assets have increased \$420,061, its total liabilities have increased \$122,604, and its surplus as regards policyholders has increased \$297,457.

In addition to the undersigned, North Dakota Insurance Department Examiner Andrea Rebsom participated in this examination.

The Examiners express their appreciation for the courteous cooperation extended them during the course of this examination.

Respectfully submitted,



Colton Schulz, CFE
Supervising Examiner
North Dakota Insurance Department

COMMENTS AND RECOMMENDATIONS

It is again recommended that the Board of Directors or a Board-appointed Investment Committee thereof approve investment transactions and review the Company's investment guidelines pursuant to N.D. Admin. Code § 45-03-12-05 (3-4).

It is recommended that the Company non-renew the identified publically accessible nonresidential risk located within the platted limits of an incorporated city and discontinue the practice of insuring risks that do not comply with N.D.C.C. § 26.1-13-15.

It is recommended that the Company only produce business through appointed agents and agencies in accordance with N.D.C.C. § 26.1-26-06.

It is recommended that the Company complete a monthly reconciliation from the Claims Log to the reinsurance treaties in force to ensure the proper submission of all potential reinsurance recoverables.

It is recommended that the Company report its advance premiums net of commissions.