

REPORT ON EXAMINATION

of the

**TENNESSEE FARMERS MUTUAL INSURANCE COMPANY
147 BEAR CREEK PIKE
COLUMBIA, TENNESSEE**

as of

DECEMBER 31, 2005

DEPARTMENT OF COMMERCE AND INSURANCE

STATE OF TENNESSEE

NASHVILLE, TENNESSEE

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Columbia, Tennessee
June 13, 2008

Honorable Leslie A. Newman
Commissioner
State of Tennessee
Department of Commerce and Insurance
Nashville, Tennessee 37243

Dear Commissioner:

Pursuant to your instructions and in accordance with Tennessee Insurance Laws, regulations, and resolutions adopted by the National Association of Insurance Commissioners (NAIC), a financial examination was made of the condition and affairs of the

TENNESSEE FARMERS MUTUAL INSURANCE COMPANY
147 BEAR CREEK PIKE
COLUMBIA, TENNESSEE 38401

hereinafter and generally referred to as the Company, and a report thereon is submitted as follows:

INTRODUCTION

This examination was called by the Commissioner of Commerce and Insurance of the State of Tennessee on August 7, 2006. On-site examination work commenced on September 25, 2006. With the Company having authority to write business only in the State of Tennessee, the examination was not classified as an Association Examination under NAIC Guidelines. The examination was performed by duly authorized representatives of the Department of Commerce and Insurance, State of Tennessee ("TDCI") and was conducted simultaneously with three (3) other insurance companies in the Tennessee Farmers Insurance Group, all based in Columbia, Tennessee as follows:

Tennessee Farmers Assurance Company
Tennessee Farmers Life Insurance Company
Tennessee Farmers Life Reinsurance Company

SCOPE OF EXAMINATION

This examination report covers the period from January 1, 2001 to the close of business on December 31, 2005, and includes any material transactions and/or events occurring subsequent to the examination date and noted during the

course of the examination.

The examination of the financial condition was conducted in accordance with guidelines and procedures contained in the NAIC Financial Condition Examiners Handbook. During the course of examination, assets were verified and valued and liabilities were determined and estimated as of December 31, 2005. The financial condition of the Company and its amount of solvency were thereby established. Test checks were made of income and disbursement items for selected periods, and a general review was made of the Company's operations, practices, and compliance with applicable statutes and regulations. All asset and liability items contained in the financial statement of this report were examined and verified with relative emphasis according to their amount and potential impact on capital and surplus.

In addition, the following topics were reviewed:

- Comments – Previous Examinations
- Company History
- Charter and Bylaws
- Management and Control
- Corporate Records
- Fidelity Bonds and Other Insurance
- Territory (includes inforce/premium by state)
- Plan of Operation
- Reinsurance
- Retirement Plan and Other Employee Benefits
- Loss Experience
- Accounts and Records
- Statutory Deposits
- Agreements with Parent, Subsidiaries and Affiliates
- Pecuniary Interest Tenn. Code Ann. § 56-3-103
- Commission Equity
- Dividends or Distributions
- Litigation
- Subsequent Events
- Financial Statement

COMMENTS –PREVIOUS EXAMINATIONS

The previous financial examination was conducted as of December 31, 2000, by authorized representatives of the TDCI. This examination resulted in a decrease of \$13,248,809 in surplus due to an adjustment in the value of common stock investments owned in subsidiary corporations, TFIC, Inc., TFHC, Inc. and Tennessee Farmers Life Insurance Company. This adjustment was related to mortgage loans in default held by the referenced subsidiaries and the related

accrued investment income in addition to impaired common stock held by TFIC, Inc.

No regulatory requirements resulted from the previous examination. Several comments were made in the previous examination report to which the Company made a formal reply. These comments and replies are outlined as follows:

- **Registered Agent:** The report cited the comment from the examination as of December 31, 1995 stating that the Registered Agent for the Company had changed and that this was not reflected via a charter amendment. The Company advised that the change of registered agent is made in the annual filing with the Secretary of State, State of Tennessee and does not warrant a change in the charter. The TDCI has made no regulatory requirement in this matter and no charter amendment has been deemed necessary.
- **Corporate Records – Board Approval for Actuaries and Independent Auditors:** The report cited the fact that formal board approval was absent for the actuary and independent auditor for the years under examination. The Company agreed with finding; however, their reply stated that formal approval was present for subsequent years. Said approval was also verified during the current examination.
- **Insurance Products and Related Practices – Complaints:** The report stated that complaint information was recorded on logs in two different locations and that some information may have not been recorded. The Company responded that going forward all complaints would be recorded on the log located in the Chief Operating Officer's office which will centralize the information and resolution process.
- **Litigation and Contingent Liabilities:** The report referenced the Franchise and Excise Tax Audit by the Department of Revenue, State of Tennessee with an amount of \$5,287,684 assessed including interest. The Company subsequently paid the amount in question under protest and prepared to file legal suit to recover. The legal proceedings were terminated during 2006 and are discussed under the caption, "Litigation."

The United States Internal Revenue Service conducted an audit through year, 1997. Some adjustments resulted and these adjustments were carried forward to tax years, 1998 through 2000. These adjustments are of an immaterial overall amount. The Company agreed with the statement.

- **Commons Stocks:** Value was reduced by \$13,248,809 per examination due to default in mortgages held in subsidiaries and impaired assets held by TFIC, Inc. Company replied that said assets would be non-admitted by

a direct charge to surplus on future financial filings.

- Cash: The Company listed some money market investment accounts as cash rather than short-term investments in the 2000 Annual Statement. The Company replied that they were in agreement with said interpretation of NAIC Accounting Practices and Procedures and made the proper classification on future financial filings.

Findings reviewed during the present examination indicated that the Company has addressed all comments made during previous financial examinations.

During 2004, the TDCI performed a Target Financial Examination of the Company. The Report on Examination was made as of December 31, 2003 and was signed on December 22, 2004. The recommendations from the examination report are as follows:

- It is recommended that the Company file and report transactions within its holding company system in a holding company registration statement in accordance with Tenn. Code Ann. § 56-11-205.
- It is recommended that the Company's investment subsidiary, TFIC, Inc. should submit financial statements to the TDCI in accordance with SAP and NAIC Annual Statement instructions.
- It is recommended that the Company adopt a corporate investment policy for the Investment Committee with Board of Director level supervision and periodic review and approval.
- It is recommended that the Company revise its conflict of interest policy and procedures such that investments by the Company that create a conflict of interest in violation of Tenn. Code Ann. § 56-3-103 are identified and prevented.

Findings reviewed during the present examination indicated that the Company has complied with the above recommendations. As to the last recommendation, on April 25, 2005, Tenn. Code Ann. § 56-3-103 was amended and the Company's practices are in compliance with the statute as amended.

COMPANY HISTORY

The Company was incorporated on December 22, 1952 pursuant to the provisions of the General Corporate Act of Tennessee, Chapter 90 of the Public Acts of 1929, codified as Sections 3709-3771, inclusive, of the Williams Code of Tennessee.

The Company was organized as a successor corporation to the business and affairs of Tennessee Farmers Insurance Company, a stock Tennessee corporation, chartered on November 5, 1948 and located in Columbia, Tennessee. The effect of this reorganization was to convert the operations and business of Tennessee Farmers Insurance Company from a stock proprietorship to a mutual plan. On December 30, 1952 the Company commenced the transaction of insurance business as a state mutual insurance company.

During 1952 and 1953 the Company received subscriptions for advanced surplus and issued certificates in the aggregate amounts of \$348,400 and \$172,350 respectively, for a total of \$520,750 of which \$80,550 was advanced by the Tennessee Farm Bureau Federation of Columbia, Tennessee, and \$440,200 was advanced by 910 members of the Farm Bureau Federation. Subsequent to the issuance of the original surplus receipts, transfers of receipts have been made to other members of the Tennessee Farm Bureau Federation and many of these receipts have been redeemed. Therefore, as of December 31, 2005 a total of surplus-receipts were issued and outstanding in the aggregate amount of \$7,200.

Effective December 30, 1952 the Company was issued an initial Certificate of Authority by the Department of Insurance and Banking, State of Tennessee, (currently known as the Department of Commerce and Insurance, State of Tennessee) to transact the business of insurance in the State of Tennessee. On July 1, 1986 a perpetual certificate was issued which continues until suspended or revoked. This certificate was amended effective July 29, 1987 to include the Surety line of business. At the examination date, the Company is authorized to conduct the business of Property, Vehicle, Casualty and Surety in the State of Tennessee.

At December 31, 2005, the Company was licensed in one state, Tennessee.

The following exhibit depicts certain aspects of the growth and financial history of the Company since the previous examination, according to annual statements filed with the TDCI.

<u>Date</u>	<u>Earned Premiums</u>	<u>Incurred Losses & LAE</u>	<u>Admitted Assets</u>	<u>Liabilities</u>	<u>Total Surplus</u>
12/31/2001	\$288,937,884	\$220,120,469	\$1,229,585,476	\$245,989,841	\$983,595,635
12/31/2002	357,161,140	299,949,784	1,357,636,022	328,234,386	1,029,401,636
12/31/2003	344,311,711	305,664,431	1,426,088,040	358,649,639	1,067,438,401
12/31/2004	359,713,686	256,098,734	1,571,506,971	380,095,424	1,191,411,548
12/31/2005	389,828,726	270,108,990	1,675,650,110	344,572,603	1,331,077,507

CHARTER AND BYLAWS

Charter:

The Charter was filed and recorded with the Secretary of State, State of Tennessee on December 22, 1952. The Charter had been approved by the Department of Insurance and Banking, State of Tennessee on December 22, 1952.

The Charter provided for the operation of a mutual insurance company with a perpetual existence and established its location in Columbia, Maury County, Tennessee. The primary purposes are as follows:

1. "Operation of a mutual insurance company under and by virtue of the laws of the State of Tennessee, and particularly under and by virtue of Sections 6317-6440, inclusive, of Williams Code of Tennessee"
2. "Empowerment to make contracts of insurance and/or to reinsure or accept reinsurance upon a mutual basis for the kinds of insurance as follows

Fire
Liability
Disability
Automobile
Steam Boiler
Use and Occupancy
Miscellaneous (except Life)"

3. "Authorization of general and specific rights, privileges and powers of the Company consistent with the provisions of Sections 6317-6340, inclusive, of the Williams Code of Tennessee pertaining to mutual insurance companies and by virtue of the General Corporation Act of Tennessee, Chapter 90 of the Public Acts of 1929, Sections 3709-3771, inclusive, of the Williams Code of Tennessee"

The Company's charter requires the term of all officers to be established by the bylaws not to exceed two (2) years and a Board of Directors to be composed of not less than five (5) nor more than 25 members.

Bylaws:

The Restated Bylaws of the Company in effect at December 31, 2005 were enacted effective April 9, 1992 in order to comply with the Tennessee Corporation Act of 1986 and alleviate any technical deficiencies that may have surfaced since the Company was incorporated.

The Bylaws provide for an annual meeting of members at which a Board of Directors is elected. Officers are elected by the Board annually at the first Board meeting after the annual meeting of members.

The Board is charged with managing the business and affairs of the Company. Each director must be a member in good standing of the Company and the Tennessee Farm Bureau Federation. Two (2) directors shall be residents of each of the geographical divisions into which the State of Tennessee has been divided for membership purposes by the Tennessee Farm Bureau Federation. The remaining directors shall be selected or elected from the state at large.

The current Bylaws are such as generally found in corporations of this type and contain no unusual provisions. They provide for regulation of the business and for the conduct of the affairs of the Company, directors and its members.

Said Bylaws have not been amended during the period of examination.

MANAGEMENT AND CONTROL

Board of Directors:

Management of the Company is vested in a Board of Directors elected annually. In accordance with the Bylaws, the Board shall consist of not less than five nor more than 25 members. The composition of the board has been identical for all four companies comprising the Tennessee Farmers Group. The following persons had been duly elected and were serving as members of the Company's Board of Directors at December 31, 2005:

<u>Name, Address and County</u>	<u>Principal Occupation</u>
Flavius Barker Columbia, TN (Sequatchie)	President & Chairman of the Board/Farmer
Lacy Upchurch Crossville, TN (Cumberland)	Vice President/Farmer
Jeff Aiken Telford, TN (Washington)	Farmer
Malcolm Burchfiel Newbern, TN (Dyer)	Farmer
Linda Davis Rutherford, TN (Gibson)	Farmer/Homemaker

Joan Fussell Erin, TN (Houston)	Farmer/Homemaker
Charles Hancock Bumpus Mills, TN (Stewart)	Farmer
Dan Hancock Smithville, TN (DeKalb)	Farmer
David Mitchell Blaine, TN (Grainger)	Farmer
William Danny Rochelle Nunnely, TN (Hickman)	Farmer
Bobby Willis Hillsboro, TN (Coffee)	Farmer
Willard Brown Cookeville, TN (Putnam)	Farmer
Martin Davis Shelbyville, TN (Bedford)	Farmer
Robert Earhart Bristol, TN (Sullivan)	County Executive
Allen Peddy Henderson, TN (Chester)	Farmer
Jack Sanders Charleston, TN (Bradley)	Farmer

The Board of Directors is charged with managing the business and affairs of the Company. Each director must be a member in good standing of the Tennessee Farm Bureau Federation, which in turn requires membership in good standing of a county Farm Bureau. Unlike the members of the other companies in the Tennessee Farmers Group, the Company's Bylaws further require two directors to be residents of each of the geographical divisions into which the State of Tennessee has been divided for membership purposes by the Federation, with the remaining directors to be elected from the state at large. Though not required by the Charter or Bylaws of the Company, historically 11 members of the Board have also served on the Federation Board of Directors.

Officers:

The Bylaws of the Company provide that the Board of Directors shall elect annually a president, a first vice president, a chief executive officer, a secretary, a treasurer, and such additional officers as the chief executive officer may propose and the Board of Directors approve. The following officers were duly elected and were serving in the positions indicated for the Company at December 31, 2005:

Flavius Barker	President & Chairman of the Board
Lacy Upchurch	First Vice President
Matthew M. Scoggins, Jr.	Chief Executive Officer
Wayne Harris Edward Lancaster	Chief Financial Officer General Counsel, Secretary
John Law	Chief Operating Officer, P&C Operations
Neal Townsend	Chief Marketing Officer

The Board of Directors has given authority to the Chief Executive Officer (CEO) to appoint such other officers as needed to operate the Company. The following officers were appointed by the CEO and serving in positions indicated for the Company at December 31, 2005:

Wayne Merrill	Vice President, Accounting
Vickie Knight	Vice President, Property Underwriting
Sam McDaniel	Vice President, Automobile Underwriting
Steve Burt	Vice President, Information Services
Wayne Erwin	Vice President, Claims

The President functions as the Chairman of the Board of Directors and presides over all meetings of the members and the Board of Directors. The President also serves as a conduit to the executive personnel concerning policy established by the Board of Directors. Subject to the control of the Board of Directors, the Chief Executive Officer shall have general management and control of the affairs and business of the Company, and shall perform all other duties and exercise all other powers commonly incident to his office, or which are required by law.

The Company's Investment Committee at December 31, 2005 is as follows:

<u>Name</u>	<u>Title</u>
Flavius Barker	President
Matthew M. Scoggins, Jr.	Chief Executive Officer
Hulet Chaney	Chief Executive Officer Emeritus
Wayne Harris	Chief Financial Officer
Dennis Stephen	Chief Operating Officer – Life Operations

Non Voting Members

Randy Maxwell	Investment Portfolio Manager
David Williamson	Investment Portfolio Manager
Edward Lancaster	Secretary

The administrative and executive functions of the Company are performed by the home office staff. The Company has its own marketing division located in the home office in Columbia, Tennessee. The Company is a direct writer marketing insurance products through captive agents. Offices are typically located in county farm bureau offices throughout Tennessee. These offices are staffed by licensed agents who operate as independent contractors. Underwriting activities are also performed by home office staff.

Certain services are purchased from outside contractors if needed and are not available from in house personnel. Such services include actuarial analysis and independent audit.

Actuarial Services: Patrick J. Crowe, FCAS, MAAA
7371 Wolf Spring Trace
Louisville, Kentucky

Auditing Services: PricewaterhouseCoopers, LLC
500 West Main
Louisville, Kentucky

A holding company organizational chart is included at the last page of this examination report.

CORPORATE RECORDS

Minutes of meetings of the Company's members, Board of Directors including Executive Session and Investment Committee were reviewed for the period under examination. In general, such minutes appear to be in proper order and accurately report the proceedings of each respective meeting.

FIDELITY BOND AND OTHER INSURANCE

The Company has elected to not obtain fidelity coverage with the exception of its retirement plan. Minimum fidelity bond coverage of \$1,250,000 to \$1,500,000 is suggested by guidelines published in the NAIC Financial Condition Examiners Handbook. The outline of the bond coverage for the retirement plan is included in the schedule of insurance maintained by the Company at December 31, 2005 which follows:

<u>Type of Coverage</u>	<u>Coverage Limits</u>
-------------------------	------------------------

- | | |
|--------------------------------------|-----------|
| 1. Fidelity Bond for Retirement Plan | |
| Employee dishonesty | \$500,000 |

Coverage is underwritten by Travelers Casualty and Surety Company of American which is licensed in Tennessee as a "Foreign Property and Casualty Insurer."

- | | |
|--|-------------|
| 2. Commercial General Liability | |
| Each occurrence | \$2,000,000 |
| General aggregate | \$2,000,000 |
| Products-Completed operations
aggregate limit | \$2,000,000 |
| Personal & advertising limit | \$2,000,000 |
| Damage to premises rented | \$50,000 |
| Medical expense limit (any one person) | \$5,000 |

Coverage is underwritten by the Company on their policy form. The policy is issued to the Tennessee Farm Bureau Federation Et Al with the Company listed as a named insured.

- | | |
|---|-------------|
| 3. Commercial Leased Computer Equipment | |
| Aggregate | \$1,400,000 |

Coverage is underwritten by the Company on their policy form and covers any computer equipment owned by the Company which is leased to subsidiaries or other parties.

- | | |
|---------------------------|--------------|
| 4. Directors and Officers | |
| Aggregate | \$10,000,000 |
| Deductible each claim | \$100,000 |

Coverage is underwritten by Great American Insurance Company which is licensed in Tennessee as a "Foreign Property and Casualty Insurer."

- | | |
|---|--|
| 5. Workers Compensation Excess Coverage | |
|---|--|

Workers compensation	Tennessee statutory limit
Specific retention	\$350,000 each accident, each employee
Employers liability	
Bodily injury by accident	\$1,000,000 each accident
Bodily injury by disease	\$1,000,000 each accident
Specific retention	\$350,000
Aggregate limit	\$1,000,000

Coverage is underwritten by Midwest Employers Casualty Company which is licensed in Tennessee as a "Foreign Property and Casualty Insurer."

TERRITORY

As of December 31, 2005, and as of the date of this examination report, the Company was licensed to transact business in the State of Tennessee. The Certificate of Authority for that jurisdiction was reviewed.

During 2005, the Company wrote direct premium in one (1) state:

<u>State</u>	<u>Amount</u>
Tennessee	<u>\$804,279,292</u>
Total	\$804,279,292

PLAN OF OPERATION

The Company operates as a direct writer of property and casualty insurance under the mutual plan insuring risks of the following lines of business:

Fire	Inland marine	Auto physical damage
Allied lines	Earthquake	Surety
Farmowners	Other liability occurrence	Burglary and theft
Homeowners	Auto liability	

The insurance business of the Company was produced by a sales and production staff under the supervision of a Chief Marketing Officer assisted by Regional Agency Managers. The Company's 419 captive agents at December 31, 2005 are independent contractors serving as either Agency Managers or

Agents. These agents also market business for the affiliated companies; Tennessee Farmers Assurance Company, Tennessee Farmers Life Insurance Company and Tennessee Farmers Life Reassurance Company.

The production offices are primarily located in local Farm Bureau offices in the 95 counties of the State of Tennessee. The Agency Managers authorize the Company to withhold certain prescribed amounts from earned commissions and fees in order to reimburse the individual county Farm Bureau for the cost of facilities and services used by the agents in the production of business.

During the period under review and through the date of this report, all policy preparation was performed in the home office and was subject to the underwriting rules adopted by the Company and promulgated in accordance with approved rates. The adjustment of claims is also administered by the Company through its regional claim offices located throughout the State of Tennessee.

The largest net amount insured by the Company in any one risk is \$400,000. In order to purchase a policy with the Company, the potential insured must be a member of the Tennessee Farm Bureau Federation. The policies issued are non-assessable in relation to contingency premiums. Dividends may be paid to policyholders from earned surplus funds as declared by the Board.

The Company provides a \$1,500.00 accidental death benefit to members of local Farm Bureaus' who choose to participate in this program by paying a fee for each member in the county. This premium is ceded to Tennessee Farmers Life Reassurance Company.

REINSURANCE

The Company routinely assumes and cedes reinsurance with other insurance companies. The Company's significant reinsurance agreements are summarized below.

Assumed Reinsurance with Affiliates

Tennessee Farmers Assurance Company (TFAC)

The company assumes, thru a quota share agreement, 50% of all lines of business issued by Tennessee Farmers Assurance Company (TFAC) effective January 1, 1999. This agreement covers liabilities that existed on and after January 1, 1999.

Tennessee Farmers Life Insurance Company (TFLIC)

The company assumes 100% of the annuity risks of Tennessee Farmers Life

Insurance Company (TFLIC) thru a coinsurance/modified coinsurance agreement effective January 1, 2002.

This agreement was terminated December 31, 2005. The business covered was Single Premium Deferred Annuities, Plan 917 and 918 issued between January 1, 2002 and December 31, 2002. Reserves related to these policies were returned to Tennessee Farmers Life Insurance Company.

Ceded Reinsurance with Affiliates

Tennessee Farmers Assurance Company (TFAC)

The company cedes, thru a quota share agreement, 50% of all lines of business issued by the Company to Tennessee Farmers Assurance Company (TFAC) effective August 1, 1991. This agreement covers liabilities that existed on and after August 1, 1991.

Tennessee Farmers Life Reassurance Company (TFLRC)

The company cedes, thru two quota share agreements, 100% of the automobile blanket accidental death policies issued by the Company to Tennessee Farmers Life Reassurance Company (TFLRC) effective January 1, 1988. These agreements cover liabilities that existed on and after January 1, 1988.

The company cedes, thru a quota share agreement, 100% of the property blanket accidental death policies issued by the Company to Tennessee Farmers Life Reassurance Company (TFLRC) effective February 1, 1990. This agreement covers liabilities that existed on and after February 1, 1990.

The company cedes, thru a quota share agreement, 100% of the blanket tractor and/or farm premises accidental death and broad form accidental death policies issued by the Company to Tennessee Farmers Life Reassurance Company (TFLRC) effective January 1, 1988. This agreement covers liabilities that existed on and after January 1, 1988.

Ceded Reinsurance with Non-Affiliates

American Agricultural Insurance Company

The Company cedes the following to American Agricultural Insurance Company:

- | | |
|--------------------|--|
| 1) Effective Date: | January 1, 2003 |
| Description: | Covers certain: |
| | 1. Personal umbrella policies and endorsements |
| | 2. Farm and Ranch umbrella policies |

3. Commercial umbrella policies

Retention: 10% of 1st layer (\$ 1 million limit)
Maximum Ceded Amounts: 90%

Effective January 1, 2005, the Company's umbrella reinsurance was combined with the Company's excess liability reinsurance.

2) Effective Date: January 1, 2005
Description: Excess Liability and Umbrella
Retention: \$ 400,000
Maximum Ceded Amounts: \$ 11.5 million

3) Effective Date: January 1, 2005
Description: Multi-line aggregate excess of loss ratio agreement for all the property and casualty coverages written by the company
Retention: 80% with 2.5% participation
Maximum Ceded Amounts: \$ 37 million

4) Effective Date: January 1, 2005
Description: An occurrence property catastrophe excess of loss for personal and commercial property coverages.
25% of net earned premium
Retention:
Maximum Ceded Amounts: 95% of \$ 140 million

5) Effective Date: January 1, 2005
Description: An occurrence property catastrophe (terrorism) excess of loss for personal and commercial coverages.
Retention: \$ 12,432,650
Maximum Ceded Amounts: \$ 24,865,300

6) Effective Date: January 1, 2004
Description: A property surplus share for personal and commercial coverages.
Retention: \$ 500,000
Maximum Ceded Amounts: \$ 40 million aggregate
\$ 10 million per occurrence/\$ 1.6 million per event (15% deductible)

Other Considerations:

All of the Company's significant reinsurance agreements were found to contain

such language as recommended by the NAIC and as required for reinsurance credit pursuant to Tenn. Code Ann. § 56-2-207(a)(2). All agreements also appear to effectuate proper transfer of risk in accordance with SSAP No. 62 and NAIC guidelines.

Property Quota Share Reinsurance Contract (special)

Guy Carpenter & Company, Inc. (Intermediary)

The company cedes, thru a quota share agreement, 46% of the Company's Net Retained Liability as respects Homeowners property sections and Farmowners property sections. The liability of the Reinsurer shall not exceed \$600,000 any one Risk, any one Loss, subject to a maximum recovery hereon of \$750,000 any one Loss Occurrence as respects Wind Storm and Hail. Other perils shall not be subject to occurrence limitations of any kind. A deductible of \$50,000,000 any one Loss Occurrence shall apply as respects the perils of earthquake and fire following earthquake. However, fire following losses shall only contribute a maximum of 20% to the deductible amount. No other perils shall be subject to an occurrence deductible of any kind.

This contract covers risks insured by the Company in 15 West Tennessee Counties and takes effect on July 1, 2005 as respects losses occurring at or after that date. Contract is effective until terminated.

"Company's Net Retained Liability means the remaining portion of the Company's gross liability on each risk reinsured under this contract after deducting recoveries from all reinsurance, other than the reinsurance provided hereunder and the reinsurance specified in the Other Reinsurance Article."

RETIREMENT PLAN AND OTHER EMPLOYEE BENEFITS

At December 31, 2005, the following benefits were available to the Company's employees:

Group Life, Accidental Death and Dismemberment, Long Term Disability Insurance

The referenced benefits are provided to all full-time employees on a non-contributory basis and to dependents on a contributory basis. Each insurance plan has a six (6) month waiting period and will become effective on the first day of the following month after their waiting period. The life insurance benefit is two (2) times the employee's annual earnings subject to a maximum amount of \$300,000. The accidental death and dismemberment benefit is the same amount as the life benefit. The long term disability benefit equals 66 2/3% of the employee's gross monthly income up to \$6,000 and can continue until age 65.

The plan sponsor for these benefits is Tennessee Farm Bureau Federation and the plan administrator is Standard Insurance Company.

Health Insurance

Medical and dental insurance is provided to all full-time employees on a contributory basis. Employees may also elect and pay for dependent coverage. The plan additionally covers well care, psychiatric care and prescription drugs.

Tennessee Rural Health Improvement Association on behalf of The Company coordinates the self-funded employee health plans. The Administrative Coordinator is TRH Health Insurance Company and the Claims Administrator is BlueCross BlueShield of Tennessee. Participants in the plan are entitled to certain rights and protections under the Employee Retirement Income Security Act of 1974 (ERISA) and a Statement of ERISA Rights is included in the plan information summary provided to participants.

Retirement Plan (Defined Benefit Plan)

The Company sponsors a defined benefit pension plan for all eligible employees on a non-contributory basis. An employee becomes eligible for the plan when they have reached 21 years of age and completed one (1) year of eligibility service. The benefits are based on years of service and the employee's highest three (3) consecutive years' average compensation.

Retirement Age

- 65 years (normal retirement)
- 62 years with 22 years service
- 55 years with 25 years service

Retirement Savings Plan (Defined Contribution Plan, 401-K)

The Company offers a 401-K Plan for all eligible employees. An employee becomes eligible on the first April or October following their one (1) year anniversary of employment and attainment of 21 years of age. The Company matches 30% of the employee contribution up to a maximum of six percent (6%) of eligible earnings. The match is made in the form of Tennessee Farmers Life Insurance Company and Tennessee Farmers Assurance Company common stock.

Years of Service Bonus Program

The Company has a tenure bonus program where the employee earns a bonus based on their years of service. The bonus is calculated using \$20 per year for each year of service.

Other Benefits

Other benefits available for employees include holidays, sick leave, vacation leave, service recognition awards, and educational assistance. The time of service with the Company determines the eligibility and amounts of time available to the employee.

LOSS EXPERIENCE

<u>Year</u>	<u>Losses Incurred</u>	<u>LAE Incurred</u>	<u>Premiums Earned</u>	<u>Loss Ratio</u>
2001	\$ 199,622,424	\$ 20,498,045	\$ 288,937,884	76.2%
2002	278,842,855	21,106,929	357,161,140	84.0%
2003	283,868,663	21,795,768	344,311,711	88.8%
2004	233,842,853	22,255,881	359,713,686	71.2%
2005	247,223,523	22,885,467	389,828,726	69.3%
Total	\$1,243,400,318	\$108,542,090	\$1,739,953,147	77.7%

ACCOUNTS AND RECORDS

During the course of examination, such tests and audit procedures were made as were considered necessary, including substantial verification of postings, extensions and footings and reconciliation of subsidiary ledgers to control accounts where necessary. General ledger trial balances were reconciled with copies of annual statements for the years 2001, 2002, 2003, 2004 and 2005.

Accounting records conform to generally accepted insurance accounting practices and appear to properly reflect the operations during the period under examination and the status of the Company at the date of examination.

The Company's Risk Based Capital Report was reviewed. The Company was in compliance with Title 56, Chapter 46, of the Tennessee Code Annotated (Risk Based Capital for Insurers).

An annual audit of the Company is performed by an independent accounting firm, PricewaterhouseCoopers, LLP

Books and records of the Company are kept at the home office location:

147 Bear Creek Pike
Columbia, Tennessee 38401

STATUTORY DEPOSITS

In compliance with statutory requirements, the Company maintained the following deposits at December 31, 2005.

<u>Where Deposited and Description</u>	<u>Par Value</u>	<u>Statement Value</u>	<u>Market Value</u>
Tennessee			
Tenn. St 5%, due 5/01/2014	\$ 620,000	\$ 638,335	\$ 673,549
Tenn. St 4.875%, due 3/01/2010	1,000,000	1,003,936	1,055,880
Total general deposits held for the benefit of all policyholders and creditors of the Company	<u>1,620,000</u>	<u>1,642,271</u>	<u>1,729,429</u>
Total	<u>\$1,620,000</u>	<u>\$1,642,271</u>	<u>\$1,729,429</u>

The above deposit was confirmed with the custodian at the Division of Insurance.

AGREEMENTS WITH PARENT, SUBSIDIARIES AND AFFILIATES

The Company meets the definition of a holding company pursuant to Tenn. Code Ann. § 56-11-201.

The insurance companies in the Tennessee Farmers Group had previously been exempt from the statute based upon an order from Commissioner Elaine McReynolds dated February 12, 1987 which granted the exemption pursuant to Tenn. Code Ann. § 56-11-205(j).

During 2004, the TDCI performed a Target Financial Examination of the four (4) companies (Tennessee Farmers Mutual Insurance Company, Tennessee Farmers Assurance Company, Tennessee Farmers Life Insurance Company, Tennessee Farmers Life Reassurance Company) in the Holding Company. The Report on Examination was made as of December 31, 2003 and was signed on December 22, 2004. The TDCI and the four (4) Companies subsequently agreed that, henceforth, all parties are subject to the registration requirements under Title 56, Chapter 11 Tennessee Code Annotated, "Insurance Holding Company System Act of 1986".

The Company started filing Form B "Insurance Company System Annual Registration Statement" and Form C "Summary of Registration Statement" with the TDCI for the year, 2004. This information was filed on April 29, 2005 in compliance with Tenn. Code Ann § 56-11-205.

A Form D "Prior Notice of a Transaction" filing for the agreements referenced under this caption was also filed with the TDCI on April 29, 2005.

Management Services Agreements:

The Company entered into Management Services Agreements with three (3) of its affiliates, Tennessee Farmers Assurance Company, Tennessee Farmers Life Insurance Company, and Tennessee Farmers Insurance Agency, Inc. Under these agreements, the parent performs all management, administrative and other services that are reasonably necessary for the operation of the Companies. These services include, but are not limited to: employee, legal, claims, managerial and accounting.

The agreements provide for the Company to be paid for services and supplies an amount determined in accordance with Treasury Regulation Section 1.482-2(b)(3) et seq. as codified in United States Internal Revenue Code Title 26. The agreements call for settlement to be remitted on a quarterly basis.

The agreement with Tennessee Farmers Assurance Company was dated April 25, 1991 and had an ending date of December 31, 1991 with the option to renew on calendar year basis thereafter.

The agreement with Tennessee Farmers Life Insurance Company was dated December 21, 1973 and had an ending date of December 31, 1973 with the option to renew on calendar year basis thereafter.

The agreement with Tennessee Farmers Insurance Agency, Inc. was dated September 30, 1980 and had an ending date of December 31, 1980 with the option to renew on calendar year basis thereafter.

During 2005, the Company was paid \$63,561,332 by Tennessee Farmers Assurance Company, \$6,043,738 by Tennessee Farmers Life Insurance Company and \$41,403 by Tennessee Farmers Insurance Agency, Inc.

Agreement To Allocate Consolidated Federal Income Tax Liability:

The Company files a consolidated tax return including the following named subsidiaries:

Tennessee Farmers Assurance Company
TFHC, Inc.
TFIC, Inc.

The Agreement to Allocate Consolidate Federal Income Tax Liability was entered into effective December 31, 2004. The previous agreement had

been effective as of December 31, 2000.

Federal Income Tax Allocation for 2005:

The Company	\$18,274,474
Tennessee Farmers Assurance Company	\$16,699,330
TFIC,, Inc.	\$ 1,565,833
Tennessee Farmers Insurance Agency, Inc	\$ 10,692

Equipment Lease:

The Company entered into Lease Agreement with Tennessee Farmers Life Insurance Company on January 1, 2004 maturing December 31, 2004. The lease automatically renews unless either party gives notice to discontinue. Tennessee Farmers Life purchases most of the equipment used within the holding company group and then leases back to various members. Expense is calculated based upon the expected useful life of the equipment and any other expense associated with the equipment.

During 2005, the Company paid \$4,585,062.16 under this lease.

Lease for Office Space:

The Company rents office space from the Tennessee Farm Bureau Federation which owns and maintains the land and building at 147 Bear Creek Pike, Columbia, Tennessee. Management of both Farm Bureau and the Company determine appropriate square footage rates based on periodic discussions with other lessors in the geographic area.

During 2005, the Company paid \$1,585,113.96 under this arrangement.

PECUNIARY INTEREST TENN. CODE ANN. § 56-3-103

The Company established a conflict of interest policy for its directors and officers to attest to compliance with Tenn. Code Ann. § 56-3-103, prohibiting officers and directors from having pecuniary interest in investment or disposition of Company funds. The officers and directors file annual conflict of interest statements.

COMMISSION EQUITY

The Company correctly reports commission equity of \$19,800,788 in the notes to financial statement in compliance with NAIC Annual Statement Instructions. \$18,927,947 of this amount is related to the Quota Share Reinsurance Agreement (50%) with its subsidiary, Tennessee Farmers Assurance Company.

The remaining \$872,841 is related to treaties with various reinsurers and is considered an immaterial amount.

No contingent liability is proposed due to the financial strength of the subsidiary and the other reinsurers together with the unlikelihood that the reinsurance agreements would be commuted.

DIVIDENDS OR DISTRIBUTIONS

During the period of examination the Company paid the following amounts in policyholder dividends.

Policyholder Dividends

Year	Amount
2001	\$12,352,175
2002	7,780,797
2003	9,057,439
2004	14,740,244
2005	<u>9,608,362</u>
Total Paid During Period of Examination	\$53,539,017

LITIGATION

As of December 31, 2005, the Company has committed no reserves to cover any contingent liability. Various lawsuits against the Company have arisen in the normal course of business relating to insurance claims' settlements. Contingent liabilities arising from litigation are not considered material in relation to the financial position of the company.

The Department of Revenue, State of Tennessee assessed additional Franchise and Excise Taxes for the period 1/1/95 – 12/31/98 in the amount of \$5,287,684 including accrued interest. A second examination for the period covering years, 1999 -2002 assessed \$3,734,167 including accrued interest. The Company paid the assessed amounts including interest for both of the audits under protest and contested these findings in court.

On January 26, 2005, the Company filed suit to recover the disputed assessment arising from the years 1999 – 2002. The trial court had previously granted the Company's motion for summary judgment on the assessment for the period 1/1/95 – 12/31/98 and the State of Tennessee appealed to the Court of Appeals.

The Company made the determination to terminate both legal proceedings during 2006 after review of the evidence that was still available and the cost

effectiveness of further litigation.

SUBSEQUENT EVENTS

Settlement of the Franchise and Excise Tax issue per audit of the Department of Revenue, State of Tennessee was discussed previously under the caption, "LITIGATION."

The Company and its two (2) custodians, The Northern Trust Company and First Farmers and Merchants Bank completed amendments to their custodian agreements during the course of the examination to insure that the documents complied with the technical language pursuant to Tenn. Comp. R. & Regs. ch. 0780-1-46-.03(2)(a), which became effective on July 12, 2005. The rule states:

"The custodial agreement required by this rule shall contain the following:

1. A provision stating that the standard of responsibility on the part of the custodian shall not be less than that of the responsibility of a bailee for hire or a fiduciary under statutory or case law of Tennessee;
2. A provision stating that the securities held by the custodian are subject to instructions of the insurance company;
3. A provision stating that the securities may be withdrawn immediately upon demand of the insurance company; and
4. A provision stating that the agreement is between the custodian and the insurance company, and not the parent or affiliate of the insurance company."

The original documents had protective language; however, that language was written in a more generic form than the specific four (4) provisions of the above rule. These amendments were transacted at the request of the Company.

The Northern Trust Company Amendment was effective on March 1, 2007 exhibiting language compliant with Tenn. Comp. R. & Regs. ch. 0780-1-46-.03(2)(a). Signature date for the Company was March 22, 2007 and signature date for Northern Trust was April 19, 2007.

The First Farmers and Merchants Bank Amendment was effective on March 1, 2007 exhibiting language compliant with Tenn. Comp. R. & Regs. ch. 0780-1-46-.03(2)(a). Signature date for the Company and First Farmers was June 6, 2007.

As of December 31, 2005, Northern Trust held \$86,995,689 in common stock and \$14,958,218 in short-term investments. First Farmers and Merchants Bank

held \$756,482,737 in bonds, \$2,728,694 in common stocks, \$115,966 in short-term investments and \$15,406,191 in cash equivalent funds.

The Company determined in August, 2007 that a change would be made in their auditors from PricewaterhouseCoopers, LLP to Blackman Kallick Bartelstein, LLP. This change was related to customer service issues and did not involve any disputed audit findings. This was confirmed and attested by letter from PricewaterhouseCoopers, LLP dated September 24, 2007 in compliance with Tenn. Comp. R. & Regs. ch. 0780-1-65-.06. Official notice of the change was given to the TDCI via letter from the Company dated August 31, 2007.

FINANCIAL STATEMENT

There follows a statement of assets, liabilities and statement of income at December 31, 2005, together with a reconciliation of capital and surplus for the period under review, as established by this examination:

ASSETS

	<u>Ledger Assets</u>	<u>Assets Not Admitted</u>	<u>Net Admitted Assets</u>
Bonds	\$758,125,008		\$758,125,008
Preferred Stocks	0		0
Common Stocks	770,590,063		770,590,063
Cash and short-term investments	26,666,146		26,666,146
Receivables for securities	0		0
Investment income due and accrued	10,386,828		10,386,828
Uncollected premiums and agents, balances In course of collection	84,311,891		84,311,891
Amounts recoverable from reinsurers	1,397,512		1,397,512
Current federal income tax recoverable	2,502,638		2,502,638
Electronic data processing equipment	2,055,185	2,034,773	20,412
Receivable from parent, subsidiaries and Affiliates	21,629,244		21,629,244
Healthcare and other amounts receivable	462,000	462,000	0
Aggregate write-ins for other than invested Assets	<u>50,253,359</u>	<u>50,232,991</u>	<u>20,368</u>
Totals	<u>\$1,728,379,874</u>	<u>\$52,729,764</u>	<u>\$1,675,650,110</u>

LIABILITIES, SURPLUS, AND OTHER FUNDS

Losses	\$111,341,541
Reinsurance payable on paid loss and loss adjustment expenses	0
Loss adjustment expenses	22,961,596
Commissions payable, contingent commissions and other similar charges	6,583,998
Other expenses (excluding taxes, licenses and fees)	5,140,667
Taxes, licenses and fees (excluding federal and foreign income tax)	798,996
Federal and foreign income taxes	0
Net deferred tax liability	18,480,075
Unearned premiums	142,929,150
Advance premiums	8,718,970
Dividends declared and unpaid: policyholders	9,874,067
Ceded reinsurance premiums payable (net of ceding commissions)	3,068,158
Amounts withheld or retained by company for account of others	2,954,529
Payable to parent, subsidiaries and affiliates	2,717,714
Payable for securities	0
Aggregate write-ins for liabilities (related to retirement and deferred benefits)	<u>9,003,142</u>
Total Liabilities	344,572,603
Aggregate write-ins for special surplus funds	7,200
Common capital stock	0
Gross paid in and contributed surplus	0
Unassigned funds (surplus)	<u>1,331,070,307</u>
Surplus as regards policyholders	1,331,077,507
Total liabilities and surplus	<u>\$1,675,650,110</u>

STATEMENT OF INCOME

UNDERWRITING INCOME

Premiums earned		\$389,828,726
Deductions: Losses incurred	\$247,223,523	
Loss expenses incurred	22,885,467	
Other underwriting expenses incurred	<u>52,937,414</u>	
Total underwriting deductions		<u>323,046,404</u>
Net underwriting gain		66,782,322

INVESTMENT INCOME

Net investment income earned	43,192,858	
Net realized capital gains (losses)	<u>3,987,624</u>	
Net investment gain		47,180,482

OTHER INCOME

Finance and service charges not included in premiums		4,039,649
Aggregate write-ins for miscellaneous income		<u>1,845,915</u>
Total other income		5,885,564
Net income before dividends to policyholders and before federal income taxes		119,848,368
Dividends to policyholders		9,608,362
Federal income taxes incurred		<u>17,620,970</u>
Net income		<u>\$92,619,036</u>

CAPITAL AND SURPLUS

Surplus as regards policyholders, December 31 prior year		\$1,191,411,548
Net income	\$92,619,036	
Change in net unrealized capital gains (losses)	72,196,147	
Change in net deferred income tax	(6,319,046)	
Change in non-admitted assets	(18,651,830)	
Cumulative effect of changes in accounting principles	0	
Capital changes: Paid in	0	
Capital changes: Transferred from surplus (Stock Dividend)	0	
Surplus adjustments: Paid in	0	
Surplus adjustments: Transferred to capital (Stock Dividend)	0	
Aggregate write-in for gains and losses in surplus	(178,348)	
Change in surplus as regards policyholders for the year		139,665,959
Surplus as regards policyholders, December 31 current year		<u>\$1,331,077,507</u>

**RECONCILIATION OF CAPITAL AND SURPLUS
FOR THE PERIOD UNDER EXAMINATION**

Surplus as regards policyholders December 31	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>	<u>2005</u>
Previous Year	\$955,687,302	\$983,595,635	\$1,029,401,636	\$1,067,438,401	\$1,191,411,548
Net Income	41,646,273	34,919,615	21,602,539	75,893,261	92,619,036
Net unrealized capital gains or (losses)	3,770,858	6,349,580	0	0	0
Change in net unrealized capital gains or (losses)	0	0	29,297,260	69,507,455	72,196,147
Change in net deferred income tax	9,073,674	11,775,265	(3,348,297)	(10,129,013)	(6,319,046)
Change in non-admitted Assets	(2,546,304)	(260,039)	(9,159,651)	(10,922,315)	(18,651,830)
Change in provision for Reinsurance	0	0	0	0	0
Cumulative effect of changes In accounting principles	(24,232,307)	(8,296,048)	0	0	0
Capital changes: Paid in	0	0	0	0	0
Capital changes: Transferred From surplus (Stock Dividend)	0	0	0	0	0
Surplus adjustments: Paid in	0	0	0	0	0
Surplus adjustments: Transferred To capital (Stock Dividend)	0	0	0	0	0
Aggregate write-ins for gains and losses in surplus	<u>196,139</u>	<u>1,317,628</u>	<u>(355,086)</u>	<u>(376,241)</u>	<u>(178,348)</u>
Surplus as regards policyholders, December 31 current year	<u>\$983,595,635</u>	<u>\$1,029,401,636</u>	<u>\$1,067,438,401</u>	<u>\$1,191,411,548</u>	<u>\$1,331,077,507</u>

**ANALYSIS OF CHANGES IN FINANCIAL STATEMENT AND COMMENTS
RESULTING FROM EXAMINATION**

Differences in various items were noted during the course of examination; however, none were considered to produce a material effect on surplus funds, as regards policyholders, either singly or in aggregate.

**SUMMARY SCHEDULE FOR "ANALYSIS OF CHANGES
IN FINANCIAL STATEMENT AND COMMENTS RESULTING FROM
EXAMINATION" AS THEY AFFECT SURPLUS**

No schedule or comment is applicable. All noted differences were within the tolerable error and planning materiality established for examination purposes.

COMMENTS AND RECOMMENDATIONS

Comments:

- The Company amended its two (2) custodial agreements with The Northern Trust Company and First Farmers and Merchants Bank during the course of the examination to clarify some technical language pursuant to Tennessee Regulations. These agreements were discussed previously in the report under the caption "Subsequent Events."

Recommendations:

- None

CONCLUSION

Insurance examination practices and procedures, as promulgated by the National Association of Insurance Commissioners, have been followed in connection with the verification and valuation of assets and the determination of liabilities of Tennessee Farmers Mutual Insurance Company of Columbia, Tennessee.

In such manner, it was determined that, as of December 31, 2005, the Company had admitted assets of \$1,675,650,110 and liabilities, exclusive of unassigned funds, of \$344,572,603. Thus, there existed for the additional protection of the policyholders, the amount of \$1,331,077,507 in the form of surplus receipts and unassigned funds (surplus).

The courteous cooperation of the officers and employees of the Company extended during the course of the examination is hereby acknowledged.

In addition to the undersigned, Gregory S. Wilson, FCAS, MAAA of the actuarial firm, Lewis & Ellis, Inc, Richardson, Texas and Norman Chandler, CPA, CPCU, AIAF, ARC, ACP of the firm, TaylorChander, LLC, Montgomery, Alabama participated in the work of this examination. Insurance Examiners; David N. Bobo, Stephanie D. Brooks, Gregory Bronson and Mitchell Walker, Jr. also participated in this examination.

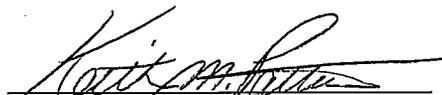
Respectfully submitted,



Keith M. Patterson
Insurance Examiner
State of Tennessee
Southeastern Zone, N.A.I.C.

AFFIDAVIT

The undersigned deposes and says that he has duly executed the attached examination report of Tennessee Farmers Mutual Insurance Company dated June 13, 2008, and made as of December 31, 2005, on behalf of the Department of Commerce and Insurance, State of Tennessee. Deponent further says he is familiar with such instrument and the contents thereof, and that the facts therein set forth are true to the best of his knowledge, information and belief.



Keith M. Patterson
Insurance Examiner
State of Tennessee
Southeastern Zone, N.A.I.C.

Subscribed and sworn to before me

this 13th day of

June, 2008

Notary

County

State

Commission Expires



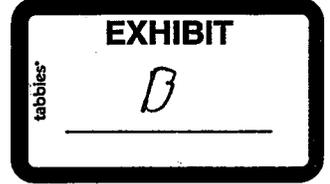
09-2012



**Tennessee Farmers
Insurance Companies**

Corporate Headquarters

Post Office Box 998 • Columbia, TN 38402-0998
931.388.7872 • www.tennesseefarmers.com



June 19, 2008

RECEIVED

JUN 20 2008

Dept. Of Commerce & Insurance
Company Examinations

Phil Blustein
Chief Examiner
TN Department of Commerce and Insurance
Nashville, TN 37243

RE: Financial Condition Examination made as of December 31, 2005 for
Tennessee Farmers Mutual Insurance Company
Tennessee Farmers Assurance Company

Dear Phil:

We are satisfied with the Final Reports for the companies referenced above and hereby waive our right of rebuttal. Thank you.

Yours,

Wayne Harris
CFO

C: Matthew M. Scoggins, Jr.
Ed Lancaster