

REPORT ON EXAMINATION

of the

**TENNESSEE FARMERS ASSURANCE COMPANY
147 BEAR CREEK PIKE
COLUMBIA, TENNESSEE**

RECEIVED

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Dept. of Commerce & Insurance
Company Examinations

as of

DECEMBER 31, 2010

DEPARTMENT OF COMMERCE AND INSURANCE

STATE OF TENNESSEE

NASHVILLE, TENNESSEE



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Columbia, Tennessee
June 14, 2012

Honorable Julie Mix McPeak
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 and market conduct review were made of the condition and affairs of the

TENNESSEE FARMERS ASSURANCE 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 January 24, 2011. On-site examination work commenced on June 27, 2011. 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 two other insurance companies in the Tennessee Farmers Insurance Group, all based in Columbia, Tennessee as follows:

Tennessee Farmers Mutual Insurance Company
Tennessee Farmers Life Insurance Company

SCOPE OF EXAMINATION

This examination report covers the period from January 1, 2006 to the close of business on December 31, 2010, and includes any material transactions and/or events occurring subsequent to the examination date and noted during the course of the examination.

The examination was conducted in accordance with the NAIC Financial Condition Examiners Handbook. The examination was planned and performed to evaluate the financial condition and identify prospective risks of the Company by obtaining information about the Company including corporate governance, identifying and assessing inherent risks within the Company, and evaluating system controls and procedures used to mitigate those risks. The examination also included assessing the principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation and management's compliance with Statutory Accounting Principles and annual statement instructions.

All accounts and activities of the Company were considered in accordance with the risk-focused examination process. Independent actuaries were used in the review of the Company's reserves.

In addition, the following topics were reviewed:

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

COMMENTS – PREVIOUS EXAMINATIONS

The previous financial examination was conducted as of December 31, 2005 by authorized representatives of the TDCI. This examination did not result in any adverse findings or adjustments to surplus; however, during the course of the examination, the Company amended its two custodial agreements with The Northern Trust Company and First Farmers and Merchants Bank to clarify some technical language pursuant to Tennessee Regulations.

COMPANY HISTORY

The Company was incorporated under the provisions of the Tennessee General Corporation Act on April 3, 1991. The Company operates as a stock property and casualty insurance company and was issued a Certificate of Authority by the TDCI on May 2, 1991. Business commenced on August 1, 1991.

Subsequent to the Company's incorporation, TFHC, Inc. purchased 24,400,000 shares of one dollar par value common stock. Through additional purchases and declared dividends, TFHC, Inc., as of December 31, 2010, owned 42,164,071 shares of the Company, which represents 90.81% of the outstanding shares.

As of December 31, 2010, there are 46,431,088 shares of common stock issued and outstanding. The remaining shares are issued to policyholders, agents, officers and directors of the Tennessee Farmers Mutual Insurance Company and its affiliates.

Since August, 1992 and until December 31, 2010, the only changes in the Company's outstanding common stock and paid in and contributed surplus resulted from small repurchases of common stock and new stock certificates issued to Tennessee Farmers Mutual Insurance Company in order to contribute to its 401(k) retirement plans. Also, a few new shares were issued to new agents and directors. The Company has also declared stock dividends at various times over the years.

At December 31, 2010, 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</u> | <u>Admitted Assets</u> | <u>Liabilities</u> | <u>Total Capital and Surplus</u> |
|-------------|----------------------------|----------------------------|----------------------------|--------------------|--------------------------------------|
| 12/31/2010 | \$448,675,880 | \$350,911,982 | \$ 919,019,274 | \$ 298,718,640 | \$ 620,300,634 |
| 12/31/2009 | 425,420,427 | 330,390,046 | 892,629,141 | 289,227,787 | 603,401,354 |
| 12/31/2008 | 429,001,527 | 345,695,871 | 883,308,173 | 318,781,546 | 564,526,627 |
| 12/31/2007 | 423,131,394 | 261,741,930 | 878,604,809 | 319,519,754 | 559,085,055 |
| 12/31/2006 | 400,432,977 | 306,023,016 | 786,863,021 | 307,815,538 | 479,047,483 |

CHARTER AND BYLAWS

Charter:

The Charter was filed and recorded with the Secretary of State, state of Tennessee on April 3, 1991 and was filed and recorded with the Maury County Register of Deeds on April 9, 1991. The Charter had been approved by the TDCI on April 3, 1991.

The Charter provided for the operation of a "for-profit" corporation and authorized a maximum number of 100,000,000 shares of common capital stock with a par value of one dollar per share. These shares have unlimited voting rights and have the right to receive the net assets of the Company upon dissolution.

The principal purposes of the Company are as follows:

1. "To issue contracts of insurance and/or to reinsure or accept reinsurance of all forms of property and casualty insurance, including but not limited to, all forms of fire insurance, use and occupancy insurance; and all other insurance against loss or damage by any hazard for any risk not otherwise provided for in this section which is not prohibited by statute of common law from being the subject of insurance, excepting life insurance."
2. "To engage in any lawful act or activity for which corporations for profit may be organized under the laws of the State of Tennessee; and the corporation shall have all powers necessary to conduct such business and engage in such activities, including, but not limited to, the powers enumerated in the Tennessee Business Corporation Act or any amendment thereto."

The principal office of the Company was established as follows:

Highway 412, Bear Creek Pike
Columbia, Tennessee 38401
Maury County, Tennessee

Bylaws:

The Restated Bylaws of the Company in effect at December 31, 2010 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 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 were not 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 three 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, 2010:

| <u>Name, Address and County</u> | <u>Principal Occupation</u> |
|---|---|
| Lacy Upchurch Crossville, TN (Cumberland) | President & Chairman of the Board/Farmer |
| Jeff Aiken Telford, TN (Washington) | Farmer |
| Willard Brown Cookeville, TN (Putnam) | Farmer |
| Malcolm Burchfiel Newbern, TN (Dyer) | Farmer |
| Martin Davis Shelbyville, TN (Bedford) | General Manager, Bedford County Utility District; Farmer |
| Robert Earhart Bristol, TN (Sullivan) | County Executive |
| Charles Hancock Bumpus Mills, TN (Stewart) | Farmer |
| Dan Hancock Smithville, TN (DeKalb) | Farmer |
| James Haskew, Jr. South Pittsburg, TN (Marion) | Farmer |

| <u>Name, Address and County</u> | <u>Principal Occupation</u> |
|--|----------------------------------|
| Jason Luckey Humboldt, TN (Gibson) | Farmer |
| William Eric Mayberry Hurricane Mills, TN (Humphreys) | Farmer |
| Jane May Newbern, TN (Dyer) | State FB Women's Chairman/Farmer |
| David Mitchell Blaine, TN (Grainger) | Farmer |
| William Danny Rochelle Nunnely, TN (Hickman) | Farmer |
| Jack Sanders Charleston, TN (Bradley) | Farmer |
| Catherine Via Bells, TN (Crockett) | Farmer/Homemaker |

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, 2010:

| | |
|--------------------------|---|
| Lacy Upchurch | President & Chairman of the Board |
| William Danny Rochelle | First Vice President |
| Matthew M. Scoggins, Jr. | Chief Executive Officer |
| John Law | Chief Operating Officer, P&C Operations |
| Wayne Harris | Treasurer |
| Edward Lancaster | General Counsel and Secretary |
| 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, 2010:

Wayne Merrill
Steve Burt

Vice President, Accounting/Controller
Chief Information Officer

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, 2010 is as follows:

| <u>Name</u> | <u>Title</u> |
|--------------------------|---|
| Wayne Merrill | Controller, Chairman of Committee |
| Lacy Upchurch | President |
| Matthew M. Scoggins, Jr. | Chief Executive Officer |
| Wayne Harris | Treasurer/Chief Financial Officer |
| Dennis Stephen | Chief Operating Officer – Life Operations |
| Edward Lancaster | Secretary/General Counsel |

Non Voting Members

| | |
|------------------|------------------------------|
| Randy Maxwell | Investment Portfolio Manager |
| David Williamson | Investment Portfolio Manager |

The Company's Audit Committee at December 31, 2010 is as follows:

| <u>Name</u> | <u>Title</u> |
|------------------------|--------------|
| Jeff Aiken | Director |
| Martin Davis | Director |
| Eric Mayberry | Director |
| William Danny Rochelle | Director |
| Jack Sanders | Director |

Non Voting Members

| | |
|--------------------------|--------------------------------------|
| Matthew M. Scoggins, Jr. | Chief Executive Officer |
| Wayne Harris | Treasurer/Chief Financial Officer |
| Edward Lancaster | Secretary/General Counsel |
| Wayne Merrill | Controller/Vice President Accounting |

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: Johnson Lambert & Co., LLP
700 Spring Forest Road
Raleigh, North Carolina

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.

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.

FIDELITY BOND AND OTHER INSURANCE

The Company has elected to self-insure its fidelity coverage. Minimum fidelity bond coverage of \$1,500,000 is suggested by guidelines published in the NAIC Financial Condition Examiners Handbook. The Company is presently a named insured under a policy issued to its ultimate parent, Tennessee Farmers Mutual Insurance Company (TFMIC) as follows:

Type of Coverage

Coverage Limits

Executive Liability and Entity Security Liability Policy including Directors', Officers, Insured Entity and Employment Practices Liability Insurance

Limit of Liability (inclusive of costs of Defense) \$10,000,000

Coverage is underwritten by Federal Insurance Company which is licensed in Tennessee. A retention of \$100,000 per claim applies to Employment Practices Claims, \$10,000 retention per claim applies to Fiduciary Claims and \$100,000 retention applies to other specific defined claims outlined in sections of the policy.

The Company's administrative and other services are performed under a Management Service Agreement with TFMIC. Therefore, any workers' compensation coverage would be provided under policies issued to TFMIC. The Company is additionally covered under a Commercial General Liability Policy issued by its parent, Tennessee Farmers Mutual Insurance Company with coverage as follows:

Type of Coverage

Coverage Limits

| | |
|--|-------------|
| 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 TFMIC on their policy form. The policy is issued to the Tennessee Farm Bureau Federation, et al, with the Company listed as a named insured.

RETIREMENT PLAN AND OTHER EMPLOYEE BENEFITS

The Company has no employees. Any services performed on behalf of the Company are provided by employees of TFMIC under recitals of a Management Services Agreement. This agreement is discussed under the caption, "AGREEMENTS WITH PARENT, SUBSIDIARIES AND AFFILIATES."

TERRITORY

As of December 31, 2010, 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 2010, the Company did not write any direct premium.

PLAN OF OPERATION

The Company ceased writing direct premium in 2009. As in-force policies expired during 2009, new policies were written by TFMIC, so that no in-force policies remained after December 31, 2009. The Company currently assumes 50% of the premium written by TFMIC, as well as 50% of the associated losses and loss adjustment expenses, underwriting expenses and policyholder dividends of TFMIC.

LOSS EXPERIENCE

The loss experience of the Company for the period under examination, as reported in its Annual Statements, is as follows:

| <u>Year</u> | <u>Losses Incurred</u> | <u>LAE Incurred</u> | <u>Premiums Earned</u> | <u>Loss Ratio</u> |
|-------------|------------------------|---------------------|------------------------|-------------------|
| 2006 | \$306,023,016 | \$18,850,634 | \$400,432,977 | 81.1% |
| 2007 | 261,741,930 | 26,211,367 | 423,131,394 | 68.1% |
| 2008 | 345,695,871 | 29,113,439 | 429,001,527 | 87.4% |
| 2009 | 330,390,046 | 31,042,836 | 425,420,427 | 85.0% |
| 2010 | 350,911,982 | 28,473,239 | 448,675,880 | 84.6% |
| Total | \$1,594,762,845 | \$133,691,515 | \$2,126,662,205 | 81.3% |

AGREEMENTS WITH PARENT, SUBSIDIARIES AND AFFILIATES

The Company meets the definition of a holding company pursuant to Tenn. Code Ann. § 56-11-101.

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). (It is noted that the former part 2, §§ 56-11-201-56-11-215, was redesignated as part 1, §§56-11-101 – 56-11-115, by the code commission in 2008.)

During 2004, the TDCI performed a Target Financial Examination of the four 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 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.

Management Services Agreements:

The Company is a party to a Management Services Agreement with TFMIC. Under this agreement, TFMIC performs all management, administrative and other services that are reasonably necessary for the operation of the Company. These services include, but are not limited to: employee, legal, claims, managerial and accounting services.

The agreements provide for the Company to pay 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 agreement calls for settlement to be remitted on a quarterly basis. The agreement was dated April 25, 1991 and had an ending date of December 31, 1991 with the option to renew on calendar year basis thereafter.

Agreement To Allocate Consolidated Federal Income Tax Liability:

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

Tennessee Farmers Mutual Insurance Company
Tennessee Farmers Support Services
TFIC, Inc.
TF Support Services Corporation

The Agreement to Allocate Consolidated Federal Income Tax Liability was entered into effective December 31, 2010. The previous agreement had been effective as of December 31, 2009.

MARKET CONDUCT ACTIVITIES

The Company ceased writing direct premium in 2009. As in-force policies expired during 2009, new policies were written by TFMIC, so that no in-force policies remained after December 31, 2009. The Company currently assumes 50% of the premium written by TFMIC, as well as 50% of the associated losses and loss adjustment expenses, underwriting expenses and policyholder dividends of TFMIC. A market conduct review was made as of December 31, 2010, in conjunction with this examination. The following items were addressed:

Policy Rate and Form Filings:

A sample of eight policy rate and form filings were selected for examination for compliance with Tenn. Code Ann. § 56-5-305 (a) and § 56-7-2311 (a). It was found that all Company filings were made prior to their use in accordance with statutory requirements. The Company's filings with the Department are consistent in form and well documented.

Underwriting:

The Company uses a series of in-house underwriting manuals that are posted on the Company intranet for agent use. Changes to the manuals are posted as needed. All manuals were reviewed and found to be reasonable, easily understandable and user-friendly for use in agent and underwriter determination of acceptable risk.

In the examination of Company underwriting procedures and contract administration, contracts for open auto and property contracts and terminated property contracts were reviewed in accordance with the requirements of Tenn. Code Ann. § 56-8-104 (Unfair methods of competition and unfair or deceptive acts or practices defined), Tenn. Comp. R. & Regs. § 0780-1-34 (Eliminating Unfair Discrimination) and established Company guidance. In the examination, 39 open auto and property and 26 terminated property contracts were selected. In the examination of the above contracts, there were no instances of unfair methods of competition or unfair or deceptive acts found, and underwriting procedures and policy administration complied with the Company's established underwriting guidance.

Advertising:

All advertising items including print, internet and television materials issued by the Company were examined in accordance with Tenn. Code Ann. § 56-8-104 (1) (Unfair methods of competition and unfair or deceptive acts or practices defined - False Information and Advertising) and the NAIC Market Regulation Handbook (Chapter 16 - Marketing and Sales). In the examination of the above materials, no incidents of misrepresentation or false advertising were found and all appear to be in compliance with statutory requirements. The Company was also found to have strong

controls in place for the production and use of all advertising materials with only company-approved materials authorized for use.

Complaints:

The Company has a complaint register as required by Tenn. Code Ann. § 56-8-104 (11). A sample of 26 complaint files out of the population of 611 provided by the Company was selected for examination. The Company's records were found not to be in compliance with the statute in the following areas:

- The Company's records do not show the time it took to process each complaint. Therefore, the Company's average complaint processing time could not be determined as part of this examination.
- The Company's complaint records do not include data on complaints received through the Tennessee Department of Commerce and Insurance. The Company stated that all complaints received through the Department are resolved quickly, with a response provided back to the Department in a timely manner; however no record of these complaints is maintained.

Nature of Complaints: In the 26 complaints selected, two types of complaints were prominent: 11 complaints (42%) were associated with agent rudeness or poor service, and 6 complaints (23%) concerned denied insurance coverage - either initial or renewal.

Claims:

A sample of 52 open and unpaid auto and property claims were examined for adequacy of the Company's claim process in accordance with Tenn. Code Ann. § 56-8-104 (8) and requirements listed in Chapter 16 (Claim Standards) of the NAIC 2010 Market Regulation Handbook. Listed below is a summary of examination findings:

- In the review of all file material, Company actions and dates were readily ascertained;
- In the review of actions once a claim is received, the Company appears in all cases to acknowledge and act promptly once the claim is received;
- Other than when legal issues beyond the Company's control cause a significant delay in settlement, the Company appears to settle claims in a timely manner once liability is determined.
- The Company appears to settle claims in good faith, providing equitable settlements based on the coverage purchased.

Because of legal issues that caused a significant delay in the settlement of claims selected, average payment processing time for the sample was not determined; however, detailed review of each file showed that the Company acted promptly where required in response to claims involved in litigation.

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 Mutual Insurance Company (TFMIC)

The Company assumes, through a quota share agreement, 50% of all lines of business issued by Tennessee Farmers Mutual Insurance Company (TFMIC) effective August 1, 1991. This agreement covers liabilities that existed on and after August 1, 1991.

The Company assumes, through a quota share agreement, 50% of the business assumed by TFMIC from American Agricultural Insurance Company (AAIC), related to the Columbus line of business. This business is assumed by AAIC and retroceded to TFMIC. The Company uses the Columbus line of business to spread its geographical risk exposure.

Ceded Reinsurance with Affiliates

Tennessee Farmers Mutual Insurance Company (TFMIC)

The Company cedes, through a quota share agreement, 50% of all lines of business issued by the Company to Tennessee Farmers Mutual Insurance Company (TFMIC) effective January 1, 1999. This agreement covers liabilities that existed on and after January 1, 1999.

The Company cedes, through an all-lines aggregate agreement, losses in excess of 77% of the Company's net earned premium to Tennessee Farmers Mutual Insurance Company (TFMIC) effective January 1, 2009. TFMIC's limit is 83.33% of \$60 million annually (\$180 million in aggregate).

Ceded Reinsurance with Non-Affiliates

American Agricultural Insurance Company (AAIC)

The Company cedes, through an all-lines aggregate agreement, losses in excess of 77% of the Company's net earned premium to American Agricultural Insurance Company (AAIC) effective January 1, 2009. This agreement covers liabilities that

existed on and after January 1, 2009. AAIC's limit is 16.67% of \$60 million annually (\$180 million in aggregate).

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.

COMMISSION EQUITY

The Company reports commission equity of \$28,501,436 in the notes to financial statement in compliance with NAIC Annual Statement Instructions. This entire amount is related to the Quota Share Reinsurance Agreement (50%) with its parent, TFMIC.

No contingent liability is proposed due to the financial strength of TFMIC together with the unlikelihood that the reinsurance agreement would be commuted.

ACCOUNTS AND RECORDS

During the course of the examination, accounts were verified by various tests and procedures deemed necessary to confirm values for assets and liabilities appearing in the Company's financial statements. All of the Company's investment securities were confirmed with the custodian of such securities as of the date of this examination. General ledger trial balances were reconciled with copies of annual statements for the years 2006, 2007, 2008, 2009, and 2010. 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).

The Company is audited annually by Johnson Lambert & Co., LLP, Raleigh, North Carolina. Tenn. Comp. R. & Regs. § 0780-01-65-.08(4) requires that no partner or other person having primary responsibility for rendering a report by a certified public accounting firm may act in that capacity for more than five consecutive years. The Company is in compliance with this regulation.

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, 2010:

| <u>Where Deposited and Description</u> | <u>Par Value</u> | <u>Statement Value</u> | <u>Market Value</u> |
|--|--------------------|------------------------|---------------------|
| Tennessee Tennessee State Bond, 4.25%, Due 8/1/2026, CUSIP# 880541HK6 | \$ 2,500,000 | \$ 2,496,998 | \$2,514,125 |
| Total general deposits held for the benefit of all policyholders and creditors of the Company | <u>2,500,000</u> | <u>2,496,998</u> | <u>2,514,125</u> |
| Total | <u>\$2,500,000</u> | <u>\$2,496,998</u> | <u>\$2,514,125</u> |

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

DIVIDENDS OR DISTRIBUTIONS

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

Policyholder Dividends

| Year | Amount |
|--|------------------|
| 2006 | \$ 6,249,255 |
| 2007 | 12,603,537 |
| 2008 | 3,601,718 |
| 2009 | 3,235,347 |
| 2010 | <u>3,549,255</u> |
| Total Paid During Period of Examination | \$29,239,112 |

LITIGATION

As of December 31, 2010, 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.

FINANCIAL STATEMENT

There follows a statement of assets, liabilities and statement of income at December 31, 2010, 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 | \$782,303,058 | | \$782,303,058 |
| Preferred stocks | 625,000 | 625,000 | 0 |
| Common stocks | 44,575,742 | | 44,575,742 |
| Real estate: properties held for sale | 809,132 | | 809,132 |
| Cash and short-term investments | 39,913,498 | | 39,913,498 |
| Other invested assets | 14,295,187 | 1,095,573 | 881,439,859 |
| Receivables for securities | 648,815 | 9,602 | 639,213 |
| Investment income due and accrued | 11,518,093 | | 11,518,093 |
| Amounts recoverable from reinsurers | 1,046,445 | | 1,046,445 |
| Net deferred tax asset | 29,262,222 | 10,152,709 | 19,109,513 |
| Receivable from parent, subsidiaries and affiliates | 5,905,364 | | 5,905,364 |
| Aggregate write-ins for other than invested assets | <u>230,108</u> | <u>230,108</u> | <u>0</u> |
| Totals | <u>\$931,132,664</u> | <u>\$12,113,390</u> | <u>\$ 919,019,274</u> |

LIABILITIES, SURPLUS, AND OTHER FUNDS

| | |
|---|-----------------------|
| Losses | \$84,212,932 |
| Reinsurance payable on paid loss and loss adjustment expenses | 0 |
| Loss adjustment expenses | 23,123,757 |
| Other expenses (excluding taxes, licenses and fees) | 5,603 |
| Taxes, licenses and fees (excluding federal and foreign income tax) | 1,217,559 |
| Unearned premiums | 177,027,554 |
| Dividends declared and unpaid: policyholders | 3,680,550 |
| Amounts withheld or retained by company for account of others | 60,740 |
| Payable to parent, subsidiaries and affiliates | 8,701,619 |
| Payable for securities | <u>688,326</u> |
| Total Liabilities | 298,718,640 |
| | |
| Common capital stock | 46,431,088 |
| Gross paid in and contributed surplus | 27,994,525 |
| Unassigned funds (surplus) | <u>545,875,021</u> |
| Surplus as regards policyholders | 620,300,634 |
| | |
| Total liabilities and surplus | <u>\$ 919,019,274</u> |

STATEMENT OF INCOME

UNDERWRITING INCOME

| | | |
|--------------------------------------|-------------------|--------------------|
| Premiums earned | | \$448,675,880 |
| Deductions: Losses incurred | \$350,911,982 | |
| Loss adjustment expenses incurred | 28,473,239 | |
| Other underwriting expenses incurred | <u>72,055,296</u> | |
| Total underwriting deductions | | <u>451,440,517</u> |
| Net underwriting gain (loss) | | (2,764,637) |

INVESTMENT INCOME

| | | |
|-------------------------------------|------------------|------------|
| Net investment income earned | 34,705,416 | |
| Net realized capital gains (losses) | <u>3,362,530</u> | |
| Net investment gain | | 38,067,946 |

OTHER INCOME

| | | |
|--|--|---------------------|
| Aggregate write-ins for miscellaneous income | | <u>4,167,626</u> |
| Total other income | | 4,167,626 |
| Net income before dividends to policyholders and before federal income taxes | | 39,470,935 |
| Dividends to policyholders | | 3,549,255 |
| Federal income taxes incurred | | <u>10,283,129</u> |
| Net income | | <u>\$25,638,551</u> |

CAPITAL AND SURPLUS

| | | |
|--|--------------|----------------------|
| Surplus as regards policyholders, December 31 prior year | | \$603,401,354 |
| Net income | \$25,638,551 | |
| Change in net unrealized capital gains (losses) | (8,307,214) | |
| Change in net deferred income tax | 10,451,645 | |
| Change in non-admitted assets | (11,726,927) | |
| Cumulative effect of changes in accounting principles | 0 | |
| Capital changes: Paid in | (13,933) | |
| Capital changes: Transferred from surplus (Stock Dividend) | 1,353,200 | |
| Surplus adjustments: Paid in | (205,260) | |
| Surplus adjustments: Transferred to capital (Stock Dividend) | (1,353,200) | |
| Aggregate write-in for gains and losses in surplus | 1,062,418 | |
| Change in surplus as regards policyholders for the year | | 16,899,280 |
| Surplus as regards policyholders, December 31 current year | | <u>\$620,300,634</u> |

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

| Surplus as regards policyholders December 31 | <u>2006</u> | <u>2007</u> | <u>2008</u> | <u>2009</u> | <u>2010</u> |
|---|-----------------------------|-----------------------------|-----------------------------|-----------------------------|-----------------------------|
| Previous Year | \$430,996,986 | \$479,047,483 | \$559,085,055 | \$564,526,627 | \$603,401,354 |
| Net Income | 42,495,278 | 82,083,969 | 16,257,174 | 28,267,807 | 25,638,551 |
| Change in net unrealized capital gains or (losses) | 771,459 | (1,531,786) | (7,937,536) | 5,099,546 | (8,307,214) |
| Change in net deferred income tax | 3,231,932 | (619,274) | (3,849,728) | 3,778,709 | 10,451,645 |
| Change in non-admitted Assets | (75,370) | (1,215) | 913,934 | (151,639) | (11,726,927) |
| Capital changes: Paid in | 18,646 | 7,477 | 4,567 | (30,619) | (13,933) |
| Capital changes: Transferred From surplus (Stock Dividend) | 1,948,617 | 2,046,699 | 2,149,344 | 0 | 1,353,200 |
| Surplus adjustments: Paid in | 195,712 | 98,401 | 53,161 | (401,499) | (205,260) |
| Surplus adjustments: Transferred To capital (Stock Dividend) | (1,948,617) | (2,046,699) | (2,149,344) | 0 | (1,353,200) |
| Aggregate write-ins for gains and losses in surplus | <u>1,412,840</u> | <u>0</u> | <u>0</u> | <u>2,312,422</u> | <u>1,062,418</u> |
| Surplus as regards policyholders, December 31 current year | <u>\$479,047,483</u> | <u>\$559,085,055</u> | <u>\$564,526,627</u> | <u>\$603,401,354</u> | <u>\$620,300,634</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 has a complaint register as required by Tenn. Code Ann. § 56-8-104 (11); however, the Company's records were found not to be in compliance with the statute in the following areas:

- The Company's records do not show the time it took to process each complaint. Therefore, the Company's average complaint processing time could not be determined as part of this examination.
- The Company's complaint records do not include data on complaints received through the Tennessee Department of Commerce and Insurance. The Company stated that all complaints received through the Department are resolved quickly, with a response provided back to the Department in a timely manner; however no record of these complaints is maintained.

Prior to completion of the examination, the Company upgraded its complaint handling system so that the date each complaint is received is logged. The system also tracks the date that the complaint was resolved. In addition, complaints received from the Tennessee Department of Commerce and Insurance are now tracked using the complaint register.

It appears that the Company is now in compliance with Tenn. Code Ann. § 56-8-104 (11).

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 Assurance Company of Columbia, Tennessee.

In such manner, it was determined that, as of December 31, 2010, the Company had admitted assets of \$919,019,274 and liabilities, exclusive of unassigned funds, of \$298,718,640. Thus, there existed for the additional protection of the policyholders the amount of \$620,300,634 in the form of capital, gross paid in and contributed surplus 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, David N. Bobo and Gregory Bronson, CIE, MCM, Insurance Examiners for the state of Tennessee, and Norman Chandler, CPA, CPCU, CFE, ARe, AIAF, ARC, ACP of the firm TaylorChander, LLC, Montgomery, Alabama, participated in the work of this examination. An actuarial review was performed by Gregory S. Wilson, FCAS, MAAA of the actuarial firm Lewis & Ellis, Inc. of Richardson, Texas.

Respectfully submitted,



Rhonda Bowling-Black, CFE
Examiner- in-Charge
State of Tennessee
Southeastern Zone, NAIC

AFFIDAVIT

The undersigned deposes and says that she has duly executed the attached examination report of Tennessee Farmers Assurance Company dated June 14, 2012, and made as of December 31, 2010, on behalf of the Department of Commerce and Insurance, state of Tennessee. Deponent further says she is familiar with such instrument and the contents thereof, and that the facts therein set forth are true to the best of her knowledge, information and belief.

Rhonda Bowling-Black
Rhonda Bowling-Black, CFE
Examiner-in-Charge
State of Tennessee
Southeastern Zone, N.A.I.C.

Subscribed and sworn to before me

this 15th day of

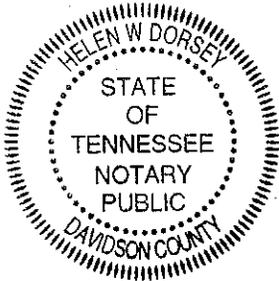
June, 2012

Notary *Helen W. Dorsey*

County *Davidson*

State *Tennessee*

Commission Expires *03/03/2014*



**Tennessee Farmers Assurance Company
Organizational Chart
December 31, 2010**

