



MARKET CONDUCT EXAMINATION REPORT

of

**Lake County Farmers' Mutual
Insurance Company
POLSON, MONTANA**

as of December 31, 2009

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SCOPE OF EXAMINATION

The Montana Insurance Department conducted a market conduct examination of Lake County Farmers' Mutual Insurance Company, (hereinafter also referred to as the Company), that covered a four-year period from January 1, 2006, through December 31, 2009.

The examination was conducted pursuant to the provisions of Mont. Code Ann. §§ 33-1-401 *et seq.* and 33-4-316, and in accordance with the procedures and guidelines outlined in the Market Conduct Examiners Handbook as adopted by the National Association of Insurance Commissioners and the Office of the Commissioner of Securities and Insurance, Montana State Auditors (CSI). The examination took place at the Company's home office located at 410 First Street East, Suite 1, Polson, Montana 59860.

OPERATIONS AND MANAGEMENT

The Company was originally incorporated as a county farm mutual insurer on October 11, 1928, under the provisions of then existing Montana statutes. In 1971 the Company inadvertently allowed its corporate existence to lapse. The Company reincorporated under the same name effective October 30, 1989. The Company's current articles of incorporation were filed in accordance with Mont. Code Ann. § 33-4-203, and approved by the Montana Secretary of State on January 25, 1990. The Company amended its articles of incorporation to change from a county mutual to a state mutual on October 7, 1997.

The Company is authorized to insure for property and liability risks in keeping with the provisions of Mont. Code Ann. § 33-4-501. The Company is currently insuring property against the risk of fire and lightning. The Company does not insure for liability exposures. The Company currently writes business primarily in the Montana counties of Lake, Flathead, Missoula and Sanders.

The Company's articles of incorporation provide for management conducted by a board of directors made up of 11 members. Directors are elected to serve staggered, three-year terms, with at least one director to be elected at each annual meeting of the Company. The directors during the time period of the examination are as follows:

<u>Director Name and Address</u>	<u>Term Expires</u>	<u>Additional Term(s) Expires</u>
Bruce Campbell (V.P.) Polson, MT	12/31/2006	12/31/2009

Garry Ray Keirn Trout Creek, MT	12/31/2006	12/31/2009
Jim Stobie Hot Springs, MT	12/31/2006	12/31/2009
Jerry Cederstrom Polson, MT	12/31/2007	12/31/2010
Stuart Fryberger* Charlo, MT	12/31/2007	12/31/2010
Lisa French Plains, MT	12/31/2007	12/31/2010
Sherry Wolf** Ronan, MT	12/31/2007	12/31/2010
George Christopher Arlee, MT	12/31/2008	12/31/2011
Ross McAlpin (Pres.) Big Fork, MT	12/31/2008	12/31/2011
Duane Obenchain Pablo, MT	12/31/2008	12/31/2011
Amelia Gipe***	12/31/2006	

*Stuart Fryberger resigned effective July 1, 2008. At the annual meeting of the Company on January 17, 2009, Nancy Fryberger was elected to fill the remainder of the term.

**Sherry Wolf resigned effective January 16, 2010. The vacated directorship was not filled at the annual meeting on January 16, 2010.

*** Amelia Gipe resigned eff. January 21, 2006. The vacated directorship was not filled during the time period under examination.

Ross McAlpin and Bruce Campbell were elected to serve successive annual terms as President and Vice-President, respectively, during the time period covered by the examination. Gerald L. Newgard has served as the Company's Secretary/Treasurer during the time period covered by the examination.

During the time period covered by the examination, the Company has not filled two of the vacated director positions; therefore, the Company has been operating with fewer directors than required by its articles of incorporation.

The terms of the Company's directors expire at the end of the calendar year. Several weeks go by before the annual meeting at which time elections are held to fill the already expired terms. During the gap in time between expiration of directors' terms and the annual meeting at which director elections occur the Company is operating with fewer directors than provided for in the articles of incorporation.

The Company's articles of incorporation and Mont. Code Ann. §33-4-309(2) require individuals serving as directors to be a member of the insurer. Director Lisa French did not have a policy in force with the Company as of December 31, 2009. This was rectified prior to the Company's receipt of notice of the examination.

The Company has not developed written policies or procedures for the treatment and protection of nonpublic personal financial information as required by Mont. Admin. R. 6.6.7007.

The Company does not provide insureds with a notice of information practices or a notice of privacy practices as required by Mont. Code Ann. § 33-19-202.

The computer program used by the Company contains nonpublic personal financial information belonging to insureds and is not password protected in accordance with the provisions and intent of Mont. Code Ann. Title 33, Chapter 19 and corresponding administrative rules of Montana including, but not limited to, Mont. Admin. R. 6.6.7007.

The apostrophe used in the Company name appears in the Company's By-Laws as Farmer's. The name set forth on the Company's certificate of authority and articles of incorporation appears as Farmers'. The apostrophe is altogether absent on checks issued by the Company.

Policyholder records meet retention requirements as to time, however, records are not well documented as to status or specific underwriting action taken. The Company is undergoing development of a software program intended to aid in the accessibility of basic policyholder information.

COMPLAINT HANDLING

During the time period covered by the examination, the Company did not maintain a complaint register in compliance with Mont. Code Ann. § 33-18-1001. The Company did maintain and provide documentation relevant to the single complaint lodged with the CSI during time period covered by this examination and has adequate procedures in place to address and respond to complaints in a timely manner.

MARKETING AND SALES

The Company utilizes a print media advertisement. The content of the advertisement is straightforward and no exceptions were noted. During the time period covered by the examination, the Company did not make use of any type of sales brochure or marketing materials.

PRODUCER LICENSING

The Company relies solely on its directors to act as producers. The Company does not insure liability exposures; therefore, directors of the Company are not required to be licensed by the CSI or appointed by the Company in accordance with Mont. Code Ann. § 33-4-312.

POLICYHOLDER SERVICE

Applications are processed and policies issued in a prompt and accurate manner. The Company makes use of a policy change request form to communicate and process insured requested changes during the policy term.

In accordance with the Company's By-Laws, insured-requested cancellations must be received in writing and the policy must be surrendered to the Company. In the event the insured is unable to locate and return the policy to the Company, a lost policy affidavit is supplied. Refunds are promptly and accurately calculated and mailed to the insured upon the Company's receipt of the required documentation. In the event an insured requests cancellation of a policy prior to the first year anniversary, a short rate fee applies. The method of refund calculation and short rate fee are provided to policyholders at the time of policy issuance in the form of an endorsement recorded as #LCFM-1.

UNDERWRITING AND RATING

The Company issues policies on the basis of a five-year policy period. The Company does not write multiple physical locations on a single policy. The Company provides its insureds with timely notice of the impending policy expiration and the necessity to complete and submit a new application in order to avoid a lapse in coverage. Director agents are responsible for expediting this process. The Company requires payment of the entire five-year premium at or within ninety days of policy inception. In the event the Company fails to receive payment, or is in receipt of only a partial payment within the 30 days following the policy effective date, a premium reminder notice is mailed. The reminder notice requests payment in full within the ensuing 30 days. In the event premium remains due at the end of this cumulative 60 day period

a notice is mailed to the insured advising of policy cancellation. Cancellation is effective 30 days from the date of mailing unless the stated amount of premium due is received by the Company prior to the effective date of cancellation.

During the time period under examination there have been no policy rescissions. The examiners did not observe any Company initiated mid-term cancellations or non-renewals.

Applications and Change request forms are thoroughly completed and accurately reflect the nature of the risks being insured. The Company's underwriting guidelines and practices are consistent with the Company's by-laws and do not appear to be unfairly discriminatory. Rates are uniform and non-discriminatory in nature.

The by-laws of the Company are to be made part of the contracts of insurance issued to its members pursuant to Mont. Code Ann. § 33-4-303. The Company provides a copy of the by-laws to its insureds; however, the by-laws have not been filed with the CSI in accordance with Mont. Code Ann. § 33-4-509.

CLAIMS

Examiners reviewed all claims reported during the time period covered by the examination. Claims were resolved in a timely manner; however, there was no documentation in the files to demonstrate that a complete and thorough investigation was conducted. Claim files did not contain a "Report of Loss" claim form as required by the terms and conditions of the policy nor did they contain statements, photographs, ACV evaluations, etc., to support the company's final handling of the claim. Claim files did contain adequate information to establish the company's evaluation of the policyholders' loss and final adjudication of the claim.

Sworn "Proof of Loss" forms were often used by the company to record additional information thus altering the legal purpose of the document and loss settlement policy provisions were often applied inconsistently when replacement cost and depreciation was an issue.

SUMMARY OF SIGNIFICANT FINDINGS

The Company has been conducting operations utilizing fewer directors than set forth by its Articles of Incorporation.

During the time period covered by the examination the Company did not maintain a complaint register in compliance with Mont. Code Ann. § 33-18-1001.

The Company does not provide insureds with a notice of information and privacy practices as required by Mont. Code Ann. § 33-19-202.

The Company has not taken measures to protect the integrity of electronically recorded, non-public personal financial information in accordance with Mont. Code Ann. § 33-19-106 and corresponding administrative rules of Montana including, but not limited to, A.R.M. 6.6.7007.

The Company's by-laws do not accurately reflect the name of the Company in accordance with its certificate of authority and articles of incorporation.

The Company's by-laws were not filed with the Forms division of the CSI pursuant to Mont. Code Ann. § 33-4-509.

Claim files did not contain sufficient documentation to determine the cause and origin of the loss.

Claim files did not contain sufficient documentation to determine the actual scope and extent of the loss.

Claim files did not contain a sworn "Proof of Loss" form that complied with the legal intent of the policy.

Claim files did not demonstrate the Actual Cash Value provisions of the policy were always applied consistently.

Claim files did not contain a "Report of Loss" form as required by the terms of the policy.

CONCLUSION

The Market Conduct Examination Report of Lake County Farmers' Mutual Insurance Company is respectfully submitted to the Honorable Monica J. Lindeen, State Auditor and Commissioner of Securities and Insurance of the state of Montana.

The examiners wish to express their appreciation for the courteous and prompt cooperation and assistance of the officers and employees of the Company during the course of the examination.

RECOMMENDATIONS FOR CORRECTIVE ACTION

The Company must fill positions vacated by departing directors or amend its Articles of Incorporation to accurately reflect current operations.

The Company must institute the use of a complaint register that is compliant with the provisions of Mont. Code Ann. § 33-18-1001.

The Company must provide its insureds with notice of information practices and an annual notice of privacy practices in accordance with Mont. Code Ann. § 33-19-202.

The Company must take measures to password protect the operating system containing policyholder records in accordance with Mont. Code Ann. § 33-19-106 and corresponding administrative rules of Montana; including, but not limited to Mont. Admin. R. 6.6.7007.

The Company must amend its by-laws in order to accurately reflect the name of the Company; consistent with its certificate of authority and articles of incorporation. The amended by-laws must be filed with the Forms division of the CSI in order to comply with Mont. Code Ann. § 33-4-509.

The company must adopt procedures to obtain sufficient documentation to determine the cause and origin of a loss.

The company must adopt procedures to obtain sufficient documentation to determine the actual scope and extent of a loss.

The company must adopt procedures to insure that "Proof of Loss" forms comply with the legal intent of the policy.

The company must adopt procedures to insure the Actual Cash Value provisions of the policy are always applied consistently.

The company must adopt procedures to obtain a "Report of Loss" form, as required by the terms of the policy, from every policyholder that files a claim with the company.

ADDITIONAL SUGGESTIONS AND COMMENTS

It is suggested that the Company, in identifying and developing its software program, consider the ability to maintain an electronic record of active policyholders' information including name, policy number, location of insured risk, mailing address, policy coverage limits, effective date of policy, the expiration date of policy, the number assigned to any previous policy that was replaced by the current policy and the coverage amounts afforded by the policy.

It is further suggested that the Company maintain an electronic record of cancelled policies containing the policy cancellation date, amount of premium refund, and the reason for cancellation; such as: sold, insured elsewhere, non-payment of premium, or company initiated cancellation in addition to the information suggested in the previous paragraph.

The checking account used by the Company should reflect the name of the Company as it exists on the Certificate of Authority, including the correct positioning of the apostrophe.

