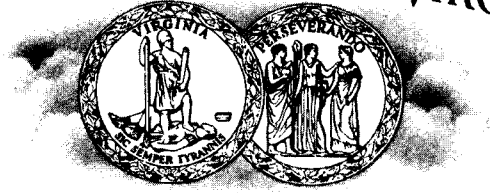


**EXAMINATION REPORT  
OF  
VIRGINIA FARM BUREAU  
TOWN AND COUNTRY INSURANCE COMPANY  
Richmond, Virginia  
as of  
December 31, 2008**

# COMMONWEALTH OF VIRGINIA

ALFRED W. GROSS  
COMMISSIONER OF INSURANCE  
STATE CORPORATION COMMISSION  
BUREAU OF INSURANCE



P.O. BOX 1157  
RICHMOND, VIRGINIA 23218  
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I, Alfred W. Gross, Commissioner of Insurance of the Commonwealth of Virginia, do hereby certify that the annexed copy of the Examination Report of Virginia Farm Bureau Town and Country Insurance Company as of December 31, 2008, is a true copy of the original report on file with this Bureau.

**IN WITNESS WHEREOF**, I have hereunto set my hand  
and affixed to the original the seal of the Bureau at the City  
of Richmond, Virginia this 21<sup>st</sup> day of December, 2009

A handwritten signature in cursive script that reads "Alfred W. Gross".

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Alfred W. Gross  
Commissioner of Insurance

(SEAL)

**TABLE OF CONTENTS**

DESCRIPTION..... 1

HISTORY ..... 1

MANAGEMENT AND CONTROL ..... 2

RELATED PARTY TRANSACTIONS..... 5

DIVIDENDS TO SHAREHOLDER ..... 5

FIDELITY BOND AND OTHER INSURANCE ..... 5

TERRITORY AND PLAN OF OPERATION ..... 5

GROWTH OF THE COMPANY ..... 7

REINSURANCE..... 8

SCOPE ..... 11

FINANCIAL STATEMENTS ..... 12

RECOMMENDATION FOR CORRECTIVE ACTION ..... 18

CONCLUSION..... 19

September 4, 2009  
Richmond, Virginia

Honorable Alfred W. Gross  
Commissioner of Insurance  
Commonwealth of Virginia  
Richmond, Virginia

Dear Sir:

Pursuant to your instructions and by authority of § 38.2-1317 of the Code of Virginia, an examination of the affairs and financial condition of

**VIRGINIA FARM BUREAU  
TOWN AND COUNTRY INSURANCE COMPANY**

Richmond, Virginia

hereinafter referred to as the Company, has been completed. The report thereon is submitted for your consideration.

**DESCRIPTION**

The Company is a stock property and casualty insurer and was incorporated on April 5, 1993, and became licensed in Virginia on October 13, 1994. It was last examined by representatives of the Virginia State Corporation Commission's Bureau of Insurance (Bureau) as of December 31, 2005. This examination covers the period from January 1, 2006 through December 31, 2008.

**HISTORY**

The Company was issued a certificate of incorporation on April 5, 1993, by the Virginia State Corporation Commission (Commission). According to the Articles of Incorporation, the purposes for which the Company was organized are as follows:

To make, issue and effect contracts or policies of insurance providing coverage for any and all classes of insurance, excluding life insurance, annuities and title insurance, ...

To cede to or accept from any insurer reinsurance upon the whole or any part of any risk, with or without contingent liability or participation.

To have and to exercise all powers necessary or convenient to carry into effect any or all of the purposes for which the corporation is organized, including the conduct of any and all acts incidental to carrying into effect the purposes as aforesaid.

The Company's authorized capital is 10,000,000 shares of common stock with a par value of \$2 per share. Initial capitalization consisted of 500,000 shares issued and outstanding, with paid in surplus in the amount of \$3,500,000. At initial licensing, Virginia Farm Bureau Mutual Insurance Company (VFBMIC) was the sole owner of the Company and held all of the issued and outstanding stock. On October 31, 1994, VFBMIC transferred 100% of the common capital stock of the Company, along with \$953,620 in cash and 100% of the common capital stock of Virginia Farm Bureau Fire and Casualty Insurance Company (VFBFCIC) to Farm Bureau Holdings of Virginia, Inc. (Holdings) in exchange for 100% of the common capital stock of Holdings. At the conclusion of the exchange, Holdings contributed an additional \$5,000,000 in surplus to the Company. In 1998, the Company received \$5,000,000 in additional paid in capital from the parent.

### **MANAGEMENT AND CONTROL**

The bylaws of the Company provide for its affairs to be managed by a Board of Directors consisting of one or more individuals, but the number of directors shall be the same as the number of elected directors of Virginia Farm Bureau Federation (Federation). None of the members of the Board of Directors need to be a stockholder of the Company, but all must be members of the Board of Directors of the Federation. The bylaws further provide that the directors be elected at the regular annual meeting of the Company by the stockholders for the term of one year. A majority of the members of the Board of Directors constitutes a quorum for the transaction of business.

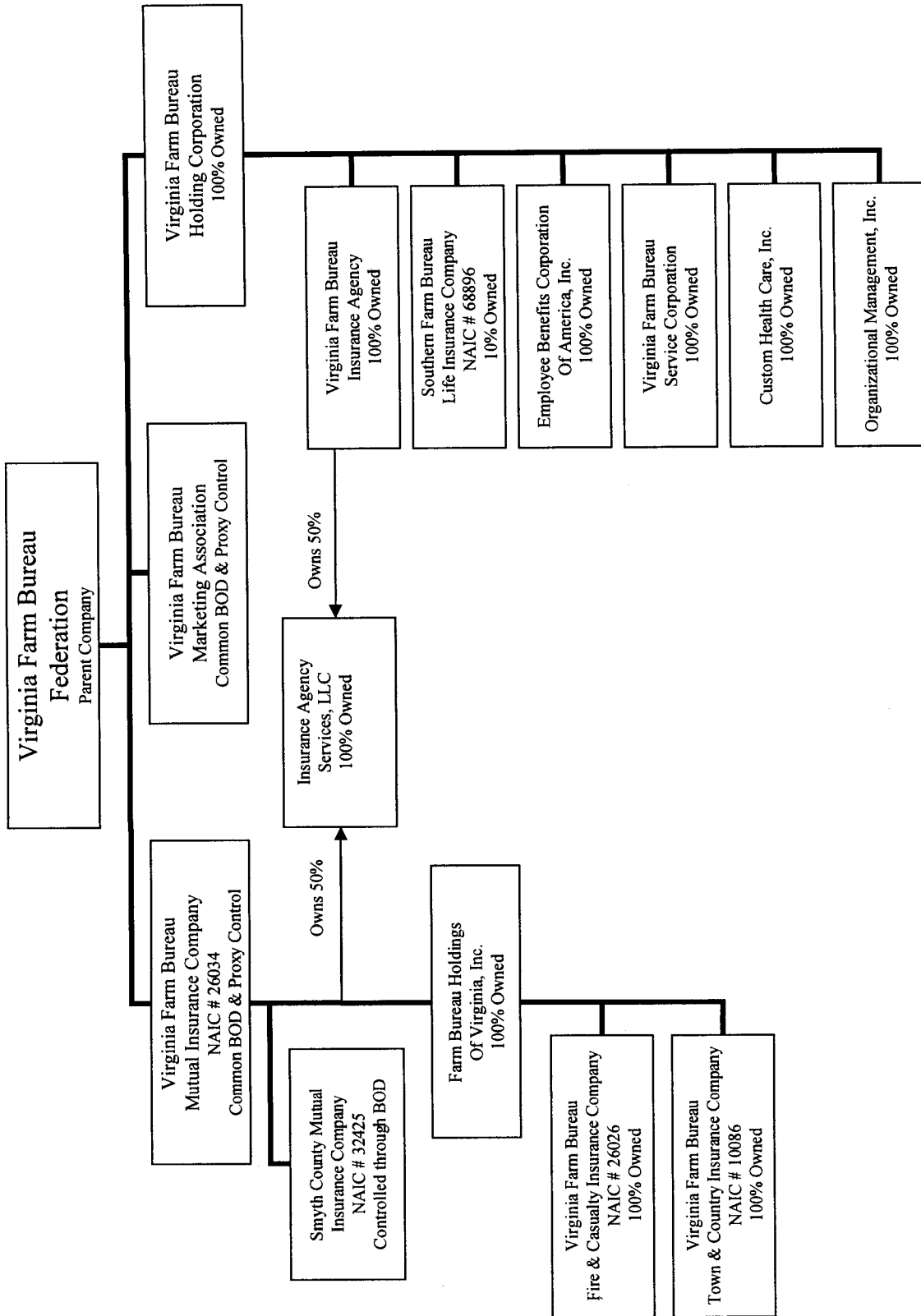
The bylaws do not require any committees to be established; however, two standing committees, a budget and audit committee and an investment and finance committee, have been established to date. The bylaws also provide that the officers of the Company shall be a president, a first vice president, an executive vice president, a secretary and a treasurer, and such other officers and positions as the Board of Directors may deem necessary.

At December 31, 2008, the Board of Directors and Officers were as follows:

<u>Directors</u>	<u>Business or Affiliation</u>	<u>County of Residence</u>
Wayne F. Pryor	Farmer/President of the Company	Goochland
Archie B. Atwell	Farmer	Smyth
Janice A. Burton	Farmer	Halifax
Martin L. Everett	Farmer	Southampton
Emily F. Edmondson	Farmer	Tazwell
Thomas E. Graves, Jr.	Farmer	Orange
Robert E. Hall	Farmer	Northumberland-Lancaster
David L. Hickman	Farmer	Accomack
Evelyn H. Janney	Farmer	Montgomery
Jordan M. Jenkins, Jr.	Farmer	Lunenburg
Gordon R. Metz, Jr.	Farmer	Henry
Stephen L. Saufley	Farmer	Rockingham
Edward A. Scharer	Farmer	Albemarle
Howard C. Tinder, Sr.	Farmer	Albemarle
Joseph H. Williams	Farmer	Pittsylvania
Henry E. Wood, Jr.	Farmer	Buckingham
James A. Yankey	Farmer	Prince William/Fairfax
John R. Zirkle, Sr.	Farmer	Shenandoah

<u>Officers</u>	<u>Title</u>
Wayne F. Pryor	President, Administrative Officer and Chief Executive Officer
Richard L. Rivers	Executive Vice President and General Manager
Edward A. Scharer	First Vice President
Vacant	Treasurer
Jonathan S. Shouse	Secretary
Peggy L. McClelland	Assistant Treasurer
David A. Priddy	Assistant Treasurer

The Company is a member of a holding company system as defined by the Code of Virginia. The Company is a wholly-owned subsidiary of Holdings. Holdings is 100% owned by VFBMIC, which is controlled by the Federation by means of a common board of directors and through proxy control. The following organizational chart illustrates this relationship at December 31, 2008:



## **RELATED PARTY TRANSACTIONS**

### **Administrative Services Agreement**

The Company entered into an Administrative Services Agreement with VFBMIC effective September 14, 1994. Under the terms of the Agreement, VFBMIC is responsible for performing and providing accounting, financial, investment, actuarial, underwriting, claims and computer services for the Company. As compensation for these services, the Company will pay VFBMIC a quarterly fee equal to the actual cost of the labor and expenses incurred in the performance of the services. In 2008, 2007 and 2006, the Company paid VFBMIC \$15,099,294, \$13,730,213 and \$12,577,885, respectively.

### **Federal Income Tax Allocation Agreement**

Effective January 1, 2007, the Company entered into a federal income tax allocation agreement with VFBMIC AND VFBFCIC. The purpose of this agreement is to provide for the filing of consolidated federal income tax returns for the allocation of federal income tax liability and savings among the companies. The method of allocation between the companies is made primarily on a separate return basis. The intercompany tax balances are settled quarterly. The final settlement shall be made within 30 days after the filing of the consolidated income tax return.

## **DIVIDENDS TO SHAREHOLDER**

The Company paid no dividends to its sole shareholder during the period covered by this examination.

## **FIDELITY BOND AND OTHER INSURANCE**

At December 31, 2008, the Company was a named insured on a fidelity bond with a \$2,000,000 policy limit, subject to a \$20,000 deductible. In addition, the Company was a named insured on the following insurance policies: Fleet Automobile, Workers' Compensation and Employers' Liability, Directors' and Officers' Liability, Professional Liability, Blanket Building and Business Personal Property and Commercial Umbrella Liability.

## **TERRITORY AND PLAN OF OPERATION**

The Company confines its operations to Virginia where it is licensed to transact the business of accident and sickness, fire, miscellaneous property, farmowners' multiple peril, homeowners' multiple peril, commercial multiple peril, ocean marine, inland marine, workers' compensation and employers' liability, liability other than automobile,



automobile liability, automobile physical damage, aircraft liability, aircraft physical damage, fidelity, surety, glass, burglary and theft, boiler and machinery, animal and water damage insurance.

Business is produced by approximately 265 agents, who are compensated based on the amount of premiums written plus bonuses which are dependent upon a combination of the growth and profitability of the agent's book of business plus the companies' net income before taxes. Office space and clerical help are furnished to the agents in their territories by county Farm Bureaus under a Memorandum of Agreement with the Federation, which are compensated by the Company based upon a percentage of premium income, or under a Joint Operations Agreement whereby the Company would incur all operational costs of the office.

Risks are bound by the agents when applications are accepted in the field from qualified applicants, after which policies are issued from the Richmond office. If an insured is subsequently found not to meet the Company's underwriting requirements, the policyholder may be notified that his coverage will be canceled.

Losses are reported to the county Farm Bureau through which the application was taken. Claims are confirmed and adjusted by the Company's salaried personnel where practicable, otherwise independent professional adjusters or Farm Bureau insurance companies in other states are used.

## GROWTH OF THE COMPANY

The following data, obtained from annual statements and this examination report, indicate the growth of the Company from inception to December 31, 2008:

<u>Year</u>	<u>Admitted Assets</u>	<u>Liabilities</u>	<u>Common Capital Stock</u>	<u>Gross Paid-in and Contributed Surplus</u>	<u>Unassigned Funds (Surplus)</u>
1999	\$24,824,325	\$14,145,935	\$1,000,000	\$13,500,000	(\$3,821,610)
2000	27,023,480	16,228,693	1,000,000	13,500,000	(3,705,213)
2001	28,261,369	16,862,922	1,000,000	13,500,000	(3,101,553)
2002	30,307,437	19,090,556	1,000,000	13,500,000	(3,283,119)
2003	32,924,092	21,683,056	1,000,000	13,500,000	(3,258,964)
2004	40,766,155	28,495,941	1,000,000	13,500,000	(2,229,786)
2005	42,132,699	29,004,287	1,000,000	13,500,000	(1,371,588)
2006	46,718,946	32,214,306	1,000,000	13,500,000	4,640
2007	48,365,036	32,819,120	1,000,000	13,500,000	1,045,916
2008	49,997,493	34,404,948	1,000,000	13,500,000	1,092,545

<u>Year</u>	<u>Premiums Earned</u>	<u>Loss and Loss Adjustment Expenses Incurred</u>	<u>Other Underwriting Expenses</u>	<u>Net Underwriting Gain or (Loss)</u>
1999	\$14,560,737	\$11,618,740	\$1,963,877	\$978,120
2000	14,211,285	11,735,323	3,358,547	(882,585)
2001	16,612,090	13,407,952	4,528,859	(1,324,721)
2002	17,538,879	14,518,461	4,375,744	(1,355,326)
2003	18,651,593	15,603,213	4,760,797	(1,712,417)
2004	19,858,896	14,491,107	5,280,342	87,447
2005	20,486,531	13,423,977	7,599,452	(536,898)
2006	25,376,167	17,449,009	8,402,136	(474,978)
2007	24,080,618	16,641,909	8,466,387	(1,027,678)
2008	23,527,686	14,750,988	8,167,918	608,780

**REINSURANCE**

The Company had the following reinsurance agreements in force at December 31, 2008:

**Ceded:**

<u>Type of Agreement</u>	<u>Class of Business</u>	<u>Company Retention</u>	<u>Reinsurers' Limits</u>
Surplus Share	Property (except auto physical damage)	\$300,000 each risk	\$40,000,000; occurrence cap of \$10,000,000
Quota Share	Property (except auto physical damage)	60% of net subject premium and net retained insurance liability	\$6,000,000 per occurrence
Excess of Loss	Property (Catastrophe)	12% of subject net earned premium with a 5% participation	\$170,000,000
Excess of Loss	Property (Catastrophe -Terrorism)	\$3,050,000	\$6,100,000
Over Other Protections	Property		\$100,000,000 for any one occurrence; \$200,000,000 annually

<u>Type of Agreement</u>	<u>Class of Business</u>	<u>Company Retention</u>	<u>Reinsurers' Limits</u>
Excess of Loss	Liability	\$550,000	\$22,000,000; occurrence cap of \$1,200,000
	Workers' Compensation	\$500,000	\$30,000,000 (\$1,200,000 maximum employers' liability limit)
Quota Share	Casualty (Umbrella Liability)	10% of \$1,000,000	90% of first \$1,000,000; 100% up to \$15,000,000
Excess of Loss	Insurance Agents Professional Liability (Claims Made)	\$100,000 each loss event; \$100,000 aggregate	\$1,900,000 aggregate limit
Excess of Loss	Farm Pollution Liability (Claims Made)	\$500 each incident	\$1,000,000

Affiliate Agreements:

On September 20, 1994, the Company entered into a Net Premiums Reinsurance Agreement with VFBMIC, to be effective September 1, 1994. The agreement provides for reinsurance of 95% of the Company's net losses and underwriting expenses incurred, for which VFBMIC receives 95% of earned premiums less a commission of one half of one percent of premiums ceded. The Bureau approved this agreement.

On December 19, 1997, the Company entered into a separate Net Premiums Reinsurance Agreement with VFBMIC, which became effective beginning with accident year 1998. This agreement provides for the reinsurance of 100% of the Company's net losses and underwriting expenses incurred for all lines of business except automobile, for which VFBMIC receives 100% of earned premiums less a commission of one half of one percent of premiums ceded business. The Bureau approved this agreement.

Reinsurance Pooling Agreement:

Effective January 1, 1998, the Company entered into a Reinsurance Pooling Agreement with VFBMIC and VFBFCIC for automobile policies. Each of the companies is an insured as well as a participant in the agreement. Pursuant to this agreement, each of the companies will cede 100% of their direct automobile business earned and assumed, after deduction for any reinsurance ceded to others (with the exclusion of the quota share agreement), after the effective date of this agreement. For the 1998 accident year, each participant will assume an initial retrocession from the Pool in the following percentages:

Virginia Farm Bureau Mutual Insurance Company	60%
Virginia Farm Bureau Fire and Casualty Insurance Company	20%
Virginia Farm Bureau Town and Country Insurance Company	20%

Each participant will assume their proportionate share of the net premiums earned, net losses and loss adjustment expenses incurred, and underwriting expenses incurred that are ceded to the Pool, but shall not be liable for any amounts beyond said proportionate share, irrespective of the inability of other participants or reinsureds to meet their respective obligations. The cession under the quota share agreement occurs after the cessions to the Pool and before the retrocessions back to the Pool participants.

For the 1999 accident year and for each subsequent accident year, each participant will assume a retrocession from the Pool in a percentage that will be determined by the Board of Directors of the participating companies in January of the applicable year. For the accident year 2006 through 2008, the respective Boards elected to retain the above percentages.

All agreements have an insolvency clause.

## SCOPE

This is a full scope financial condition examination initiated and conducted under the provisions of Article 4, Chapter 13 of Title 38.2 of the Code of Virginia. The examination covers the period from January 1, 2006 through December 31, 2008. Assets were verified and liabilities were established at December 31, 2008. A review of income and disbursements for the period was made to the extent deemed necessary.

The items comprising the Balance Sheet for which Specific Risk Analyses (SRA) were required had medium or low risk assessments as determined from the National Association of Insurance Commissioners *Examiners' Handbook*. Analytical review procedures were applied for non-SRA items.

The services of Oliver Wyman Actuarial Consulting, Inc. were engaged pursuant to the provisions of Code of Virginia § 38.2-1318 E. This engagement was made to provide an actuarial report as to the reasonableness of the Company's total loss and loss adjustment expense reserves as of December 31, 2008.

In addition, the following items were reviewed, several of which are discussed separately under their respective captions in this report.

- History
- Corporate Records
- Management and Control
- Fidelity Bond
- Conflict of Interest
- Territory and Plan of Operation
- Reinsurance
- Contracts and Underwriting
- Special Reserves and Deposits
- Growth of the Company
- Accounts and Records
- Financial Statements

**FINANCIAL STATEMENTS**

There follows a statement of financial condition as of December 31, 2008, a statement of income for the period ending December 31, 2008, a reconciliation of surplus for the period under review, and a statement of cash flow for the period ending December 31, 2008. The financial statements are presented in accordance with Statutory Accounting Principles.

**ASSETS**

	<u>Assets</u>	<u>Nonadmitted Assets</u>	<u>Net Admitted Assets</u>
Bonds	\$30,430,069		\$30,430,069
Common stocks	5,682,540		5,682,540
Cash	1,000		1,000
Investment income due and accrued	489,881		489,881
Uncollected premiums and agents' balances in course of collection	1,496,207	12,566	1,483,641
Deferred premiums, agents' balances and installments booked but deferred and not yet due	6,967,377	10,028	6,957,349
Amounts recoverable from reinsurers	3,172,036		3,172,036
Net deferred tax asset	1,311,217		1,311,217
Guaranty funds receivable or on deposit	18,266		18,266
Receivables from parent, subsidiaries and affiliates	451,494		451,494
Aggregate write-ins for other than invested assets	15,038	15,038	
Totals	<u>\$50,035,125</u>	<u>\$37,632</u>	<u>\$49,997,493</u>



**LIABILITIES, SURPLUS AND OTHER FUNDS**

Losses		\$10,081,956
Reinsurance payable on paid losses and loss adjustment expenses		1,732,664
Loss adjustment expenses		1,643,154
Taxes, licenses and fees		125,832
Current federal income taxes		800,001
Unearned premiums		15,522,900
Advance premium		365,833
Ceded reinsurance premiums payable		2,154,347
Payable to parent, subsidiaries and affiliates		1,601,761
Aggregate write-ins for liabilities		<u>376,500</u>
 Total liabilities		 \$34,404,948
 Common capital stock	\$1,000,000	
Gross paid in and contributed surplus	13,500,000	
Unassigned funds	<u>1,092,545</u>	
 Surplus as regards policyholders		 <u>15,592,545</u>
 Totals		 <u><u>\$49,997,493</u></u>

**STATEMENT OF INCOME**

## UNDERWRITING INCOME

Premiums earned	<u>\$23,527,686</u>
Deductions:	
Losses incurred	\$12,544,597
Loss adjustment expenses incurred	2,206,391
Other underwriting expenses incurred	<u>8,167,918</u>
Total underwriting deductions	<u>\$22,918,906</u>
Net underwriting gain	<u>\$608,780</u>

## INVESTMENT INCOME

Net investment income earned	\$1,512,571
Net realized capital losses	<u>(787,083)</u>
Net investment gain	<u>\$725,488</u>

## OTHER INCOME

Net loss from agents' or premium balances charged off	(\$12,790)
Finance and service charges not included in premiums	<u>263,973</u>
Total other income	<u>\$251,183</u>
Net income before federal income taxes	\$1,585,451
Federal income taxes incurred	<u>812,626</u>
Net income	<u><u>\$772,825</u></u>

**CAPITAL AND SURPLUS**

	<u>2006</u>	<u>2007</u>	<u>2008</u>
Surplus as regards policyholders, December 31, previous year	<u>\$13,128,412</u>	<u>\$14,504,640</u>	<u>\$15,545,916</u>
Net income	\$755,254	\$753,497	\$772,825
Change in net unrealized capital gains or (losses)	484,528	226,790	(718,790)
Change in net deferred income tax	109,404	53,189	11,854
Change in nonadmitted assets	<u>27,042</u>	<u>7,800</u>	<u>(19,260)</u>
Change in surplus as regards policyholders for the year	<u>\$1,376,228</u>	<u>\$1,041,276</u>	<u>\$46,629</u>
Surplus as regards policyholders, December 31, current year	<u><u>\$14,504,640</u></u>	<u><u>\$15,545,916</u></u>	<u><u>\$15,592,545</u></u>

**CASH FLOW****Cash From Operations**

Premiums collected net of reinsurance	\$24,728,520
Net investment income	1,405,965
Miscellaneous income	251,183
Total	<u>\$26,385,668</u>
Benefit and loss related payments	\$14,562,233
Commissions, expenses paid and aggregate write-ins for deductions	10,377,187
Federal income taxes paid	193,350
Total	<u>\$25,132,770</u>
Net cash from operations	<u>\$1,252,898</u>

**Cash From Investments**

Proceeds from investments sold, matured or repaid:	
Bonds	\$14,155,286
Stocks	19,892,235
Total investment proceeds	<u>\$34,047,521</u>
Cost of investments acquired (long-term only):	
Bonds	\$19,116,984
Stocks	20,487,451
Total investments acquired	<u>\$39,604,435</u>
Net cash from investments	<u>(\$5,556,914)</u>

**Cash From Financing and Miscellaneous Sources**

Cash provided (applied):	
Other cash applied	<u>(\$173,618)</u>
Net cash from financing and miscellaneous sources	<u>(\$173,618)</u>
Net change in cash and short-term investments	<u>(\$4,477,634)</u>

**RECONCILIATION OF CASH AND SHORT-TERM INVESTMENTS**

Cash and short-term investments:	
Beginning of year	\$4,478,634
End of year	1,000
Net change in cash and short-term investments	<u>(\$4,477,634)</u>

**RECOMMENDATION FOR CORRECTIVE ACTION****Management and Control**

The Company receives investment management services from AAIC. AAIC purchases bonds and stocks for the Company's investment portfolio pursuant to the investment policy established by the Company's Board of Directors. However, the Company and AAIC have not executed a contract to provide for such services.

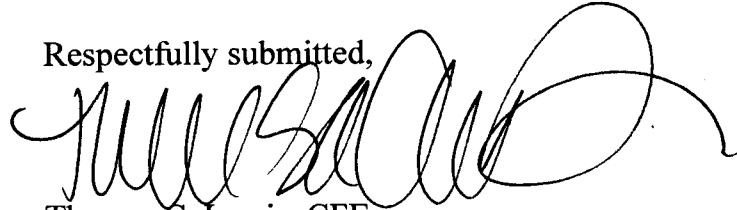
The Examiner recommends that the Company and AAIC execute an agreement for AAIC to provide investment management services to the Company.

**CONCLUSION**

The courteous cooperation extended by the Company's officers and employees during the course of the examination is gratefully acknowledged.

In addition to the undersigned, T. Bradford Earley, CFE, Jennifer K. Crawley, CFE, Mario A. Cuellar, CFE and Gina M. Gainer of the Bureau participated in the work of the examination.

Respectfully submitted,

A handwritten signature in black ink, appearing to read 'Theresa C. Lewis', written in a cursive style.

Theresa C. Lewis, CFE  
Senior Insurance Examiner



## VIRGINIA FARM BUREAU INSURANCE SERVICES

12580 West Creek Parkway • P.O. Box 27552 • Richmond, Virginia 23261 • 804-290-1000 • www.vafb.com

November 20, 2009

Mr. David H. Smith, CFE, CPA, CPCU  
Chief Examiner  
State Corporation Commission  
Bureau of Insurance  
P. O. Box 1157  
Richmond, Virginia 23218

Dear Mr. Smith:

RE: Virginia Farm Bureau Town & Country Ins. Co.  
Examination Report as of December 31, 2008

The following is in response with respect to the recommendations for corrective action in the above referenced examination report.

### Management and Control

Virginia Farm Bureau Town & Country Insurance Company receives investment management services from American Agricultural Insurance Company. We agreed that the terms and services provided should be more formalized, and therefore a written agreement between the parties describing the service, fees, and terms was executed on September 10, 2009.

We appreciate the guidance and cooperation extended by all participating throughout the course of the examination. We would appreciate receiving five copies of the final report.

Sincerely,

VIRGINIA FARM BUREAU TOWN & COUNTRY  
INSURANCE COMPANY

Jeff Dillon  
Senior Vice President and Treasurer