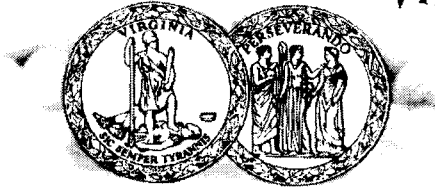


EXAMINATION REPORT
on
SHENANDOAH MUTUAL FIRE INSURANCE COMPANY
WOODSTOCK, VIRGINIA
as of
DECEMBER 31, 2010

COMMONWEALTH OF VIRGINIA
STATE CORPORATION COMMISSION
BUREAU OF VIRGINIA

COMMONWEALTH OF VIRGINIA

JACQUELINE K. CUNNINGHAM
COMMISSIONER OF INSURANCE
STATE CORPORATION COMMISSION
BUREAU OF INSURANCE



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I, Jacqueline K. Cunningham, Commissioner of Insurance of the Commonwealth of Virginia, do hereby certify that the annexed copy of the Examination Report of Shenandoah Mutual Fire Insurance Company as of December 31, 2010, 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 5th day of August, 2011

A handwritten signature in cursive script that reads "Jacqueline K. Cunningham".

Jacqueline K. Cunningham
Commissioner of Insurance

(SEAL)

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Richmond, Virginia
March 24, 2011

Honorable Jacqueline K. Cunningham
Commissioner of Insurance
Commonwealth of Virginia
Richmond, Virginia

Dear Madam:

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

SHENANDOAH MUTUAL FIRE INSURANCE COMPANY
Woodstock, Virginia

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

DESCRIPTION

The Company is a mutual assessment property and casualty insurer licensed pursuant to Chapter 25 of Title 38.2 of the Code of Virginia. It was last examined by representatives of the State Corporation Commission's Bureau of Insurance (Bureau) as of December 31, 2007. The current examination covers the three year period from January 1, 2008 through December 31, 2010.

HISTORY

The Company was granted a charter on February 7, 1876, as Shenandoah Farmers Mutual Fire Insurance Company. The name was shortened to its present form by charter amendment on December 14, 1943. The charter was restated on September 9, 1965, and as it presently reads, the purpose of the Company is as follows:

The conduct of a mutual assessment fire insurance business,
within the widest definition of Section 38.1-659, Chapter 15,
Code of Virginia of 1950, as amended from time to time.

On May 1, 1967, Frederick Mutual Fire Insurance Company of Winchester, Virginia was merged into the Company and on April 1, 1970, East Rockingham and Page Farmers Home Mutual Fire Insurance Company of Luray, Virginia were merged into the Company.

MANAGEMENT AND CONTROL

Management of the Company is vested in a board of nine directors who are required to be members of the Company. Directors are elected by the members at the annual meeting in February of each year for a term of one year.

With respect to authority established in the bylaws, the board of directors shall fix their own compensation and that of all officers, set remuneration for travel expenses and establish the rate of commissions or other compensation for agents of the Company.

Officers of the Company shall be elected by the board at its annual meeting. The officers of the Company shall be a chairman of the board (if elected), president, one or more vice presidents, secretary, treasurer, and such other officers as may be needed. The board of directors may, by a resolution passed by a majority of the whole board, designate the chairman of the board (if elected), president, vice president, secretary, and treasurer to constitute an executive committee. To the extent provided in the resolution, the committee shall have and exercise the power of the board of directors in the management and control of the business and affairs of the Company.

The bylaws also provide that any vacancy of a director or officer whose term has not expired may be filled by the board of directors for the unexpired term.

At December 31, 2010, the directors and officers were as follows:

<u>Directors</u>	<u>Principal Occupation</u>
Donald L. Atwood	Farmer Front Royal, Virginia
Larry A. Carbaugh	Customer Service Representative Stephens City, Virginia
Dennis K. Fleming	Self-Employed Luray, Virginia
Donald E. Foltz	Self Employed Edinburg, Virginia

Mark K. Getz	Treasurer/VP of Operations Edinburg, Virginia
Randall S. Jones	Secretary/Claims Manager Woodstock, Virginia
Gary D. Ramsey	Farmer Fort Valley, Virginia
Dudley H. Rinker	Self-Employed Stephens City, Virginia
Calvin F. Swartz	Retired Edinburg, Virginia

Officers

Calvin F. Swartz	Chairman of the Board
Donald L. Atwood	President
Gary D. Ramsey	Vice President
Mark K. Getz	Treasurer
Randall S. Jones	Secretary

FIDELITY BOND AND OTHER INSURANCE

The Company had a fidelity bond in force at December 31, 2010, in the amount of \$500,000 covering its employees and the two trustees of the retirement fund. In addition, the Company was insured under building and personal property and business catastrophe liability policies. Other coverages include workers' compensation and employment practices liability, robbery, directors' and officers' liability, and agents' errors and omissions.

EMPLOYEE WELFARE

Since 2002, the Company provides full-time employees with a defined contribution plan and a 401(k) plan.

The Company also furnishes full-time employees with life, health, and disability insurance as well as paid vacations.

TERRITORY AND PLAN OF OPERATION

The Company may operate throughout the Commonwealth of Virginia. However, business is currently written only in the counties of Augusta, Clarke, Culpeper, Fauquier, Frederick, Greene, Loudoun, Madison, Page, Rappahannock, Rockingham, Shenandoah, Warren and the cities of Harrisonburg, Staunton, Waynesboro and Winchester.

Marketing of insurance is conducted through 31 commissioned captive or independent agents, including five employees who are licensed agents. The lines of insurance written include fire and allied lines, comprehensive personal liability, dwelling properties, homeowner's, farm machinery, and livestock floaters. It is the practice of the Company to retain \$55,000 on property, bodily injury, property damage, and medical payment coverages. The balance of coverage is reinsured and is limited only by the amount the facultative reinsurer will accept.

Company personnel in conjunction with the binding authority of agents underwrite business. Property is classified according to use, construction, location, and occupancy.

All rates are set by the board of directors, who frequently establish special rates as needed for risks with unique hazards. Two full-time employees who also have secondary responsibilities for underwriting handle claims adjustment. The services of independent adjusting firms are used at times.

REINSURANCE

The Company had the following reinsurance agreements in force at December 31, 2010:

<u>Type of Contract</u>	<u>Lines</u>	<u>Net Retention</u>	<u>Reinsurance Limits</u>
First Per risk Excess of Loss (property)	Fire, Inland Marine, and Multiple Lines	\$55,000	\$145,000, any one loss
Second Property Per risk Excess of Loss	Fire, Inland Marine, and Multiple Lines	\$200,000	100% of \$400,000 in excess of \$200,000, any one loss
Third Property Per Risk Excess of Loss	Fire, Inland Marine, and Multiple Lines	\$600,000	100% of \$600,000 in excess of \$600,000, any one loss
Property Facultative Pro Rata	Property	\$45,000	\$750,000 any one risk
Property Catastrophe Excess of Loss	Fire, Inland Marine, and Multiple Lines	\$150,000	100% of \$1,000,000 in excess of \$150,000 combined net loss, each occurrence
Casualty Excess of Loss	Bodily Injury, Property Injury, Personal Injury, and Medical Payments	\$45,000	100% of \$1,000,000 in excess of \$45,000, per occurrence
Special Casualty Excess of Loss	Bodily Injury, Property Injury, Personal Injury, and Medical Payments	\$500,000	100% of \$500,000 in excess of \$500,000 combined net loss, per occurrence

<u>Type of Contract</u>	<u>Lines</u>	<u>Net Retention</u>	<u>Reinsurance Limits</u>
Aggregate Excess of Loss	All	57.50% of the Company's gross net premiums earned, or \$929,200 whichever is the greater, plus 10% of any excess loss recoverable hereunder	90% of 150% of Company's net premiums earned or 90% of \$3,636,000 whichever is lesser in excess of an amount which exceeds 57.50% of the Company's gross net premiums earned, or \$929,200 whichever is the greater
Umbrella Facultative	Personal, Farm and Commercial Umbrella Liability	\$5,000	95% of \$1,000,000 of Ultimate Net Loss, each occurrence, each policy

Note: Under the terms of the facultative agreement, the Company has binding authority for \$500,000 of additional risk in excess of \$600,000. For risks greater than \$1,100,000, Guy Carpenter & Company, Inc., a reinsurance intermediary (Guy Carpenter), will, upon approving an application, place the additional reinsurance with other multiple lines reinsurance companies. These placements are subject to the provisions set forth in its reinsurance intermediary contract with the Company. Individual certificates of coverage are issued for each facultative reinsured risk.

All reinsurance agreements are placed through Guy Carpenter. Each reinsurance agreement contains an insolvency clause.

GROWTH OF THE COMPANY

The following data, obtained taken from Annual Statements filed with the Bureau and the financial statements contained in examination reports, reflects the growth of the Company for the ten-year period ending December 31, 2010:

<u>Year</u>	Net Assessments <u>Received</u>	Investment <u>Income</u>	Net Losses <u>Paid</u>
2001	\$934,631	\$125,292	\$221,965
2002	1,204,662	126,026	341,758
2003	1,342,626	127,723	717,184
2004	1,519,209	116,292	827,114
2005	1,954,639	114,783	523,150
2006	2,121,011	118,012	1,093,192
2007	1,940,801	141,966	1,250,732
2008	1,711,571	127,126	868,609
2009	1,943,595	116,069	1,121,635
2010	2,138,031	85,511	663,865

<u>Year</u>	Number Of <u>Policies</u>	Insurance In <u>Force</u>	Admitted <u>Assets</u>	<u>Liabilities</u>	Surplus As Regards <u>Policyholders</u>
2001	5,479	\$669,857,579	\$2,760,380	\$783,272	\$1,977,108
2002	5,720	789,343,020	3,088,229	936,534	2,151,695
2003	6,099	945,254,200	3,175,078	1,268,457	1,906,621
2004	6,415	1,126,645,000	3,455,434	1,619,510	1,835,924
2005	6,555	1,326,917,325	3,911,976	1,642,730	2,269,246
2006	6,699	1,594,112,520	3,934,540	1,783,206	2,151,334
2007	6,716	1,753,077,070	3,615,447	1,770,042	1,845,405
2008	6,642	1,801,715,050	3,295,427	1,737,320	1,558,107
2009	6,431	1,751,963,350	2,966,997	1,741,495	1,225,502
2010	6,167	1,677,178,875	3,109,059	1,914,269	1,194,790

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, 2008 through December 31, 2010. Assets were verified and liabilities were established at December 31, 2010. A review of income and disbursements for the period was made to the extent deemed necessary.

This examination was conducted in accordance with the NAIC Financial Condition *Examiners' Handbook* (Handbook). The Handbook allows flexibility in the conduct of the examination based upon the nature and size of the entity being examined. This flexibility allows the examiners the ability to structure the examination in the manner best suited for each entity.

For this examination, all accounts and activities of the Company were considered in accordance with the risk-focused examination process.

FINANCIAL STATEMENTS

There follows a statement of income and disbursements for the period under review, a statement of financial condition and a summary of examiners' changes as of December 31, 2010.

INCOME FOR THE PERIOD UNDER REVIEW

	<u>2008</u>	<u>2009</u>	<u>2010</u>
Net assessments received	\$1,711,571	\$1,943,595	\$2,138,031
Interest on bonds	103,866	91,845	74,676
Interest on cash deposits	11,260	5,034	2,682
Dividends on stocks	8,318	5,647	6,130
Real estate income	3,000	3,000	3,000
Gain on sale of investments	682	10,543	(977)
Reconciling amounts	84,516	78,421	73,213
Other income	13,871	18,674	18,588
Increase by adjustment in book value	<u>6,122</u>		<u>2,669</u>
 Total Income	 \$1,943,206	 \$2,156,759	 \$2,318,012
 Deduct total disbursements for the year	 <u>2,259,740</u>	 <u>2,473,020</u>	 <u>2,091,803</u>
 Net Income	 (\$316,534)	 (\$316,261)	 \$226,209
 Add Ledger Assets December 31, previous year	 <u>3,382,650</u>	 <u>3,066,116</u>	 <u>2,749,855</u>
 Ledger Assets December 31, current year	 <u><u>\$3,066,116</u></u>	 <u><u>\$2,749,855</u></u>	 <u><u>\$2,976,064</u></u>

DISBURSEMENTS FOR THE PERIOD UNDER REVIEW

	<u>2008</u>	<u>2009</u>	<u>2010</u>
Net losses paid	\$868,609	\$1,121,635	\$663,865
Loss adjustment expense	31,944	31,649	50,876
Net commission and brokerage	417,425	429,364	476,245
Gross salaries	379,826	380,948	363,830
Directors' fees	9,455	9,285	8,755
Travel and travel items	10,040	8,789	8,401
Boards, bureaus and associations	5,667	5,751	6,061
Legal and auditing, not in connection with losses	32,200	30,000	31,884
Furniture, fixtures and equipment	15,219	11,603	8,803
Rent, office and equipment maintenance	26,445	26,492	21,193
Advertising	18,874	13,675	12,457
Printing and stationery	4,745	3,467	6,185
Postage, telephone and express	20,077	21,162	21,164
Insurance and fidelity bonds	32,135	26,911	27,073
Data processing			19,986
General operating expenses	75,744	59,841	77,622
Taxes, licenses and fees	63,400	63,937	65,089
Payroll items	182,009	169,514	159,646
Real estate	38,207	41,839	41,952
Decrease by adjustment in book value		2,152	
Borrowed money repaid	12,094		
Interest paid on borrowed money	15,625	15,006	20,716
	<u>\$2,259,740</u>	<u>\$2,473,020</u>	<u>\$2,091,803</u>
Total disbursements	<u>\$2,259,740</u>	<u>\$2,473,020</u>	<u>\$2,091,803</u>

ASSETS

	<u>Ledger Assets</u>	<u>Non- Ledger Assets</u>	<u>Assets Not Admitted</u>	<u>Net Admitted Assets</u>
Bonds	\$1,434,339			\$1,434,339
Stocks	593,847	114,527		708,374
Cash in company's office	200			200
Cash on deposit	348,236			348,236
Real estate	585,390		21,628	563,762
Amount due from agents	3,176			3,176
Interest due and accrued		10,010		10,010
Equipment, furniture and supplies	10,876		5,314	5,562
Deferred income taxes		35,400		35,400
Totals	<u>\$2,976,064</u>	<u>\$159,937</u>	<u>\$26,942</u>	<u>\$3,109,059</u>

LIABILITIES, SURPLUS AND OTHER FUNDS

Net unpaid losses	\$335,100
Loss adjustment expenses unpaid	20,800
Fees or commissions payable	11,059
Payroll items due or accrued	3,943
Other expenses due or accrued	85,128
Taxes, licenses and fees	35,142
Ceded reinsurance balances payable	1,044
Assessments unearned	1,381,100
Advertising, auditing and legal	3,739
Utilities, janitorial and printing	6,750
Amount due reinsurers	<u>30,464</u>
Total liabilities	\$1,914,269
Excess of admitted assets over liabilities (surplus)	<u>1,194,790</u>
Totals	<u>\$3,109,059</u>

EXAMINERS' CHANGES TO SURPLUS

	<u>Amount per Company</u>	<u>Amount per Examiners</u>	<u>Increase (Decrease) in Surplus</u>
<u>Assets:</u>			
Cash on Deposit	\$371,358	\$348,236	(\$23,122)
Amount Due from Agents	14,236	3,177	(11,059)
<u>Liabilities:</u>			
Fees or Commissions Payable	\$34,181	\$11,059	23,122
Examiners' net increase (decrease) in surplus			<u><u>(\$11,059)</u></u>
Surplus as regards policyholders per Examiners			\$1,194,790
Surplus as regards policyholders per Company			<u>1,205,849</u>
Examiners' net increase (decrease) in surplus			<u><u>(\$11,059)</u></u>

RECOMMENDATIONS FOR CORRECTIVE ACTION

Management and Control

1. The Company has historically reported administrative expenses that are high compared to the assessments received. Although the percentage of the administrative expenses improved during the three year period under review, they still remain relatively high. In addition, the Company has experienced an increased level of losses over the last five years. The increased level of losses and the continued high administrative expenses resulted in a decrease in policyholders' surplus from \$2,269,246 at December 31, 2005 to \$1,194,790 at December 31, 2010. It is recommended that the Company evaluate its losses and expenses and take the necessary steps to improve profitability and increase policyholders' surplus.

Accounts and Records

2. Cash on Deposit \$348,236

This asset, as reported in the Company's 2010 Annual Statement, was decreased by \$23,122. The decrease resulted from the reversal of an adjusting entry which had increased Cash on Deposit and Fees or Commissions Payable. The Examiners determined that \$23,122 in commissions were paid prior to year-end. The Examiners recommend that the Company properly report cash on deposit in future filings.

3. Amount Due from Agents \$3,177

This asset, as reported in the Company's 2010 Annual Statement, was decreased by \$11,059. The decrease resulted from the reversal of an adjusting entry which improperly increased the asset. The Examiners recommend that the Company properly report amounts due from agents in future filings.

4. Fees or Commissions Payable \$11,059

This liability, as reported in the Company's 2010 Annual Statement, was decreased by \$23,122. The decrease resulted from the reversal of an adjusting entry which had increased Cash on Deposit and Fees or Commissions Payable. The Examiners determined that \$23,122 in commissions were paid prior to year-end. The Examiners recommend that the Company properly report commissions payable in future filings.

CONCLUSION

The courteous cooperation extended by the officers and employees of the Company during the course of the examination was sincerely appreciated.

In addition to the undersigned, Jennifer K. Blizzard, CFE, Chris Collins, AFE and Milton Parker, participated in the work of the examination.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Mario Cuellar". The signature is fluid and cursive, with a long horizontal stroke at the end.

Mario A. Cuellar, CFE
Senior Insurance Examiner
Commonwealth of Virginia



Fire Insurance Company
P. O. Box 106
Woodstock, VA 22664-0106

Calvin F. Swartz – *Chairman Of The Board*
Donald L. Atwood – *President*
Gary D. Ramsey – *Vice President*
Mark K. Getz – *VP of Operations & Treasurer*
Randall S. Jones – *Secretary & Claims Manager*

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11 AUG 2011 8:56

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July 27, 2011

Mr. David H. Smith
Chief Examiner
Commonwealth of Virginia
State Corporation Commission
Bureau of Insurance
P.O. Box 1157
Richmond Va 23218

RE: Acknowledgement of Receipt of Report

Dear Mr. Smith:

Please be advised that we are in receipt of the Examination report of Shenandoah Mutual Fire Insurance Company as of December 31, 2010 and have no issues with any matter contained in the report.

Regarding the Recommendations for Corrective Actions listed on Page 13, we will strive to properly report Cash on Deposit and the Amounts due to and from Agents. We have been reviewing and continue to monitor both our losses and administrative expenses.

Please supply us with 12 copies of the report for future use.

It was a pleasure working with the examiners during the course of the examination.

Yours truly,

Mark K. Getz
Vice-President of Operations & Treasurer