

MARKET CONDUCT EXAMINATION REPORT

FARMERS INSURANCE COMPANY, INC.

NAIC # 21628; Group 69
17000 W. 119th Street
Olathe, KS 66061

ETS # KS057-M18

As of

December 31, 2014



KANSAS INSURANCE DEPARTMENT

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The Honorable Ken Selzer
Insurance Commissioner
Kansas Insurance Department
420 SW Ninth Street
Topeka, KS 66612

Dear Commissioner Selzer:

In accordance with your respective authorization, and pursuant to K.S.A. 40-222, a market conduct examination has been conducted on the business affairs of:

Farmers Insurance Company, Inc.
NAIC # 21628
17000 W. 119th Street
Olathe, KS 66061

hereafter referred to as “Farmers” or the “Company”, the following report of such examination is respectfully submitted,

Stacy Rinehart, FLMI, AMCM, CIE, AIRC
Market Conduct Manager
Examiner-in-Charge

PURPOSE AND SCOPE OF REVIEW

A market conduct examination of Farmers Insurance Company, Inc. also referred to as the “Company”, was conducted pursuant to, but not limited to K.S.A. 40-222.

The purpose of this targeted examination was to follow up on various issues noted in a prior market conduct examination (ETS # KS057-M12). The prior exam entailed a review of company operations and management, complaint handling, claims handling, underwriting and rating regarding both homeowners and private passenger automobile data for the review period of July 1, 2010 through June 30, 2012. For this re-examination, interrogatories were submitted regarding issues noted in the initial exam for findings involving complaint handling, claim handling, underwriting, and rating. The main focus of this re-examination was to review private passenger auto rating practices, as this is the area in which more significant findings were noted previously.

The exam period for this re-examination was July 1, 2014 through December 31, 2014. The Kansas Insurance Department (KID) reviewed the Company’s rating practices of private passenger automobile policies at the KID office in Topeka, Kansas by accessing electronic documents provided by the Company. The review was conducted according to the guidelines and procedures recommended in the 2014 NAIC Market Regulation Handbook (MRH). The exam team utilized the standards and tests recommended in the Handbook which allows an error tolerance of 10%. This examination report is written by test rather than by exception, which means all standards that were used are described and the results indicated. Silence on any NAIC standard or Company practice does not imply KID acceptance or endorsement of such practices. Applicable statutes and regulations cited throughout the report may be found in Appendix A.

EXECUTIVE SUMMARY

A targeted market conduct re-examination of Farmers Insurance Company, Inc. also referred to as the “Company”, was conducted pursuant to, but not limited to K.S.A. 40-222. The examination period was from July 1, 2014 through December 31, 2014. The primary focus of the exam was policyholder rating related to private passenger auto insurance. In addition to the rating review, follow up was done on previous exam recommendations. Changes made by the Company in response to the prior exam findings were found by the examiners to be adequate.

The Company was cooperative and timely in responses to inquiries from the examiners. There were some rating violations noted, but none were repeated from the prior exam. There were areas where the Company was rating policies in a manner inconsistent with the rates and rules on file with the Department. However, it did appear the Company was using rates systematically and in a nondiscriminatory manner.

The exam team has made several recommendations for the Company to amend their rate and rule filings with KID to ensure they adequately reflect the Company’s rating practices. Some of the recommendations were not based on specific violations, but more for the purposes of clarification on the rating practices being used.

Within 60 days of the conclusion of the final exam:

1. The Company must update their definition of “Specialty Policy” in the filed rule manual.
2. The Company must update Rule V09 (Luxury Vehicle to Credit Group Factor) to update the luxury vehicle model years.
3. The Company must update the rate filing to reflect the use of the Rate Level Adjustment Factor for campers and trailers.
4. The Company must add all of the relationship codes used in determination of the Household Structure factor to the filed rate manual.
5. The Company must update the description at the top of Exhibit 16 (Points/Tier) in the rate manual to accurately describe what rating characteristics are combined to generate the table of factors shown.
6. The UM rating description on Exhibit 3 (UM/UIM Rate Order of Calculation) of the rate manual should be amended to show that the UM base rate is only applied once per household; not once per vehicle as the other coverages are.
7. The Company should add the definition of a “High Performance” vehicle to the filed rule manual.

8. The Company should file their list of approved companies for the Transfer discount with the Department.

DESK EXAMINATION

UNDERWRITING AND RATING

General Underwriting and Rating Standards

Standard 1

The rates charged for the policy coverage are in accordance with filed rates (if applicable) or the regulated entity's rating plan.

Sample Type	Sample Size	Number of Errors	Percent Compliance
Auto Policies	25	*see below	

One policy in the sample contained a motorcycle that was not rated as having a Farmers Specialty Policy. However according to the definitions in the approved rate filings, if the insured has an additional policy with another company within the Farmers Group of Companies then the insured should be rated accordingly. As the policy was not rated in accordance to filed rates and rules, this is a violation of K.S.A. 40-955(g). The Company reports 1,970 policies issued or renewed during the exam period with motorcycles, boats, watercraft, motor homes, or recreational vehicles which were affected by this rating issue.

One policy in the sample was rated with an outdated rule regarding luxury vehicles, in violation of K.S.A. 40-955(g). The Company indicated they had inadvertently missed filing the particular rule, which updated the vehicle year by three years. The Company reports that 1,208 policies were issued during the time period affected by this filing error, which would have resulted in undercharges.

One policy in the sample contained a camper/trailer and it was discovered that the filed and approved rate order of calculation did not accurately reflect how the Company was rating policies with campers and trailers, as they were applying a Rate Level Adjustment Factor that was not approved for these coverages. This is a violation of K.S.A. 40-955(g). The Company reports that 2,854 policies were issued or renewed with campers and/or trailers during the exam period that were affected.

During review of the auto rating the company found and informed the examiners that the credit tier table on file with the Department was incorrect. The table being used was not filed. Since the table is used in the formulation of individual rates, this affects the rating of all policies in the exam period. This is a violation of K.S.A. 40-955(a)(g). The Company reports that there were 89,782 policies issued or renewed during the period rated that used the unfiled tier table. It should be noted, however, that the table used was similar to the table on file, so a majority of policyholders were likely charged the same rate as filed. There may have been under or overcharges based on the use of the different table. After the examination commenced, the Company filed the credit tier table they had been using to replace the previously filed table.

Result: Fail

*The specific files from our sample listed above contained violations that result in an 88% pass rate (3 of the 25 policies sampled), which fails the standard according to the Market Regulation Handbook. In addition, these particular errors affected multiple policies (see descriptions above). Also, the Company used a credit tier table in rating policies within our examination period which was not the table on file with our Department, thus all policies were rated using an unapproved rate page (though this did not necessarily result in different premiums being charged).

Recommendations: The Company is required to submit numerous updates to their auto rate and rule filing to the Department for approval. See Executive Summary for details.

Standard 4

The regulated entity's underwriting practices are not unfairly discriminatory. The regulated entity adheres to applicable statutes, rules and regulations and regulated entity guidelines in the selection of risks.

While rating errors were noted, there is no evidence of discrimination in the Company's rating practices.

Recommendation: None

SUMMARIZATION

Review of the items of concern noted in the prior market conduct examination report revealed that the Company appears to have adequately addressed all issues. There were some auto rating errors found in this re-examination that affect multiple policyholders. There were also several areas where the examiners recommended clarification be made in the rate and rule filings, but did not find these to be individual rating violations. The Company will be required to submit updates to their auto rate and rule filings, which are described in the Executive Summary.

CONCLUSION

I would like to acknowledge the cooperation and courtesy extended to the examination team by the Farmers Insurance Company staff. The following examiners from the Office of the Commissioner of Insurance in the State of Kansas participated in the review:

Market Conduct Division

Stacy Rinehart
Market Conduct Manager

Shannon Lloyd
Market Conduct Examiner

Tate Flott
Market Conduct Examiner

Respectfully submitted,



Stacy Rinehart, FLMI, AMCM, CIE, AIRC
Market Conduct Manager
Examiner-In-Charge

APPENDIX A

Related Kansas Insurance Statutes and Administrative Regulations

K.S.A. 40-222. Examinations

(a) Whenever the commissioner of insurance deems it necessary but at least once every five years, the commissioner may make, or direct to be made, a financial examination of any insurance company in the process of organization, or applying for admission or doing business in this state. In addition, at the commissioner's discretion the commissioner may make, or direct to be made, a market regulation examination of any insurance company doing business in this state.

(b) In scheduling and determining the nature, scope and frequency of examinations of financial condition, the commissioner shall consider such matters as the results of financial statement analyses and ratios, changes in management or ownership, actuarial opinions, reports of independent certified public accountants and other criteria as set forth in the examiner's handbook adopted by the national association of insurance commissioners and in effect when the commissioner exercises discretion under this subsection.

(c) For the purpose of such examination, the commissioner of insurance or the persons appointed by the commissioner, for the purpose of making such examination shall have free access to the books and papers of any such company that relate to its business and to the books and papers kept by any of its agents and may examine under oath, which the commissioner or the persons appointed by the commissioner are empowered to administer, the directors, officers, agents or employees of any such company in relation to its affairs, transactions and condition.

...

(g) The refusal of any company, by its officers, directors, employees or agents, to submit to examination or to comply with any reasonable written request of the examiners shall be grounds for suspension or refusal of, or nonrenewal of any license or authority held by the company to engage in an insurance or other business subject to the commissioner's jurisdiction. Any such proceedings for suspension, revocation or refusal of any license or authority shall be conducted in accordance with the provisions of the Kansas administrative procedures act.

...

K.S.A. 40-955. Same; rate filings; review and approval of certain lines; effective dates; exemptions from filing; certain workers compensation policies; rules and regulations.

(a) Every insurer shall file with the commissioner, except as to inland marine risks where general custom of the industry is not to use manual rates or rating plans, every manual of classifications, rules and rates, every rating plan, policy form and every modification of any of the foregoing which it proposes to use. Every such filing shall indicate the proposed effective date and the character and extent of the coverage contemplated and shall be accompanied by the information upon which the insurer supports the filings. A filing and any supporting information shall be

open to public inspection after it is filed with the commissioner, except that disclosure shall not be required for any information contained in a filing or in any supporting documentation for the filing when such information is either a trade secret or copyrighted. For the purposes of this section, the term "trade secret" shall have the meaning ascribed to it in K.S.A. 60-3320, and amendments thereto. An insurer may satisfy its obligations to make such filings by authorizing the commissioner to accept on its behalf the filings made by a licensed rating organization or another insurer. Nothing contained in this act shall be construed to require any insurer to become a member or subscriber of any rating organization.

...

(g) No insurer shall make or issue a contract or policy except in accordance with filings which have been filed or approved for such insurer as provided in this act

...