
REPORT ON EXAMINATION

Modified

(Limited Scope Market Conduct)

of

FARMERS INSURANCE EXCHANGE

NAIC COMPANY CODE: 21652

NAIC GROUP CODE: 0212

as of

December 31, 2006

(Property and Casualty)

**By Representatives of the
Oklahoma Insurance Department**

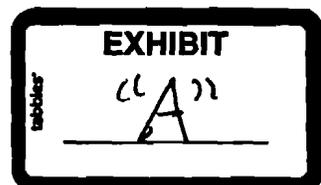


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SALUTATION

Oklahoma City, Oklahoma
March 26, 2009

Honorable Kim Holland
Insurance Commissioner
State of Oklahoma
2401 N W 23rd Street, Suite 28
Oklahoma City, Oklahoma 73107

Commissioner Holland:

Pursuant to instructions and in compliance with the provisions of Title 36 of the Oklahoma Statutes, rules, regulations and procedures of the Oklahoma Insurance Department, and the procedures established by the National Association of Insurance Commissioners, a limited scope examination of the market conduct activities has been conducted of:

FARMERS INSURANCE EXCHANGE

**Statutory Home Office
4680 Wilshire Boulevard
Los Angeles, California 90010**

The following Report of Examination (Limited Scope Market Conduct), as of December 31, 2006, is hereby respectfully submitted.

FOREWORD

This limited scope market conduct examination report, as of December 31, 2006 reflects certain Oklahoma insurance activities of Farmers Insurance Exchange, hereafter referred to as "Farmers" or the "Company." The examination was conducted in the Company's branch office at 2245 Sequoia Drive, Aurora, Illinois. The examination is, in general, a report by test, wherein each test applied during the examination is stated and the results are reported, whether the results are favorable or unfavorable.

SCOPE OF EXAMINATION

This examination covers the period July 1, 2004, through December 31, 2006.

The purpose of the examination was to determine compliance by the Company with provisions of the law, and any other facts relative to its business methods, management or equity of its dealings with its policyholders.

The examination was conducted in accordance with the guidelines and procedures recommended by the National Association of Insurance Commissioners (NAIC), rules, regulations and directives of the Oklahoma Insurance Department and pursuant, but not limited to, Title 36 O.S. §§ 309.1 – 309.7, 1204 – 1220, 1250.1, 1250.10, 1435.14.A, 1435.15A, and 3636.

In reviewing material for this report, the examiners relied primarily on records and material furnished by the Company.

File sampling was based on a review of randomly selected, unless otherwise indicated, samples of underwriting and claim files by category.

In cases where samples were selected and file sizes warrant, error ratios are projected to indicate a maximum high or low at a 95% level of confidence. Some files may contain multiple errors, which are indicated by category, but are counted only once in determining the error ratio.

During the course of this examination, the Company's operations were reviewed, including, but not limited to, the following:

- Operations and Management;
- Complaint Handling;
- Producer Licensing;
- Underwriting
- Policyholder Service; and
- Claims.

Certain unacceptable or non-complying practices may not have been discovered in the course of this examination. Failure to identify or criticize specific practices does not constitute acceptance of such practices by the Oklahoma Insurance Department. Any alleged violations identified in this report and any criticisms of practices have not undergone a formal administrative or judicial

process. This report should not be construed to endorse or discredit any insurance company or insurance product. This report is prepared for a particular audience and for a particular use. The materials contained in it are not necessarily suitable for any other purpose.

PRIOR EXAMINATION REPORT

There was no prior examination report on Farmers Insurance Exchange by the Oklahoma Insurance Department.

COMPANY OPERATIONS AND MANAGEMENT

History and Profile

Farmers Insurance Exchange was organized on March 28, 1928 under the Reciprocal or Inter-Insurance Act of California and commenced business on April 6, 1928 with the title Farmers Automobile Inter-Insurance Exchange. The present title was adopted on May 1, 1947. Farmers Insurance Exchange is licensed in all states except AK, CT, DE, HI, NY, PA, VT and WV.

Affiliated Parties

The Company and its affiliates are members of an Insurance Holding Company System as defined in Title 36 O.S. §1651 (d).

The following abbreviated description of the organizational chart depicts the Company's ownership:

Farmers Insurance Exchange, Fire Insurance Exchange and Truck Insurance Exchange, along with their subsidiaries, comprise the Farmers Insurance Group, which is based in Los Angeles, California. The three reciprocal insurers are owned by their respective policyholders. The policyholders of each Exchange appoint an exclusive attorney-in-fact to provide management services to the Exchange.

Farmers Group Inc. DBA Farmers Underwriters Association, is the attorney-in-fact for Farmers Insurance Exchange and the parent company of Fire Underwriters Association (attorney-in-fact of Fire Insurance Exchange) and Truck Underwriters Association (attorney-in-fact of Truck Insurance Exchange).

- ❖ During the course of this examination the Company denied the examiner's request for access to the Company's Board of Director meeting minutes for review. Reference: Title 36 O.S. § 309.3.B.

Direct Written Premium

The Company's reported total direct written premium for Oklahoma for the period under review was as follows:

Lines of business	2006	2005	2004
Fire	\$ 13,250	\$ 16,628	\$ 16,143
Allied lines	20,805	25,374	24,722
Commercial multiple peril (non-liability)	2,618,391	2,353,304	2,590,947
Commercial multiple peril (liability)	1,430,610	1,717,764	1,521,585
Inland marine	535	602	268
Earthquake	434	349	221
Workers' compensation	2,327,819	2,641,786	2,773,068
Other liability	1,662,286	1,528,663	1,451,675
Products liability	3,717	6,115	5,515
Other commercial auto liability	1,708,205	1,745,880	1,699,840
Commercial auto physical damage	636,412	672,742	570,475
Aggregate write-in for other lines of business	0	388	-4,562
Total	\$10,422,464	\$10,709,595	\$10,649,897

The Company's reported total direct written premium for the period under review was as follows:

Lines of business	2006	2005	2004
Federal flood	\$ 16,553,281	\$ 16,695,104	\$ 17,767,412
Allied lines	8,509,133	8,247,325	8,208,564
Homeowners multiple peril	532,316,729	553,309,055	523,602,404
Commercial multiple peril	458,055,184	439,261,868	418,931,180
Inland marine	6,403,212	6,877,534	6,322,987
Earthquake	1,118,188	1,308,406	1,448,488
Workers' compensation	76,650,452	86,965,959	92,341,286
Other liability-occurrence	76,198,920	68,389,148	62,623,655
Product's liability-occurrence	270,143	274,491	257,296
Private passenger auto liability	1,459,631,448	1,619,902,460	1,579,193,174
Commercial auto liability	61,305,165	61,776,198	58,146,491
Auto physical damage	1,112,686,722	1,269,421,366	1,334,270,078
Fidelity	7,689	31,095	29,816
Burglary and theft	220	698	533
Boiler and machinery	3,508	1,471	1,486
Aggregate write-in for other lines	0	-3,166	-48,072
Total	\$3,809,709,994	\$4,132,459,014	\$4,103,096,779

COMPLAINT HANDLING

In the review of the Company's complaint handling, attention was given to the Company's analysis of the complaint, the candor of the response, comparison of the response and actual file contents. The Company's own complaint records and the complaint listing maintained by the Oklahoma Insurance Department were utilized in this review.

Complaint History

Years	2004	2005	2006
Number of Complaints	3	6	7

The Company's complaint history was reviewed and no exceptions were noted.

Commercial Complaints

Cause of Complaint	2004	2005	2006
Commercial Property	2	2	3
Auto	1	0	3
Worker Comp	0	4	1
OID: Total Number of Complaints	3	6	7

Complainant Time Studies

For this study, time was measured from date the Company received the complaint until the date of response. No exceptions were noted.

Days	Number of Complaints	Percentage
0-20	15	93.75%
Over 20	1	6.25%
Total	16	100.0%

Complaint Compliance Review

In this study sixteen (16) complaint files were reviewed from a population 16 complaints. No errors were noted.

MARKETING AND SALES

Marketing

The Company's products are marketed mostly through captive agents/agencies.

PRODUCER LICENSING

Producers Licensing and Appointments

The Company's listing of agencies commissions paid was compared to the Oklahoma Insurance Department listing of appointed agents. In that review, no exceptions were noted.

Adjuster Licensing

The Company's claims are handled for the most part by the Company's adjusters. On each claim reviewed the adjuster's license was checked against the Oklahoma Insurance Department listing of adjusters.

- ❖ In this study, twelve (12) employees who hold themselves out to be adjusters were not found as licensed. Reference: Title 36 O.S. § 6204.A

POLICYHOLDER SERVICE

The policyholder service portion is designed to test the Company's compliance with statutes regarding notice/billing, delays, no response and premium refunds. In that study, one hundred (100) commercial physical damage policies and commercial multiple peril policies were reviewed from a population of 2,129 cancelled policies. In this study, no errors were noted.

COMPANY FORMS

The Company's forms were pulled from Sircon and check against the Company's forms used. In that review no exceptions were noted.

UNDERWRITING AND RATING

The Company's underwriting and rating practices were reviewed, including filing of forms in use during the period under examination.

Application of Rates and Underwriting

The most appropriate statistic to measure accuracy is the number of files in error. An error is taken to be any failure of the Company to:

- Correctly calculate premium;
- Correctly code;
- Comply with statutes, regulations or policy provisions; or
- Properly issue.

Cancelled Commercial Auto Multi Peril Policies

Field Size	Type of Sample	Size of Sample
508	Random	25

In this study, no error was noted.

Cancelled Commercial Auto Physical Damage Policies

Field Size	Type of Sample	Size of Sample
1621	Random	25

In this study, no error was noted.

CLAIMS

- ❖ During the course of the examination a request was made for the internal claims audit records and they were denied by the Company. Their response was as follows: "In accordance with the self-audit, self-evaluative privilege, we are unable to provide you with our confidential internal audit reports." This appears to be a violation Title 36 O.S. § 309.3.B.

Claim Time Studies

For these studies, claim payments are measured from the following:

ACKNOWLEDGEMENT TIME:

From the date of receipt by the insurer or agent of notification of a claim to a company's initial communication or acknowledgement to the claimant. Reference: Title 36 O.S. § 1250.6.A.

INVESTIGATION TIME:

From the date the company or agent receives notification of a claim to the date the investigation is completed. Reference: Title 36 O.S. § 1250.7.C.

ACCEPTANCE TIME:

From the date the company has received all necessary proof of loss information to the date of acceptance or denial. Reference: Title 36 O.S. § 1250.7.A.

The following one hundred twenty-five (125) claims were randomly selected for time studies. Following is a report of that review:

Lines of Business	Field Size	Sample Size	Error Noted
Commercial Multi Peril Claims	217	28	0
Commercial Physical Damage Claims	118	26	0
Open Physical Damage Claims	4	4	0
Subrogation Claims	11	11	0
CWP Workers Comp Claims	35	35	0
Workers Comp Claims	48	21	0
Total	433	125	0

Claim Practices

The claims practices of the Company were examined for efficiency of handling, accuracy of payment, compliance to Oklahoma Statutes and Regulations, and adherence to contract provisions. A claim is taken to be a demand for payment by an insured or claimant under a coverage against the insurer, which claim is:

Paid by the Insurer as:

1. Full recompense
2. Partial recompense

Closed without payment by reason of:

1. No relevant coverage
2. No liability
3. Recompense by other legal means

Commercial Multi Peril Claims

Twenty-eight (28) claims were random selected for review from a population of 217 claims closed during the time frame of the examination. In this study, no errors were noted.

Commercial Physical Damage Claims

Twenty-six (26) claims were random selected for review from a population of 118 claims closed during the time frame of the examination. In that sample, two errors were noted which resulted in an error ratio of 7.69%. At a 95% level of confidence, the discovered error ratio of 7.69% will be a probability of acceptance of 75.54% when applied to the entire field. Following is a report of the errors noted.

- ❖ Claim number 1007695663 (3): The Company failed to pay taxes and license fees on total loss settlement. The Company agreed and paid the policyholders a total amount of \$1,217.25. Reference Title 36, O.S. § 1250.8.A.1.
- ❖ Claim number 1007189448 (2A): The Company failed to pay taxes and license fees to replace a total loss vehicle with like and quality. This vehicle was a constructed total loss that was left with the policyholders and not repairable to drive on the highway. Reference Title 36, O.S. § 1250.8.A.1.

Open Physical Damage Claims

Four (4) claims were selected for review from a population of four (4) claims closed during the time frame of the examination. In this study, no errors were noted.

Subrogation Claims

Eleven (11) claims were selected for review from a population of eleven (11) claims closed during the time frame of the examination. In this study, no errors were noted.

Closed Without Payment Worker Comp Claims

Thirty-five (35) claims were selected for review from a population of thirty-five (35) claims closed during the time frame of the examination. In that sample, no errors were noted.

Workers' Comp Claims

Twenty-one (21) claims were selected for review from a population of forty-eight (48) claims closed during the time frame of the examination. In this study, no errors were noted.

COMMENTS

Affiliated Parties

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During the course of this examination the Company denied the examiner's request for access to the Company's Board of Director meeting minutes for review. Reference: Title 36 O.S. § 309.3.B.

Adjuster Licensing

5

In this study twelve (12) employees who hold themselves out to be adjusters, were not found be licensed. Reference: Title 36 O.S. § 6204.A

Claims

6

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Commercial Physical Damage Claims

7-8

Twenty-six (26) claims were reviewed and two (2) errors were noted resulting in an error ratio of 7.69%.

Claim number 1007695663 (3): The Company failed to pay taxes and license fees on total loss settlement. The Company agreed and paid the policyholders a total amount of \$1,217.25. Reference Title 36, O.S. § 1250.8.A.1

Claim number 1007189448 (2A): The Company failed to pay taxes and license fees to replace a total loss vehicle with like and quality. This vehicle was a constructed total loss that was left with the policyholders and not repairable to drive on the highway. Reference Title 36, O.S. § 1250.8.A.1

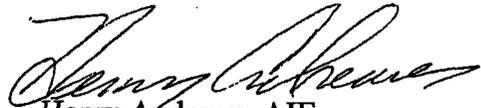
ACKNOWLEDGMENT

The Market Conduct Examination Report of Farmers Insurance Exchange is respectfully submitted to the Honorable Kim Holland, Insurance Commissioner of the State of Oklahoma.

In addition to the undersigned, Mr. Jim Mitchell, AFE, participated in the examination.

The Examiners wish to express their appreciation for the courteous cooperation and assistance given by the officers and employees of the Company during the course of this examination.

Respectfully Submitted,

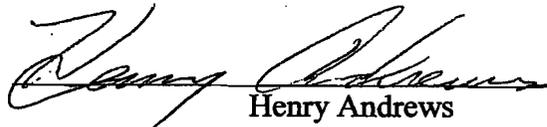


Henry Andrews, AIE
Examiner-in Charge, State of Oklahoma
Midwestern Zone III, NAIC

AFFIDAVIT

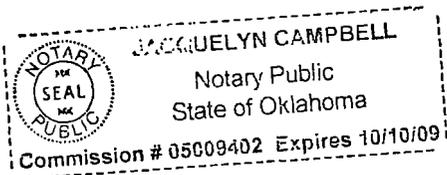
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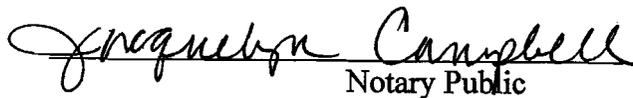
I, Henry Andrews, of lawful age, being first duly sworn, upon oath state that I have been charged with examining Farmers Insurance Exchange, as of December 31, 2006, that I have prepared and read the foregoing Report of Examination, that I am familiar with the matters set forth therein, and I certify the Report is true and complete to the best of my knowledge and belief.


Henry Andrews

Subscribed and sworn to before me this 30th day of April, 2008, by Henry Andrews.

[seal]




Notary Public

My commission expires: 10/10/09