

STATE OF OREGON

DEPARTMENT OF CONSUMER AND BUSINESS SERVICES

INSURANCE DIVISION

REPORT OF MARKET CONDUCT EXAMINATION

OF

FARMERS INSURANCE COMPANY OF OREGON
TIGARD, OREGON

NAIC COMPANY CODE 21636

AS OF

DECEMBER 31, 2004

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September 22, 2005

Honorable Cory Streisinger, Director
State of Oregon
Department of Consumer and Business Services
350 Winter Street, NE, Room 440-4
Salem, OR 97310

Dear Director:

In accordance with your instructions and pursuant to ORS 731.300, we have examined the business affairs of

Farmers Insurance Company of Oregon
13333mSW 68th Parkway
Tigard, Oregon 97223

NAIC Company Code 21636

hereinafter referred to as the "Company." The following report of examination is respectfully submitted.

EXECUTIVE SUMMARY

The following report is intended to provide a comprehensive summary of the findings discovered during this examination of the Company's efforts to comply with standards pertaining to the settlement of total loss personal automobile claims and the use of credit history or insurance score in its underwriting process.

To measure the Company's compliance with requirements pertaining to use of Oregon Revised Statutes and Oregon Administrative Rules as they apply to Claims, the following Standards were applied to the Company's operation:

Claim Standard #1 – Company completes its claim investigation not later than the 45th day after its receipt of notification of claim in accordance with ORS 746.230(1) and OAR 836-080-0230.

Claim Standard #2 – The Company responds to claim correspondence in 30 days in accordance with ORS 746.230(1) and OAR 836-080-0225.

Claim Standard #3 – Claim files are adequately documented as required by ORS 733.170 and OAR 836-080-0215.

Claim Standard #4 - Total loss settlements are handled in accordance with policy provisions and applicable statues, rules and regulations pursuant to OAR 836-080-0240.

To measure the Company's compliance with requirements pertaining to use of Credit History and Insurance Scores, the following Standards were applied to the Company's operation:

Underwriting Standard #1 – The Company or its producer provides the required notice to a consumer before obtaining the consumer's credit history or insurance score in accordance with OAR 836-080-0430(1).

Underwriting Standard #2 – The Company provides instructions to each of its producers regarding the notice to be provided to a consumer before obtaining the consumer's credit history or insurance score in accordance with OAR 836-080-0430(3).

Underwriting Standard #3 – The Company provides the required notice to consumers that they may request a written statement describing the Company's use of credit histories and insurance scores in accordance with OAR 836-080-0430(4).

Underwriting Standard #4 – The Company provides the required written statement describing the Company's use of credit histories and insurance scores to a consumer who requests it in accordance with OAR 836-080-0430(4).

Underwriting Standard #5 – The Company provides the required information to a consumer when the Company takes an adverse action against the consumer based in whole or in part upon a credit history or insurance score in accordance with ORS 746.650(5) and OAR 836-080-0438(1) and (2).

Underwriting Standard #6 – The Company takes the required action when a consumer disputes the accuracy or completeness of information in a consumer report and the dispute results in a change in the consumer's credit history or insurance score in accordance with ORS 746.661 and OAR 836-080-0438(1) and (2).

Underwriting Standard #7 – The Company has established the required written policy regarding use of credit histories and insurance scores in their rating or underwriting process in accordance with ORS 746.661 and OAR 836-080-0435.

Underwriting Standard #8 – The Company does not cancel or non-renew personal insurance that has been in effect for more than 60 days based in whole or in part on a consumer's credit history or insurance score in accordance with ORS 746.661.

Underwriting Standard #9 – The Company does not use a consumer's credit history to decline coverage of personal insurance in the initial underwriting decision without other substantive underwriting factors in accordance with ORS 746.661.

The Company passed Claim Standard #2, and Underwriting Standards #1, #2, #8, and #9 without comment. The Company passed Claim Standard #1 and #3, with comment. The Company failed Claim Standard #4 and Underwriting Standards #3, #4, #5, #6, and #7.

Additional Finding - Claims:

In circumstances where the Company did not complete its claim investigation in accordance with OAR 836-080-0230, it did not notify the claimant of the reason for the delay or the reason more time was needed to complete the investigation in accordance with OAR 836-080-0235(4).

The Company did not conduct a reasonable investigation based on all available information in accordance with ORS 746.230 unfair claim settlement practices.

SCOPE OF EXAMINATION

The Target Market Conduct examination of the Company was conducted as of December 31, 2004, covering the period of January 1, 2004 through December 31, 2004, and included a review of material transactions or events which occurred subsequent to the examination cut-off date and were noted during the examination.

The Target Market Conduct examination was limited to a review of the Company's claims practices as they pertain to the settlement of total loss personal automobile claims and the Company's underwriting practices as they pertain to the use of credit history or insurance score in its underwriting process.

The examination of the Company was conducted pursuant to ORS 731.300 and in accordance with procedures and guidelines established by the Oregon Insurance Division Market Conduct Program. The program generally follows the Market Conduct Examination Handbook as adopted by the National Association of Insurance Commissioners (NAIC) to the extent that it is consistent with Oregon law. The purpose was to determine the Company's ability to fulfill and manner of fulfillment of its obligations, the nature of its operations, whether it has given proper treatment to policyholders, and its compliance with the Oregon Insurance Code and Administrative Rules.

In order to determine the practices and procedures of the Company's operations, one or more of the following procedures was performed in each phase:

1. A sample of files was selected from listings provided by the Company. The examiner then reviewed each file.

2. The procedure manuals and/or memorandum were evaluated.

3. The Company responded to a series of questions regarding the phase being examined.

The examination was comprised of the following phases:

Claims

Underwriting

The Company's underlying data was measured against an established standard. A list of all standards considered can be found in Appendix A at the end of the report. The examiner used the following three classifications to disclose the examination results:

Passed without Comment	The standards the Company passed are displayed in a chart at the beginning of the Findings section of each phase. Items included in this category passed the standard and the examiner did not find it necessary to comment on the findings.
Passed with Comment	Standards the Company passed with some errors noted are included in this classification. Items in this category are not considered to be indicative of a general business practice of noncompliance. Usually, a recommendation is not warranted, but in certain instances a recommendation might be made.
Failed	The Company has not demonstrated compliance with standards that fall into this category. A recommendation for compliance is usually made for each recommendation the Company fails.

Information regarding some items might be noted in the examination without remarks.

Other areas of concern discovered during the examination that do not fall within the scope of the standards might appear in the report as the last section of each phase and titled Additional Findings.

Certain unacceptable or non-complying practices may not have been discovered in the course of this examination. Failure to identify or criticize specific Company practices does not constitute acceptance or approval by the Oregon Insurance Division. Examination findings may result in administrative action or further inquiry.

CLAIMS

The Company provided a population run of 4,704 total loss claims paid during the examination period from which a random sample of 50 claims (1.06%) was drawn.

Findings

The Company passed the following standard without comment:

STANDARD
Claim Standard #2 – The Company responds to claim correspondence in 30 days in accordance with ORS 746.230(1) and OAR 836-080-0225.

The following exceptions were noted:

Claim Standard #1 – Company completes its claim investigation not later than the 45th day after its receipt of notification of claim in accordance with ORS 746.230(1) and OAR 836-080-0230.

Findings: Pass with comments. 94% compliance. This Standard applied to 49 of the 50 Units tested. Three units (6%) failed this standard for the reasons shown below.

OAR 836-080-0230 requires the Company to complete its claim investigation not later than the 45th day after its receipt of notification of claim, unless the investigation cannot reasonably be completed within that time.

The claim investigations for the three units that failed this standard were not completed in accordance with OAR 836-080-0230.

A failure rate of 6% does not appear to represent a pattern of noncompliance; therefore, no recommendation is warranted.

Claim Standard #3 – Claim files are adequately documented as required by ORS 733.170 and OAR 836-080-0215.

Findings: Pass with comments. 94% compliance. This standard applied to 49 of the 50 units tested. Three units (6%) failed this standard for the reasons shown below.

Pursuant to OAR 836-080-0215 the Company's claim files must contain the information pertaining to each claim in sufficient detail that pertinent events and their dates can be reconstructed.

The information in the claim files of the three units that failed this standard did not provide sufficient detail as to why there was a delay in the settling of the claim after the adjuster completed his/her investigation.

A failure rate of 6% does not appear to represent a pattern of noncompliance; therefore, no recommendation is warranted.

Claim Standard #4 - Total loss settlements are handled in accordance with policy provisions and applicable statutes, rules and regulations pursuant to OAR 836-080-0240.

Findings: Failed. 0% compliance. This standard applied to 46 of the 50 units tested. Forty-six units (100%) failed this standard for the reasons shown below.

# Units*	Reason
8	Company used vehicle(s) that were not comparable to the loss vehicle as their mileage was unknown; however, the Company still made a cost adjustment for a difference in the number of miles of those vehicles as compared to the known mileage of the loss vehicle.
46	Use of data from across the United States, Western Region, and regional averaging to determine the fair market value of a totaled vehicle, principally garaged in the area where the loss vehicle was garaged.
3	Company used vehicle(s) that were not comparable to the loss vehicle as their body style was different, i.e., loss vehicle 2dr coupe, Company's comparable vehicle 4dr wagon.

***** A unit may have failed the above standard for more than one reason.

I recommend the Company process total loss settlements in accordance with policy provisions and applicable rules and regulations pursuant to OAR 836-080-0240.

Additional Findings

OAR 836-080-0230 requires the Company to complete its claim investigation not later than the 45th day after its receipt of notification of claim, unless the investigation cannot reasonably be completed within that time.

If the claim investigation cannot be completed within that time, OAR 836-080-0235(4) requires the Company to notify the claimant not later than the 30th day after receipt of the proofs of loss, giving the reason more time is needed. Forty-five days from the date of such initial notification and every 45 days thereafter while the investigation remains incomplete, the insurer shall notify the claimant in writing of the reason additional time is needed for investigation.

The claim investigation of four units was not completed in accordance with OAR 836-080-0230 and the claim file did not contain a copy of the required OAR 836-080-0235(4) notice.

I recommend the Company notify the claimant not later than the 30th day after receipt of the proofs of loss, giving the reason more time is needed in accordance with OAR 836-080-0235(4).

The Company chose to use vehicles with unknown mileage as comparable vehicles in eight units. Contained in the files of these eight units is detailed information regarding the vehicles with unknown mileage. The details include options, location (which included dealerships), take price, and contact phone number. The Company made cost adjustments based on the difference of the known mileage of the loss vehicle and the unknown mileage of the chosen comparable vehicle. The Company used a regional average calculation to assign mileage to the chosen comparable vehicles instead of using the contact phone numbers and asking the owners of the vehicles for the pertinent information. The Company's claim investigation did not give consideration to all available information in accordance with ORS 746.230.

I recommend the Company conduct a reasonable investigation based on all available information in accordance with ORS 746.230.

UNDERWRITING

For this phase of the examination, Company procedure manuals, bulletins, and memorandum were evaluated. The Company also provided population runs of new business issued, non-renewed business, and cancelled and declined business. A sample of files was selected from the population runs provided by the Company from which random samples were drawn. The examiner then reviewed each file in the sample.

Findings

The Company passed the following standards without comment:

STANDARD
Underwriting Standard #1 – The Company or its producer provides the required notice to a consumer before obtaining the consumer's credit history or insurance score in accordance with OAR 836-080-0430(1).
Underwriting Standard #2 – The Company provides instructions to each of its producers regarding the notice to be provided to a consumer before obtaining the consumer's credit history or insurance score in accordance with OAR 836-080-0430(3).
Underwriting Standard #8 – The Company does not cancel or non-renew personal insurance that has been in effect for more than 60 days based in whole or in part on a consumer's credit history or insurance score in accordance with ORS 746.661.
Underwriting Standard #9 – The Company does not use a consumer's credit history to decline coverage of personal insurance in the initial underwriting decision without other substantive underwriting factors in accordance with ORS 746.661.

The following exceptions were noted.

Underwriting Standard #3 – The Company provides the required notice to consumers that they may request a written statement describing the Company's use of credit histories and insurance scores in accordance with OAR 836-080-0430(4).

Findings: Failed.

Oregon Administrative Rule (OAR) 836-080-0430(4), requires an insurer that uses the credit history or insurance score of a consumer when considering the consumer's application for insurance to disclose to the consumer during the application process that the consumer may request a written statement describing its use of credit histories or insurance scores.

A review of the Company's procedures indicates that it does not have a procedure that instructs its producers to provide the required disclosure to consumers whose applications for insurance are being considered by the Company. The Company provided the following forms to show how it is in compliance with the provisions of the administrative rule:

Form 25-4219 3-03, titled "Farmers Use of Insurance Scores", is a notice that is addressed "Dear Valued Customer". This form, which is issued with new policies and not during the application process, does not inform the Company's producers of when to provide the required OAR 836-080-0430(4) disclosure to the consumer.

Form 25-7405, titled "Fair Credit Reporting Act Notification", is a notice used when the Company has taken an adverse action based on credit score or insurance score. This form does not inform the Company's producers of when to provide the required OAR 836-080-0430(4) disclosure to the consumer.

Form SRN 32-2191, "Fair Credit Reporting Act Notification", is a notice used when the Company has taken an adverse action based on credit score or insurance score. This form does not inform the Company's producers of when to provide the required OAR 836-080-0430(4) disclosure to the consumer.

The Company is not in compliance with OAR 836-080-0430(4), as it does not have procedures in place that instructs its producers to provide the required disclosure to consumers whose applications for insurance are being considered by the Company.

I recommend the Company provides the required notice to consumers that they may request a written statement describing the Company's use of credit histories and insurance scores in accordance with OAR 836-080-0430(4).

Underwriting Standard #4 – The Company provides the required written statement describing the Company's use of credit histories and insurance scores to a consumer who requests it in accordance with OAR 836-080-0430(4).

Findings: Failed.

Oregon Administrative Rule (OAR) 836-080-0430(4), requires an insurer that uses the credit history or insurance score of a consumer when considering the consumer's application for insurance to disclose to the consumer during the application process that the consumer may request a written statement describing its use of credit histories or insurance scores. The statement must address the following items:

(a) Why the insurer uses credit history or insurance scores.

(b) How the insurer uses credit histories or insurance scores.

(c) What kinds of credit information are used by the insurer?

(d) Whether a consumer's lack of credit history will affect the insurer's consideration of an application.

(e) Where the consumer may go with questions.

The Company could not produce a copy of a written statement that complies with the requirements of OAR 836-080-0430(4). However, the Company did provide the following forms to demonstrate its compliance with the provisions of the administrative rule:

Form 25-4219 3-03, titled "Farmers Use of Insurance Scores". Form 25-4219 3-03 appears to not be in compliance as it is provided with each issued policy and not when an OAR 836-080-0430(4) request is made. Additionally, Form 25-4219 3-03 appears to not be in compliance with ORS 746.661(6) as it indicates the Company will use the credit score to calculate premium at renewal and that the Company runs a credit report every three years, these practices are prohibited pursuant to ORS 746.661(6).

Form 25-4219 3-03 appears to not be in compliance with OAR 836-080-0430(4)(d) as it does not provide the consumer with an explanation of the impact that a lack of a credit history will have upon the rate used to calculate premium.

The Company could not produce a written statement describing its use of credit histories or insurance scores to be given to consumers who requested such information at time of application in accordance with OAR 836-080-0430(4).

I recommend the Company provides the required written statement describing the Company's use of credit histories and insurance scores to a consumer who requests it in accordance with OAR 836-080-0430(4).

Underwriting Standard #5 – The Company provides the required information to a consumer when the Company takes an adverse action against the consumer based in whole or in part upon a credit history or insurance score in accordance with ORS 746.650(5) and OAR 836-080-0438(1) and (2).

Findings: Failed.

Oregon Revised Statute 746.650(5) requires when an adverse underwriting decision is based in whole or in part on credit history or insurance score, the Company provide the applicant, policyholder or individual proposed for coverage with the specific reason or reasons for the adverse underwriting decision in writing.

The notice must include a summary of no more than four of the most significant credit reasons for the adverse underwriting decision. The notice must also include the name, address and telephone number, including a toll-free telephone number, of the consumer-reporting agency that provided the information for the consumer report.

The notice must inform the applicant, policyholder or individual proposed for coverage that the consumer-reporting agency used by the Company to obtain the credit history of the consumer did not make the adverse underwriting decision and is unable to provide the consumer with specific reasons why the Company made an adverse underwriting decision.

The notice must also provide information on the right of the consumer to obtain a free copy of the consumer's consumer report from the consumer reporting agency and the right of the

consumer to dispute the accuracy or completeness of any information in a consumer report furnished by the consumer-reporting agency.

The Company could not produce a copy of an Adverse Action Notice that complies with the requirements of ORS 746.650(5) and OAR 836-080-0438(1) and (2). However, the Company did provide the following forms to demonstrate its compliance with the provisions of the statute and administrative rule:

Form 25-4219 3-03, titled "Farmers Use of Insurance Scores", is a notice that is addressed "Dear Valued Customer", and is distributed with new policies. This form is not in compliance with ORS 746.650 as it does not provide the significant reasons for the adverse action or the name, address, toll free number of the consumer reporting agency that provided the consumer report and it is not issued at the time the adverse action is taken. Nor is this form in compliance with OAR 836-080-0438, as it does not inform the consumer of their right to request, no more than once annually, that the insurer re-rate the consumer and of potential negative consequences of re-rating, if any.

Form 25-7878 8-03, titled "Fair Credit Reporting Act Notice" is not in compliance with OAR 836-080-0438 as it does not inform the consumer of their right to request, no more than once annually, that the insurer re-rate the consumer and of potential negative consequences of re-rating, if any.

Form 25-7878 7-04, titled "Fair Credit Reporting Act Notice" is not in compliance with OAR 836-080-0438 as it does not inform the consumer of their right to request, no more than once

annually, that the insurer re-rate the consumer and of potential negative consequences of re-rating, if any.

I recommend the Company provides the required information to a consumer when the Company takes an adverse action against the consumer based in whole or in part upon a credit history or insurance score in accordance with ORS 746.650(5) and OAR 836-080-0438(1) and (2).

Underwriting Standard #6 – The Company takes the required action when a consumer disputes the accuracy or completeness of information in a consumer report and the dispute results in a change in the consumer's credit history or insurance score in accordance with ORS 746.661 and OAR 836-080-0438(1) and (2).

Findings: Failed.

If an insurer uses disputed credit history to determine eligibility for coverage of personal insurance and places a consumer with an affiliate that charges higher premiums or offers less favorable policy terms and if the consumer resolves the credit dispute under the process set forth in the federal Fair Credit Reporting Act (15 U.S.C. 1681) and notifies the insurer in writing that the dispute has been resolved, then, pursuant to ORS 746.661(3), the insurer must re-rate the policy retroactive to the effective date of the current policy term and the policy, as reissued or re-rated, must provide the premiums and policy terms for which the consumer would have been eligible if accurate credit history had been used to determine eligibility.

If an insurer charges higher premiums due to disputed credit history and if the consumer resolves the credit dispute under the process set forth in the Federal Fair Credit Reporting Act (15 U.S.C. 1681) and notifies the insurer in writing that the dispute has been resolved, then, pursuant to ORS 746.661(4), the insurer must re-rate the policy retroactive to the effective date of the current policy term. As re-rated, the insurer must charge the consumer the same premiums the consumer would have been charged if accurate credit history had been used to calculate an insurance score.

A review of the Company's procedures indicates that it does not have a procedure that complies with the requirements of ORS 746.661 and OAR 836-080-0438(1) and (2). The Company, to show how it complied with the provisions of ORS 746.661 and OAR 836-080-0438(1) and (2), provided a copy of page III-D-28 of its "Personal Lines Procedures Manual". Under the heading of "Investigations Used in Auto and Fire" and sub-heading "Corrected Credit Score Procedure (RPM)" is an investigative procedure concerning corrected credit scores.

The procedure that the Company is relying on to show it was in compliance with ORS 746.661 and OAR 836-080-0438 was effective July 23, 2004. Oregon Revised Statute 746.661 was effective January 1, 2004. The Company, without having a procedure that complied with ORS 746.661 in place during the first six and a half months of 2004 was not in compliance with ORS 746.661 during that time period.

The procedure that the Company is relying on to show it was in compliance with ORS 746.661 describes an investigative procedure regarding corrected credit scores; however, it does not indicate how the procedure is implemented. The procedure begins by stating "Credit Reports for which Farmers has made an inquiry, but which have been changed or corrected by the credit

reporting agency…" there is no mention of notice received from the consumer regarding the resolution of a disputed credit report. Pursuant to ORS 746.661, subsections (3) and (4) of this section of the statute apply only if the consumer resolves the credit dispute under the process set forth in the Federal Fair Credit Reporting Act (15 U.S.C. 1681) and notifies the insurer in writing that the dispute has been resolved.

The procedure also states that if a corrected credit score is worse than the one on record then it is to be applied to the policy upon renewal. Pursuant to ORS 746.661, subsections (3) and (4) do not allow the re-rating of a policy due to the outcome of a disputed credit report to occur at renewal it is to be applied retroactive to the effective date of the current policy term.

The procedures described in the Company's "Personal Lines Procedures Manual", under the heading of "Investigations Used in Auto and Fire" and sub-heading "Corrected Credit Score Procedure (RPM)" are not in compliance with ORS 746.661.

I recommend the Company takes the required action when a consumer disputes the accuracy or completeness of information in a consumer report and the dispute results in a change in the consumer's credit history or insurance score in accordance with ORS 746.661 and OAR 836-080-0438(1) and (2).

Underwriting Standard #7 – The Company has established the required written policy regarding use of credit histories and insurance scores in their rating or underwriting process in accordance with ORS 746.661 and OAR 836-080-0435.

Findings: Failed.

Pursuant to ORS 746.661(6) except as provided in subsections (2), (3) and (4) of this section, an insurer may only use rating factors other than credit history or insurance score to re-rate the policy at renewal.

A review of the Company's procedures indicates that it is the Company's policy and procedure to use credit history or insurance score in the form of "Risk Assessment Indicators" at policy renewal.

The Company, to show how it was in compliance with the provisions of ORS 746.661 as they apply to this standard, provided a copy of "Procedure Bulletin PB# 03-178:1". This procedure bulletin states "Farmers calls insurance scores "Risk Assessment Indicators", it further states "A Farmers Risk Assessment Indicator is generated using proprietary risk scoring models that apply numerical values to credit characteristics contained in an individual's credit report."

The procedure bulletin describes the following procedure "The system will automatically order Risk Assessment Indicators for renewals and apply the indicators after 36 months."

As an insurer may only use rating factors other than credit history or insurance score to re-rate the policy at renewal this procedure is not in compliance with ORS 746.661(6).

I recommend the Company establish the required written policy regarding use of credit histories and insurance scores in their rating or underwriting process in accordance with ORS 746.661 and OAR 836-080-0435.

CONCLUSIONS/RECOMMENDATIONS

#	RECOMMENDATION	PAGE
1	I recommend the Company process total loss settlements in accordance with policy provisions and applicable rules and regulations pursuant to OAR 836-080-0240.	11
2	I recommend the Company notify the claimant not later than the 30th day after receipt of the proofs of loss, giving the reason more time is needed in accordance with OAR 836-080-0235(4).	12
3	I recommend the Company conduct a reasonable investigation based on all available information in accordance with ORS 746.230.	12
4	I recommend the Company provide the required notice to consumers that they may request a written statement describing the Company's use of credit histories and insurance scores in accordance with OAR 836-080-0430(4).	15
5	I recommend the Company provides the required written statement describing the Company's use of credit histories and insurance scores to a consumer who requests it in accordance with OAR 836-080-0430(4).	16
6	I recommend the Company provides the required information to a consumer when the Company takes an adverse action against the consumer based in whole or in part upon a credit history or insurance score in accordance with ORS 746.650(5) and OAR 836-080-0438(1) and (2).	19
7	I recommend the Company takes the required action when a consumer disputes the accuracy or completeness of information in a consumer report and the dispute results in a change in the consumer's credit history or insurance score in accordance with ORS 746.661 and OAR 836-080-0438(1) and (2).	21
8	I recommend the Company establish the required written policy regarding use of credit histories and insurance scores in their rating or underwriting process in accordance with ORS 746.661 and OAR 836-080-0435.	22

ACKNOWLEDGMENT

The cooperation and assistance rendered by the officers and employees of the Company during this examination is hereby acknowledged and appreciated.

A special thanks is extended to the Examination Coordinator for his courtesy and assistance providing, correlating, or coordinating all requested documents and statistics necessary to ensure a smooth transition during the overall examination process. The responsibilities that were undertaken during this examination were in addition to the scope of his regular assigned duties.

In addition to the undersigned, Gary M. Stephenson, AIE, AIRC, Gary Holliday, AIE and Cliff Nolen, AIE, AIRC participated in this examination.

Respectfully submitted,

_____

Mike Lydon, CPCU
Manager, Market Surveillance
Insurance Division
Department of Consumer and Business Services
State of Oregon

AFFIDAVIT

STATE OF OREGON }
} ss
County of Marion }

Mike Lydon, being duly sworn, deposes and says that the foregoing Market Conduct Report of Examination as of December 31, 2004 subscribed by him is true to the best of his knowledge and belief.

_____
Mike Lydon, CPCU
Manager, Market Surveillance
Insurance Division
Department of Consumer and Business Services
State of Oregon

Subscribed and sworn to before me on the _____ day of _____, 2007.

_____
Linda J. Rothenberger
Notary Public for the State of Oregon
My Commission Expires: March 22, 2009

APPENDIX A

Farmers Insurance Company of Oregon
Market Conduct Target Examination

Claims

#	Phase	Standard	Findings
1	Claims	Company completes its claim investigation not later than the 45th day after its receipt of notification of claim in accordance with ORS 746.230(1) and OAR 836-080-0230.	Passed w/comments
2	Claims	The Company responds to claim correspondence in 30 days in accordance with ORS 746.230(1) and OAR 836-080-0225.	Passed
3	Claims	Claim files are adequately documented as required by ORS 733.170 and OAR 836-080-0215.	Passed w/comments
4	Claims	Total loss settlements are handled in accordance with policy provisions and applicable statutes, rules and regulations pursuant to OAR 836-080-0240.	Failed

Underwriting

#	Phase	Standard	Findings
1	Underwriting	The Company or its producer provides the required notice to a consumer before obtaining the consumer's credit history or insurance score in accordance with OAR 836-080-0430(1).	Passed
2	Underwriting	The Company provides instructions to each of its producers regarding the notice to be provided to a consumer before obtaining the consumer's credit history or insurance score in accordance with OAR 836-080-0430(3).	Passed
3	Underwriting	The Company provides the required notice to consumers that they may request a written statement describing the Company's use of credit histories and insurance scores in accordance with OAR 836-080-0430(4).	Failed
4	Underwriting	The Company provides the required written statement describing the Company's use of credit histories and	Failed

		insurance scores to a consumer who requests it in accordance with OAR 836-080-0430(4).	
5	Underwriting	The Company provides the required information to a consumer when the Company takes an adverse action against the consumer based in whole or in part upon a credit history or insurance score in accordance with ORS 746.650(5) and OAR 836-080-0438(1) and (2).	Failed
6	Underwriting	The Company takes the required action when a consumer disputes the accuracy or completeness of information in a consumer report and the dispute results in a change in the consumer's credit history or insurance score in accordance with ORS 746.661 and OAR 836-080-0438(1) and (2).	Failed
7	Underwriting	The Company has established the required written policy regarding use of credit histories and insurance scores in their rating or underwriting process in accordance with ORS 746.661 and OAR 836-080-0435.	Failed
8	Underwriting	The Company does not cancel or non-renew personal insurance that has been in effect for more than 60 days based in whole or in part on a consumer's credit history or insurance score in accordance with ORS 746.661.	Passed
9	Underwriting	The Company does not use a consumer's credit history to decline coverage of personal insurance in the initial underwriting decision without other substantive underwriting factors in accordance with ORS 746.661.	Passed

FARMERS

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Fax (323) 964-8095

February 16, 2006

Cindy Jones, AIE, CPCU, CRM
Manager, Market Surveillance
Consumer and Business Services Insurance Division
350 Winter Street, NE
Salem, OR 97310-0220

RE: Targeted Market Conduct Exam – Farmers Insurance Company of Oregon

Dear Ms. Jones:

We have received the second draft Report of the Targeted Market Conduct Examination of Farmers Insurance Company of Oregon. The following is our response to the findings, comments and concerns contained in the second draft Report

Before we re-address particular areas of the draft Report, we wish to point out that the Companies and Exchanges of the Farmers Insurance Group of Companies® seriously consider all insurance department examinations and the recommendations of the examiners. Therefore, we have thoroughly reviewed each of the findings and comments.

This response includes those areas where procedures have been, or will be, amended or where we dispute the findings of the examiners. We ask that further consideration be given to any disputed items in the course of drafting a final Report. Unless otherwise noted, the response tracks with the order and sequence of the findings in the draft Report.

Please note that neither these comments nor any of our actions are admissions on our part of any violation, wrongdoing or fault, and should not be interpreted by the Department or any other party as constituting any admissions. Please further note that we are providing these comments and taking actions without waiver of any defense, legal or equitable, and without waiver of any applicable privilege in connection with the information provided.

CLAIMS

Recommendation 3 (page 11):
I recommend the Company process total loss settlements in accordance with policy provisions and applicable rules and regulations pursuant to OAR 836-080-0240.

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We strongly disagree with the examiner's findings on all 46 files found to have failed this standard.

As noted in our prior response, the examiner cites the following three issues with the CCC computer data-based evaluations used in the 46 claim files:

1. "Company used vehicle(s) that were not comparable to the loss vehicle as their mileage was unknown; however, the company still made a cost adjustment for a difference in the number of miles of those vehicles as compared to the known mileage of the loss vehicle."
2. "Use of data from across the United States, Western Region, and regional averaging to determine the fair market value of a totaled vehicle, principally garaged in the area where the loss vehicle was garaged."
3. "Company used vehicle(s) that were not comparable to the loss vehicle as their body style was different, i.e., loss vehicle 2dr coupe, Company's comparable vehicle 4 door wagon."

With regard to the first issue cited above, CCC's mileage adjustments are based on the following: On a quarterly basis, using its extensive database of vehicles, CCC calculates the average mileage of each model year vehicle, by vehicle type, for each region of the country. When a comparable vehicle without mileage listed is used in performing an evaluation, that regional average is used for the comparable vehicle. We have been advised that CCC described this process to the Department of Insurance during a September 15, 2004, meeting which included Larry Culbertson, Cliff Nolen, Cece Newell, Douglas Beck, Jan Vitus, Jan White, Carol Simila, John Hardiman, Linh Nguyens, Gary Stephenson, Kathleen Kalk, Jann Goodpaster, Gayle Woods, Michael Morter and Pat Neesham. A CCC Valuescope valuation and its contents were reviewed and discussed in detail. The sample valuation form used for that meeting contained comparables without mileage and there was no indication that the use of vehicle with unlisted mileage was inappropriate. This process is not intended to identify exact replacement vehicles, but rather to arrive at a fair cash settlement amount, consistent with the applicable regulations.

Regarding the second issue cited above, CCC's methodology is premised upon the continuous collection of local market vehicle values to provide prompt valuations upon receipt of a request. These currently or recently available vehicles are used to perform the valuations, and we understand the values of these vehicles to be the "data" to which OAR 836-080-0240(3)(a)(F) applies. Again, the evaluation is based on these local market vehicle values. Since vehicle conditions and mileage vary, appropriate adjustments are made in the equating process. We do not believe it would be reasonable to construe the rule to require

that every such adjustment be premised solely on data collected from the area surrounding the location of the principally garaged location, nor have we ever been made aware of such an interpretation by the Department of Insurance. This issue was discussed during a meeting between CCC and the Department on May 24, 2001, in Salem, Oregon with Joel Ario, Carl Lundbert, Pat Fitzgerald and Larry Culbertson. During a meeting on September 15, 2004, a CCC Valuescope valuation and its content were reviewed and discussed in detail. CCC answered various questions asked by the Department. The Valuescope used in that meeting contained the verbiage, "all dollar adjustments are determined by surveys, inspections, and interviews with dealerships across the United States." There were no questions to suggest that the use of this language was inappropriate.

With regard to the third issue cited above, vehicles are determined to be comparable to the loss vehicle based on nearness to the loss vehicle's primary garage location, similarity of model equipment and odometer and precision of the data (inspected versus advertised). Four-door wagons and three-door hatchback models may be used in a valuation of a 4-door model when these are the most comparable vehicles available in the market at the time of the valuation. Adjustments are made to compensate for the differences in body style and options. Again, this process cannot always identify exact replacement vehicles, but it does arrive at a fair cash settlement amount, consistent with the applicable regulations. This issue was also discussed during the May 24, 2001, meeting between CCC and the Department.

Recommendation 4 (page 12)
I recommend the Company notify the claimant not later than the 30th day after receipt of the proofs of loss, giving the reasons more time is needed in accordance with OAR 836-080-0235(4).

Again, we strongly disagree with the examiner's finding that waiting for the necessary total loss paperwork to be completed and mailed backed from a claimant equates to an incomplete investigation. Moreover, **OAR 836-080-0235(4)** reads: "If an insurer needs more time to determine whether the claim of a **first party claimant** should be accepted or denied, it shall so notify the claimant not later than the 30th day after receipt of the proofs of loss, giving the reason more time is needed. Forty-five days from the date of such initial notification and every 45 days thereafter while the investigation remains incomplete, the insurer shall notify the claimant in writing of the reason additional time is needed for investigation" (emphasis added).

The examiner cited a failure to comply with this rule on third party claimants. Specifically, unit 33, claim number 1004915765-1-1, involves a third party claimant. The rule clearly
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applies to first party claimants.

Recommendation 5 (page 13):
I recommend the Company conduct a reasonable investigation based on all available information in accordance with ORS 746.230.

The investigations conducted by the company with regard to the fair market values of the loss vehicles involved in this exam were reasonable and resulted in a fair resolution of the claim and were in compliance with ORS 746.230 unfair claim settlement practices.

Again, CCC's mileage adjustments are based on the following: On a quarterly basis, using its extensive database of vehicles, CCC calculates the average mileage of each model year vehicle, by vehicle type, for each region of the country. When a comparable vehicle without mileage listed is used in performing an evaluation, that regional average is used for the comparable vehicle. We have been advised that CCC has described this process to the Department of Insurance in past meetings, and we are not aware of any reason why this process is not permissible under the governing regulations. This process is not intended to identify exact replacement vehicles, but does arrive at a fair cash settlement amount, consistent with the applicable regulations.

We believe the methodology described above constitutes a fair and reasonable investigation of a loss vehicle's fair market value.

We would like to schedule a meeting with representatives from the Department, CCC and Farmers to discuss total loss processes and evaluations if the Department continues to disagree with the above outlined procedures.

UNDERWRITING

Recommendation 4 (page 15)
I recommend the Company provide the required notice to consumers that they may request a written statement describing the Company's use of credit histories and insurance scores in accordance with OAR 836-080-0430(4).

Recommendation 4 was issued in conjunction with underwriting standard three. The report states the company is not in compliance with OAR 836-080-0430(4) as we don't have procedures in place that instruct our producers to provide the required disclosure regarding their right to request a written statement describing the Company's use of credit histories and insurance scores. We have thoroughly reviewed our procedures, forms and publications referenced in the report. We have attached our written procedures reflecting the need for our agents to provide the required notice. (Exhibit I).

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Recommendation 5 (page 17)
I recommend the Company provides the required written statement describing the Company's use of credit histories and insurance scores to a consumer who requests it in accordance with OAR 836-080-0430(4).

Recommendation 5 was issued in conjunction with underwriting standard four. The report states that our use of insurance scores notice, form number 25-4219 (Exhibit II), does not comply with OAR 836-080-0430(4) or ORS 746.661(6). We disagree with the criticism. Form 25-4219 is used during the application processes and is included with each new business and renewal policy delivered. The notice complies with OAR 836-080-0430(4a-e) by addressing the following items:

1. Why we use credit history (see paragraph 1 second sentence)
2. How we use credit histories or insurance scores (See paragraph 1 second Sentence)
3. What kinds of credit information are used by us (See paragraph 2 second Sentence)
4. Whether a consumer's lack of credit history will affect our consideration of the application (See paragraph 2 last sentence)
5. Where the consumer may go with questions (see paragraph 4)

The examiner is incorrect when stating that this form is not provided during the application process and we request that this wording be removed.

ORS 746.661(6) states "Except as provided in subsections (2), (3) and (4) of this section, an insurer may only use rating factors other than credit history or insurance score to rerate the policy at renewal." The report states that form 25-4219 is not in compliance with ORS 746.661(6) as it indicates the Company will use the credit score to calculate premium at renewal and that the Company runs a credit report every three years. We disagree with the criticism. First, in both the 1-05 and 9-05 versions of notice 25-4219, the reference to calculating premium at policy inception and on renewal was removed. The current 9-05 version of the notice is attached. (Exhibit II) Also, while we do not currently order scores on renewal, ORS 746.661(6) does not state you cannot use credit scores at renewal. It states you can't use credit history to rerate the policy at renewal.

For those customers that request a new score be ordered, we do not apply new scores during the renewal process or on new business for existing households unless the score has improved. This applies to any customer request we receive on an annual basis to rerun a credit score. This serves to the benefit our customers. The examiner's statements regarding the Company's use of credit scores to calculate premium at renewal are incorrect and we
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request the wording be removed from the report.

We disagree with the Examiner's interpretation of OAR 836-080-0430(4)(d). The law states our notice must address, "Whether a consumer's lack of credit history will affect the insurer's consideration of an application." This part of the rule in no way relates to the rate used to calculate premium; rather it relates to whether lack of credit will cause an insurer to deny an application. Our notice says, "Lack of credit history is not considered in determining whether to accept or deny an application for insurance." This sentence was specifically added to our 25-4219 notice to address OAR 836-080-0430(4)(d). The examiner's statement that we do not comply is incorrect and we request that this wording be removed from the report. However, we will voluntarily revise the wording in the notice to adhere to the examiner's interpretation.

Recommendation 6 (page 19)
I recommend the Company provides the required information to a consumer when the Company takes an adverse action against the consumer based in whole or in part upon a credit history or insurance score in accordance with ORS 746.650(5) and OAR 836-080-0438(1) and (2).

Recommendation 6 was issued in conjunction with underwriting standard five. The report states that we failed standard five because form 25-4219 3-03, titled "Farmers Use of Insurance Scores", did not contain the significant reasons for adverse action or the name, address, and toll free number of the consumer reporting agency that provided the consumer report, and it is not issued at the time the adverse action is taken. We respectfully disagree with the criticism. Form 25-4219 is not our adverse action notice. It was provided to the examiner to demonstrate that we do publish a notice that states the consumer has the right no more than once annually to request us to re-rate their policy and of potential negative consequences of re-rating, if any. Form 25-4293, titled "Fair Credit Reporting Act Notice," was earlier provided to the examiner, is attached to our response (Exhibit VIII). The notice contains the required language and up to four primary reasons for the adverse action, as required to comply with ORS 746.650(5) and OAR 836-080-0438(1). OAR 836-080-0438(2) requires an insurer to include in a notice of adverse underwriting decision required by ORS 746.650(5), an explanation of the consumer's right to request, no more than once annually, that an insurer rerate the consumer, and of potential negative consequences of rerating, if any.

While we do believe we comply with the rule by using forms 25-4219 and 25-7878 in combination, we have taken the portion of notice 25-4219 required by ORS 746.650(5) that

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we already provide to our customers and included it on our Adverse Action Notice form. A copy of the revised notice is attached. (Exhibit III)

Recommendation 7 (page 21)
I recommend the Company takes the required action when a consumer disputes the accuracy or completeness of information in a consumer report and the dispute results in a change in the consumer's credit history or insurance score in accordance with ORS 746.661 and OAR 836-080-0438(1) and (2).

Recommendation 7 was issued in conjunction with underwriting standard six. The report states we were unable to demonstrate we were in compliance with ORS 746.661 and OAR 836-080-0438(1) and (2). First, we did have a procedure in place to handle consumer disputes as of January 1, 2004. The examiner is incorrect that our procedure was effective July 23, 2004. While this was the date on the procedure manual page, that only indicates a change to that particular procedure manual page was made on July 23, 2004. Attached is a historical copy of our procedure manual page III-D-28 dated March 1, 2001 (Exhibit IV). Therefore, we request that any reference to not having a procedure in place from January 1, 2004, to July 23, 2004, be removed from the report.

The criticism also states that our procedure does not address inquiries received directly from consumers regarding the resolution of a dispute, and that if the score worsens the new score will be applied at renewal. Although we agree that our printed procedure requires revision, we do not agree with the criticism. It has been our practice since we began using credit scoring to resolve disputes resulting in a corrected credit score by applying the discount generated from the corrected score retroactively to the application or renewal date (renewal date applied before ORS 746.661 was effective). We have attached the page from our "Questions you may have about Risk Assessment Indicators", (Exhibit V) which states "…Farmers will apply any changes to your premium retroactively to the original application or renewal date." This is given to applicants at the time of application. When a customer requests us to reorder, we apply a new score only if it is an improvement over the old score. If the score does not improve, we will not use it. While we believe we are in compliance, we have voluntarily revised our procedure manual page III-D-28 to remove any possibly confusing reference regarding applying new scores at renewal and to include language specific to handling disputes received directly from our customer. We request that the wording of the report be changed to state the company is satisfying the requirements of ORS 746.661 subsections (3) and (4).

Recommendation 8 (page 23)
I recommend the Company establish the required written policy regarding use of credit histories and insurance scores in their rating or underwriting process in accordance with ORS 746.661 and OAR 836-080-0435.

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Recommendation 8 was issued in conjunction with underwriting standard seven. The exam states that procedure bulletin PB# 03-178:1 implies that we will automatically order Risk Assessment Indicators for renewals and apply the indicators after 36 months. It is no longer the Company's practice to reorder indicators every 36 months. The examiner chose to ignore Breaking News Bulletin number 0-8513 (Exhibit VI), with which he was also provided which clearly states we no longer automatically re-order scores. However, we have published a revised Procedure Bulletin to add additional clarity (attached PB# 03-178:3 – Exhibit VII). We believe this Recommendation should be dropped.

As set forth in this letter, we have attempted to address the concerns, comments and recommendations outlined in the Follow-up Market Conduct Examination Report in an expeditious and responsible manner. We ask that these comments be considered and the draft Report be revised accordingly. However, if the Department has no intent to reconsider some of the findings, then we believe it would be in the best interest for all parties to meet in person before any final Report is issued. Our intent is to arrive at a mutual understanding regarding any outstanding issues. Therefore, in an effort to further our efforts toward resolution, we would like to meet with you and Joel Ario to discuss these issues. Please let me know what dates are available so that I can make the necessary arrangements.

We would hope that there is no further action anticipated by the Division in connection with this Examination. If there is, we do not waive our right to invoke any other administrative remedies.

We await the release of the final report. Please feel free to contact Jan Walker of my staff at (323) 932-3579, or me, if there is anything further you might need.

Sincerely,

Bennett Katz
Assistant Vice President
Regulatory Affairs