

REPORT OF EXAMINATION
OF THE
MID-CENTURY INSURANCE
COMPANY
AS OF
DECEMBER 31, 2017

Filed on June 28, 2019

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Los Angeles, California
May 16, 2019

Honorable Ricardo Lara
Insurance Commissioner
California Department of Insurance
Sacramento, California

Dear Commissioner:

Pursuant to your instructions, an examination was made of the

MID-CENTURY INSURANCE COMPANY

(hereinafter also referred to as the Company) at its former administrative office located at 4680 Wilshire Boulevard, Los Angeles, California 91010. The Company's current statutory home office and main administrative office is located at 6301 Owensmouth Avenue, Woodland Hills, California 91367.

SCOPE OF EXAMINATION

We have performed our multi-state examination of the Company. The previous examination of the Company was made as of December 31, 2013. This examination covers the period from January 1, 2014 through December 31, 2017.

The examination was conducted in accordance with the National Association of Insurance Commissioners *Financial Condition Examiners Handbook (Handbook)*. The Handbook requires the planning and performance of the examination to evaluate the Company's financial condition, assess corporate governance, identify current and prospective risks, and evaluate system controls and procedures used to mitigate those risks. An examination also includes identifying and evaluating significant risks that could cause an insurer's surplus to be materially misstated both currently and prospectively.

All accounts and activities of the Company were considered in accordance with the risk-focused examination process. This may include assessing significant estimates made by management and evaluating management's compliance with Statutory Accounting Principles. The examination does not attest to the fair presentation of the financial statements included herein. If, during the course of the examination, an adjustment is identified, the impact of such adjustment will be documented separately following the Company's financial statements.

This examination report includes findings of fact and general information about the Company and its financial condition. There might be other items identified during the examination that, due to their nature (e.g., subjective conclusions, proprietary information, etc.), were not included within the examination report but separately communicated to other regulators and/or the Company.

This examination was a coordinated examination with California as the lead state of the Farmers Insurance Exchange subgroup of the Farmers Insurance Group. The states of Illinois and Washington participated on the examination, and it was conducted concurrently with the examinations of the following insurance entities in the holding company group:

Group/Company	NAIC CoCode	Domiciled State
FARMERS INSURANCE EXCHANGE GROUP		
Farmers Insurance Company of Arizona	21598	AZ
Farmers Insurance Exchange	21652	CA
Truck Insurance Exchange	21709	CA
Fire Insurance Exchange	21660	CA
Civic Property and Casualty Company	10315	CA
Neighborhood Spirit Property and Casualty Company	10317	CA
Exact Property and Casualty Company	10318	CA
Mid-Century Insurance Company (the Company)	21687	CA
Farmers Insurance Company of Idaho	21601	ID
Farmers New Century Insurance Company	10806	IL
Illinois Farmers Insurance Company	21679	IL
Farmers Insurance Company Inc.	21628	KS
Farmers Insurance of Columbus, Inc.	36889	OH
Farmers Insurance Company of Oregon	21636	OR
Texas Farmers Insurance Company	21695	TX
Farmers Texas County Mutual Insurance Company	24392	TX
Mid Century Insurance Company of Texas	28673	TX
Farmers Insurance Company of Washington	21644	WA

Group/Company	NAIC CoCode	Domiciled State
COAST NATIONAL/BRISTOL WEST GROUP		
Coast National Insurance Company	25089	CA
Security National Insurance Company	33120	FL
Bristol West Preferred Insurance Company	12774	MI
Bristol West Casualty Insurance Company	11034	OH
Bristol West Insurance Company	19658	OH

Group/Company	NAIC CoCode	Domiciled State
FOREMOST GROUP		
Foremost Insurance Company Grand Rapids, Michigan	11185	MI
Foremost Property and Casualty Insurance Company	11800	MI
Foremost Signature Insurance Company	41513	MI
Farmers Specialty Insurance Company	43699	MI
Foremost County Mutual Insurance Company	29254	TX
Foremost Lloyds of Texas	41688	TX

Group/Company	NAIC CoCode	Domiciled State
21st CENTURY INSURANCE GROUP		
21st Century Casualty Company	36404	CA
21st Century Insurance Company	12963	CA
21st Century Superior Insurance Company	43761	CA
21st Century Pacific Insurance Company	23795	CO
21st Century Assurance Company	44245	DE
American Pacific Insurance Company, Inc.	10805	HI
Farmers Insurance Hawaii, Inc.	28487	HI
21st Century Advantage Insurance Company	25232	MN
21st Century Auto Insurance Company of New Jersey	10184	NJ
21st Century Pinnacle Insurance Company	10710	NJ
21st Century National Insurance Company (a)	36587	NY
21st Century North America Insurance Company	32220	NY
21st Century Centennial Insurance Company	34789	PA
21st Century Indemnity Insurance Company	43974	PA
21st Century Preferred Insurance Company	22225	PA
21st Century Premier Insurance Company	20796	PA
21st Century Security Insurance Company (b)	23833	PA
21st Century Insurance Company of the Southwest	10245	TX

- (a) 21st Century National Insurance Company was sold to Plymouth Rock Assurance Corporation (Plymouth), effective April 1, 2018.
- (b) 21st Century Security Insurance Company (Security) was sold to Plymouth, which assigned its right to acquire Security to High Point Preferred Insurance Company, effective August 1, 2018.

Group/Company	NAIC CoCode	Domiciled State
ZURICH GROUP		
Farmers Reinsurance Company	10873	CA

With the exception of the Farmers Reinsurance Company, which is part of the Zurich Group, all the above companies are part of the Farmers Insurance Group of companies. Although owned by Farmers Group, Inc. (FGI), the attorney-in-fact for the Farmers Insurance Group, the Farmers Reinsurance Company operates as one of the Farmers property and casualty companies.

COMPANY HISTORY

The Company was incorporated in the state of California on December 3, 1949, for the purpose of transacting property and casualty business. The business commenced on February 17, 1953.

Capitalization

The Company had 500,000 shares of \$10 par value common stock authorized of which 480,000 shares were issued and outstanding as of December 31, 2017. The Company has no preferred stock authorized or outstanding.

Dividends

In 2016, the Company received, in cash, ordinary dividends in the amount of \$2,000,000 from FFS Holding, LLC.

MANAGEMENT AND CONTROL

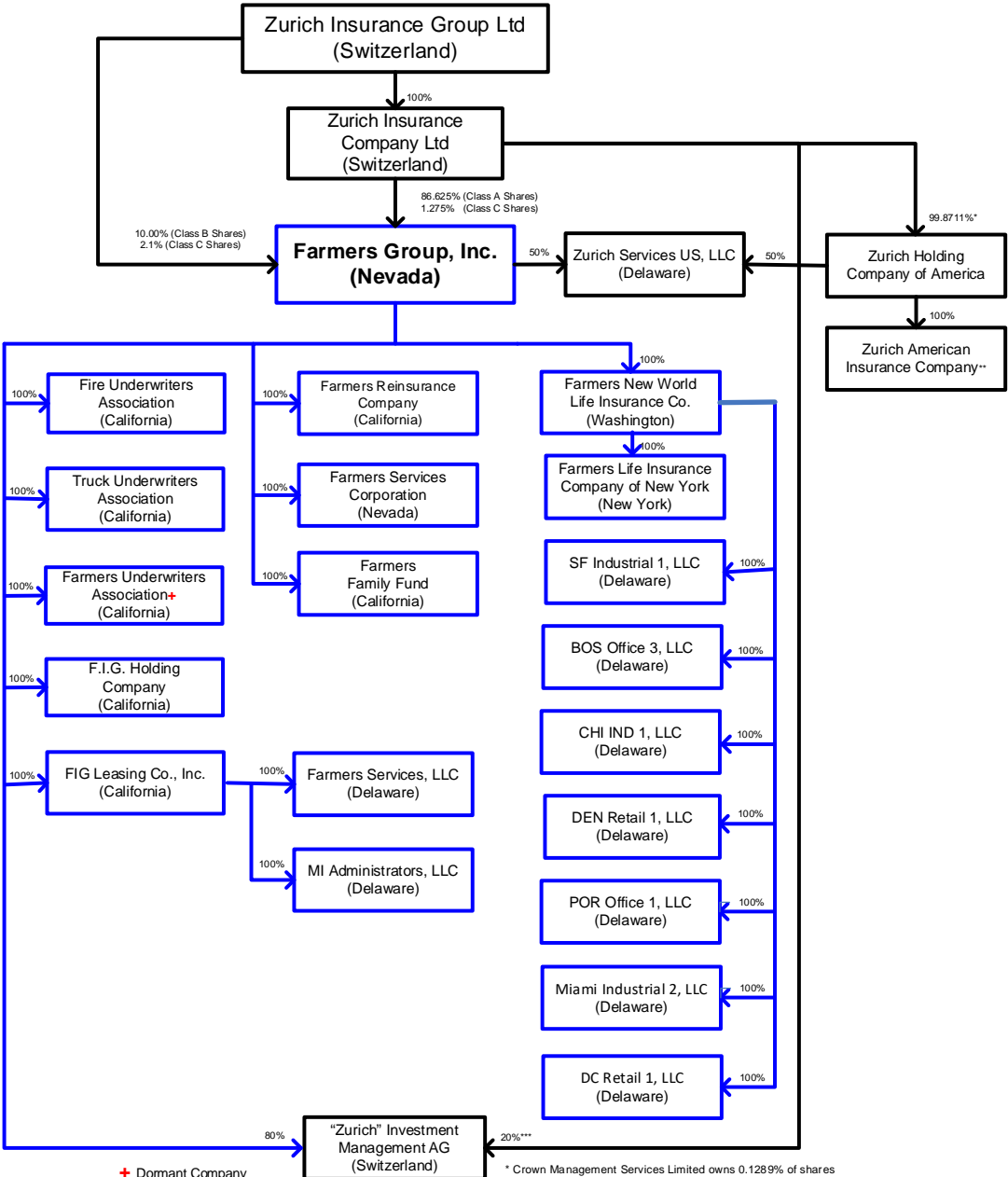
The Company is a subsidiary of Farmers Insurance Exchange (80%), Fire Insurance Exchange (10%), and Truck Insurance Exchange (10%). Through its 80% ownership interest, Farmers Insurance Exchange is the ultimate controlling person of the Company.

With the approval of the California Department of Insurance (CDI) in December 2013, a unique National Association of Insurance Commissioners (NAIC) Group Code has been assigned to the Farmers Group of companies (previously part of the Zurich NAIC Group Code 0212 and now included in the Farmers Group Code 0069). As such Zurich Insurance Company (ZIC), is no longer named as an Ultimate Controlling Party for the Farmers Group of companies. However, disclosure continues to be provided in the Holding Company Annual Registration Statements regarding the relationship with Zurich Insurance Group Ltd. (ZIG) and transactions involving entities with the ZIC NAIC Group Code 0212.

The Farmers Exchanges (Farmers Insurance Exchange, Fire Insurance Exchange, and Truck Insurance Exchange) and the Company are provided certain non-claims services by the Farmers Exchanges Attorney-In-Fact, Farmers Group, Inc. (FGI). FGI is a U.S. subsidiary of ZIG, a Swiss holding company. ZIG was formerly known as Zurich Financial Services until it changed its name in 2012.

The following abridged organizational charts show the relationships of FGI to its ultimate parent ZIG, and of the Farmers Exchanges to their subsidiaries and affiliates as of December 31, 2017:

ZURICH ORGANIZATION (NAIC GROUP CODE 0212)



+ Domant Company

* Crown Management Services Limited owns 0.1289% of shares
 ** Listing of Zurich's numerous North American Insurance subsidiaries is available upon request
 *** 20% of share owned by Zurich Finance Company Ltd

**FARMERS EXCHANGES ORGANIZATION
(NAIC GROUP CODE 0069)**

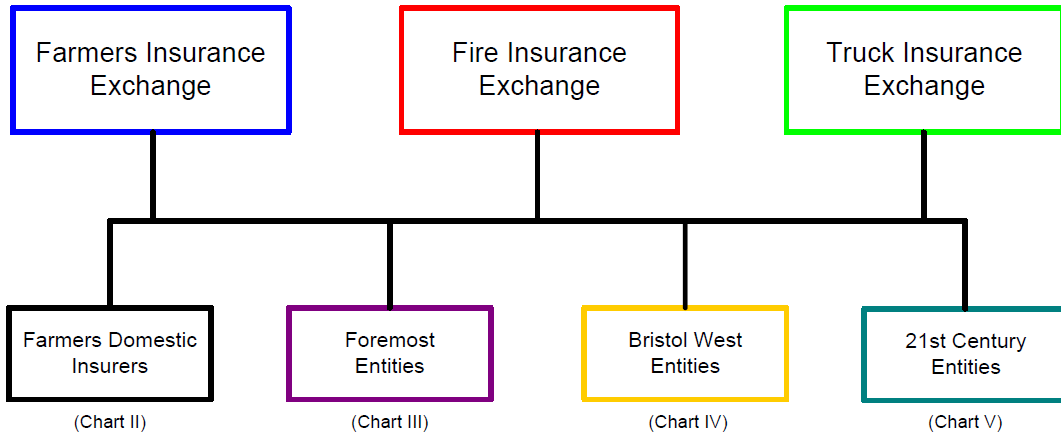


CHART II: EXCHANGES/FARMERS ENTITIES ORGANIZATION

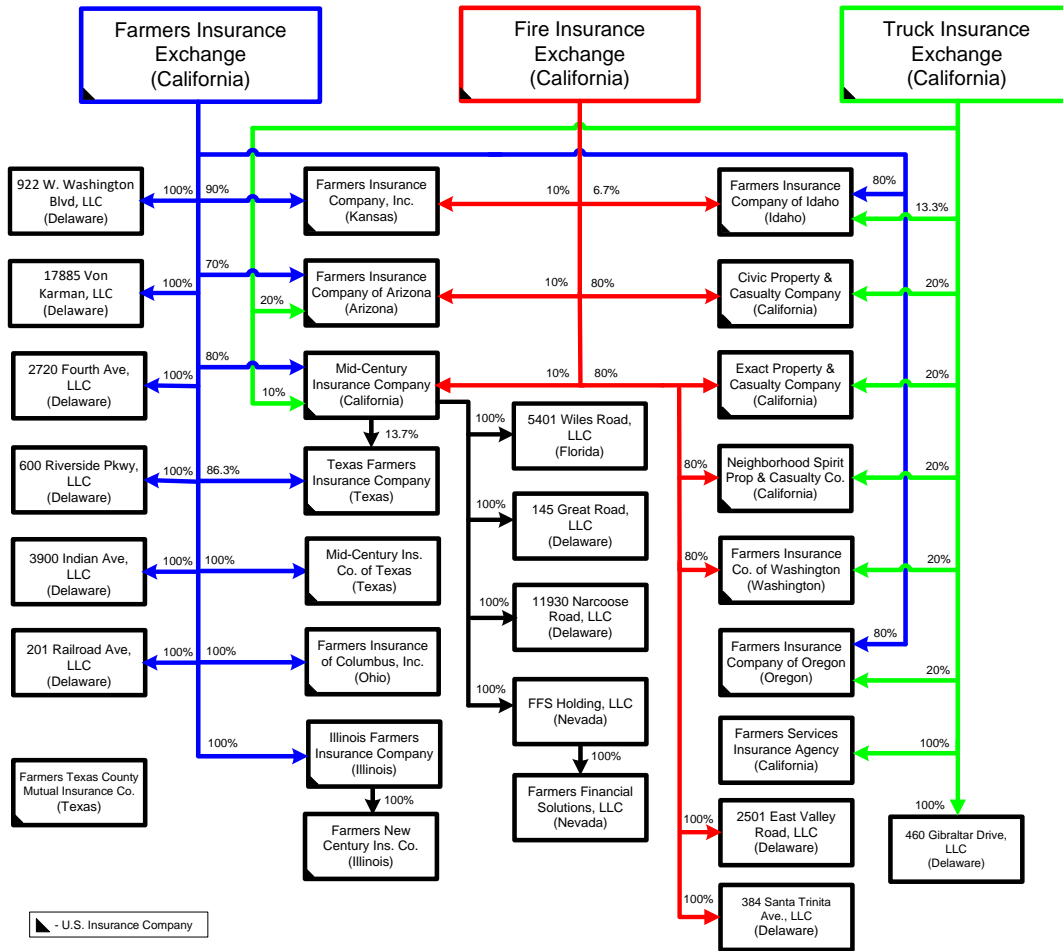


CHART III: EXCHANGES/FOREMOST ORGANIZATION

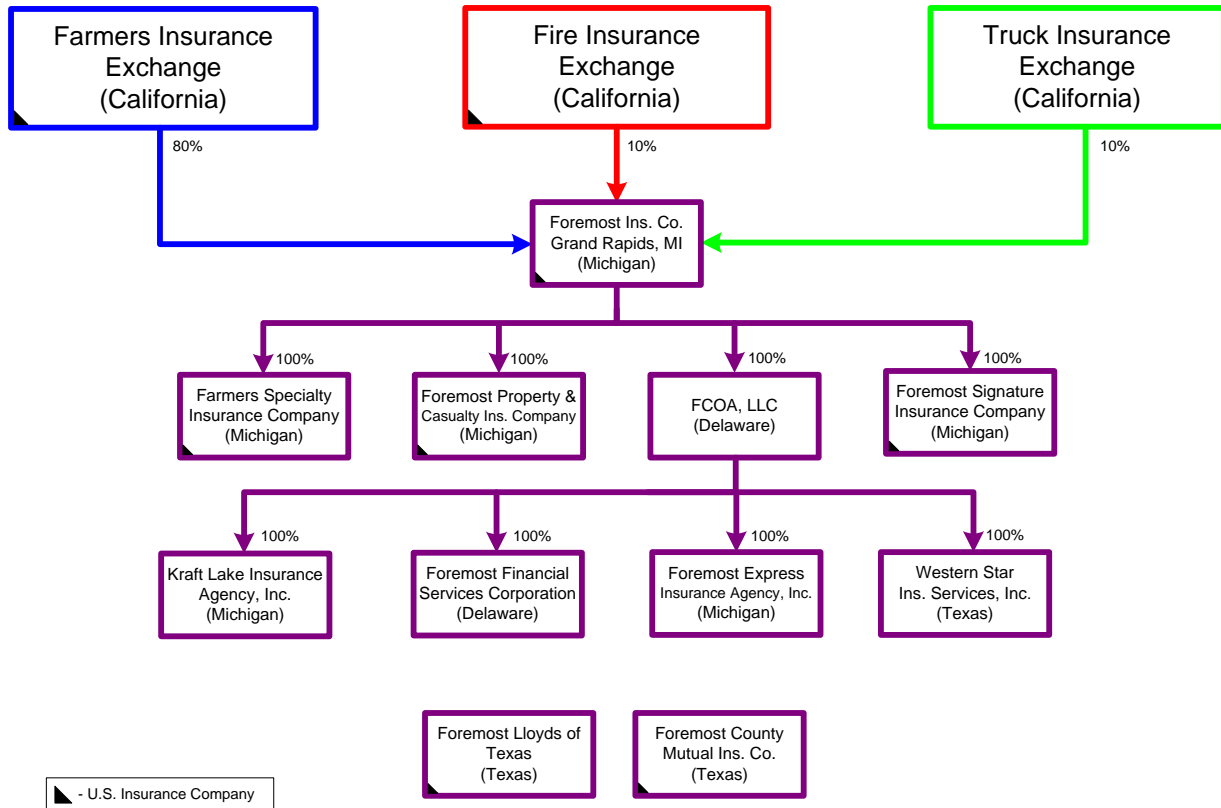


CHART IV: EXCHANGES/BRISTOL WEST ORGANIZATION

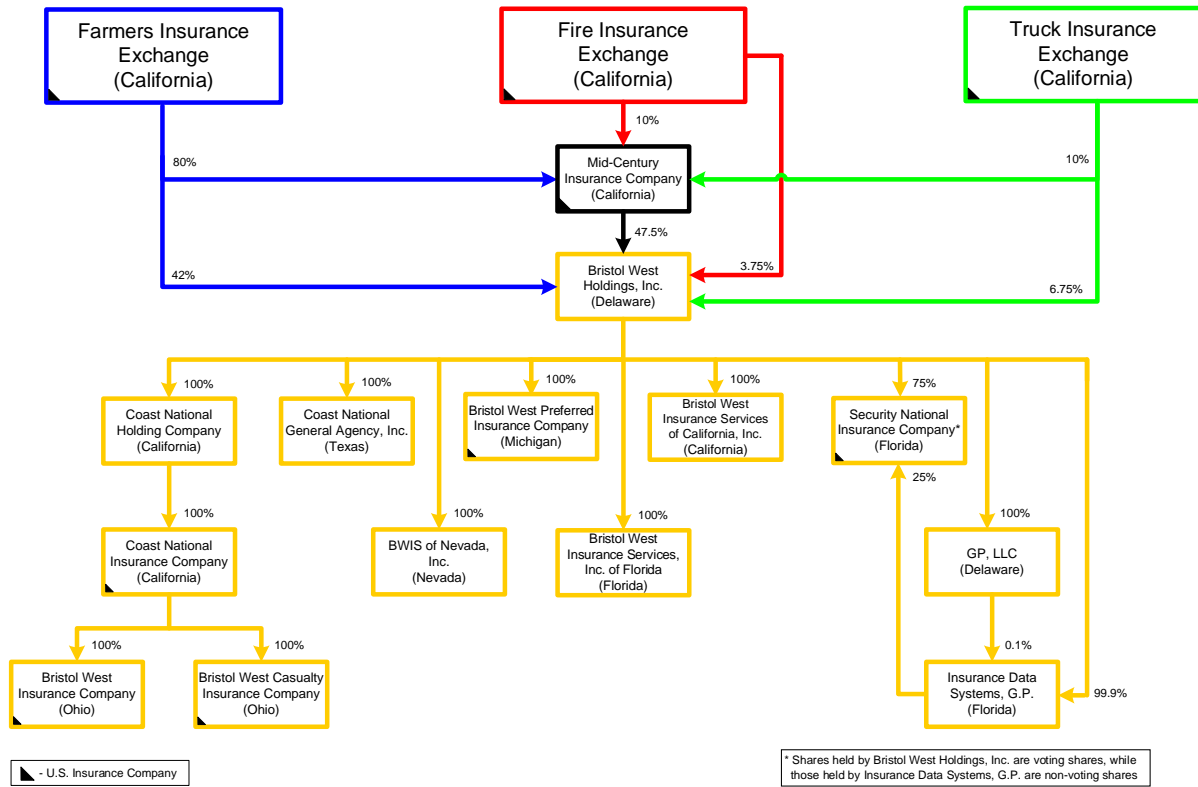
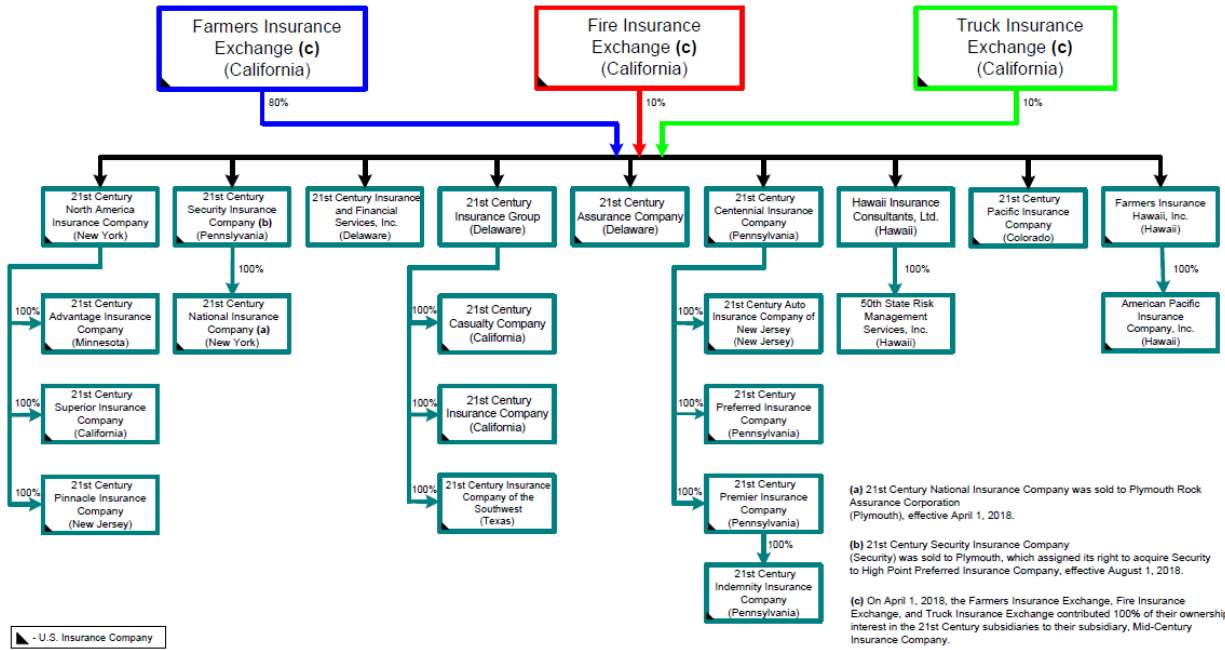


CHART V: EXCHANGES/21st CENTURY ORGANIZATION



Management of the Company is vested in a seven-member board of directors, elected annually. A listing of the members of the board and principal officers serving on December 31, 2017 follows:

Board of Directors

<u>Name and Location</u>	<u>Principal Business Affiliation</u>
Gisselle Acevedo (a) New Canaan, Connecticut	Child Therapist The Child and Family Guidance Center
Thomas G. Allen (b) Denver, Colorado	President Intermountain Electric, Inc.
Keith G. Daly (c) Westlake Village, California	Chief Claims Officer Farmers Insurance Exchange
Ronald L. Marrone Pittsburg, Kansas	Co-owner Family Food Services Corporation
Ronald G. Myhan (d) Malibu, California	Chief Financial Officer Farmers Exchanges
Donald E. Rodriguez (e) Long Beach, California	Executive Director Boys and Girls Club
Richard M. Shriver (f) Stevenson Ranch, California	Head of Zone Field Operations Farmers Group, Inc.

- (a) Replaced by Richard S. Shriver effective June 6, 2018. Richard S. Shriver, replaced by Keith G. Daly September 18, 2018.
- (b) Replaced by Frederick R. Kruse effective June 6, 2018. Frederick R. Kruse, replaced by Alan R. Gildemeister effective March 19, 2019.
- (c) Replaced by Stanley R. Smith effective June 6, 2018. Stanley R. Smith replaced by Gary R. Martin effective March 19, 2019.
- (d) Replaced by Julio A. Da Silva effective March 19, 2019.

Principal Officers

<u>Name</u>	<u>Title</u>
Richard Michael Shriver (a)	President
Maite I. Baur	Vice President
Keith G. Daly (b)	Vice President
Victoria L. McCarthy	Vice President
Ronald G. Myhan (c)	Vice President and Treasurer
James L. Nutting	Vice President and Actuary
Doren E. Hohl	Secretary

(a) Replaced by Keith G. Daly, effective September 18, 2018

(b) Replaced by Robert P. Howard, effective June 11, 2018

(c) Replaced by Thomas S. Noh, effective June 1, 2019

Management Agreements

Farmers Group, Inc. (FGI), as the Attorney-In-Fact (AIF) for the Farmers Insurance Exchange (FIE), provides operating services, including staffing and occupancy to FIE. The operating services do not include claims adjustment services, nor do they include the payment of claims, commissions, and the payment of premium and income taxes, all of which are the responsibility of the FIE. These operating services are provided to FIE pursuant to Subscription Agreements entered into between FGI and each of the Farmers Exchange's individual policyholders. There is no specific management services agreement required between FIE and FGI for these services provided. The compensation to the AIF for these services is derived through membership fees and subscription fees under the terms of the Subscription Agreements.

Service Agreements: On July 1, 2015, FIE and its subsidiaries (including the Company) entered into separate Service Agreements (Agreements). In accordance with the terms of the Agreements, FIE provides various services which include policy and premium administration, agents and commissions, including claims adjustment services, accounting and financial reporting services, investment management services, and other administrative services. FIE provides these services at a cost which are allocated in accordance with the methods prescribed in the NAIC Accounting Practices and Procedures Manual, Statement of Statutory Accounting Principle (SSAP) No. 70.

Allocations occur prior to the Intercompany Reinsurance and Pooling Agreement (see the “REINSURANCE” section of this examination report).

The parties acknowledge that FIE shall provide these services either directly or through its attorney-in-fact, agents, representatives or affiliates; however, FIE shall continue to be liable at all times. The parties to the Agreements are:

Bristol West Casualty Insurance Company	Bristol West Insurance Company
Bristol West Preferred Insurance Company	Civic Property and Casualty Company
Coast National Insurance Company	Exact Property and Casualty Company
Farmers Insurance Company of Arizona	Farmers Insurance of Columbus, Inc.
Farmers Insurance Company of Idaho	Farmers Insurance Company of Oregon
Farmers Insurance Company of Washington	Farmers New Century Insurance Company
Farmers New World Life	Foremost Insurance Company, Grand Rapids, Michigan
Illinois Farmers Insurance Company	Mid-Century Insurance Company
Mid-Century Insurance Company of Texas	Neighborhood Spirit Property and Casualty Company
Security National Insurance Company	Texas Farmers Insurance Company

These Agreements were approved by the California Department of Insurance (CDI) on December 9, 2015.

FIE charges a portion of the compensation it pays FGI to its subsidiaries based on each company’s percentage participation in the Intercompany Reinsurance and Pooling Agreement.

For 2014, 2015, 2016, and 2017, the pooled share of the compensation paid by FIE and its subsidiaries to FGI for its services was as follows (including membership, installment, and policy fees):

<u>Company</u>	<u>Compensation Paid to Farmers Group, Inc. (for Exchange Issued Policies)</u>			
	<u>2017</u>	<u>2016</u>	<u>2015</u>	<u>2014</u>
Farmers Insurance Exchange	\$ 1,431,844,943	\$ 1,414,798,318	\$ 1,371,514,957	\$ 1,370,276,762
Truck Insurance Exchange	214,430,885	211,878,009	205,395,960	205,210,530
Fire Insurance Exchange	207,513,760	205,043,235	198,770,284	198,590,835
Mid-Century Insurance Company	442,696,021	437,425,567	424,043,272	423,660,448
Civic Property and Casualty Company	27,668,501	27,339,098	26,502,704	26,478,778
Exact Property and Casualty Company	27,668,501	27,339,098	26,502,704	26,478,778
Neighborhood Spirit Property and Casualty Company	27,668,501	27,339,098	26,502,704	26,478,778
Subtotals	\$ 2,379,491,112	\$ 2,351,162,423	\$ 2,279,232,585	\$ 2,277,174,909
All Other Subsidiaries	387,359,018	382,747,371	371,037,863	370,702,891
Totals - Compensation Paid	<u>\$ 2,766,850,130</u>	<u>\$ 2,733,909,794</u>	<u>\$ 2,650,270,448</u>	<u>\$ 2,647,877,800</u>
Totals - Membership, Installment, and Policy Fees Paid	<u>\$ 94,726,319</u>	<u>\$ 104,002,073</u>	<u>\$ 104,490,270</u>	<u>\$ 101,774,982</u>

As previously noted, the above amounts paid to FGI by FIE and its subsidiaries do not include the cost of claims adjustment services, nor do they include the payment of claims, commissions, and the payment of premium and income taxes, all of which are the responsibility of FIE and its subsidiaries.

Tax Sharing Agreement: FIE is the lead party to a Tax Sharing Agreement (Agreement), effective September 1, 2013, with various insurance and non-insurance affiliates and subsidiaries, including certain companies in the Foremost Insurance Group, Bristol West Insurance Group, and 21st Century Insurance Group, respectively. The CDI approved this Agreement on February 18, 2014. There have been no changes to the Agreement since FIE's financial examination as of December 31, 2013.

FIE is the party primarily responsible for filing and making all tax payments on behalf of the Company and the other parties to this Agreement. Allocation of taxes is based upon separate return calculations with intercompany tax balances payable or receivable being settled in amounts equal to the amounts which would be due to or from federal taxing authorities as if separate returns were filed. Intercompany balances are settled monthly, and the final settlement is made within 30 days after the filing date of the consolidated return.

The Company's portion of the federal income taxes paid under the Agreement for 2014, 2015, 2016, and 2017 was \$24,997,992, \$15,239,313, \$3,458,893, and \$12,083,158, respectively.

Agreements with Non-Affiliates

Third-Party Administrative and Managed Care Agreements: Zurich American Insurance Company (ZAIC) or its affiliates provide administrative, underwriting, policy issuance and related services to the Company, FIE, Fire Insurance Exchange (Fire), and Truck Insurance Exchange (Truck), in conjunction with the following specific insurance programs:

- Effective November 1, 2000, Zurich Services Corporation (ZSC) entered into a Third-Party Administrator Agreement (Agreement) with the Company, FIE and other affiliates (Truck, Exact Property and Casualty Company, and Civic Property and Casualty Company, Neighborhood Spirit Property and Casualty). Under this Agreement, ZSC provides claims administration and risk engineering services which are subject to a reinsurance agreement for equipment breakdown coverage provided by ZAIC.
- Effective November 6, 2000, a Managed Care Services Agreement (Agreement) was entered into between ZSC and the Company, FIE, Fire, and Truck. Under this Agreement, ZSC makes available a provider network and managed care services to the named insured of this Agreement.

Investment Management Agreement: FGI, acting on behalf of the Exchanges (Farmers Insurance Exchange, Fire Insurance Exchange, Truck Insurance Exchange, and the subsidiaries of these Exchanges), entered into an Investment Management Agreement with the following third-party advisors to act as the investment manager:

- Deutsche Investment Management Americas, Inc: FGI entered into an Investment Management Agreement dated July 1, 1998 with its affiliate, Scudder Kemper Investments Inc. (Scudder). There have been multiple amendments since then, mostly related to Schedule III, of which the latest is dated April 12, 2011. In 2002, Scudder was acquired and replaced by Deutsche Asset Management (DeAM), and the name changed to Deutsche Investment Management Americas, Inc. (now called DWS Investment Management Americas, Inc. since March 2018) (DWS). DWS, a non-affiliate, manages the fixed income and equity asset portfolios. Fees

are based on a sliding scale percentage on the value of the portfolio being managed.

- Clarion Partners, LLC.: FGI entered into an Investment Management Agreement dated October 14, 2014 and amended July 17, 2017 with Clarion Partners, LLC, a non-affiliate, to manage the investment of certain real estate assets.
- Medley SMA Advisors, LLC.: FGI entered into an Investment Management Agreement dated December 14, 2016 with Medley SMA Advisors, LLC, a non-affiliate, to manage the senior loan securities portfolio.
- Prudential Private Investors, L.P.: FGI entered into an Investment Management Agreement dated January 30, 2013, and amended June 9, 2017 with Prudential Private Investors, L.P., a non-affiliate, to manage the private placement securities portfolio.
- Wells Capital Management, Inc.: FGI entered into an Investment Management Agreement, dated March 6, 2015, with Wells Capital Management, Inc., a non-affiliate, to manage the municipal and tax-exempt securities portfolio.

Service Level Agreement: FGI was also a party to the Service Level Agreement dated November 4, 1998 with Scudder, which was replaced in 2002 by DeAM. DeAM, a non-affiliate, provided accounting and reporting services in connection with the Farmers Exchanges and their stock subsidiaries' investment portfolios, including Securities Valuation Office reporting. DeAM was given the authority to vote the proxies of the common stock. The services under this agreement are no longer provided as of 2015.

Related Party Transactions

Revolving Credit Facility Framework Agreement: Effective January 25, 2017, the Farmers Companies, all of whom are affiliate insurers within the Farmers Insurance Holding Company system, became signatories to a Revolving Credit Facility Framework Agreement (Agreement) for the purposes of eliminating the need to maintain large cash balances or unnecessarily liquidating investments during the monthly reinsurance cash settlement process among participating affiliates.

The revolving credit framework allows participating affiliates to make short term loans to each other to cover debt arising from the monthly reinsurance settlement process. The

loans, executed on an as-needed basis, mature in ninety (90) days and cannot exceed in the cumulative aggregate three percent (3%) of a borrower's or lenders admitted assets. Loans may be collateralized with a pledge of securities at lender's option, and in any event, must be collateralized if the loan crosses from one calendar year into the next calendar year such that the loan is secured and perfected as of December 31 of the year the loan was made.

Parties to the Agreement will renegotiate the terms of the Agreement at least once every three (3) years. The Agreement was approved by the California Department of Insurance on January 18, 2017, pursuant to California Insurance Code (CIC) Section 1215.5(b)(1)(A) as well as by the regulators of the domiciliary states of the FIE's affiliates outside of California. The parties to the Agreement are:

21st Century Advantage Insurance Company	21st Century Assurance Company
21st Century Casualty Company	21st Century Centennial Insurance Company
21st Century Indemnity Insurance Company	21st Century Insurance Company
21st Century National Insurance Company	21st Century North America Insurance Company
21st Century Pacific Insurance Company	21st Century Pinnacle Insurance Company
21st Century Preferred Insurance Company	21st Century Premier Insurance Company
21st Century Security Insurance Company	American Pacific Insurance Company
Bristol West Casualty Insurance Company	Bristol West Insurance Company
Bristol West Preferred Insurance Company	Civic Property and Casualty Company
Coast National Insurance Company	Exact Property and Casualty Company
Farmers Insurance Company, Inc.	Farmers Insurance Company of Arizona
Farmers Insurance of Columbus, Inc.	Farmers Insurance Company of Idaho
Farmers Insurance Company of Oregon	Farmers Insurance Company of Washington
Farmers Insurance Exchange	Farmers Insurance Hawaii, Inc.
Farmers New Century Insurance Company	Farmers Specialty Insurance Company
Farmers Texas County Mutual	Foremost County Mutual Insurance Company
Foremost Insurance Company Grand Rapids, Michigan	Foremost Lloyds of Texas
Foremost Property & Casualty Insurance Company	Foremost Signature Insurance Company
Fire Insurance Exchange	Illinois Farmers Insurance Company
Mid-Century Insurance Company	Mid-Century Insurance Company of Texas
Neighborhood Spirit Property and Casualty Company	Security National Insurance Company
Texas Farmers Insurance Company	Truck Insurance Exchange

Effective January 31, 2017, the Company entered into a promissory note pursuant to the terms of the Agreement as a borrower with the Farmers Insurance Exchange as lender for a loan in the amount of \$71.2 million. The promissory note related balance was settled within 90 days in 2017 pursuant to the terms of the underlying agreement.

The loan transaction and settlement were consistent with the terms of the Agreement and in accordance with CIC Section 1215.5(b)(1)(A).

TERRITORY AND PLAN OF OPERATION

The Company is licensed to transact insurance business in the District of Columbia and the following 48 states:

Alabama	Indiana	Nebraska	Rhode Island
Arizona	Iowa	Nevada	South Carolina
Arkansas	Kansas	New Hampshire	South Dakota
California	Kentucky	New Jersey	Tennessee
Colorado	Louisiana	New Mexico	Texas
Connecticut	Maryland	New York	Utah
Delaware	Massachusetts	North Carolina	Vermont
Florida	Michigan	North Dakota	Virginia
Georgia	Minnesota	Ohio	Washington
Hawaii	Mississippi	Oklahoma	West Virginia
Idaho	Missouri	Oregon	Wisconsin
Illinois	Montana	Pennsylvania	Wyoming

In 2017, the Company wrote \$2.9 billion of direct premiums. Of the direct premiums written, \$1.3 billion (45.8%) was written in California, \$182.3 million (6.2%) was written in Utah, \$144.0 million (4.9%) was written in Pennsylvania, \$142.3 million (4.9%) was written in Washington, \$132.3 million (4.5%) was written in Nevada, \$125.6 million (4.3%) was written in Georgia, \$122.0 million (4.2%) was written in New Jersey, and \$734.7 million (25.2%) was written in the remaining states.

The private passenger automobile liability (38.4%), automobile physical damage (23.9%), homeowners multiple perils (17.3%), and commercial multiple peril (10.8%) lines account for 90.4% of the direct writings of the Company. The Company is also a 16% participant in the Intercompany Reinsurance and Pooling Agreement (Pooling Agreement).

Farmers Insurance Exchange (FIE) and its pooled subsidiaries and affiliates write most of the property and casualty lines of business with a heavy emphasis on personal lines. The principal lines assumed by the Company from FIE (the lead insurer in the Pooling

Agreement) were private passenger automobile liability, homeowners multiple perils, and automobile physical damage.

Business is produced by an agency force of more than 48,000 agents (including nearly 13,800 exclusive agents) and is supported by 15 territory offices, 5 service operation segments, and 11,000 claims employees.

LOSS EXPERIENCE

The following schedule reflects the net underwriting and net investment results along with the net income and losses as reported by the Company in its financial statements for the years under examination and through December 31, 2018:

Year	Net Premiums Written	Net Underwriting Gains/(Losses)	Net Investment Gains/(Losses)	Net Income/(Losses)
2014	\$ 2,249,967,483	\$ (21,601,887)	\$ 80,238,138	\$ 58,864,520
2015	2,388,911,132	(50,296,511)	91,630,393	45,133,504
2016	2,361,893,877	(83,261,929)	86,240,254	28,393,973
2017	2,269,558,332	(51,495,778)	91,531,352	48,232,579
Sub-totals	\$ 9,270,330,824	\$ (206,656,105)	\$ 349,640,137	\$ 180,624,575
2018	2,214,006,049	(38,942,994)	299,816,121	284,339,019
Totals	<u>\$ 11,484,336,873</u>	<u>\$ (245,599,099)</u>	<u>\$ 649,456,258</u>	<u>\$ 464,963,594</u>

The Company reported net underwriting losses in all years under examination and through December 31, 2018. In aggregate, the Company reported \$245.6 million of net underwriting losses for the five years from 2014 through 2018. Also, as noted, the Company reported net incomes in all of the last five years.

Underwriting performance deteriorated during the intervening years subsequent to the prior examination in 2013 due to several factors, mainly because of the heightened and susceptibility to the industry-wide catastrophe losses that significantly impacted the Company's property lines. Weather and storm-related catastrophe losses added an

average of over 6.0 percentage points to the Company's overall combined ratios reported during the years subsequent to the prior examination.

Another factor for the poor underwriting performance experienced in recent years was principally the result of higher severity and frequency in non-catastrophe related activities that impacted the industry as a whole, driven primarily by loss trends in personal lines automobile, which management believes is due to higher vehicle miles traveled, distracted drivers, and an improved economy (newer cars on the road). Lower gas prices and more miles driven have also contributed to higher losses paid, along with adverse loss development in the prior accident years.

Also contributing to increased underwriting losses was the strengthening of reserves on defense and cost containment costs due to relatively higher litigation and attorney costs incurred, as well as higher adjusting and other expenses incurred to indemnify and settle claims.

Lastly, increased other expenses in 2017 partially resulting from the seed money expended to support the expansion of the Farmers brand and products to states in the eastern third of the country, including Florida and South Carolina, as well as increased advertising and other operating costs during 2017.

Net underwriting losses totaled \$38.9 million on December 31, 2018 compared to an underwriting loss of \$51.5 million in 2017, representing an underwriting loss reduction of \$12.6 million between years, primarily due to rate and underwriting actions. Net income also improved by \$236.1 million due to these actions, along with a significant increase in investment income, primarily driven by the impact of extraordinary dividends from affiliates.

As noted above, the Company has maintained its surplus as regards policyholders for the period covered by this examination primarily through net investment gains of \$349.6 million.

REINSURANCE

Intercompany Reinsurance and Pooling Agreement

The Farmers Insurance Exchange (FIE) is the lead insurer in an Intercompany Reinsurance and Pooling Agreement (Pooling Agreement) under which the Company and the insurers listed below pool their risks and obtain a proportional share of profits and/or losses of the pooled business. The Pooling Agreement became effective on January 1, 1999. Under the Pooling Agreement, business is allocated among the pool participants as follows:

<u>Pool Participant</u>	<u>Percentage</u>
Farmers Insurance Exchange (FIE)	51.75
Mid-Century Insurance Company	16.00
Truck Insurance Exchange	7.75
Fire Insurance Exchange	7.50
Farmers Insurance Company of Oregon	7.00
Farmers Insurance Company of Washington	2.00
Civic Property and Casualty Company	1.00
Exact Property and Casualty Company	1.00
Neighborhood Spirit Property and Casualty Company	1.00
Texas Farmers Insurance Company	1.00
Farmers Insurance of Columbus, Inc.	1.00
Farmers Insurance Company, Inc.	0.75
Illinois Farmers Insurance Company	0.75
Farmers New Century Insurance Company	0.75
Farmers Insurance Company of Idaho	<u>0.75</u>
Total	<u>100.00</u>

The last amendment to this long-standing Pooling Agreement was approved by the California Department of Insurance (CDI) on January 12, 1999.

Assumed

Other than a participation in the intercompany pool, the Company has no reinsurance assumed.

Ceded - Affiliated

Treaties ceding risks to affiliated reinsurers were written with FIE and all of its subsidiaries and affiliates (including the Company) as the cedents. The following is a summary of the principal affiliated ceded reinsurance treaties in-force as of December 31, 2017.

Automobile Physical Damage Reinsurance Agreement (APD Agreement): A quota share reinsurance agreement, which has been amended over the years, that covers automobile physical damage, was initially entered into on April 1, 2001, between FIE, Farmers Reinsurance Company (Farmers Re), and Zurich Insurance Company (ZIC). Under the APD Agreement, FIE, on behalf of itself and its pooling participants, cedes up to \$1 billion per year of its automobile physical damage premiums. Through December 31, 2014, the subscribing reinsurers were Farmers Re, with a 10% quota share participation, ZIC, with an 80% quota share participation and Swiss Reinsurance Company Ltd. (Swiss Re), a third-party reinsurer, assuming the remaining 10%. Effective January 1, 2015, Farmers Re reduced its quota share participation to 7.14%, ZIC decreased its participation to 64.29%, and Swiss Re increased its participation to 28.57%. The APD Agreement was not renewed in 2016 and all recoveries and prior year's business in run-off were settled in 2017.

All Lines Quota Share Reinsurance Agreement (ALQS Agreement): Effective December 31, 2002, FIE, on behalf of itself and its pooling participants, began participating in an ALQS Agreement with Farmers Re and ZIC which has been amended over the years. The ALQS Agreement covers all lines after the APD Agreement has been applied. The aggregate participation percentage was originally at 10% in 2002, and through amendments approved by the California Department of Insurance (CDI), the aggregate participation percentage and participants have varied over the years. The following are the amendments during the examination period:

- Effective December 31, 2014, the aggregate participation percentage was decreased by 6% from 20% to 14%. Farmers Re reduced its participation to 1.0% and ZIC to 9.0%. In addition to this change, Swiss Re replaced Swiss Reinsurance

America Corporation with a participation percentage of 4.0%. The CDI approved this amendment on March 26, 2015.

- Effective December 31, 2015, the aggregate participation percentage was increased by 6% from 14% to 20%. Farmers Re was removed as a participant and Transatlantic Reinsurance Company (Trans Re), and Ariel Re Bermuda Limited (Ariel Re) were added as participants at 4.0% and 1.0%, respectively. In addition, ZIC and Swiss Re changed their participation to 8% and 7%, respectively. The CDI approved this amendment on May 3, 2016.
- Effective December 31, 2016, the participation percentage was increased by 4% from 20% to 24%. In addition, Hannover Rueck SE (Hannover Re), and Catlin Reinsurance Switzerland Limited (Catlin Re) were added as new participants at 2% each. The CDI approved this amendment on September 26, 2017.
- Effective December 31, 2017, the participation percentage was increased by 5% from 24% to 29%. In addition, ZIC was removed as a participant, and Farmers Re, and Munich Reinsurance America, Inc., were added as 1% and 5% participants, respectively. In addition, Hannover Re, and Catlin Re increased their participation to 7% and 4%, respectively. The CDI approved this amendment on March 19, 2018.
- Effective December 31, 2018, Trans Re decreased its participation percentage from 4% to 3.5%, and Catlin Re increased its participation percentage from 4% to 4.5%. The overall participation remains at 29% with all other participating reinsurers' percentages remaining the same. The CDI approval of this amendment is still pending.

There are a series of 100% Equipment Breakdown Quota Share Reinsurance Agreements effective November 1, 2000, under which Zurich American Insurance Company reinsures the Company and certain of its affiliates for specified industry programs.

As of December 31, 2017, reinsurance recoverables totaled \$3.6 billion, or 334.1% of surplus as regards policyholders. All of the ceded reinsurance recoverables were attributable to the Pooling Agreement.

Ceded - Non-Affiliated

The Company, along with its parent and affiliates, were listed as cedents on various catastrophe treaties and other treaties ceding risk on an excess-of-loss basis to non-affiliated reinsurers.

ACCOUNTS AND RECORDS

California Insurance Code (CIC) Section 734 requires that every company or person from whom information is sought, and its officers, directors, employees, and agents, shall provide to the examiners appointed pursuant to this article, timely, convenient, and free access at all reasonable hours at its offices to all books, records, accounts, papers, documents, and any or all computer or other recordings relating to the property, assets, business, and affairs of the company being examined. During the course of this examination, the examiners were not provided full access to all of the information requested from the Company. It is recommended that the Company adhere to CIC Section 734 by providing full access to all books, records, accounts, papers, documents, and any or all computer or other recordings relating to the property, assets, business, and affairs of the companies being examined and implement procedures to ensure future compliance with CIC Section 734.

FINANCIAL STATEMENTS

The following financial statements are based on the statutory financial statements filed by the Company with the California Department of Insurance and present the financial condition of the Company for the period ending December 31, 2017. The accompanying comments on financial statements reflect any examination adjustments to the amounts reported in the annual statements and should be considered an integral part of the financial statements.

Statement of Financial Condition as of December 31, 2017

Underwriting and Investment Exhibit for the Year Ended December 31, 2017

Reconciliation of Surplus as Regards Policyholders
from December 31, 2013 through December 31, 2017

Statement of Financial Condition
as of December 31, 2017

<u>Assets</u>	<u>Ledger and Nonledger Assets</u>	<u>Assets Not Admitted</u>	<u>Net Admitted Assets</u>	<u>Notes</u>
Bonds	\$2,557,728,961	\$	\$ 2,557,728,961	
Common stocks	404,381,081		404,381,081	
Properties held for production of income	134,714,039		134,714,039	
Cash, cash equivalents and short-term investments	14,987,750		14,987,750	
Investment income due and accrued	20,925,852		20,925,852	
Uncollected premiums and agents' balances in course of collection	40,832,895	10,986,683	29,846,212	
Deferred premiums, agents' balances and installments booked but deferred and not yet due	409,715,079		409,715,079	
Accrued retrospective premiums	175,997		175,997	
Amounts recoverable from reinsurers	262,887,679		262,887,679	
Current federal and foreign income tax recoverable and interest thereon	225		225	
Net deferred tax asset	64,208,411	19,689	64,188,722	(1)
Guaranty funds receivable or on deposit	396,438		396,438	
Aggregate write-ins for other than invested assets	<u>41,693,191</u>	<u>88,511</u>	<u>41,604,680</u>	
 Total assets	 <u>\$3,952,647,598</u>	 <u>\$ 11,094,883</u>	 <u>\$ 3,941,552,715</u>	
 <u>Liabilities, Surplus, and Other Funds</u>				
Losses and loss adjustment expenses			\$ 1,414,193,718	(2)
Reinsurance payable on paid loss and loss adjustment expenses			146,413,516	
Other expenses			2,786,403	
Taxes, licenses and fees			11,761,630	
Unearned premiums			882,771,017	
Advance premiums			22,797,092	
Ceded reinsurance premiums payable			153,665,935	
Amounts withheld or retained by company for account of others			1,182,518	
Provision for reinsurance			15,516	
Payable to parent, subsidiaries and affiliates			175,281,872	
Payable for securities lending			7,037,576	
Aggregate write-ins for liabilities			<u>46,065,700</u>	
 Total liabilities			 2,863,972,493	
 Common capital stock		4,800,000		
Gross paid in and contributed surplus		1,639,750,000		
Unassigned funds (surplus)		<u>(566,969,778)</u>		
Surplus as regards policyholders			<u>1,077,580,222</u>	
 Total liabilities, surplus and other funds			 <u>\$3,941,552,715</u>	

Underwriting and Investment Exhibit
for the Year Ended December 31, 2017

Statement of Income

Underwriting Income

Premiums earned		\$2,323,348,390
Deductions:		
Losses incurred	\$ 1,374,601,089	
Loss adjustment expenses incurred	234,677,926	
Other underwriting expenses incurred	765,875,403	
Aggregate write-ins for underwriting deductions	<u>(310,249)</u>	
Total underwriting deductions		<u>2,374,844,169</u>
Net underwriting loss		(51,495,779)

Investment Income

Net investment income earned	\$ 82,457,872	
Net realized capital gains	<u>9,073,481</u>	
Net investment gain		91,531,353

Other Income

Net loss from agents' or premium balances charged off	\$ (13,881,594)	
Finance and service charges not included in premiums	33,404,231	
Aggregate write-ins for miscellaneous income	<u>(2,109,671)</u>	
Total other income		<u>17,412,966</u>
Net income before dividends to policyholders and before federal income taxes		57,448,540
Dividends to policyholders		107,593
Net income after dividends to policyholders but before federal income taxes		57,340,947
Federal and foreign income taxes incurred		<u>9,108,369</u>
Net income		<u>\$ 48,232,578</u>

Capital and Surplus Account

Surplus as regards policyholders, December 31, 2016		\$1,052,750,833
Net income	\$ 48,232,578	
Change in net unrealized capital gains less capital gains tax	19,579,971	
Change in net deferred income tax	(49,194,426)	
Change in nonadmitted assets	6,131,423	
Change in provision for reinsurance	136	
Aggregate write-ins for gains and losses in surplus	<u>79,707</u>	
Change in surplus as regards policyholders for the year		<u>24,829,389</u>
Surplus as regards policyholders, December 31, 2017		<u>\$1,077,580,222</u>

Reconciliation of Surplus as Regards Policyholders
from December 31, 2013 through December 31, 2017

Surplus as regards policyholders, December 31, 2013 per Examination				\$ 921,264,018
	<u>Gain in Surplus</u>	<u>Loss in Surplus</u>		
Net income	\$ 180,624,573	\$		
Change in net unrealized capital losses less capital gains tax	25,261,752			
Change in net deferred income tax		55,526,482		
Change in nonadmitted assets	7,247,009			
Change in provision for reinsurance	68,924			
Cumulative effect of changes in accounting principles		2,370,499		
Aggregate write-ins for gains and losses in surplus	<u>1,010,927</u>			
Total gains and losses	<u>\$ 214,213,185</u>	<u>\$ 57,896,981</u>		
Net increase in surplus as regards policyholders				<u>156,316,204</u>
Surplus as regards policyholders, December 31, 2017, per Examination				<u>\$1,077,580,222</u>

COMMENTS ON FINANCIAL STATEMENT ITEMS

(1) Net Deferred Tax Asset

The Tax Cuts and Jobs Act (H.R.1) was enacted into law on December 22, 2017. The Company re-valued the deferred tax assets and liabilities from a 35% corporate tax rate to the enacted 21% corporate tax rate at December 31, 2017. The re-valuation resulted in a decrease in net admitted deferred tax assets amounting to \$42.8 million and is reflected as a direct charge to surplus in the appropriate categories in the accompanying financial statements.

(2) Losses and Loss Adjustment Expenses

Since the business of the Company was pooled, it was necessary to review the losses and loss adjustment expenses on a group-wide basis. Based on an analysis by a Casualty Actuary for the California Department of Insurance, the Company's loss and loss adjustment expense reserves as of December 31, 2017 were found to be reasonably stated and have been accepted for purposes of this examination.

SUBSEQUENT EVENTS

Contribution of 21st Century Subsidiaries to the Company

On April 1, 2018, Farmers Insurance Exchange, Fire Insurance Exchange, and Truck Insurance Exchange contributed 100% of their ownership interest in their 21st Century subsidiaries to the Company. This non-cash transaction was accounted for as a reorganization and change in ownership interest in all of the 21st Century subsidiaries.

The restructuring transaction qualified for an exemption to the Form A requirements under California Insurance Code Section 1215.2(g) and the exemption was granted by the California Department of Insurance on February 27, 2018.

The following is a summary of the transfer/cost of the acquired equity for each of the acquired entities:

Acquired Entity	Transfer/Cost of Acquired Equity
21st Century North America Insurance Company and its subsidiaries	\$ 364,934,606
21st Century Assurance Company	49,764,837
21st Century Pacific Insurance Company	33,846,757
21st Centennial Insurance Company and its subsidiaries	303,797,480
Farmers Insurance of Hawaii, Inc. and its subsidiaries	61,674,560
21st Century Insurance Group and its subsidiaries	771,815,822
Totals	<u>\$ 1,585,834,062</u>

On August 1, 2018, the Company sold for cash 100% of its ownership in 21st Century Security Insurance Company to Plymouth Rock Assurance Corporation (Plymouth Rock), a Massachusetts domiciled company. The sale was approved by both the Pennsylvania and New York Departments of Insurance. Prior to this transaction, on April 1, 2018, the Company had sold the 21st Century National Insurance Company, a subsidiary of the 21st Century Security Insurance Company, to Plymouth Rock. This was also approved by the New York Department of Insurance.

Catastrophe Losses in 2018

Camp and Woolsey Fires

In November 2018, Camp and Woolsey fires had a major impact on the Farmers Insurance Group (Group). The Camp Fire was the deadliest and most destructive fire in California history. The gross loss for the Group from the Camp and Woolsey fires was \$2.1 billion, and a net loss of \$324.8 million was recorded as of December 31, 2018. Under the Intercompany Reinsurance and Pooling Agreement, the Company's participation is 16.0% of the pooled losses. As such, the Company's share of the net loss was \$51.9 million.

All Catastrophe Losses

The gross and net losses for all catastrophes in the 2018 calendar year (including the Camp and Woolsey fires) were \$3.3 billion and \$1.3 billion, respectively. The Company's share of the Group's gross and net catastrophe losses after pooling was \$531.0 million and \$211.8 million, respectively.

Dividends

In January 2019, the state of Hawaii Insurance Department approved an extraordinary cash dividend of \$70.8 million from Farmers Insurance Hawaii, Inc. to the Company. The dividend was paid on February 12, 2019.

SUMMARY OF COMMENTS AND RECOMMENDATIONS

Current Report of Examination

Accounts and Records (Page 26): It is recommended that the Company adhere to California Insurance Code (CIC) Section 734 by providing full access to all books, records, accounts, papers, documents, and any or all computer or other recordings relating to the property, assets, business, and affairs of the companies being examined and implement procedures to ensure future compliance with CIC Section 734.

Previous Report of Examination

Accounts and Records (Page 22): It was recommended that the Company continue to address the recommendations made regarding its information systems controls. The Company continues to address these recommendations.

ACKNOWLEDGMENT

Acknowledgment is made of the assistance extended by the Company's officers and employees during the course of this examination.

Respectfully submitted,

/S/ _____

Richard M. Stone, CFE
Examiner-In-Charge
Contract Insurance Examiner
Department of Insurance
State of California

/S/ _____

Grace F. Asuncion, CFE
Senior Insurance Examiner, Supervisor
Department of Insurance
State of California