

REPORT OF EXAMINATION
OF THE
COAST NATIONAL INSURANCE COMPANY
AS OF
DECEMBER 31, 2021

Insurance Commissioner

A handwritten signature in blue ink, appearing to read "D. R. [unclear]", is positioned to the right of the "Insurance Commissioner" text.

Filed on October 27, 2023

TABLE OF CONTENTS

	<u>PAGE</u>
SCOPE OF EXAMINATION	1
COMPANY HISTORY:	5
Capitalization	5
MANAGEMENT AND CONTROL:.....	5
Management Agreements.....	8
Agency Agreements.....	9
TERRITORY AND PLAN OF OPERATION.....	11
REINSURANCE:	12
Assumed.....	12
Ceded	12
ACCOUNTS AND RECORDS:.....	13
Certificate of Authority Requirements	15
Premium Tax Filing.....	16
Vehicle Fraud Assessment	16
FINANCIAL STATEMENTS:	18
Statement of Financial Condition as of December 31, 2021	19
Underwriting and Investment Exhibit for the Year Ended December 31, 2021	20
Reconciliation of Surplus as Regards to Policyholders from December 31, 2017 through December 31, 2021	21
COMMENTS ON FINANCIAL STATEMENT ITEMS:.....	22
Loss and Loss Adjustment Expenses	22
SUBSEQUENT EVENTS	22
SUMMARY OF COMMENTS AND RECOMMENDATIONS:	23
Current Report of Examination	23
Previous Report of Examination	24
ACKNOWLEDGMENT	25

Los Angeles, California
September 26, 2023

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

Dear Commissioner:

Pursuant to your instructions, an examination was made of the

COAST NATIONAL INSURANCE COMPANY

(hereinafter also referred to as the Company). The Company's statutory home 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 as of December 31, 2017. This examination covered the period from January 1, 2018 through December 31, 2021.

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 was a coordinated examination with California as the lead state of the Bristol West subgroup of the Farmers Insurance Group (Group) of companies. It was conducted concurrently with other insurance entities in the holding company group, including Security National Insurance Company, Bristol West Preferred Insurance Company, Bristol West Casualty Insurance Company, and Bristol West Insurance Company. The following states participated on the examination: Florida, Michigan, and Ohio.

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	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 Pacific Insurance Company (b)	23795	CO
Toggle Insurance Company f/k/a 21st Century Assurance Company	44245	DE
American Pacific Insurance Company, Inc.	10805	HI
Farmers Insurance Hawaii, Inc.	28487	HI
21st Century Advantage Insurance Company (c)	25232	MN
21st Century Auto Insurance Company of New Jersey (b)	10184	NJ
21st Century Pinnacle Insurance Company	10710	NJ
21st Century North America Insurance Company (a)	32220	NY
21st Century Centennial Insurance Company	34789	PA
21st Century Indemnity Insurance Company (b)	43974	PA
21st Century Premier Insurance Company	20796	PA
American Federation Insurance Company f/k/a 21st Century Insurance Company of the Southwest	10245	TX

- (a) On January 13, 2020, 21st Century Superior Insurance Company was merged into 21st Century North America Insurance Company and subsequently dissolved.
- (b) Effective January 1, 2022, 21st Century Auto Insurance Company of New Jersey, 21st Century Indemnity Insurance Company, and 21st Century Pacific Insurance Company were sold, and therefore they ceased to be part of the Farmers Holding Company system.
- (c) Effective April 1, 2023, 21st Century Advantage Insurance Company was sold and ceased to be part of the Farmers Holding Company system.

Group/Company	NAIC CoCode	Domiciled State
FARMERS WORKPLACE SOLUTIONS GROUP (f/k/a METROPOLITAN INSURANCE GROUP)		
Economy Fire & Casualty Company	22926	IL
Economy Preferred Insurance Company	38067	IL
Economy Premier Assurance Company	40649	IL
Farmers Casualty Insurance Company f/k/a Metropolitan Casualty Insurance Company	40169	RI
Farmers Direct Property and Casualty Insurance Company f/k/a Metropolitan Direct Property and Casualty Insurance Company	25321	RI
Farmers Group Property and Casualty Insurance Company f/k/a Metropolitan Group Property and Casualty Insurance Company	34339	RI
Farmers Property & Casualty Insurance Company f/k/a Metropolitan Property & Casualty Insurance Company	26298	RI
Farmers Lloyds Insurance Company of Texas f/k/a Metropolitan Lloyds Insurance Company of Texas	13938	TX

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

With the exception of the Farmers Reinsurance Company (Farmers Re), 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 (AIF) for the Farmers Insurance Exchange, Farmers Reinsurance Company operates as one of

the Farmers property and casualty companies.

COMPANY HISTORY

The Company was organized in the state of California on July 8, 1986 and commenced business on March 3, 1987. The Company is a wholly owned subsidiary of Coast National Holding Company, which in turn is wholly owned by Bristol West Holdings, Inc., a Delaware corporation, with Farmers Insurance Exchange being the ultimate controlling entity.

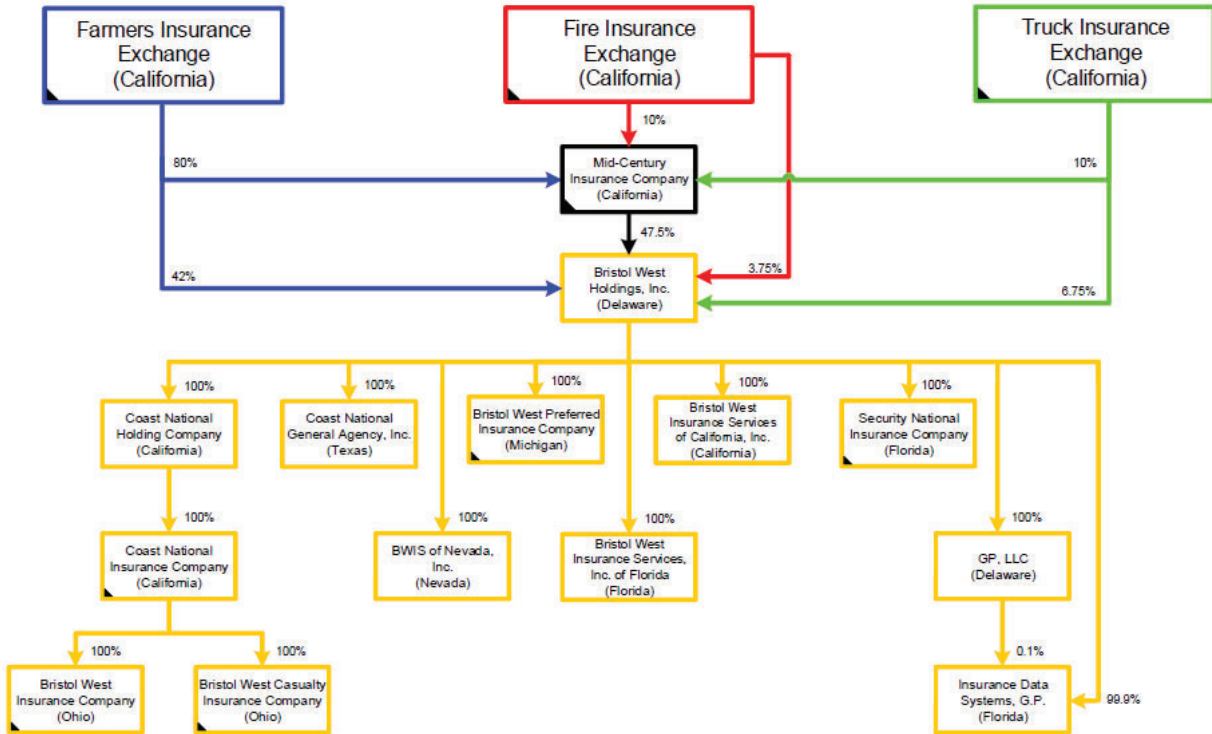
Capitalization

The Company is authorized to issue 500,000 shares of common stock with a par value of \$150 per share. As of December 31, 2021, there were 20,000 shares issued and outstanding.

MANAGEMENT AND CONTROL

The Company is a member of an insurance holding company system. The following abridged chart shows the relationships of the Company with its ultimate parents, along with its subsidiaries, and depicts the Company's relationship within the holding company system:

EXCHANGES / BRISTOL WEST GROUP



▲ - U.S. Insurance Company

Management of the Company is vested in the board of directors, which consists of not less than five but not more than fifteen -members who are elected annually. Following are members of the board and principal officers of the Company serving on December 31, 2021:

Directors

<u>Name and Location</u>	<u>Principal Business Affiliation</u>
Thomas D. Brown ^(a) Urbandale, Iowa	Owner Truck Leasing Corporation
Bronwyn E. Koopman ^(b) Aurora, Ohio	President Bristol West Insurance Group
Dennis J. Lorch ^(a) Advance, Colorado	Retired
Ronald G. Myhan ^(c) Austin, Texas	Retired
Todd M. Williams ^(a) Oviedo, Florida	Head of Claims Bristol West Insurance Group

Principal Officers

<u>Name</u>	<u>Title</u>
Bronwyn E. Koopman ^(b)	President
Maria E. Aguilera	Vice President & Treasurer
Thomas S. Noh	Vice President
Todd M. Williams	Vice President
James L. Nutting	Vice President & Actuary
Maura C. Popp	Secretary

The following changes in management occurred subsequent to the examination date:

- (a) These individuals were replaced by Angela L. DePaoli, Chau T. Do, and Al B. Reid as Directors, effective March 22, 2022. Chau T. Do was replaced by Todd M. Williams as Director, effective June 12, 2023.
- (b) Replaced by Eric E. Kappler as Director and President, effective October 1, 2022.
- (c) Replaced by Donald E. Rodriguez as Director, effective June 12, 2023.

Management Agreements

The following is a summary of the most significant management agreements in-force as of December 31, 2021:

Service Agreement: On July 1, 2015, the Farmers Insurance Exchange (FIE) and the Company entered into a Service Agreement pursuant to which FIE will provide, or arrange for the provision of, various services, including claims adjustment services, accounting and financial reporting services, investment management services, preparation of insurance policies, billing and collections, and other administrative services to the Company. FIE shall provide or arrange for the provision of services at cost. This agreement was approved by the California Department of Insurance (CDI) on December 9, 2015.

Tax Sharing Agreement: Effective September 1, 2013, the Company entered into a Tax Sharing Agreement with FIE and its various insurance and non-insurance affiliates and subsidiaries. FIE is the party primarily responsible for filing and making all tax payments on behalf of the parties to this agreement. Allocation of taxes is based upon separate return calculations, with intercompany tax balances payable or receivable being settled in amounts as if separate returns were filed. Intercompany balances are settled monthly, with the final settlement made within 30 days after the final filing date of the consolidated return. This agreement was approved by the CDI on February 18, 2014, pursuant to California Insurance Code (CIC) Section 1215.5(b)(4), as well as by the insurance departments of the domiciliary states of the affiliated parties outside of California. The Company's portion of the federal income taxes paid under the Tax Sharing Agreement for 2018, 2019, 2020, and 2021 was \$1,852,866, \$2,029,736, \$2,457,623, and \$1,860,402, respectively. The agreement was amended as of January 1, 2022 to remove certain parties that were sold and include the FWS subsidiaries.

Related Party Transactions

Revolving Credit Facility Framework Agreement: January 25, 2017, FIE and various affiliates and subsidiaries, including the Company, 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 and 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 Company's admitted assets. Loans may be collateralized with a pledge of securities at the lender's option, and in any event, must be collateralized if the loan crosses from one calendar year to 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 CDI on January 18, 2017, pursuant to 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. At December 31, 2021, the Company had no outstanding loan balance on this revolving credit facility.

On March 10, 2022, in accordance with CIC Section 1215.5(b), FIE and various affiliates and subsidiaries, including the Company, filed a Form D application with the CDI seeking approval of the Amended and Restated Revolving Credit Facility Framework agreement. Under the terms of the amended agreement, the loans, executed on an as-needed basis, mature in ninety (90) days, and cannot exceed in the cumulative aggregate the lesser of three percent (3%) of a borrower's or lenders admitted assets or twenty-five percent (25%) of a borrower's or lender's policyholder surplus. The CDI approved the agreement on March 20, 2023 pursuant to CIC Section 1215.5(b).

Agency Agreements

The following is a summary of the most significant agency agreements in-force as of December 31, 2021:

General Agency Agreement: Effective July 9, 1998 and amended and superseded as of March 25, 2014, the Company entered into a General Agency Agreement with Bristol West Insurance Services of California Inc. (Agent). The Agent acts as the Company's general agent with respect to the sale of private auto insurance policies issued by the Company in California. The Agent may enter into agreements with brokers (Producers) to produce the Company's business and shall pay commissions to the Producers pursuant to the Company's underwriting guidelines and the Company's commissions schedules. The Company may withdraw, supplement or amend any commissions schedule at any time. The Company reimburses the Agent for commissions and operating costs on a monthly basis. The amendment was approved by the CDI on November 7, 2013.

General Agency Agreement: Effective July 10, 1998 and superseded on March 25, 2014, the Company entered into a General Agency Agreement with BWIS of Nevada, Inc. (Agent). The Company authorizes the Agent to act as the general agent with respect to sales of private passenger automobile insurance policies in Nevada and Arizona. The Company reimburses the Agent for commissions and operating costs on a monthly basis. The amendment was approved by the CDI on November 7, 2013.

Agency Agreement: Effective October 6, 2021, the Company and its various insurer affiliates (Companies) entered into an Agency Agreement with Farmers General Insurance Agency, Inc. (Agent). The agreement appoints the Agent to sell, solicit, and service insurance for the Companies for the classes and lines underwritten by the Companies. Companies shall compensate the Agent in accordance with the rules established by the Companies, based on actual cost, without a profit factor built into cost, and allocated in accordance with the methods prescribed in the Statement of Statutory Accounting Principles (SSAP) 70. The agreement was non-disapproved by the CDI on September 23, 2021.

Agency Agreement: Effective December 9, 2021, the Company and various affiliates of FX Insurance Agency, LLC (Companies) entered into an Agency Agreement with FX Insurance Agency, LLC (Agent). The agreement appoints the Agent to sell, solicit, and

service insurance for the Companies for the classes and lines underwritten by the Companies. Companies shall compensate the Agent in accordance with the rules established by the Companies, based on actual cost, without a profit factor built into cost, and allocated in accordance with the methods prescribed in the SSAP 70. The agreement was non-disapproved by the CDI on November 18, 2021.

TERRITORY AND PLAN OF OPERATION

The Company writes primarily non-standard private passenger automobile liability and physical damage coverage, and began writing commercial automobile liability in August of 2019. Its business is produced through both independent and exclusive agents. The Company wrote a total of \$421.4 million of direct premiums in 2021.

As of December 31, 2021, the Company was licensed to transact multiple lines of property and casualty insurance in the states of Arizona, California, Georgia, Mississippi, Nevada, Oregon, Pennsylvania, Tennessee, and Washington. For the year ended December 31, 2021, the majority of premiums were written in the following five states:

State	Direct Written Premium	Percentage of Total
California	\$ 211,048,499	50.09%
Arizona	110,755,513	26.29%
Georgia	33,010,271	7.83%
Oregon	23,561,578	5.59%
Mississippi	14,477,945	3.44%

REINSURANCE

Assumed

Effective April 1, 2001, the Company entered into a Quota Share Reinsurance Agreement with Home State County Mutual Insurance Company (HSCM), domiciled in the state of Texas. Pursuant to this Agreement, the Company assumes one hundred percent (100%) of the HSCM business produced through Coast National General Agency, an affiliate, who acts as HSCM's managing general agent. The ceding commission paid by the Company to HSCM can range from one percent (1%) to three percent (3%) of net premiums written.

Effective as of June 1, 2010, the Company and 21st Century Premier Insurance Company and the Company entered into an Assumption Reinsurance Agreement, pursuant to which the Company assumes from 21st Century Premier Insurance Company on an assumption reinsurance basis the gross liabilities and obligations of 21st Century Premier Insurance Company under all Auto business insurance policies written by 21st Century Premier Insurance Company (excluding policies covering motorcycles or recreational vehicles) and issued in California.

Ceded

Effective July 1, 2008 and amended July 1, 2009, the Company entered into a one hundred percent (100%) Quota Share Reinsurance Agreement with Farmers Insurance Exchange (FIE), wherein the Company cedes all of its direct and assumed personal and commercial insurance to FIE. FIE is responsible for the costs associated with the issuance and administration of the policies reinsured, including claims adjustment services under the agreement. The original agreement was approved by the CDI on August 20, 2008. The amendment was consented to by the CDI on September 2, 2009.

ACCOUNTS AND RECORDS

An examination is conducted to determine the financial condition of insurance companies in accordance with the California Insurance Code (CIC) Section 700(c), 730(b), and (c) 733, 734, and prescribed accounting practices as promulgated by the National Association of Insurance Commissioners (NAIC). One must consider, among other things, the results of financial statement analyses and ratios, have open access to all the books and papers of the company, and conduct the examination in accordance with the NAIC's *Financial Condition Examiners Handbook* (Handbook), which requires the examination to evaluate the insurer's financial condition, assess corporate governance, identify current and prospective risks, and evaluate systems controls and procedures used to mitigate those risks.

During the course of the examination, the California Department of Insurance (CDI) experienced significant delays in obtaining access to various supporting documentation because the Farmers Insurance Group (Group) initially would not provide certain documentation and asserted the documentation was under the protection of the Attorney-Client Privilege (ACP), which resulted in significant delays in the progress and timing of the completion of the examination. The following is the list of compliance findings that were a result of the limitations in receiving the requested documentation:

1. 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 Group.

Furthermore, CIC Section 730(f) requires an admitted insurer to maintain all records necessary to determine its financial condition for the current year plus five previous years. Certain communication and/or documentation to support the review/testing were not maintained due to the Groups' one-year email retention policy.

It is recommended that the Company adhere to CIC Sections 734 and 730(f) 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. The documentation should be prepared in sufficient detail as to allow for a full and complete audit trail. If the maintenance of such audit trail is against the Groups' policy, then the records should be kept separately within the required maintenance period pursuant to CIC Section 730(f).

2. California Code of Regulation (CCR) Section 2309.13 and NAIC Model Audit Regulation (MAR) Section 13, Paragraph B, requires that "Every insurer required to file an audited financial report shall require the accountant to make available for review by Insurance Department examiners, all work papers prepared in the conduct of the accountant's audit and any communications related to the audit between the accountant and the insurer, at the offices of the insurer, at the Insurance Department or at any other reasonable place designated by the commissioner. The insurer shall require that the accountant retain the audit work papers and communications until the Insurance Department has filed a report on examination covering the period of the audit but no longer than seven (7) years from the date of the audit report."

In the process of authorizing the release of the external audit's audit workpapers, the Group obtained the audit workpaper index of the archived workpapers from the external auditor. The Company initially declined to consent to the release of 13 workpapers listed on the index on the basis of attorney client privilege. All but one of the 13 withheld documents were later provided. The observed process of reviewing and approving the release of the audit workpaper does not comply with CCR Section 2309.13 and MAR Section 13, paragraph B. It is recommended that the Company comply with CCR Section 2309.13 and MAR Section 13, Paragraph B and not interfere with the requirements of the external auditors to provide the state examiners with full access to the external workpapers without company involvement.

3. CIC Section 900.3 and NAIC MAR Section 15, Paragraph B–D, require an insurer or group of insurers doing business in California to establish an internal audit (IA) function to provide independent, objective, and reasonable assurance to the insurer's audit committee and management regarding the insurer's governance, risk management, and internal controls. To ensure that an internal auditor remains objective, the IA function shall be organizationally independent. Organizational independence does not preclude dual-reporting relationships. The IA function shall not defer ultimate judgment of the responsibilities or audit matters to others. Furthermore, the head of the IA function shall report to the Audit Committee regularly, but no less than annually, on the periodic audit plan, factors that may adversely impact the IA function's independence or effectiveness, material findings from completed audits, and the appropriateness of corrective actions implemented by management as a result of audit findings.

During the course of the examination, it was determined that:

(a) The IA function performs a significant number of its audits of key activities under the protection of Attorney-Client Privilege, with the audits being performed under the advisement of the legal counsel within the Office of the General Counsel (OGC);

(b) The IA Reports prepared under the advisement of the legal counsel are not shared directly with the Audit Committee but with the selected legal counsel from OGC and senior management. IA shares with the Audit Committee a summary of all audit reports concluded during the quarter; and

(c) The Internal Controls over Financial Reporting (ICFR) function, which is responsible for testing controls in compliance with MAR regulations, is not aligned under IA, but is a centralized assurance unit within the Company's Finance Department, reporting directly to the management, therefore, not an independent function despite being responsible for internal control testing.

It is recommended that the Company take necessary steps to adjust the reporting structure for both IA and ICFR to comply with the CIC Section 900.3 and MAR, Section 15, Paragraphs B-D. These steps shall include but are not limited to:

- 1) Ensure the IA function is organizationally independent, which shall directly report to the Audit Committee; however, dual reporting is allowed;
- 2) The IA function shall not defer ultimate judgment on the responsibilities or audit matters to others; the scope of the IA function shall be determined independently based on the operational needs; and
- 3) Having the ICFR function align with the IA function, whose purpose is to test controls in compliance with MAR, and report directly to the Audit Committee. Dual reporting is allowed.

Certificate of Authority Requirements

CIC Section 706.7 requires that a domestic insurer shall not enter into a contract of insurance upon the life or person of a resident of, or property or operations located in, a reciprocal state unless it is authorized pursuant to the laws of that state to transact such insurance therein. The commissioner shall, every four years, mail notice to every domestic insurer, specifying the reciprocal states.

The Company was licensed in various states outside the state of California, and many states require annual renewal of the Certificate of Authority (COA) to continue operations in the state. During the course of this examination, it was noted that there were a material number of COAs issued by states outside of California that were expired with no proof of

renewal, and several COAs that were not available for review. The oversight was a result of the frequent change of personnel and the shift in the work environment during and after the pandemic. It is recommended that the Company adhere to CIC Section 706.7 by implementing processes and procedures to obtain, track, and maintain up-to-date COAs, company name changes, and proof of payment of licensing fees.

Premium Tax Filing

Pursuant to the CDI Bulletin No. 80-6, "All payments by the insureds which are a part of the cost of insurance are premium and subject to premium tax." During the review of the premium tax return filings under the examination years, it was noted that various policy-related fees collected were not included in the 2020 and 2021 Premium Tax Returns for the Company. This resulted in an understatement of the taxable income by approximately \$2.2 million and \$2.0 million in 2020 and 2021, respectively. It is recommended that the Company amend its 2020 and 2021 premium tax returns to reflect the correct policy-related fees collected. It is further recommended that the Company take necessary action to improve procedures for quality assurance reviews of its premium tax returns for accuracy prior to filing.

Vehicle Fraud Assessment

CIC Section 1872.8 states, in part, that each insurer doing business in the state of California must pay an annual "Vehicle Fraud Assessment Fee" for each vehicle insured under an insurance policy it issues in California. The fee provides funding for the investigation and prosecution of fraudulent automobile insurance claims and automobile theft in the state of California. CCR Section 2698.62(d) requires that the Auto Assessment File (AAF) contain vehicle identification, policy number, and transaction for every vehicle for which a policy was in force for each quarter or any part thereof. The data shall be kept in a computer format for a minimum of five years after each calendar year quarter.

During the course of this examination, it was noted that the AAF provided did not reconcile with the Vehicle Fraud Assessment filings and contained duplicate Vehicle Identification

Numbers (VINs). The difference in vehicle count between the AAF and the filings were immaterial. It is recommended that the Company establish and implement procedures to ensure the filings are accurate and maintain accurate and adequate documentation to support its Vehicle Fraud Assessment filings with the CDI to comply with CCR Section 2698.62(d).

Upon being notified by the CDI of the above-mentioned violations, the Company has acknowledged the oversight and took corrective actions, although not all violations were remediated during the examination. It is recommended that the Company continue the corrective actions to ensure full compliance with the above laws and regulations.

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, 2021. The accompanying comments to the amounts reported in the annual statements should be considered an integral part of the financial statements. No adjustments were made to the financial statements.

Statement of Financial Condition as of December 31, 2021

Underwriting and Investment Exhibit for the Year Ended December 31, 2021

Reconciliation of Surplus as Regards Policyholders
from December 31, 2017 through December 31, 2021

Statement of Financial Condition
as of December 31, 2021

<u>Assets</u>	<u>Ledger and Nonledger Assets</u>	<u>Assets Not Admitted</u>	<u>Net Admitted Assets</u>	<u>Notes</u>
Bonds	\$ 441,116,652	\$	\$ 441,116,652	
Common stocks	55,214,505		55,214,505	
Cash and short-term investments	10,257,926		10,257,926	
Investment income due and accrued	2,651,806	10,256	2,641,550	
Premiums and agents' balances in course of collection	11,069,625	6,091,141	4,978,484	
Premiums, agents' balances and installments booked but deferred and not yet due	96,145,940		96,145,940	
Amount recoverable from reinsurers	28,446,736		28,446,736	
Net deferred tax asset	1,934,998		1,934,998	
Guaranty funds receivable or on deposit	10,813		10,813	
Receivable from parent, subsidiaries and affiliates	487,922		487,922	
Aggregate write-ins for other than invested assets	<u>395,716</u>		<u>395,716</u>	
Total assets	<u>\$ 647,732,639</u>	<u>\$ 6,101,397</u>	<u>\$ 641,631,241</u>	
<u>Liabilities, Surplus and Other Funds</u>				
Losses and Loss Adjustment Expenses		\$	-	(1)
Reinsurance payable on paid loss and loss adjustment expenses			126,465	
Commissions payable, contingent commissions and other similar charges			1,150,982	
Other expenses			765,754	
Taxes, licenses and fees			2,527,379	
Advance premium			1,015,777	
Ceded reinsurance premiums payable			159,401,066	
Amounts withheld or retained by company for account of others			2,951	
Payable to parent, subsidiaries and affiliates			82,049	
Aggregate write-ins for liabilities			<u>1,592,830</u>	
Total liabilities			166,665,253	
Common capital stock	\$ 3,000,000			
Gross paid-in and contributed surplus	226,278,921			
Unassigned funds (surplus)	<u>245,687,067</u>			
Surplus as regards policyholders			<u>474,965,988</u>	
Total liabilities, surplus and other funds			<u>\$ 641,631,241</u>	

Underwriting and Investment Exhibit
for the Year Ended December 31, 2021

Statement of Income

Underwriting Income

Premiums earned	\$	0
Deductions:		
Losses and loss expenses incurred	\$	(18,026)
Total underwriting deductions		(18,026)
Net underwriting gain		18,026

Investment Income

Net investment income earned	\$	10,643,586
Net realized capital gain		635,866
Net investment gain		11,279,452

Other Income

Aggregate write-ins for miscellaneous income	\$	(8,787)
Total other income		(8,787)
Net income before federal and foreign income taxes		11,288,691
Federal and foreign income taxes incurred		1,692,027
Net income	\$	9,596,664

Capital and Surplus Account

Surplus as regards policyholders, December 31, 2020	\$	469,931,177
Net income	\$	9,596,664
Change in net unrealized capital gains		(1,829,872)
Change in net deferred income tax		626,571
Change in nonadmitted assets		(3,358,551)
Change in surplus as regards policyholders for the year		5,034,811
Surplus as regards policyholders, December 31, 2021	\$	474,965,988

Reconciliation of Surplus as Regards to Policyholders
from December 31, 2017 through December 31, 2021

Surplus as regards policyholders, December 31, 2017				\$	434,782,125
		Gain in Surplus		Loss in Surplus	
		<u> </u>		<u> </u>	
Net income	\$	42,121,129	\$		
Change in net unrealized capital gains		145,593			
Change in net deferred income tax				672,880	
Change in nonadmitted assets				<u>1,409,979</u>	
Total gains and losses	\$	<u>42,266,722</u>	\$	<u>2,082,859</u>	
Net increase in surplus as regards policyholders					<u>40,183,863</u>
Surplus as regards policyholders, December 31, 2021				\$	<u>474,965,988</u>

COMMENTS ON FINANCIAL STATEMENT ITEMS

(1) Losses and Loss Adjustment Expenses

California Department of Insurance (CDI) retained Risk Regulatory Consulting, Inc. (RRC) for the purpose of assisting this examination in determining the reasonableness of the Group's loss and loss adjustment expense reserves. The analysis of the loss and loss adjustment expense reserves was performed on a group-wide basis. Based on the analysis performed by RRC and a peer review of their work by a Casualty Actuary from the CDI, the Group's reserves for losses and loss adjustment expenses were found to be reasonably stated and have been accepted for purposes of this examination.

SUBSEQUENT EVENTS

Coronavirus Pandemic (COVID-19) and Farmers Business Resumption Plan

Pursuant to the CDI Bulletin 2020-3, California Insurance Commissioner (Commissioner) requested insurance companies to provide premium credit, reduction, return of premium or other appropriate premium adjustment to the policyholders during the pandemic. In response to the request by the Commissioner, the Farmers Insurance Group had made a \$311.2 million voluntary return of premium as an adjustment to policyholder premiums in the 2020 Annual Statements.

In mid-December 2022, the California Department of Insurance (CDI) requested that Farmers Insurance Exchange, Truck Insurance Exchange, Mid-Century Insurance Company, and the Company refund additional premiums to the private passenger automobile policyholders due to changes in driving behaviors during the pandemic. The Company negotiated with the CDI and agreed to refund an additional \$2,959,715 on January 27, 2023. The other companies continue to discuss the request with the CDI.

SUMMARY OF COMMENTS AND RECOMMENDATIONS

Current Report of Examination

Accounts and Records (Page 12): It is recommended that the Company adhere to California Insurance Code (CIC) Sections 734 and 730(f) 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. The documentation should be prepared in sufficient detail as to allow for a full and complete audit trail. If the maintenance of such audit trail is against the Groups' policy, then the records should be kept separately within the required maintenance period pursuant to CIC Section 730(f).

Accounts and Records (Page 13): It is recommended that the Company comply with California Code of Regulation (CCR) Section 2309.13 and Model Audit Rule (MAR) Section 13, Paragraph B and not interfere with the requirements of the external auditors to provide the state examiners with full access to the external workpapers without company involvement.

Accounts and Records (Page 14): It is recommended that the Company take necessary steps to adjust the reporting structure for both Internal Audit (IA) and Internal Control Over Financial Reporting (ICFR) to comply with the CIC Section 900.3 and MAR, Section 15, Paragraphs B-D. These steps shall include but are not limited to:

- 1) Ensure the IA function is organizationally independent, which shall directly report to the Audit Committee; however, dual reporting is allowed;
- 2) The IA function shall not defer ultimate judgment on the responsibilities or audit matters to others; the scope of the IA function shall be determined independently based on the operational needs; and
- 3) Having the ICFR function align with the IA function, whose purpose is to test controls in compliance with MAR, and report directly to the Audit Committee. Dual reporting is allowed.

Accounts and Records – Certificate of Authority Requirements (Page 15): It is

recommended that the Companies adhere to CIC Section 706.7 by implementing processes and procedures to obtain, track, and maintain up-to-date Certificates of Authority, company name changes, and proof of payment of licensing fees.

Accounts and Records – Premium Tax Filing (Page 16): It is recommended that the Company amend its 2020 and 2021 premium tax returns to reflect the correct policies-related fees collected. It is further recommended that the Company take necessary action to improve procedures for quality assurance reviews of their premium tax returns for accuracy prior to filing.

Accounts and Records – Vehicle Fraud Assessment (Page 16): It is recommended that the Company establish and implement procedures to ensure the accuracy of the filings and maintain accurate and adequate documentation to support its filing with the California Department of Insurance to ensure future compliance with CCR Section 2698.62(d).

Previous Report of Examination

Accounts and Records (Page 10): It was recommended that the Company provide the examiners with 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 to ensure future compliance with CIC Section 734. This is a repeat finding during the current examination; however, the Company has taken actions to remediate the violation.

ACKNOWLEDGMENT

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

Respectfully submitted,

Jennifer
Danz

Digitally signed by Jennifer Danz
DN: DC=ret, DC=ram, DC=mcgladrey, OU=Field Resources, OU=Offices, OU=Farmington
c=CT, o=Users, cn=Jennifer Danz
Reason: I am the author of this document
Location:
Date: 2023.10.26 06:41:01-05'00'
Foxit PDF Editor Version: 12.1.3

Jennifer R. Danz, CFE
Examiner-In-Charge
Contractor Examiner
Department of Insurance
State of California

Fan, Vivien

Digitally signed by Fan,
Vivien
Date: 2023.10.26
11:26:22 -07'00'

Vivien Fan, CFE
Bureau Chief
Department of Insurance
State of California