

STATE OF WASHINGTON
OFFICE OF THE INSURANCE COMMISSIONER



FINANCIAL EXAMINATION
OF
FARMERS INSURANCE COMPANY OF WASHINGTON
MERCER ISLAND, WASHINGTON

NAIC CODE 21644
December 31, 2013

Order No. 15-142
Farmers Insurance Company of Washington
Exhibit A

SALUTATION

Seattle, Washington
May 22, 2015

The Honorable Mike Kreidler, Commissioner
Washington State Office of the Insurance Commissioner (OIC)
Insurance Building-Capitol Campus
302 Sid Snyder Avenue SW, Suite 200
Olympia, WA 98504

Dear Commissioner Kreidler:

In accordance with your instructions, and in compliance with the statutory requirements of RCW 48.03.010, an examination was made of the corporate affairs and financial records of

Farmers Insurance Company of Washington

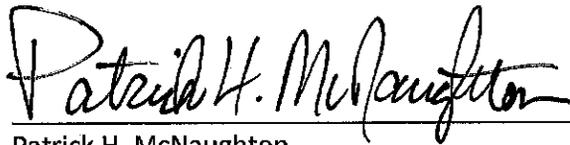
of

Mercer Island, Washington

hereinafter referred to as "FICOWA," or the "Company" at the location of its administrative office, 4680 Wilshire Boulevard, Los Angeles, CA 90010. This report is respectfully submitted showing the financial condition and related corporate matters of FICOWA as of December 31, 2013.

CHIEF EXAMINER'S AFFIDAVIT

I hereby certify I have read the attached Report of the Financial Examination of Farmers Insurance Company of Washington of Mercer Island, Washington. This report shows the financial condition and related corporate matters as of December 31, 2013.



Patrick H. McNaughton
Chief Examiner

6-26-15

Date

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SCOPE OF THE EXAMINATION

This examination covers the period January 1, 2010 through December 31, 2013 and comprises a risk focused review of the books and records of the Company. The examination followed statutory requirements contained in the Washington Administrative Code (WAC), the Revised Code of Washington (RCW), and the guidelines recommended by the National Association of Insurance Commissioners (NAIC) Financial Condition Examiners Handbook (FCEH). The examination included identification and disposition of material transactions and events occurring subsequent to the date of examination through the end of fieldwork on May 22, 2015.

Corporate records, external reference materials, and various aspects of the Company's operating procedures and financial records were reviewed and tested during the course of this examination and are commented upon in the following section of this report. In addition, the Company's Certified Public Accountant's (CPA's) work papers were reviewed and utilized, where possible, to facilitate efficiency in the examination.

This examination was performed in compliance with the 2013 NAIC FCEH which requires the examiner to consider the Company's risk management process, corporate governance structure, and control environment. The examiners utilized the information obtained during the examination to assess the Company's overall potential risks both currently and on an on-going basis, to allow the examiners to focus on the Company's greatest areas of risk, and to provide assurance on the Company's financial statements as of the examination date.

This examination was classified as a coordinated lead state examination. California was designated the lead state of the coordinated examination and examiners from the states of Washington and California participated and assessed the financial condition and corporate affairs of the Company.

INSTRUCTIONS

None

COMMENTS AND RECOMMENDATIONS

None

COMPANY PROFILE

Company History

The Company was incorporated under the laws of the state of Washington on July 14, 1970 as a stock insurer. It received its Certificate of Authority on July 28, 1970 and commenced business on October 31, 1970. The Company became a member of a holding company system on April 20, 1992 through the filing of an Insurance Holding Company System Registration Statement with the OIC. The Company has no subsidiaries.

Capitalization

Authorized capital of the Company is \$650,000 consisting of 6,500 shares of common stock with a par value of \$100. All authorized shares were issued and outstanding as of December 31, 2013. FICOWA's stock is owned by two affiliated, California domiciled insurers, as follows:

	<u>Percentage</u>	<u>Shares</u>
Fire Insurance Exchange	80 %	5,200
Truck Insurance Exchange	20	1,300
Total	<u>100 %</u>	<u>6,500</u>

The Company met the minimum capital requirements of RCW 48.05.340 with \$189,408,538 of capital and surplus as of December 31, 2013.

Territory and Plan of Operations

The Company's authorized lines of business are: property, general casualty, disability, marine and transportation, and surety. Over 93 percent of the direct business written by FICOWA was private passenger auto liability, auto physical damage, and homeowners multiple peril insurance. Sales operations of the Company are conducted through agents who are appointed as independent contractors to represent the Company.

Growth of Company

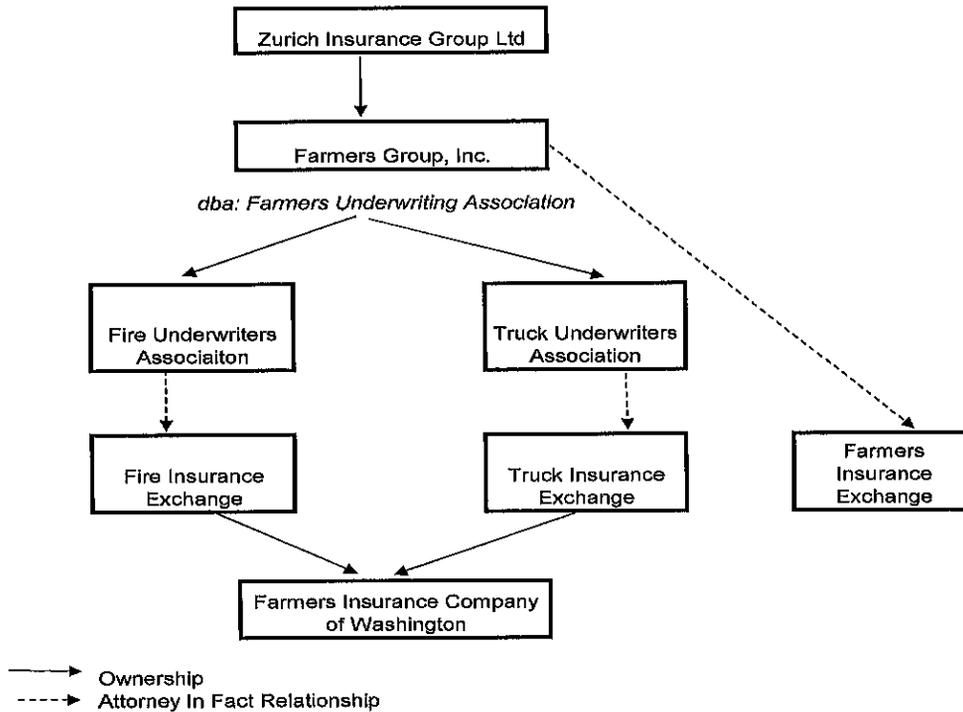
The following reflects the Company's growth as reported in its filed NAIC Annual Statements for the four year period under examination:

<u>Year</u>	<u>Admitted Assets</u>	<u>Liabilities</u>	<u>Capital & Surplus</u>	
2013	\$513,809,994	\$324,401,456	\$189,408,538	
2012	511,379,141	329,637,825	181,741,316	
2011	514,737,104	338,228,695	176,508,409	
2010	523,333,252	343,952,349	179,380,903	

<u>Year</u>	<u>Premium Earned</u>	<u>Net Underwriting Gain (Loss)</u>	<u>Net Investment Gain (Loss)</u>	<u>Net Income (Loss)</u>
2013	\$274,488,609	(\$3,802,665)	\$12,586,082	\$7,537,928
2012	273,457,183	(11,870,639)	14,124,674	4,542,515
2011	290,868,913	(21,885,963)	15,145,691	(1,533,077)
2010	213,168,914	(12,256,016)	13,503,755	(3,553,163)

Affiliated Companies

The Company is a member of the Farmers Property and Casualty companies (Farmers P&C companies), headquartered in Los Angeles, California. The Farmers P&C companies are comprised of Farmers Insurance Exchange (FIE), Fire Insurance Exchange (FIRE), Truck Insurance Exchange (TRUCK), their respective insurance subsidiaries, and several other insurers that are controlled by Farmers Group, Inc. (FGI). The Company is directly controlled by FIRE, which owns 80 percent of the Company's outstanding common stock. TRUCK owns the remaining 20 percent of the Company's common stock.



Zurich Insurance Group Ltd (formerly known as Zurich Financial Services Ltd), a Swiss holding corporation that was incorporated on April 26, 2000, is listed on the SIX Swiss Exchange.

Farmers Group, Inc. (FGI) (dba Farmers Underwriters Association), is a wholly owned subsidiary of the Zurich Insurance Group Ltd. FGI and its subsidiaries, Truck Underwriters Association and Fire Underwriters Association, provide certain administrative services for Farmers Insurance Exchange, Fire Insurance Exchange, and Truck Insurance Exchange (Exchanges) as the Exchanges’ attorneys-in-fact.

Farmers Insurance Exchange, Fire Insurance Exchange, and Truck Insurance Exchange are inter-insurance exchanges owned by their policyholders and organized under the laws of the state of California. The Exchanges, directly or through their subsidiaries, offer homeowners insurance, auto insurance, commercial insurance, and financial services throughout the United States.

The Exchanges do not hold an ownership interest in FGI, and FGI does not hold an ownership interest in the Exchanges.

Intercompany Agreements

The Company was a party to the following intercompany agreements, which were in force as of December 31, 2013 and were in compliance with the NAIC Statements of Statutory Accounting Principles (SSAP) No. 70:

Reinsurance Assumption Agreement

Under the 100 percent Reinsurance Assumption Agreement dated October 1, 1970 between FICOWA and FIE, all of the business written by FICOWA is ceded to FIE. For the year ending December 31, 2013, FICOWA

ceded to FIE \$412,253,000 in premiums written, \$416,540,000 in premiums earned, and \$229,350,000 in losses incurred.

Tax Sharing Agreement

Effective September 30, 2008, FICOWA entered into the Tax Sharing Agreement with affiliated, California-domiciled insurers FIRE, Civic Property and Casualty Company (Civic), Exact Property and Casualty Company (Exact), and Neighborhood Spirit Property and Casualty Company (Neighborhood). The agreement specifies the method by which the consolidated FIRE tax liability is allocated to subsidiaries FICOWA, Civic, Exact, and Neighborhood, respectively, in accordance with the Internal Revenue Code. The agreement also stipulates that FIRE calculates the tax liability under this agreement and the other agreement parties reimburse FIRE for the amount of tax liability due. The Tax Sharing Agreement replaced the May 1, 1995 Tax Sharing Agreement between FICOWA and FIRE. Under this current Tax Sharing Agreement, FICOWA remitted \$2,897,000 to FIRE in 2013.

1999 Inter-Company Reinsurance Agreement

Under this agreement, FIE is the lead insurer in the 1999 Inter-Company Reinsurance Agreement under which FICOWA and its affiliated insurers pool their risks and obtain a proportional share of profits and/or losses of the pooled business (i.e., the business is allocated among the pool participants). This 1999 Inter-Company Reinsurance Agreement became effective on January 1, 1999, and superseded the previously issued reinsurance pooling agreement entered into on December 31, 1985. (See page 6, Reinsurance, for a list of the participating companies.)

For the year 2013, FICOWA assumed \$272,738,000 in premiums written, \$274,489,000 in premiums earned, and \$155,940,000 in losses incurred, based on its pooling percentage of two percent under the 1999 Inter-Company Reinsurance Agreement.

Service Agreement

On March 1, 2010, FIE and FICOWA entered into the Service Agreement pursuant to which FIE will provide 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 FICOWA.

MANAGEMENT AND CONTROL

Board of Directors (BOD)

Directors as of December 31, 2013:

Kenneth Bentley
Dale Marlin
Peter Kaplan
Ronald Myhan
David Louie
Donald Rodriguez

Officers

Officers as of December 31, 2013:

Larry Pratt	President
Doren Hohl	Secretary
Ronald Myhan	Vice President, Treasurer
Bryan Murphy	Vice President
Karyn Williams	Vice President
James Nutting	Vice President
Jeffrey Sauls	Vice President

Conflict of Interest

The Company requires its officers and directors to complete a conflict of interest statement annually. All disclosures were reviewed and discussed by the BOD. No exceptions were noted in our review.

Fidelity Bond and Other Insurance

The Company, along with other members of the Farmers P&C companies, maintains a financial institution bond coverage that meets the amount suggested by NAIC guidelines. FICOWA is also listed as a named insured on various insurance policies to cover risks in the normal course of business.

Officers', Employees', and Agents' Welfare and Pension Plans

The Company does not have any direct employees, so FICOWA does not have any direct obligations for retirement plans, deferred compensation, or post employment benefits.

CORPORATE RECORDS

The Company's Articles of Incorporation, Bylaws, Certificates of Authority, and meeting minutes of the BOD and its committees were reviewed for the period under examination. All BOD meetings were conducted with a quorum present. Investment purchases, transfers, and disposals were ratified by the BOD and noted in the minutes.

UNPAID LOSSES AND LOSS ADJUSTMENT RESERVES

<u>Year</u>	<u>Losses</u>	<u>Loss Adjustment Expenses</u>
2013	\$124,492,697	\$34,474,021
2012	129,982,349	34,897,299
2011	126,332,895	35,934,853
2010	110,962,772	33,287,558

As shown above, the reserves carried by the Company for unpaid losses and loss adjustment expenses were \$124,792,697 and \$34,474,021, respectively, as of December 31, 2013.

The actuarial consulting firm contracted by the California Department of Insurance (CADOI), American Actuarial Consulting Group, LLC (AACG), reviewed the unpaid losses and loss adjustment expense reserves of the Farmers Insurance Exchange Pool (FIE Pool), which includes FICOWA, and concluded that the reserves for the insurance companies in the FIE Pool were within a range of reasonable estimates. Therefore, the Company's loss and loss adjustment expense reserves were accepted as reasonable and no adjustments were proposed to the amounts reported in the Company's 2013 NAIC Annual Statement. Furthermore, the CADOI actuary reviewed the actuarial work performed by AACG and concluded that the pooled loss and loss adjustment expense reserves, for all members of the FIE Pool, were within a reasonable range as of December 31, 2013.

REINSURANCE

In accordance with the 1970 Reinsurance Assumption Agreement, FICOWA cedes 100 percent of its business to FIE, and in accordance with the 1999 Inter-Company Reinsurance Agreement, FIE retrocedes to FICOWA its two percent pool participation percentage. As of December 31, 2013, the Company had \$21,706,283 in aggregate unsecured amounts recoverable from FIE.

Under the above agreements, the Company shares its liabilities with all other members of the FIE Pool. Therefore, it is substantially protected from its own unique exposures, but is also exposed to a portion of those from the other pooled companies. Although FIE has various reinsurance agreements with outside reinsurers and its affiliates, the Company is not party to any other reinsurance agreements on a direct basis.

The Farmers P&C companies that participated in the 1999 Inter-Company Reinsurance Agreement and their respective percentages of participation as of December 31, 2013 were:

<u>Company Name</u>	<u>Pooling Percentage</u>
Farmers Insurance Exchange	51.75%
Truck Insurance Exchange	7.75
Fire Insurance Exchange	7.50
Mid-Century Insurance Company	16.00
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
Farmers Insurance of Columbus, Inc.	1.00
Neighborhood Spirit Property and Casualty Company	1.00
Texas Farmers Insurance Company	1.00
Farmers Insurance Company of Idaho	0.75
Farmers Insurance Company, Inc.	0.75
Farmers New Century Insurance Company	0.75
Illinois Farmers Insurance Company	0.75
Total	100.00%

Reinsurance agreements were reviewed and found to be in compliance with Washington State reinsurance statutes. The reinsurers were properly classified in Schedule F of the Company's 2013 NAIC Annual Statement. The Company has controls in place to monitor its reinsurance program including the financial condition of the reinsurers.

STATUTORY DEPOSITS

The Company maintained no statutory deposits during the examination period.

ACCOUNTING RECORDS AND INFORMATION SYSTEMS

The Company maintains its accounting records on a Statutory Accounting Principles (SAP) basis and is audited annually by the certified public accounting firm of PricewaterhouseCoopers (PwC). The Company received an unqualified opinion for all years under review. The Company's accounting procedures, internal controls, and transaction cycles were reviewed during the planning and testing phase of the examination and no exceptions were noted.

CADOI contracted Ernst & Young (E&Y) to review the Company's Information Technology (IT) environment during the planning and testing phase of the examination, focusing on the following Control Objectives for Information and related Technology (COBIT) Framework domains:

- Plan and Organize
- Acquire and Implement
- Deliver and Support
- Monitor and Evaluate

For purposes of the examination of FICOWA, the examiners relied upon the review and summary reports of the E&Y review as of December 31, 2013. The IT system and controls were evaluated to gain an understanding of the IT general control risks and assess the effectiveness of these controls to determine if appropriate mitigating and internal controls have been implemented. Appropriate mitigating and internal controls have been implemented to reduce residual risk to appropriate levels. The Company has an effective Business Continuity Plan and Disaster Recovery Plan, which have been tested on a regular basis and includes the availability of an alternate site.

SUBSEQUENT EVENTS

Effective December 15, 2014, FICOWA's BOD appointed Kimberly Cummins as the Company's President, replacing Larry Pratt who left the Company in September 2014.

There were no additional material events impacting the Company between the examination date and the last day of our fieldwork.

FINANCIAL STATEMENTS

The following financial statements show the financial condition of Farmers Insurance Company of Washington as of December 31, 2013:

Assets, Liabilities, Surplus and Other Funds
Statement of Income and Capital and Surplus Account
Four Year Reconciliation of Surplus

Farmers Insurance Company of Washington
Assets, Liabilities, Surplus and Other Funds
December 31, 2013

	<u>Balance Per Company</u>	<u>Examination Adjustments</u>	<u>Balance Per Examination</u>
Assets			
Bonds	\$424,671,267	\$0	\$424,671,267
Cash, cash equivalents, and short-term investments	135,454		135,454
Derivatives	4,849		4,849
Subtotals, cash and invested assets	424,811,570	0	424,811,570
Investment income due and accrued	3,217,343		3,217,343
Premiums and considerations:			
Uncollected premiums and agents' balances in the course of collection	4,584,359		4,584,359
Deferred premiums, agents' balances and installments booked but deferred and not yet due	40,715,634		40,715,634
Accrued retrospective premiums	47,822		47,822
Amounts recoverable from reinsurers	21,706,283		21,706,283
Net deferred tax asset	14,306,979		14,306,979
Receivables from parent, subsidiaries and affiliates	1,909,827		1,909,827
Aggregate write-ins for other than invested assets	2,510,177		2,510,177
Total Assets	\$513,809,994	\$0	\$513,809,994
Liabilities, Surplus and Other Funds			
Losses	\$124,492,697	\$0	\$124,492,697
Reinsurance payable on paid losses and loss adjustment expenses	16,290,561		16,290,561
Loss adjustment expenses	34,474,021		34,474,021
Other expenses	204,394		204,394
Taxes, licenses and fees	291,424		291,424
Unearned premiums	119,943,943		119,943,943
Advance premium	2,958,474		2,958,474
Dividends declared and unpaid - Policyholders	61,531		61,531
Ceded reinsurance premiums payable	21,454,061		21,454,061
Aggregate write-ins for liabilities	4,230,350		4,230,350
Total Liabilities	324,401,456	0	324,401,456
Aggregate write-ins for special surplus funds	1,571,128		1,571,128
Common capital stock	650,000		650,000
Gross paid in and contributed surplus	143,223,500		143,223,500
Unassigned funds (surplus)	43,963,910		43,963,910
Surplus as regards policyholders	189,408,538	0	189,408,538
Total Liabilities, Surplus and Other Funds	\$513,809,994	\$0	\$513,809,994

Farmers Insurance Company of Washington
Statement of Income and Capital and Surplus Account
For the Year Ended December 31, 2013

	<u>Balance Per Company</u>	<u>Examination Adjustments</u>	<u>Balance Per Examination</u>
Underwriting Income			
Premiums earned	\$274,488,609	\$0	\$274,488,609
Deductions			
Losses incurred	155,939,848		155,939,848
Loss adjustment expenses incurred	27,603,147		27,603,147
Other underwriting expenses Incurred	94,748,279		94,748,279
Total underwriting deductions	<u>278,291,274</u>	<u>0</u>	<u>278,291,274</u>
Net underwriting gain (loss)	<u>(3,802,665)</u>	<u>0</u>	<u>(3,802,665)</u>
Investment Income			
Net investment income earned	12,549,214		12,549,214
Net realized capital gains (losses)	36,868		36,868
Net investment gain (loss)	<u>12,586,082</u>	<u>0</u>	<u>12,586,082</u>
Other Income			
Net gain (loss) from agents' or premium balances charged off	(2,105,395)		(2,105,395)
Finance and service charges not included in premiums	4,745,537		4,745,537
Aggregate write-ins for miscellaneous income	(1,018,335)		(1,018,335)
Total other income	<u>1,621,807</u>	<u>0</u>	<u>1,621,807</u>
Net income before dividends to policyholders, after capital gains tax and before all other federal and foreign income taxes	10,405,224		10,405,224
Dividends to policyholders	19,388		19,388
Net income	<u>\$10,385,836</u>	<u>\$0</u>	<u>\$10,385,836</u>
Net income, after dividends to policyholders, after capital gains tax and before all other federal and foreign income taxes	10,385,836		10,385,836
Federal and foreign income taxes incurred	2,847,908		2,847,908
Net income	<u>\$7,537,928</u>	<u>\$0</u>	<u>\$7,537,928</u>
Capital and Surplus Account			
Surplus as regards policyholders, December 31 prior year	<u>\$181,741,316</u>	<u>\$0</u>	<u>\$181,741,316</u>
Net income	7,537,928		7,537,928
Change in net unrealized capital gains or (losses)	8,149		8,149
Change in net deferred income tax	(325,355)		(325,355)
Change in net deferred income tax	463,653		463,653
Aggregate write-ins for gains and losses in surplus	(17,153)		(17,153)
Change in surplus as regards policyholders for the year	<u>7,667,222</u>	<u>0</u>	<u>7,667,222</u>
Surplus as regards policyholders, December 31 current year	<u>\$189,408,538</u>	<u>\$0</u>	<u>\$189,408,538</u>

Farmers Insurance Company of Washington
Four Year Reconciliation of Surplus
For the Years Ended December 31,

	<u>2013</u>	<u>2012</u>	<u>2011</u>	<u>2010</u>
Capital and Surplus, December 31, prior year	<u>\$181,741,316</u>	<u>\$176,508,409</u>	<u>\$179,380,903</u>	<u>\$176,974,124</u>
Net Income (loss)	7,537,928	4,542,515	(1,533,077)	(3,553,163)
Change in net unrealized capital gains (losses)	8,149	574,449	3,235	1,179,554
Changes in net deferred income tax	(325,355)	925,850	(1,603,453)	1,745,290
Change in nonadmitted assets	463,653	(862,324)	390,270	1,269,413
Aggregate write-ins for gains and losses in surplus	(17,153)	52,417	(129,469)	1,765,685
Change in surplus as regards policyholders for the year	<u>7,667,222</u>	<u>5,232,907</u>	<u>(2,872,494)</u>	<u>2,406,779</u>
Capital and Surplus, December 31, current year	<u><u>\$189,408,538</u></u>	<u><u>\$181,741,316</u></u>	<u><u>\$176,508,409</u></u>	<u><u>\$179,380,903</u></u>

NOTES TO THE FINANCIAL STATEMENTS

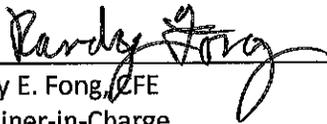
The Company has no special consents, permitted practices, or orders from the state of Washington.

ACKNOWLEDGMENT

Acknowledgment is hereby made of the cooperation extended to the examiners by the officers and employees of Farmers Insurance Company of Washington and its affiliates during the course of this examination.

In addition to the undersigned, Michael V. Jordan, CPA, CFE, MHP, Assistant Chief Examiner; Timothy F. Hays, CPA, JD, Investment Specialist; Tarik Subbagh, MSBA, CPA, CFE, Property and Casualty Field Supervising Examiner, all from the Washington State Office of the Insurance Commissioner, and examiners representing the California Department of Insurance, participated in the examination and in the preparation of this report.

Respectfully submitted,



Randy E. Fong, CFE
Examiner-in-Charge
State of Washington

