MARKET CONDUCT EXAMINATION REPORT
OF

FARMERS HOME MUTUAL INSURANCE COMPANY (NAIC # 13846) AND WESTERN HOME INSURANCE COMPANY (NAIC # 26395)

RICHFIELD, MINNESOTA

STATE OF CALIFORNIA

DEPARTMENT OF INSURANCE

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CONFIDENTIALTY STATEMENT

The Market Conduct Examination Report contained herein, including any addendum hereto, is CONFIDENTIAL unless and until the Insurance Commissioner by the authority vested in him or her pursuant to Section 735.5 of the California Insurance Code, determines otherwise.

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INTRODUCTION

This report developed by the Market Conduct examiners is a report written, in general, by exception. In addition to general information, the report contains specifics concerning the categories of claims examined and the details of noncompliant or problematic activities discovered during the course of the examination. Findings as respects claim files reviewed which did not reflect deficiencies were omitted. All unacceptable or noncompliant activities may not have been discovered, however, and failure to identify, comment on, or criticize activities does not constitute acceptance of such activities.

AUTHORITY

This Market Conduct Examination of Farmers Home Mutual and Western Home Insurance Company (hereinafter referred to as FHM or WH respectively, or "the Companies" or FHG) was conducted pursuant to the authority granted under Part 2, Chapter 1, Article 4, Sections 730, 733, 736 and Article 6.5, Section 790.04 of the California Insurance Code; and Title 10, Chapter 5, Subchapter 7.5, Section 2695.3 (a) of the California Code of Regulations.

DURATION OF EXAMINATION

This examination was conducted on-site from March 2 through May 15, 1998 and continued off site periodically through November 23, 1998. The non-litigated claims examination was conducted at the Companies local branch claims office located at 3021 West Magnolia Boulevard, Burbank, California 91510. The litigated claims examination was primarily conducted at the California Department of Insurance offices located at 45 Fremont Street, San Francisco, CA 94133.

PURPOSE OF EXAMINATION

This examination was conducted for the purpose of evaluating the Companies' compliance with

contractual obligations, its own procedures, the California Insurance Code, the Unfair Claims Settlement Practices Regulations, Fair Claims Practices Regulations as applicable, applicable case law, and other applicable legal requirements.

This examination was conducted to review claim handling practices as respects to claims presented for losses incurred as a result of the California earthquake of January 17, 1994, also known as the Northridge Earthquake.

Concurrently, a re-examination of WH was conducted to review certain non-earthquake claims to determine whether the recommendations made in the prior report of examination of 1995 had been adopted.

COMPANY PROFILE

The FHM company was incorporated under the laws of Minnesota on January 12, 1898 and began business on March 1, 1898. WH was created as a subsidiary of FHM in 1973. The Companies each conduct more than 30% of their business in California. The Companies are licensed in California, Nevada, Washington, Oregon, Arizona, Utah, Minnesota, North Dakota and South Dakota.

According to the 1996 edition of Best's Insurance Reports - Property/Casualty, California ranks first as a source of direct premium writings, by state, for each Company.

Year	Company	All Lines Total Direct Premium	All Lines California Premium	Percentage of Written Premium
1996	FHM	$24,637,000	$8,199,000.00	33.3%
1996	WH	32,654,000	12,326,000.00	37.7%

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A copy of the "Best" report is attached as Exhibit I-1.

NORTHRIDGE CLAIMS PROCEDURES

The examiners requested that FHG provide a description of the procedures adopted and the actions taken to address the needs of its policyholders affected by the Northridge earthquake. The Companies advised that they handled approximately 1600 earthquake claims. The branch office in Burbank, California was granted settlement authority to a maximum of [illegible] and could also deny claims below the deductible. Claims in which there was a determination that payments would exceed $[illegible] were referred to the home office in Minnesota. In Minnesota, three examiners reviewed, monitored, and decided issues relative to the determination of the amount of damages to be paid, the extent of construction necessary, the need for expert inspections/appraisals, interpretation of coverage, code upgrades, and asbestos removal. Normally, the home office examiner worked with the branch office to hire an independent adjusting firm. FHG required that these independent adjusters provide reports to the home office in Minnesota prior to receiving authority to pay claims. The examiners were advised that these procedures were not significantly different from those that were used under normal circumstances for non-earthquake claims.

SCOPE OF THE EXAMINATION

The examiners reviewed a total of 413 files drawn from various populations of Northridge earthquake claims in addition to 80 non- earthquake files reviewed during the re-examination of WH. Representative samples were selected as follows:

WESTERN HOME MUTUAL

CLOSED EQ CLAIMS

Category	Population	Sample
Homeowners/EQ Paid	523	70
Homeowners/EQ CWP	290	62
Dwelling Fire/EQ/Paid	72	38
Dwelling Fire/EQ/CWP	90	43
Homeowners/Paid (EQ Related)	9	9
Homeowners/CWP (EQ Related)	3	3
OPEN EQ CLAIMS		
All EQ related claims open as 10-1-97 (Except files in litigation)	86	7
Sub-total	1073	232

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WH RE-EXAMINATION

EXCLUDING NORTHRIDGE EARTHQUAKE CLAIMS

NON-EQ CLOSED CLAIMS

Category	Population	Sample
Homeowners/Paid	74	32
Homeowners/CWP	27	24
Dwelling Fire/Paid	9	9
Dwelling Fire/CWP	5	5
3RD Party Liability Paid	5	5
3RD Party Liability CWP	5	5
Sub-total	125	80
Total	2094	493

Actual file selection was accomplished through the Market Conduct Bureau's automated random sampling program.

The Population of open claims originally identified by the Companies at the time the examination was scheduled was different from that found at the examination site. Many of these open claims had been settled or were in the process of being settled by the time the on-site examination commenced. The examiners adjusted the sample to reflect the decrease in the number of open files as reported by FHG.

Additionally, California Department of Insurance legal staff reviewed litigated files and the findings of this review will be reported under separate cover.

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GLOSSARY

For the purpose of this examination, and particularly within the context of discussions in the Findings section of this report, the following terms are defined:

ALE: Additional Living Expense

CDI: California Department of Insurance

CIC: California Insurance Code

CWP: Closed Without Payment

Delay: Claims handling must reflect compliance with standards of timeliness contained in the Unfair Claims Settlement Practices Regulations. Specified types of processing transactions enumerated in the Regulations (e.g., acknowledgment and payment) are to be handled immediately, but in no event beyond the maximum number of days specified in the CIC Code and/or Regulations.

EQ: Earthquake

Error: Any violation or act of noncompliance with the UCP and/or FCP Regulations or 790.03(h); or violation or act of noncompliance or act prohibited by the CIC.

Examiners: CDI/Consumer Services Division/ Legal Division personnel

Faulty Documentation: Absence of billings, drafts, letters, diary notes, date stamps and other essential information substantiating the handling or disposition of the claim; the inclusion of material not related to the file; the misdirection of correspondence (including form letters) to parties involved in the settlement process; the failure to fully comply with existing CDI regulatory requirements

pertaining to documentation.

HO: Home Owners

Improper Settlement: Any questionable practice employed to deny or limit coverage; the failure to investigate claims; the failure to defend and/or indemnify the insured; the failure to apply consistent standards and procedures; payment inaccuracies; the failure to comply with all applicable GDI Regulations regarding full disclosure of benefits, coverages, time limits or other policy provisions.

SDA: Structural Damage Appraiser.

TLEA: Temporary Living Expense Allowance

UCP Regulation(s): Unfair Claims Settlement Practices Regulations, of the California Code of Regulations, Title 20, Chapter 5, Subchapter 7.5, effective prior to May 10, 1997.

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EXECUTIVE SUMMARY

(OVERVIEW OF CLAIM FINDINGS)

As indicated in the Scope of the Examination section, the **Market Conduct staff** examiners **reviewed a total of 413 non-litigated EQ claim files in which 483 claims handling violations of the UCP Regulations and/or CIC were identified within 187 files.** Errors detected involve deficiencies noted across EQ sample lines, however a significant number of errors occurred in the "Paid and Open Homeowners EQ and Fire Dwelling" samples. Specifically, the errors indicative of improper claims handling include: inadequate investigation and incorrect estimating of claimants' damages; unsupported depreciation reductions; failure to explain settlement reductions; and failure to clearly explain policy provisions to insureds. Also, while not cited as specific errors, the examiners noted the following: the Companies depreciated the cost of labor; failed to include general contractors' overhead and profit in ACV settlements; and were inconsistent when handling ITEA depreciation on collectibles, and overhead and profit.

Additionally, the examiners reviewed 80 non-EQ claims during the re-examination of WH. The findings include 10 claims handling violations of the FCP Regulations and/or CIC within 10 files.

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While specific citations are listed in both the **Specific Findings** section of this report, the following is a statistical overview:

Category	No. Of Files	No. Of Files with Citations	No. Of Citations
FHM & WH EQ Claims			
HO EQ Paid	130	94	280
HO EQ CWP	119	24	37
Dwelling Fire EQ Paid	63	43	114
Dwelling Fire EQ CWP	67	13	21
Homeowners Paid	11	3	1
Homeowners CWP	6	0	0
EQ Open	17	10	30
Total EQ	413	187	483
WH Re-Exam - Non EQ Claims			
Homeowners Paid	32	6	7
Homeowners CWP	24	2	1
Dwelling Fire Paid	9	2	2
Dwelling Fire CWP	5	2	0
3rd Party Liability Paid	5	0	0
3rd Party Liability CWP	5	0	0
Total Re-exam Non EQ	80	10	10
Total	493	197	493

PRELIMINARY

The following is an overview of non-litigated file citations:

TABLE OF TOTAL CITATIONS				
	CIC or UCP/FCP Description	Farmers Home Mutual Insurance Company	Western Mutual Insurance Company	Western Mutual Re-Examination
2695.3(a) & 790.03(h)(3) & 790.03(h)(5)	Unsupported Depreciation Reduction.	33	30	2
2695.4(a) & 790.03(h)(1) & 790.03(h)(3)	Failure to explain settlement reductions.	25	32	0
2695.6(a) and/or 2695.5(e)(3) & 790.03(h)(3) 790.03(h)(5)	Company failed to perform necessary and proper investigation. Inadequate or incorrect initial inspections.	42	49	1
2695.7(g) & 790.03(h)(5)	Low Settlement	32	21	0
2695.7(g) & 790.03(h)(3) & 790.03(h)(5) & 790.03(h)(12)	Low Settlement. Company failed to settle claims promptly under one portion of the insurance policy in order to influence settlements under other portions. Payment for personal contents included in the ACV amount, and not issued as a separate check.	7	6	0
2695.3(a) & 790.03(h)(3)	General Documentation Error. Claim file did not contain all documents, notes and work papers.	14	26	2
2695.7(h) & 790.03(h)(5)	Company did not tender payment within 30 days of accepting claim	8	18	3
2695.4(a) & 790.03(h)(1)	Communication did not clearly explain policy provisions, benefits and facts.	6	10	0
790.03(h)(6)	Compelling insured to instigate litigation	4	1	0
2695.4(c)(1) & 790.03(h)(13)	Company cannot deny a claim on the basis of the claimant's failure to exhibit property	1	0	0
2695.5(a) & 790.03(h)(2) & 790.03(h)(3)	Company failed to acknowledge notice of claim immediately, but in no case later than 15 calendar days.	0	1	0
2695.5(b) & 790.03(h)(3)	Agent failed to immediately transmit notice of claim to the insurer.	0	1	0

TABLE OF TOTAL CITATIONS				
	CIC or UCP/FCP Description	Farmers Home Mutual Insurance Company	Western Mutual Insurance Company	Western Mutual Re-Examination
2695.5(f) and/or 2695.5(a) & 790.03(h)(2) & 790.03(h)(3)	The Company did not respond to CDI communication within 21 days.	15	22	2
2695.5(g) & 790.03(h)(2) & 790.03(h)(3)	The Company did not respond to communication within 15 days.	4	4	0
2695.5(h) & 790.03(h)(3)	The Company failed to provide reasonable assistance, instructions, and/or claim forms.	1	0	0
2695.7(a) & 790.03(h)(3)	No insurer shall discriminate in its claims settlement practices	1	0	0
2695.7(b) & 790.03(h)(4)	Company did not accept or deny within 40 calendar days.	2	1	0
2695.7(b)(1) & 790.03(h)(3)	Factual basis for denial not stated in writing.	1	5	0
2695.7(b)(3) & 790.03(h)(3)	Company did not notify the claimant that the claim may be reviewed by the CDI.	5	8	0
2695.7(c)(1) & 790.03(h)(3)	Company did not notify the claimant additional time was needed to investigate claim	7	9	0
2695.7(d) & 790.03(h)(3) & 790.03(h)(5)	Company sought information not reasonably required for, or material to, the resolution of the claim.	3	3	1
2695.3(b)(2) & 790.03(h)(3)	Company failed to record date relevant document received	3	3	0
2695.6(a) & 790.03(h)(3)	Company failed to begin investigation within 15 days	0	1	0
790.03(h)(3)	Failing to adopt and implement reasonable standards for the prompt investigation and processing of claims.	0	2	0
790.03(h)(5)	Failing to effectuate fair and equitable payment.	1	2	0
880	Every insurer shall conduct it business in this State in its own name.	2	8	0
1871.2	Release forms do not contain the fraud wording prescribed by the Insurance Code.	0	2	0

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Sub-Total:		218	264	11
Total Non-litigated Claims Citation:	493			

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ITEMIZED SUMMARY CRITICISMS

The following is a brief summary of the major criticisms that were developed during the course of this examination. In response to each criticism, the Companies are required to identify the remedial/corrective action(s) that has/have been or will be taken to correct the deficiency. Regardless of the remedial actions taken or proposed by the Companies, it is the Companies obligation to ensure that compliance is achieved.

In response to criticisms raised by the examiners during the exit interview, FHG advised that they will implement certain procedures as outlined in their letter of 10/16/98 (Exhibit I-14) While the examiners appreciate the Companies efforts to date, the actions proposed are limited in scope and do not address "all" criticisms identified in this report. The examiners will withhold making a determination as to the adequacy of FHG's proposed remedial actions until such time as the Companies have had the opportunity to review this report in its entirely and respond to all criticisms in detail.

1. Inadequate Investigations: The examiners cited 92 instances in which the Companies failed to perform fair, adequate, correct and/or timely investigations of losses, and failed to obtain correct estimates of the insured's damages. Files in which damages were grossly underestimated by the Companies' representatives typically indicate the overlooking of attics, crawl spaces, foundations and fireplaces. Many files reveal: 1) The insureds were incorrectly advised that the damage was less than their deductibles; 2) initial inspections were performed by staff with inadequate training; 3) as a result of inadequate investigations, the insureds received low-ACV settlements or offers of settlement; 4) insureds were required to request additional inspections (after receiving estimates from contractors they hired), which resulted in payments exceeding the Companies' initial settlement offers; and 5) the Companies failed to investigate the ownership of fences prior to settlement (assuming common ownership in all cases). In response to the examiners' inquiries regarding inadequate investigation, FHG stated "Adjusters are not accustomed to looking for structural damage from earthquakes. Rather, they are primarily trained to inspect property for surface damage." The Companies' inspections/appraisals were less

than adequate and it was left it to the policyholder to discover and document foundation and structural support damage. Excerpts of claim files indicative of the deficiencies cited are included as examples in **Exhibits** I-2 & I-11.

While the examiners recognize the possibility of hidden damage and the effect of after shocks, there is substantial evidence to indicate inadequate investigations and gross oversight on the part of the Companies. Many files revealed that **the settlements were driven by the insureds,** especially when confronted with estimates by contractors indicating damage in excess of the Companies' original settlement decisions. **In many cases the examiners noted that settlement disputes arose when initial scoping performed by the Companies' independent appraiser was overruled by FHG's home office examiner.** The CDI examiners could not determine the reasons FHG refused to accept the independent appraiser's expert valuation. This type of action also prompted insureds to obtain their own estimates which repeatedly resulted in increased settlement amounts. Failure to perform adequate investigations also resulted in delays in claims settlements. These acts are violations of UCP Regulation 2695.6(a); CIC 790.03(h)(3); and 790.03(h)(5).

<u>Remedial Action:</u> To be determined.

2. **Unsupported/Excessive Depreciation:** In 65 instances the Companies failed to document the basis or justification for depreciation, especially in structural damage claims. Additionally, FHG applied excessive blanket depreciation of 30% to 60% on materials and labor and provided no supporting documentation for the method used in calculating the depreciation amounts. Further, the files do not indicate the application of depreciation was discernable, measurable and fair. In addition to taking excessive depreciation, the Companies totally removed overhead and profit and taxes from the contractors' estimates. These unsubstantiated and/or inconsistent excessive depreciation reductions and the removal of overhead and profit when determining ACV values, resulted in low and unsupported settlement offers which were substantially lower than the actual repair costs.

Additionally, the examiners discovered settlement adjustments that depreciated collectibles such as

glassware and figurines which are known to "appreciate" in value. Depreciation factors such as age and condition were not consistently found in the claim files. Indicative of the Companies approach was evident in a file in which the notations stated **"Because of the quality of these items and the fact that they do appreciate in value, we applied a minimal depreciation of 10% on all items resulting in an actual cash value figure of $17,089.20".**

Excerpts of claim files indicative of the deficiencies cited are included as examples in **Exhibit I-3**. These acts are violations of UCP Regulation 2695.3(a); CIC 790.03(h)(3); and 790.03(h)(5).

Remedial Action: To be determined

3. Improper Handling/Low Settlement:

(A). Inadequate investigations and inspections coupled with unsupported depreciation contributed to unreasonably low settlements in 53 of the claim files reviewed. Excerpts of claim files indicative of the deficiencies cited are included as examples in **Exhibit I-4**. These acts are violations of UCP Regulation 2695.7(g), and CIC 790.03(h)(5).

Remedial Action: To be determined

(B). The examiners documented 12 instances in which the personal contents settlement was incorrectly included with the dwelling settlement and one check was issued jointly to the insured and the mortgage company. Some insureds requested separate drafts at the outset while others returned the drafts and insisted that a separate check be issued for their personal contents. When presented with such requests, FHG complied. However, it is apparent that many insureds did not realize that their contents settlements were included in the structural settlements and therefore merely signed the drafts over to their mortgage companies. Most insureds never noticed the Companies were operating in this manner. These acts are violations of Regulation 2695.7(g); and CIC 790.03(h)(3); 790.03(h)(5); and 790.03(h)(12).

Remedial Action: To be determined

4. Application of Deductible: While not cited as specific violations, it should be noted when the insured suffered both personal contents and structural damage, FHG applied the deductible to the contents portion of the claim first. As the deductible equates to 10% of the structural limits the deductible often exceeded the amount of the personal contents loss. FHG then applied the balance of the deductible to the dwelling loss. In response to the examiners' concerns, FHG advised that they were protecting the lien holders' interest. The examiners determined that the insureds did not receive any payment for their contents losses in many instances.

The examiners find this practice highly questionable and this issue is herein referred to the CDI legal division for review and opinion.

5. Lack of Explanation of Settlement Reductions: The examiners documented 57 instances in which the Companies failed to explain depreciation reductions to policyholders. Additionally, in some files, the Companies entirely eliminated items from the estimates without any explanation to the insureds. Excerpts of claim files indicative of the deficiencies cited are included as examples in **Exhibit I-5**. These acts are violations of Regulation 2695.4(a); and CIC 790.03(h)(1); and 790.03(h)(3).

Remedial Action: To be determined

6. Failure to Explain Policy Benefits: The examiners documented 16 instances in which the Companies failed to disclose policy benefits to insureds. Specifically, the 180 day limit within which to recover the cost of replacing damaged property was not clearly explained to the insured in some instances. In response to the examiners inquiry, FHG advised that they never refused to refund replacement cost benefits to insureds, upon request, even if such request was received beyond the 180 day limit. The Companies' response does not address the fact that some policyholders were not

made aware of the replacement cost benefits. Excerpts from claim files indicative of the deficiencies cited are included as examples in **Exhibit I-6**. These acts are violations of Regulation 2695.4(a) and CIC 790.03(h)(1).

Remedial Action: To be determined.

7. **Failure to Tender Payment Within 30 Days:** In 29 instances, the Companies failed to tender payment immediately or within 30 days. The examiners found that in some cases the Companies failed to pay the Personal Property/Contents loss until the amount of the dwelling loss was determined. Delays ranging from 37 days to 6 months were detected. Excerpts from claim files indicative of the deficiencies cited are included as examples in **Exhibit I-7**. These acts are violations of Regulation 2695.7(h) and CIC 790.03(h)(5).

Remedial Action: To be determined.

8. **Failure to Document Files:** The examiners cited 42 instances in which the Companies failed to properly document files. As a result of missing or incomplete documentation, the examiners were unable to determine if the actions of the Companies were appropriate and in compliance with all regulations. The examiners noted that copies of payments to the policyholders were missing and log entry notations were incomplete. These acts are violations of UCP Regulation 2695.3(a) and CIC 790.03(h)(3).

Remedial Action: To be determined.

9. **Failure to include General Contractors' Overhead and Profit in ACV Settlements:** While not cited as violations, in addition to the excessive depreciation reductions previously discussed, FHG's failure to include overhead and profit resulted in unreasonably low ACV settlements. In many files the examiners noted that the insureds expressed feelings of confusion about what they were entitled to and what they would be able to collect after repairs were made.

made aware of the replacement cost benefits. Excerpts from claim files indicative of the deficiencies cited are included as examples in **Exhibit I-6**. These acts are violations of Regulation 2695.4(a) and CIC 790.03(h)(1).

Remedial Action: To be determined.

7. **Failure to Tender Payment Within 30 Days:** In 29 instances, the Companies failed to tender payment immediately or within 30 days. The examiners found that in some cases the Companies failed to pay the Personal Property/Contents loss until the amount of the dwelling loss was determined. Delays ranging from 37 days to 6 months were detected. Excerpts from claim files indicative of the deficiencies cited are included as examples in **Exhibit I-7**. These acts are violations of Regulation 2695.7(h) and CIC 790.03(h)(5).

Remedial Action: To be determined.

8. **Failure to Document Files:** The examiners cited 42 instances in which the Companies failed to properly document files. As a result of missing or incomplete documentation, the examiners were unable to determine if the actions of the Companies were appropriate and in compliance with all regulations. The examiners noted that copies of payments to the policyholders were missing and log entry notations were incomplete. These acts are violations of UCP Regulation 2695.3(a) and CIC 790.03(h)(3).

Remedial Action: To be determined.

9. **Failure to include General Contractors' Overhead and Profit in ACV Settlements:** While not cited as violations, in addition to the excessive depreciation reductions previously discussed, FHG's failure to include overhead and profit resulted in unreasonably low ACV settlements. In many files the examiners noted that the insureds expressed feelings of confusion about what they were entitled to and what they would be able to collect after repairs were made.

Excerpts of claim files indicative of this practice are included in **Exhibit I-9.**

The examiners herein refer the issue of failing to include general contractors' overhead and profit in ACV settlements to the CDI Legal Division for review and opinion.

10. Failure to include CDI referral information In 13 instances, the Companies failed to advise the policyholders that the CDI could review a denied claim. These acts are violations of UCP Regulation 2695.7(b)(3) and CIC 790.03(h)(3).

Remedial Action: To be determined.

11. Status Letters: In 16 instances the Companies failed to advise the insureds that additional time was needed to investigate their claim. These acts are violations of UCP Regulation 2695.7(c)(1), and CIC 790.03(h)(3).

Remedial Action: To be determined.

12. Failure to Respond to Communication From Insured: In 8 instances, the Companies failed to respond to communications from the insureds within 15 days. Excerpts of claim files indicative of the deficiencies cited are included as examples in **Exhibit I-10.** These acts are violations of UCP Regulation 2695.5(g); CIC 790.03(h)(2); and 790.03(h)(3).

Remedial Action: To be determined.

13. Written Basis for Denial: The examiners documented 6 instances in which FHG failed to provide the written basis for denials to insureds. These acts are violations of UCP Regulation 2695.7(b)(1), and CIC 790.03(h)(3).

Remedial Action: To be determined.

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14. **Accept or Deny Claims:** The examiners cited 3 instances in which the Companies failed to accept or deny claims within 40 days of receiving proof of claim. These acts are violations of UCP Regulation 2695.7(b) and CIC 790.03(h)(4).

Remedial Action: To be determined.

15. **Inconsistent Handling of TLEA:** While not cited as errors, TLEA was handled inconsistently. In some instances, FHG advanced security deposits and anticipated rental expenses upon receipt of a signed lease, while in other instances, the insured was reimbursed on a monthly basis "after" expenses were actually incurred.

Remedial Action: To be determined.

16. **Depreciation of Labor Costs:** While not cited as errors, the Companies depreciated labor costs when calculating the ACV settlements. Labor costs should not be depreciated.

Remedial Action: In response to inquiry, FHG provided their position which is attached to this report as **Exhibit I-12.**

The general issue of depreciating labor costs is herein referred to CDI Legal Division for review and opinion.

17. **Rental Value Loss:** While not cited as errors, inconsistent handling was noted by the examiners. Some insureds were advised that the DP3 Endorsement - U8346 - did not provide rental coverage while others were advised that coverage was, in fact, afforded. It was noted that a rental claim was denied, however, after the insured filed a complaint with CDI, the file was reviewed by FHG senior management and the denial was reversed. In a memo to staff dated 8/1/94, FHG management directed that "...loss of rents coverage for rental properties is part of the blanket earthquake limit.." See **Exhibit I-13.** The examiners were unable to determine if all applicable files

were reviewed and corrective measures were taken in accordance with the Companies directive.

<u>Remedial Action:</u> To be determined.

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