



MIKE CHANEY
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FOR IMMEDIATE RELEASE

Mike Chaney, Commissioner of Insurance/State Fire Marshal
Mississippi Insurance Department
Jackson, Mississippi
Wednesday, October 29, 2008
For additional information, please contact
Donna J. Cromeans, Public Relations Director 601-359-3569

MID Completes State Farm Market Conduct Exam

Jackson – Following over 22 months of extensive review of hundreds of thousands of documents and hours of sworn testimony, the Mississippi Insurance Department (MID) has completed its Special Target Examination of State Farm Fire and Casualty Insurance Company's claims handling practices in the aftermath of Hurricane Katrina. The report has been sent to the company and will be placed on the MID-website (www.mid.state.ms.us) for public review.

“As Insurance Commissioner, I am very aware that not everyone will be pleased with the conclusions reached in the report, therefore, I recommend that the report be read in its entirety. This report finds State Farm did some things right and some things wrong,” Commissioner Mike Chaney said.

“When I became Commissioner, I said we would put policyholders first while providing a fair, stable climate that would guarantee that Mississippians have plenty of viable insurance options. The report we are releasing today is a thorough and detailed accounting of what happened with State Farm policyholders after Katrina. I believe it is a very evenhanded report that helps identify problem areas for the insurance industry's response to the devastation caused by hurricanes and other natural disasters,” Chaney said.

Among the report's findings and discussion are:

- Some policyholders' claims were not handled appropriately, although the exam found no specific violations of the Unfair Trade Practices statute.
- The exam found no pattern of violation of the insurance fraud statute, which parallels findings of Attorney General Jim Hood's office.

- Although there were questionable decisions and irregularities by State Farm in handling claims, no scheme or plan to systematically mistreat policyholders was found.
- After numerous complaints and accusations by policyholders, State Farm agreed to reopen all slab cases through a MID-monitored program, which resulted in an additional \$88 million dollars being paid to policyholders.

Chaney added; “Hurricane Katrina was an extremely trying situation for everyone involved. The real brunt was borne by the people on the coast who lost their homes and businesses. We do not and should not expect insurance companies to pay claims that are not covered by the policy, however, we expect them to promptly pay every penny that policyholders are owed on policies paid in good faith. To this end, I will continue to advocate and require that policies be written in plain, simple understandable language. I am committed to working with insurance companies to provide a good business environment in Mississippi, but I won’t tolerate unfair treatment of policyholders. I’m confident we can use findings of the exam as a constructive tool to help make policyholders’ lives easier the next time disaster strikes.”



MISSISSIPPI INSURANCE DEPARTMENT

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MIKE CHANEY
Commissioner of Insurance
State Fire Marshal

October 17, 2008

CERTIFIED MAIL

RETURN RECEIPT REQUESTED

Mr. Edward B. Rust, Jr., Chairman and CEO
c/o Steve Simpkins, Counsel, Corporate Law Department
State Farm Fire and Casualty Insurance Company
One State Farm Plaza
Bloomington, IL 61710-0001

RE: Report of the Special Target Examination of State Farm Fire and Casualty Insurance Company

Dear Mr. Rust:

In accordance with Miss. Code Ann. §83-1-27 and §83-5-201 et seq. (Rev. 1999), an examination of your Company has been completed. Enclosed herewith is the Order adopting the report and a copy of the final report.

Pursuant to Miss. Code Ann. § 83-5-209(6)(a) (Rev. 1999), the Mississippi Department of Insurance shall continue to hold the content of said report as private and confidential for a period of ten (10) days from the date of the Order. After the expiration of the aforementioned 10-day period, the Department will open the report for public inspection. It is hereby requested that the Company waive said period.

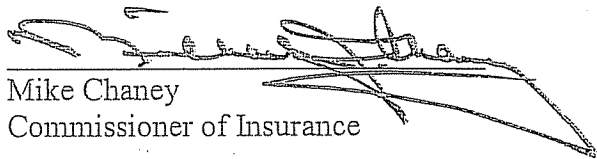
If you have any questions or comments, please feel free to contact me at 601-359-3577.

With kindest regards, I remain,

Sincerely,

DEPARTMENT OF INSURANCE

BY


Mike Chaney
Commissioner of Insurance

MC/CJK/bs
Enclosures (Order, Final Report)

**BEFORE THE COMMISSIONER OF INSURANCE
OF THE STATE OF MISSISSIPPI**

**IN RE: REPORT OF THE SPECIAL
 TARGET EXAMINATION OF
 STATE FARM FIRE AND CASUALTY
 INSURANCE COMPANY**

CAUSE NO. 08-5827

ORDER

THIS CAUSE came on for consideration before the Commissioner of Insurance of the State of Mississippi ("Commissioner"), or his designated appointee, in the Offices of the Commissioner, 1001 Woolfolk Building, 501 North West Street, 10th Floor, Jackson, Hinds County, Mississippi, pursuant to Miss. Code Ann. §83-1-27 and §83-5-201 et seq. (Rev. 1999). The Commissioner, having fully considered and reviewed the Report of Examination, together with any submissions or rebuttals and any relevant portions of the examiner's work papers, makes the following findings of fact and conclusions of law, to-wit:

JURISDICTION

I.

That the Commissioner of Insurance of the State of Mississippi has jurisdiction over this matter, pursuant to the provisions of Miss. Code Ann. §83-5-201 et seq. (Rev. 1999).

II.

That State Farm Fire and Casualty Insurance Company is domiciled in Bloomington, IL. The Company writes Automobile Physical Damage/Liability; Boiler and Machinery; Casualty/Liability; Fidelity; Fire/Allied Lines; Home/Farm Owners; Inland Marine; Ocean Marine; Plate Glass; Surety; and Workers' Compensation coverages.

FINDINGS OF FACT

III.

That the Commissioner, or his appointee, pursuant to Miss. Code Ann. §83-1-27 and §83-5-201 et seq. (Rev. 1999), called for an examination of State Farm Fire and Casualty Company and appointed Jimmy Blissett, Examiner-In-Charge, to conduct said examination.

IV.

That on or about September 22, 2008, the draft Report of Examination concerning State Farm Fire and Casualty Insurance Company for the period of October 24, 2006, through September 22, 2008, was submitted to the Department by the Examiner-In-Charge, Jimmy Blissett.

V.

The Department forwarded the draft Report of Examination to the Company pursuant to Miss. Code Ann. §83-5-209(2) (Rev. 1999) and allowed the Company to submit a written response. Following careful review of the Company's response/rebuttal, the Commissioner adopted the final Report of Examination on October 17, 2008 as attached hereto as Exhibit "A."

VI.

Following Hurricane Katrina's catastrophic landfall, the Department received hundreds of complaints, both formal and informal, from policyholders on the Gulf Coast. These complaints included accusations that various insurance companies, including State Farm, were improperly adjusting claims and/or denying claims without a legitimate or arguable basis.

In an effort to ensure that Mississippi policyholders were being treated properly, then Commissioner George Dale met with State Farm officials to discuss these complaints and

allegations. On or about March 6, 2007, the Commissioner of Insurance, as a result of concerns raised through the examination, reached an agreement with State Farm wherein the Company would re-open and re-adjust all "slab claims" located in the lower three counties that being Hancock, Jackson and Harrison counties along the Mississippi Gulf Coast. The agreement was later extended to include any claims in which the policyholder felt he/she was improperly paid for their claim.

The Department was intimately involved in this re-evaluation process which resulted in thousands of claims being re-opened and re-adjusted. Members of the examination team and other employees of the Department worked with State Farm and its policyholders on a daily basis to ensure that Mississippi residents received what they were owed under their homeowners policy. The re-evaluation process resulted in millions of additional dollars being paid to Mississippi policyholders. State Farm provided sworn testimony that it alone paid more than \$88 million as a result of the Department's re-evaluation program.

VII.

The conduct of State Farm was evaluated and assessed pursuant to the applicable laws, statutes and regulations of the State of Mississippi. Directives and bulletins issued by the Department following Hurricane Katrina were also considered. When applying Mississippi's Unfair Trade Practices statute as codified as Miss. Code Ann. §83-5-29 through §83-5-51 (Rev. 1999), to State Farm's conduct following Hurricane Katrina, the Department found that while the Company did make errors, it found no violations. Although the examination team identified certain areas and instances where some policyholders could have been treated more appropriately, no specific violations of the Unfair Trade Practices statute were identified.

CONCLUSIONS OF LAW

VIII.

The Commissioner, pursuant to Miss. Code Ann. §83-5-209(3) (Rev. 1999), must consider and review the report along with any submissions or rebuttals and all relevant portions of examiner work papers and enter an Order:

- (1) adopting the Report of Examination as final or with modifications or corrections;
- (2) rejecting the Report of Examination with directions to reopen; or
- (3) calling for an investigatory hearing.

IT IS, THEREFORE, ORDERED, after reviewing the Report of Examination, the Company's rebuttal, and all relevant examiner work papers, that the Report of Examination of State Farm Fire and Casualty Insurance Company, attached hereto as **Exhibit "A"**, should be and same is hereby adopted as final.


IT IS FURTHER ORDERED that a copy of the adopted Report of Examination, accompanied with this Order, shall be served upon the Company by certified mail, postage pre-paid, return receipt requested.

IT IS FURTHER ORDERED that the Mississippi Department of Insurance shall continue to hold the content of this report as private and confidential information for a period of ten (10) days from the date of this Order, pursuant to Miss. Code Ann. §83-5-209(6)(a) (Rev. 1999).

IT IS FURTHER ORDERED, pursuant to Miss. Code Ann. §83-5-209(4) (Rev. 1999), that within thirty (30) days of the issuance of the adopted report, State Farm Fire and Casualty Insurance Company shall file affidavits executed by each of its directors stating under oath that they have received a copy of the adopted report and related orders.

IT IS FURTHER ORDERED that State Farm Fire and Casualty Insurance Company shall take the necessary actions and implement the necessary procedures to properly and promptly address the findings as set forth in the Report of Examination and, specifically, that the Company shall reopen and reevaluate any and all claims adjusted by any independent adjuster that was released to ensure that a proper claims decision was made. The Company is further ordered to submit to the Department documentation indicating the policies and procedures that have been implemented following Hurricane Katrina to address the delays, errors and other findings identified in the Report of Examination.

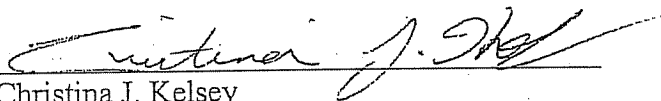
SO ORDERED, this the 17th day of October, 2008.


MIKE CHANEY
COMMISSIONER OF INSURANCE
STATE OF MISSISSIPPI

CERTIFICATE OF MAILING

I hereby certify that a true and correct copy of the above and foregoing Order and a copy of the final Report of Examination, as adopted by the Mississippi Department of Insurance, was sent by certified mail, postage pre-paid, return receipt requested, on this the 17th day of October, 2008, to:

**Mr. Edward B. Rust, Jr., Chairman and CEO
c/o Steve Simpkins, Counsel, Corporate Law Department
State Farm Fire and Casualty Insurance Company
One State Farm Plaza
Bloomington, IL 61710-0001**


Christina J. Kelsey
Senior Attorney

Christina J. Kelsey
Senior Attorney
Counsel for the Mississippi Department of Insurance
Post Office Box 79
Jackson, MS 39205-0079
(601) 359-3577
Miss. Bar No. 9853



Mississippi Department of Insurance

Report of the Special Target Examination (Katrina Homeowner Claims)

of

State Farm Insurance Companies
(Specifically State Farm Fire & Casualty
Company)

One State Farm Plaza
Bloomington, IL 61710

NAIC Company Code 25143

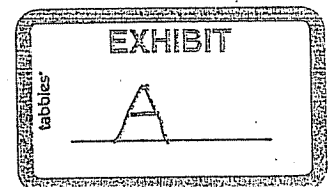


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FOREWARD

This Report is presented as the report of findings of the special target examination relating to those areas of the Company's operations as identified in the "Purpose and Scope" section of this report. Please note that this report is a report by exception and does not encompass every area reviewed. However, other matters contained herein are included as deemed necessary to give a clear understanding of how the Company handled homeowner claims in the lower six counties of Mississippi. Failure to comment on specific products, procedures, files or other areas does not constitute approval or disapproval thereof by the Mississippi Department of Insurance.

This report is not intended for any purpose other than to communicate to the Commissioner of Insurance of the State of Mississippi the findings and results of test work and investigative activities performed during the course of this special target examination. This report should not be used by the company examined or any other entity or person(s) for any other purpose not specifically approved by the Commissioner of Insurance for the State of Mississippi.

Wherever used in this Report:

"SFCC" or "Company" or "State Farm" refers to State Farm Fire & Casualty Company;

"MID" refers to the Mississippi Department of Insurance, aka Mississippi Insurance Department;

"Katrina" refers to Hurricane Katrina;

"Report" refers to the examination report;

MID Special Target Examination of State Farm Insurance Companies –Hurricane Katrina Homeowner Claims

“Slab claim” refers to claims where only foundations or piers remained;

“Wind/Water Protocol” or “WWP” refers to the Wind/Water Claim Handling Protocol

PURPOSE AND SCOPE

A special target examination was commenced pursuant to and under the authority of the provisions of Mississippi Code Annotated §83-1-27 and §83-5-201 et seq., and in accordance with the directives of the Insurance Commissioner for the State of Mississippi. Additionally, the National Association of Insurance Commissioners Market Conduct Examiners Handbook, as amended, was used as a guide.

This examination was performed by examiners, adjusters and attorneys appointed by the Commissioner of Insurance and in accordance with his statutory authority as referenced above.

On October 24, 2006, a notice of examination was mailed to State Farm formally advising the Company of the MID’s intention to commence an examination. This notice was a follow-up to a meeting held in the offices of the MID on October 19, 2006, wherein the Company was advised that a Special Target Examination was being called to commence immediately to investigate how State Farm treated its policyholders who had filed claims as a result of Hurricane Katrina. More specifically, and in accordance with the Commissioner’s instructions, the scope of the examination was to investigate the handling of homeowner claims in the lower six counties of Mississippi, specifically: Hancock, Harrison, Jackson, George, Pearl River, and Stone, filed as a result of Katrina.

MID Special Target Examination of State Farm Insurance Companies –Hurricane Katrina Homeowner Claims

The MID had received numerous complaints from policyholders during the ensuing days and months after Katrina made landfall and there were literally hundreds of lawsuits filed on behalf of policyholders against the Company. The MID complaint log revealed complaints of various nature including, but not limited to: claims being initially denied as all damages were due to excluded flood damage; coverage was denied after being told initially by adjusters that there was wind damage; coverage for wind damage was denied for anything that had been touched by storm surge; complaints regarding concerns about the timing of denials versus the timing of engineer reports; complaints alleging that State Farm instituted a policy on slab claims and other total losses that State Farm could not pay wind coverage when there was nothing left of the property; and, complaints that the adjuster determined it was all flood damage before the property was inspected.

Also of importance was the fact that the MID was aware that there were allegations of fraud and abuse made by various entities. These allegations were evidenced, at least in part, by grand jury investigations conducted by both the Mississippi Attorney General and the United States Attorney for the Southern District of Mississippi. Additionally, the Company itself had commenced an internal investigation into, among other issues, the alleged fraud and abuse.

This examination, pursuant to its authority, focused on determining whether the Company treated its policyholders fairly, honored the terms and conditions of its policies, and complied with Mississippi insurance laws and regulations, as well as related Department of Insurance bulletins.

The scope of this examination did not encompass an investigation specifically relating to fraudulent or criminal activity per se and no such conclusions have been drawn as to the presence or absence of fraud. It should be noted the MID is not a law enforcement entity and, therefore, has no authority to prosecute criminal activity. This notwithstanding, allegations of fraud were not neglected or overlooked and are addressed in more detail below.

Allegations of fraudulent activity were investigated by the Mississippi Attorney General's office. In a statement issued by the Attorney General in February 2008 and as quoted in the *SunHerald* newspaper, he stated in part that "the majority of the prosecutors working on this case determined with a high level of certainty that no fact pattern existed that fell squarely within the insurance fraud statute." At the writing of this report, it appears that the Attorney General's criminal investigation has been closed although there have been no formal filings confirming this fact. However, there appears to be an ongoing investigation by the United States Attorney's office into these or related matters.

The special target examination generally included the period from August 29, 2005, through the commencement date of the examination. Material transactions that occurred prior to or subsequent to the examination time period may also have been reviewed.

The procedures developed and used, among others, during this special target examination were designed to determine the fair treatment of policyholders as anticipated in Miss Code Ann. § 83-5-29 to 83-5-51, and should not be considered a full scope

examination or applied in any other context. Other areas of the Company's market conduct and financial condition were not considered within the scope of this examination.

The examiners also made requests to various plaintiff firms who had filed complaints against the Company alleging fraud and abuse. These requests were also met with resistance and largely ignored. Information was requested in writing in June 2007. Other than receiving a copy of the RICO complaint which had already been made public, no substantive or useful information has been received.

Added to the above limitations is the fact that there is an ongoing investigation by a federal grand jury. The grand jury investigation, in and of itself, has not limited the examination, however, many individuals and companies that we approached in the course of this examination had either testified before the grand jury, produced documents to the grand jury or were subpoenaed to testify before the grand jury.

BACKGROUND

Hurricane Katrina made landfall initially as a Category 1 hurricane in Dade/Broward counties in South Florida. The same hurricane, then as a strong category 3 storm, made a second landfall in Plaquemines Parish, Louisiana. Hurricane Katrina made its third and final landfall at approximately 10:00 CDT on August 29, 2005, near the Mississippi-Louisiana border still at Category 3 status with maximum sustained winds of 125 mph. Katrina was still at hurricane strength 100 miles inland. Hurricane Katrina was accompanied by a horrific storm surge ranging from approximately 17-22 feet on the eastern part of the coast to 24-28 feet on the western part of the coast. The surge reached

inland as far as 6 miles and up to 12 miles in areas along bays and rivers. Damage to homes and businesses in Mississippi was catastrophic and unprecedented.

As a result of Katrina, hundreds of thousands of claims were filed by residents of the state of Mississippi. State Farm alone had over 80,000 windstorm claims, of which approximately 43,000 were for property located in the lower six counties of Mississippi.

In coastal Mississippi, there were many instances where there was little or nothing left of the structures which once existed. Many houses and buildings were reduced to nothing more than a slab or piling with debris strewn everywhere. This resulted in a complicated adjustment of the claim and rendered impossible an accurate assessment of the specific cause of damages.

EXECUTIVE SUMMARY

There were approximately 43,000 homeowner claims (including 6,327 flood claims) filed for property losses located in the lower six counties of Mississippi. Out of this number, 39,044 (including 6,269 flood claims) were located in the lower three counties. An initial discovery sample of the claims was drawn for our review. Two additional stratum were chosen to review claims. One included claims in which engineers were used to assist in the determination of causation. Another was for claims in the lower three counties, in which no engineer was used. These second two stratum were selected due to the numerous allegations involving engineers and the Company's alleged failure to pay for wind damage in areas where flood was also present. A review of the complaints received by the MID indicated that the majority involved wind/water issues.

The examination encompassed an analysis of approximately 800 homeowner claims selected in the samples mentioned above. In conjunction with this, we examined, under oath, numerous individuals that were involved in the claims handling process. The examiners reviewed hundreds of thousands of documents related to State Farm's claims practices, some of which were provided by the Company while others were obtained from third parties.

It should be noted that the figures and percentages used in this Report are limited to the above mentioned sample and/or stratum and should not be extrapolated or applied to the entire population of claims. Specifically, the second and third stratum were focused on claims involving engineers and claims which were made from the lower three counties. Percentages from these stratum would not apply to the entire population.

The procedures performed in the investigation revealed that in areas where wind and water were not an issue, there was no significant evidence developed that indicated State Farm failed to fulfill policy obligations. Furthermore, when you consider that the complaints received by the MID generally tracked the areas where wind/water was involved, a reasonable inference can be drawn that the question of State Farm's fulfillment of its obligations, or not, was related primarily to areas where wind or water was at issue. This was consistent with our findings.

The examiners did find, however, that when wind and water were an issue in a claim, the Company initially failed to completely fulfill its policy obligation to some policyholders. This resulted from a combination of factors as shown below:

- When wind and water were involved, the sample revealed that 173 claim files reviewed lacked adequate documentation to support that a full or thorough investigation was completed (See page 12);
- Of the sample of claim files reviewed where wind coverage was available but no dwelling payments were made, 64 of the 101 homeowner claims reviewed were denied despite indications of some wind damage either to the insured's structure, neighboring residences or simply the existence of damaging wind in the area of the loss (See page 16);
- As evidenced by the above factors, multiple claim files did not contain adequate documentation necessary to prove that the exclusion applied to the entire loss (See page 17);
- Various aspects of the Company's claims handling process resulted in delays and confusion for policyholders (See page 19);
- Some claims were handled by independent adjusters who lacked the necessary training and skills to adjust the claims in an effective and efficient manner. It did appear that once State Farm detected these problems, the Company took action to release the adjuster from the Catastrophe site. (See page 27); and,
- There was confusion among State Farm employees and representatives regarding the Company's anti-concurrent causation language. (See page 29).

The above referenced comments as well as a discussion of allegations of fraud and abuse are addressed in more detail under the following sections of the report. Additionally, to address many of the comments above and various concerns of the MID, the Company agreed to re-evaluate hundreds of claims, at which point over \$88 million was paid to policyholders by State Farm. The resolution process is discussed in more detail below as well.

CLAIMS ANALYSIS AND REVIEW

Claims Planning and Administration

The examination team requested a complete list of homeowner claims filed with any State Farm company between August 29, 2005, and October 31, 2006, by policyholders residing in the lower six counties of Mississippi (Hancock, Harrison, Jackson, Pearl River, Stone and George). The Company provided a list of 43,054 claims. Various analytical and statistical testing was performed on the data files provided. In determining the sample size to be reviewed, a number of factors were considered, including but not limited to, the fact there were ongoing grand jury investigations, numerous lawsuits alleging varying types of misconduct, allegations involving engineer reports and high levels of complaints received by the MID. Taking these factors into consideration, the examination team selected a first tier sample of claims, using a 95% confidence level with an upper error limit of 3% and expected error rate of zero. This allowed each item in the population of 43,054 claims an equal probability of being selected without regard to dollar amount, location, type, etc. This resulted in an initial sample size of 100 claims.

MID Special Target Examination of State Farm Insurance Companies –Hurricane Katrina Homeowner Claims

In order to target more specific areas of concern that were developed through the examination planning phase, second and third tiers or stratum of claims were selected for review. The second stratum was designed to review claims in which State Farm had engaged the services of engineers to assist in determining the cause of loss. This was accomplished by segregating all claims that the Company had designated as having an engineer report associated with it. This resulted in 1,283 claims. A statistical sample was selected using a 95% confidence level, a 3% upper error limit and a judgmentally determined 10% expected error rate. This resulted in a sample size of 312 claims in this stratum.

There were approximately 39,000 claims in the lower three counties of Mississippi. This represented approximately 91% of the 43,054 claims in the six counties that were the focus of the examination. Most of the allegations mentioned above related to claims in these lower three counties (grand jury subpoenas were issued regarding this population). As this was the case, a third stratum was designed to review claims in these counties. In order to select these claims, the examination team segregated all the claims in the lower three counties and then excluded those claims with engineer reports as they would be tested in the second stratum. This left 37,772 claims in our population. A statistical sample was selected using a 95% confidence level, a 3% upper error limit and a judgmentally determined 10% expected error rate. This resulted in a sample size of 400 claims.

The entire number of sample claims selected is as follows:

Discovery Sample	2nd Tier	3rd Tier	Total
100	312	400	812

After all the files were provided and throughout the course of the examiners' review, it was determined that the sample included claims that were not applicable to some of the test procedures to be employed. These consisted of files for flood claims and files for homeowner claims with no wind coverage. As the results were not extrapolated to the entire population, no additional files were selected to replace these.

The following table provides a breakdown of the files:

Total Sample Files	Flood Files	X-Wind Files	Total
812	87	37	688

The following table shows 688 claims by policy type:

Policy Type	Policy Count
H-HO-Condo Unit Owners Policy	6
H-HO-Homeowners Policy	565
H-HO-Renters Policy Content	15
R-Renters Policy Dwelling 3	102
	Total 688

The tables included under each caption below are based on the 688 files and it should be noted that these numbers and percentages should not be extrapolated and applied to the total number of homeowner claims filed with the Company following Hurricane Katrina.

Results of Claims Review

The investigation of the claims files in conjunction with knowledge obtained from the review of thousands of pages of claims related documents revealed that on multiple

occasions the Company failed to completely fulfill its obligations to its policyholders in the lower three counties where wind and water were at issue. On occasions, this resulted in a failure to pay portions of the damage attributable to wind. These failures are outlined in detail under the captions below. It should be noted that, at times, the failures were related to each other and may be discussed in more than one of the captioned areas.

Lack of Documentation to Support a Full Investigation

The following table shows that a number of the claim files reviewed did not contain adequate documentation to support that a full and thorough investigation was completed:

Adequate Documentation of a Full Investigation	Did Not Contain Adequate Documentation of a Full Investigation	Claims That Were Less Than Deductible, etc.	Total
488	173	27	688

As previously stated, these numbers should not be extrapolated and applied to the total number of claims.

Company representatives testified under oath that “there should be a thorough and complete investigation” and that claims representatives were expected to “fully investigate homeowners’ claims before denial.” The Company’s commitment to policyholders states that they should “diligently investigate the facts to determine if a claim is valid.” The Company’s Operation Guide (OG) that outlines the guidelines for claims representatives states that “claim files should always completely reflect all

activities and support the conclusions reached.” Testimony from State Farm personnel acknowledged these requirements.

After the receipt of complaints from policyholders alleging that homeowner claims were being denied within the industry without an inspection of the damaged property, the MID issued Bulletin No. 2005-6 on September 7, 2005, which stated in part, “I (then Commissioner George Dale) am instructing all companies...to fully inspect any damaged property before a coverage decision was made.”

Notwithstanding State Farm’s letter to the Deputy Commissioner stating that the Company was administering claims in accordance with the directives outlined in MID Bulletin 2005-6 and MID Bulletin 2006-2, our review of the sample claim files reveals that a number of files did not contain adequate documentation to support a full or thorough investigation. Some of these files did not adequately determine and document the amount of damage that was a result of hurricane force winds as opposed to the excluded damage from storm surge or rising flood waters. Not to mitigate the Company’s responsibility, however, it should be noted that many claims involved properties of which there was nothing remaining but the foundation.

As referenced in the table above, 173 of the claim files reviewed did not contain adequate documentation to support a full or thorough investigation such as: adequate photographs of the loss or neighboring structures; notes or diagrams evidencing the adjusters’ investigation; evidence gathered from eyewitnesses; documentation of physical evidence or water lines; or, incomplete activity log entries. On multiple occasions claims were denied prior to the receipt of engineer reports.

Additional indications of the lack of a full, thorough or complete investigation was discovered with claims in which the Company enlisted the services of engineers to determine the “predominant”, “probable” or “primary” cause of damage. (This is discussed further under the caption “Use of Engineers”.) Although the engineers reported in their conclusions what the predominant cause of the damage was, they generally discussed the fact that there was possible, probable, or actual wind damages associated with the storm as well. There were instances where the files did not indicate the Company attempted to investigate the less than predominant damages or to quantify them. One member of State Farm’s management acknowledged that if an engineer said there was probable wind damage but failed to inform the Company of the extent of the probable wind damage, “... I would want to pursue that.”

The lack of adequate documentation to support a full and thorough investigation was further noted by comparing claims that went to mediation. Claim files that were mediated contained additional investigation such as re-inspecting the loss location, diagramming the risk (often for the first time), taking additional photographs, and preparing a speculative estimate (usually for the first time).

It should be noted that lack of documentation in a claim file is not conclusive proof that the claim was not properly or fully investigated, however, the Company’s documentation of its activities, or lack thereof, was all that the examiners had to review. The Company’s own Operation Guide states that “claim files should always completely reflect all activities and support the conclusions reached.” Stated succinctly by one of the Company’s Team Managers, “the file speaks for itself.” Another Team Manager

acknowledged that all pertinent information used to make a coverage determination should be in the file. The examiners reviewed the claim files and considered the adequacy, or not, of the applicable investigation under this premise.

(See Subsequent Resolution Process section for subsequent payments made by the Company)

Failure To Pay When There Were Indications of Wind Damage

There were numerous claims within our sample where policyholders were not paid for wind damage even though there were indications of wind in the file. These indications were noted in photographs, witness statements, adjuster comments, insured comments, engineer reports, engineer photographs, and/or adjuster inspection notes. As mentioned under the caption "Lack of Documentation to Support a Full Investigation", these indications range from specific references to "possible", "probable", or "likely" wind damage noted in engineer reports to actual evidence in the claim files determined by the examiners to be indications of damage caused by wind.

The examiners selected all claims in the sample that had zero dollars paid for wind damage (Coverage A). Claims that should not have received payments for wind damage, such as flood claims, claims with wind exclusions (X-Wind), renters and condominium policies and claims that did not exceed the deductible were extracted. The table below reveals the findings relating to this review:

Sample Claims with \$0 Payments For Coverage A	Claims that were Flood, X-Wind or Less than Deductible	Refined Number of Claims with \$0 Payments For Coverage A	Claim Files Containing Indications of Wind
175	74	101	64

As shown in the table, 64 claim files or 63.3 percent of these files contained indications of wind damage either to the insured's property, neighboring property, or simply the existence of damaging wind in the area of the loss. Of the remaining 37 files, some claims also appeared in the category of claims lacking adequate documentation of a full or thorough investigation making it impossible to know whether wind damage occurred or not.

The Company, through sworn testimony and correspondence to the MID, stated that when there was "credible evidence" of wind damage or "discernable" wind damage, the company would pay for this. Although "discernable" is not found in the Company's homeowners policies, the Company appeared to use this as the determining factor as to whether or not a payment was made for wind damage. This relates closely to the issue of lack of adequate documentation to support a full or thorough investigation. At least some State Farm supervisors, team managers and independent adjusters appear to have chosen a narrow interpretation when it applied the standard of "discernable." As one State Farm team manager stated, "If you can't see the damage, we can't pay for it." One State Farm manager stated that his "take on discernable just means something you can see with your own eyes." Obviously if there was nothing but a slab remaining, you may not be able to see the wind damage, but that is not conclusive evidence that there was no wind damage,

especially in an area where there were millions of dollars of wind damage in close proximity. This relates closely to the caption "Failure to Prove Exclusion."

The investigation also revealed a few instances where claims representatives advised policyholders that "State Farm had informed him that it would be the company policy to deny wind coverage to every policy holder in MY GENERAL AREA" or "if water touched it, we were told not to pay for wind." These quotes came directly from the Company's claims files or from specific complaints filed by policyholders with the MID. Despite these direct quotes, every State Farm representative that was questioned under oath regarding this practice, denied this was the policy. It should be noted that although these instances were not widespread, similar statements were made by more than one adjuster on more than one occasion.

(See Subsequent Resolution Process section for subsequent payments made by the Company)

Failure to Prove Exclusion

Under the all risk policy or accidental direct physical loss policy, the policyholder has to prove that an accidental direct physical loss occurred. This requirement is typically satisfied when the policyholder notifies the Company of a claim. The duty then shifts to the Company to determine whether or not it is a covered loss and whether or not an exclusion applies. The Company, at least in theory, acknowledges this concept, although there seemed to have been some disconnect between understanding the shifting of the burden and the actual handling of some claims by State Farm representatives. Inherent in

the shifting of the burden is the duty to conduct a complete investigation into the cause of loss. When there are one or more perils involved, such as wind and water, and the water is excluded, it is incumbent upon the company to calculate the separate damage attributable to each peril and adjust the claim accordingly.

State Farm, in its failure to fully and completely document its investigation, in essence, failed to prove the amount of the exclusion in some claims. The decision to pay "discernable" wind damage or wind damage that "you could see" failed to take into account the very nature of the storm and the reality that there was wind damage associated with the same storm that caused a tremendous amount of water damage. Some State Farm supervisors, team managers and independent adjustors adopted the position that because you could not quantify it or "see it", it didn't happen. The Company failed to recognize, for whatever reason, that wind caused at least some damage to most of the claims whether the damage was "discernable" or not. It should be noted once again that the Company paid millions of dollars for wind damage to the north of the surge line, only to deny some wind damage inside the surge area.

Additionally, several engineer reports referenced the "predominant" cause of loss referring only to the destruction of the structure itself. It did not quantify the entire cause of the loss or the damage that occurred prior to destruction. "Predominant" does not relate to the entire cause and leaves open at least a portion of the claim which was not substantially resolved or proven inferring that the Company, in these situations, failed to fully prove its exclusion.

The examiners also saw instances where engineers cited the “probable” damage to the structure as surge and coverage was denied with regard to the wind. These same reports also indicated there was probable wind damage to the property. In these cases, “probable” was enough to quantify the exclusion yet “probable” wind damage was insufficient to quantify payment under the homeowner policy or even prompt additional investigation into the true extent of the wind damage, if any. In other words, “probable” was enough to deny the claim but not enough to pay.

Delays and Confusion in Handling Claims

Not only did State Farm have an obligation to investigate its claims fully and completely, it had an obligation to adjust its claims in a prompt and timely fashion. The Company’s “Our Commitment to Our Policyholders” states in part, that it should “Diligently investigate the facts to determine if a claim is valid, reasonably evaluate the claim, and act promptly in resolving the claim”.

Katrina was a storm that caused unprecedented destruction. Infrastructures were demolished and resources to react to the devastation were stretched beyond the capabilities of everyone involved. Notwithstanding elements and obstacles out of its control and the overwhelming size and nature of the catastrophe, the investigation revealed not only delays, but also confusion that resulted from decisions made by State Farm.

Evidence of delays and confusion can be found initially in the Company’s decision to hire engineers on all slab claims. Although never done before on other catastrophes,

Company management made a corporate decision in mid-September to have its adjusters employ the use of engineers on specific type claims. The claims involved in this decision related to a determination of wind versus water damage and were generally located in the lower three counties. Testimony under oath from Company representatives indicated the decision was made due to a general lack of information about the damage caused by Katrina and the general lack of accurate weather data following the hurricane's landfall. Although this may have been a questionable decision, there was nothing developed by the examiners to establish this was done other than with an intent to better serve its policyholders.

Although there is no significant evidence substantiating that the initial use of engineers on all slab claims caused specific and quantifiable delays (one State Farm supervisor, however, simply said that this was a "very bad idea"), this decision, coupled with the subsequent cancellation of engineer reports on all slab claims did in fact cause delays, as well as confusion. A review of the claim files contained in the sample showed specific delays and confusion relating directly to these cancellations. Notes in the activity logs show policyholders placing calls to inquire as to the status of engineer reports when, in fact, the engineer report had been cancelled. There were also instances where an adjuster told a policyholder that an engineer would be inspecting the property only to learn later that the engineer had been canceled.

Additional delays and confusion resulted when the Company would erroneously assign two different firms to a single claim only to have one or both engineers cancelled. On occasions there was an engineer assigned to a claim only to later discover that they

never performed the inspection. As one State Farm team manager stated, "... engineers were overwhelmed as well...I think a delay was more or less expected if an engineer was assigned to a claim."

There were a number of claims that had engineer reports that were prepared and sent to the Company, and on occasion even to policyholders, which were later amended. At other times the Company would refuse to mail engineer reports to the insured stating this was their work product.

Perhaps the number one culprit causing delays was the turnaround time between when an engineer was initially assigned to perform an inspection and receipt of the final report. The Company generally paid Additional Living Expense benefits until the report was received, reviewed and a coverage decision made. The files reviewed in our sample revealed that the average time from the date the loss was reported to the date an engineer was requested was 39 days. The average time from when an engineer was assigned until the report was received was 102 days. Other information obtained from the engineer firms revealed incidences of reports that were returned in as little as 16 days from the date of assignment compared to others that took in excess of 200 days.

Other instances of delays were seen in the Company's use of unqualified or incompetent independent adjusters. This is discussed under the caption "Use of Independent Adjusters."

Another area of confusion related to the introduction of the "Wind/Water Protocol" and the Company's interpretation or application of the Anti-Concurrent Causation clause in its policy. These warrant a separate discussion and are addressed in captions below.

Use of Engineers

State Farm used engineers on approximately 1,283 claims in the lower six counties. State Farm engaged the services of ten (10) engineer firms to assist in the determination of causation, generally when wind and water were in issue. Only days after the storm, State Farm management made a decision to enlist the assistance of engineers on all slab claims. The testimony of some witnesses revealed that their understanding was that engineers would be requested on all claims. Between early to mid-October, a decision was made to “decrease the usage” of engineers. This decision was made after the Company had gathered additional information from which they could “arrive at an appropriate and correct claim decision” without the necessity of an engineer.

The examination team requested documentation from the ten (10) engineer firms engaged by State Farm. In that same vein, the examiners initially sent out letters requesting information from the engineers relating to their engagement with State Farm. However, some of these requests were ignored thus forcing the examiners to issue subpoenas to obtain the necessary documentation.

The examiners reviewed the information provided by each of the firms. This was performed in conjunction with the claims sample referenced above to determine if there were systemic improprieties involving engineers. This was not an exhaustive review of all engineer reports but rather a review of the information with the intent of detecting systemic issues. This information should be viewed in conjunction with other findings noted throughout this report.

The following are findings noted during our review:

- Although seldom, some engineer reports concluded wind was the predominant cause of the damage. (It is important to note that the majority of claims involving an engineer report were slab claims situated in areas inundated by surge water);
- Contrary to some allegations, not all engineer reports were changed, even in instances where the engineer concluded that wind damage occurred;
- Many of the claims reviewed in our sample which had an engineer report with conclusions stating that both wind and water caused damage, received payments for wind damage;
- What appeared to have been designated as “changed” reports were often drafts or unsigned reports that had not been reviewed by the signing engineer. It was not unusual to see changes between drafts or unsigned reports and the final product. Conclusions were compared between the reports to determine the basis for the changes, if any. Not all of the changes resulted in conclusions favorable to State Farm. It was notable that some final reports attributed more damage to wind than the initial or draft report; and,
- The examiners did see evidence that State Farm representatives questioned the findings of certain engineers. This was not the case across the board. The examiners noted that when this occurred, it appeared more often than not to be warranted. The majority of the reports that were questioned involved initial conclusions that were not supported by the evidence presented. At times,

conclusions in unsigned or draft reports were inconsistent with the information found in other parts of the report.

The examiners did note issues involving claims with engineer reports that at the least contributed to delays and confusion, and at most, resulted in policyholders not being paid for all damages. These are described as follows:

- Based upon testimony obtained by the examiners, there was confusion as to whether the initial decision to hire engineers applied to all claims or only slab claims. Additionally, the cancellation of engineers that occurred in mid-October, at a minimum, caused some delays and confusion. For example, the examiners noted in various activity logs where policyholders were advised that an engineer had been assigned to the claim, only to later learn that the engineer had been cancelled without notice to the policyholder;
- Engineer reports on slab claims were more often than not vague with regard to citing specific damage. The engineer reports on slab claims would generally cite what the predominant, probable or primary cause of damage to the structure was without quantifying the remaining damage. For example, reports would often cite surge as the predominant cause yet discuss that it was possible, probable, or even likely that wind caused some damage. A review of the claims files revealed that these less than predominant causes of damage were never investigated further. It is worth noting that engineers were often tasked with assessing damage to properties where there was little or nothing left to assess and allow for a precise allocation of damage to separate perils;

- The weather data used by engineers varied dramatically. Some engineer firms used data that indicated the peak surge preceded the peak winds while others held the reverse to be true. Yet others relied on data which concluded the peak surge and the peak winds occurred simultaneously. This may have resulted in inconsistent payments;
- At least one firm received assignments to conduct peer reviews of other engineers. This firm generally reversed the findings of the engineer initially assigned to the claim. At times the peer review was performed after the property had been cleared of all debris. These appear, at least on occasion, to have been done without visiting the property and looking at neighboring structures. In fact, the engineer stated they were conducting a “cursory peer review”. This particular firm based all of its findings on the premise that the high surge preceded the peak winds; and,
- State Farm had difficulty keeping track of engineer assignments and reports. This was complicated by multiple engineers erroneously being assigned the same claim and/or engineers inspecting the wrong property. Unsigned reports also reached some policyholders prior to being reviewed.

As part of our analysis, examiners compared claims wherein State Farm engaged engineers to perform an assessment with claims where engineers were not engaged. This analysis was performed to measure the payments made to the different groups. A pure analysis of the Special Form 3 and Homeowner policy types revealed the following:

	# Claims	Total Payments	Average Payment
With Engineers	287	\$5,703,703	\$19,874
Without Engineers	381	\$5,114,233	\$13,423
		Difference	\$6,451

The table above includes claims that received payments in mediation. As mediation payments ostensibly did not depend on the engineer report, a purer comparison was made by filtering out claims that received rewards as a result of mediation. The results of this analysis revealed the following:

	# Claims	Total Payments	Average Payment
With Engineers	230	\$3,025,593	\$13,155
Without Engineers	374	\$4,910,921	\$13,131
		Difference	\$24

As seen above, claims with engineers, on an average, did not appear to receive significantly less payment than those with engineer reports, thereby refuting the theory that engineers were used to mitigate State Farm's losses. Viewed conversely, the results also indicate that they did not receive increased payments.

As noted in other parts of this report numerous individuals, including State Farm employees, were examined under oath or interviewed throughout the course of the examination. A common line of questioning used in each interview or examination under oath was the question of whether the individual ever witnessed or was otherwise aware of any instances where engineer reports were used in a fraudulent manner. With the exception of the two "whistleblowers", the answer was consistently "no."

Use of Independent Adjusters

The Company enlisted the assistance of eleven independent adjusting firms to assist in the adjusting of claims resulting from Katrina.

The majority of these companies were involved in handling claims in the lower six counties. During the months subsequent to Katrina and prior to the commencement of the examination, the MID received complaints that claims were often being handled by unqualified, untrained adjusters.

In an effort to investigate the validity of the complaints, the examination team requested that State Farm provide a list of all adjusters that had been released for cause. This was done to attempt to qualify and quantify the impact that unqualified or incompetent adjusters had on the handling of claims in the lower six counties.

Our findings indicated that there were approximately 91 adjusters that were released for various reasons. Approximately 14 of these adjusters were adjusting claims on their first catastrophe assignment. Some of the reasons discovered were as follows: lack of estimating skills; failed to respond to calls from policyholders or were slow to respond; issues with determining the cause of loss; estimates were prepared weeks after the inspections were performed; complaints from policyholders; limited or no photographs were taken to document decisions; failing to keep appointments with policyholders; issues with coverage decisions; and, logging inaccurate, late or minimal information in the claim files.

The 91 adjusters referenced above were assigned thousands of claims. Of these 91 released adjusters, approximately 67 were assigned to coastal offices. Numerous claims

were inspected and closed by these adjusters. This, at a minimum, caused some delays in adjusting these claims and receiving payments.

It did appear that once State Farm detected these problems, the Company took action to release the adjuster from the catastrophe site.

Wind/Water Protocol

Based on sworn testimony from Company officials, Company management, on or about September 13, 2005, finalized the development of its Wind/Water Protocol. The Protocol was developed as "a guide for handling various wind and/or water claims in Louisiana, Mississippi and Alabama." The Protocol outlined the procedures that were to be used for determining coverage where wind and water may have been involved in the loss. This process was developed after certain State Farm management surveyed the damaged area on the Mississippi Gulf Coast where they made note of all the "total loss denials."

The Company acknowledged it had never used a wind/water protocol in previous catastrophes and it was never fully explained why such a protocol was integral to the handling of claims on the Gulf Coast. From testimony obtained from Company officials, there were inconsistencies detected regarding the purpose of the Protocol and the message the document intended to convey. At least one manager stated that he did not believe the WWP expanded coverage while other State Farm managers did view the WWP as an "expansion of coverage". As the Section Manager for the Catastrophe stated, "the way I understand the protocol is it gave us the opportunity to then go out and

identify wind damage even though it may have occurred before, after, or in any sequence with a non-covered event, meaning the surge, and allows us to identify wind damage and pay for it". (The WWP states, in part, "Where wind acts concurrently with flooding to cause damage to the insured property, coverage for the loss exists only under flood coverage, if available.") Another State Farm manager believed it was an "interpretation of the policy that gave more benefits to the policyholder." As seen under the caption "Failure to Pay When There Were Indications of Wind", obviously this was not a Company-wide interpretation because many claims had indications of wind damage and no payments were made for this damage. In other words, the review of the claims files did not support what the Protocol provided regarding how claims were to be handled.

Additionally, some managers saw it only as a "training tool", while various adjusters who were questioned about the WWP stated that they never saw it. One team manager admitted the first time he saw the WWP was "sometime in August or September of '06." With this confusion, it was difficult to determine just how the WWP was used and what the direct effects of it were but the evidence is conclusive that at least some amount of confusion occurred which may have had a detrimental affect on the Company's policyholders.

Anti-Concurrent Causation

Although the Fifth Circuit Court of Appeals (*Tuepker v. State Farm Fire and Casualty*, 507 F.3d 346 (5th Cir.2007)) has ruled that State Farm's Anti-Concurrent Causation (ACC) language is not ambiguous, its application in Katrina claims appeared

confusing, even to its own employees and claims representatives. One State Farm manager who was designated as an expert witness in one case interpreted the clause to say that if water would have taken the whole property that nothing was covered, even if wind got there first and caused damage first. (This appears to corroborate testimony from some claims representatives that if water touched it, wind was not covered.) The State Farm Catastrophe Section Manager stated, "I believe that the anti-concurrent cause language in paragraph 2 of the policy says that if you have a covered event working, you know, in any sequence, before or after, with a non-covered event or noninsured event, then that means that it's not a payable loss". When given a scenario where there was evidence of wind damage to a roof and the structure had surge damage, all from the storm, he stated the roof would be covered. This appeared to be contradictory to his interpretation and further evidence of confusion.

State Farm's letter to the Deputy Commissioner stated that, "when evidence shows that the hurricane winds (or objects driven by those winds) and rains entering the insured premises caused by the hurricane winds proximately caused damage to the insured property, those losses will be covered under the policy, and this will be the case even if flood damage, which is not covered, subsequently occurred."

Inconsistencies relative to payments for wind damage noted in the sample claim files considered with the conflicting interpretations of the ACC noted above, point to a conclusion that there was confusion in the application of the ACC in the handling of Katrina claims in the lower three counties of Mississippi.

Mediation Programs

During the ensuing months following Hurricane Katrina, then Commissioner George Dale recognized that thousands of claims remained unresolved and, in some cases, claims had been denied. He also recognized that there were disparities between the repair estimates of insurers and contractors. Pursuant to the Governor's proclamation of a state of emergency, Commissioner Dale promulgated MID emergency Regulation 2005-2 to establish a mediation process to expedite the handling and closing of claims.

As a result of the success of the MID's Hurricane Katrina Mediation Program, the MID was contacted by U.S. District Judge L. T. Senter, Jr., who was then presiding over most of the Katrina lawsuits in the Southern District of Mississippi. Judge Senter asked the MID to include in this regulation a mediation program for those insureds who had lawsuits pending in his Court. The Commissioner of Insurance thereby adopted MID Regulation 2006-4, which allowed any court of competent jurisdiction to order any party in litigation to participate in the MID mediation program.

According to statistics provided by the American Arbitration Association, as of September 26, 2008, approximately 5,099 cases industry-wide were handled through the MID's Hurricane Katrina Mediation Program with an overall settlement rate of 82%. In addition to these, approximately 369 cases were handled through the federal court mediation program with an overall settlement rate of 52%.

State Farm participated in each of the above mediation programs resulting in the resolution of hundreds of claims. Some of these claims fall under the captions listed above relating to lack of adequate documentation to support a full and thorough

investigation and failing to pay when there were indications of wind. State Farm's payments under these independently initiated programs are duly noted but do not absolve State Farm's duty and responsibilities during the initial claims handling process.

ALLEGATIONS OF FRAUD AND ABUSE

Dating back prior to the commencement of this examination there have been widespread and much publicized allegations of fraud and abuse on behalf of State Farm and some of its partners in regard to the manner in which they handled claims. At the core was the allegation that State Farm, along with certain engineering and adjusting firms, schemed to defraud policyholders by changing engineer reports to conclude that excluded water was the cause of the damage. As part of the examination, the examiners expended an enormous amount of time, effort and resources attempting to determine how these allegations may or may not have affected how policyholders were treated. The findings and conclusions of the examiners in this context are noted above under the appropriate sections.

More specifically, the genesis of these allegations seemed to have begun with "irregularities" noted by Kerri Rigsby and Cori Moran Rigsby (hereinafter referred to as "the Rigsbys" or "the Rigsby sisters") who were assigned to assist State Farm with claims on the Mississippi Gulf Coast. Cori Moran Rigsby testified to the examiners that, "...I knew that the fraud that I had witnessed all revolved around engineering reports." A review of these "irregularities", in and of themselves, revealed that while there may have been questionable decisions made by the Company, they did not appear to be a part of

any scheme to systematically mistreat policyholders. This finding should be considered in context with the "Purpose and Scope" section detailed above.

The veracity of the specific allegations of "widespread fraud and abuse" deteriorated throughout the course of the investigation. Many of the specific allegations were investigated and simply could not be substantiated. The examination team questioned many people, including those individuals specifically identified by the Rigsbys as key witnesses, but none could corroborate the allegations.

The examination team uncovered inconsistencies in the allegations leveled by the Rigsbys. Some of these are illustrated below:

- Testimony was obtained by the examiners indicating that the first "irregularity" identified by the Rigsby sisters was the decision by State Farm to employ engineers on all slab claims. This decision was made shortly after Hurricane Katrina made landfall. Another "irregularity" identified by the Rigsbys was the decision by State Farm to cancel a large amount of engineers who had previously been employed and assigned to claims. This decision was made by mid-October 2005. In late October, when the Rigsby sisters saw two engineer reports with different conclusions on one specific claim, Kerri Rigsby testified under oath, "...that kind of sealed it..." and "I don't know how much more I need to hear to know what is going on." Cori Moran Rigsby testified that, at the time she first saw the second engineer report, she believed someone with State Farm was guilty of criminal or fraudulent activity. However, when questioned by the examiners on this issue, Cori Moran Rigsby

contradicted her previous position. She testified that, “[t]hings became very clear the later and later we came into the whole situation.” When asked, “So it was after February that things become clearer”, she answered, “Yes.” It should be noted that February was when the Rigsbys admittedly met with Richard Scruggs (hereinafter referred to as “Scruggs”). Subsequent testimony from Cori Moran Rigsby regarding the second engineer report indicated that she would not dispute the second report was more accurate than the first. Interestingly, the Rigsbys could not cite to the examiners another single instance of a changed engineer report to support their allegations;

- The examiners questioned both engineers involved in the above instance and each denied the presence of fraud or mistreatment or that they were asked to change these reports to favor the Company. The drafter of the second engineer report specifically denied any pressure by the Company to change his conclusions;
- Despite the concerns relating to “fraud” they had allegedly detected, the Rigsbys testified that they did not notify or contact anyone about the Company’s alleged conduct, other than a relative, until they contacted Richard Scruggs in late February 2006. The Rigsbys never made any attempt to contact the MID. As concerned as they were, they admittedly failed to do anything to stop the alleged fraud and prevent its continuation for almost four months;

- At least by June 2006, the Rigsbys had copied and printed thousands of documents. In an interview in August of 2006 with Michael Kunzelman of the Associated Press, Cori Moran Rigsby was quoted as saying, "I think we have given him [Richard Scruggs] the smoking gun." This statement related to the documents they had collected over a period of months and turned over to Scruggs. In later testimony obtained by the examiners, Cori Moran Rigsby stated, "...if you've been through the papers, you know, there's no smoking gun in the data dump documents." She further testified that her goal for the "data dump" weekend was "...to copy some documents so the investigators would have a place to look when they decided to investigate." As is apparent from a state Grand Jury subpoena that was issued on March 16, 2006, and testimony that the Rigsbys were already meeting with investigators prior to this time, the examiners questioned this logic;
- The Rigsbys initially claimed the reasoning behind their copying and printing documents was to support the allegations of fraud that they believed were being committed by the Company. Testimony later obtained by the examiners revealed that the Rigsbys, no later than March 2006, verbally advised other adjusters working on the catastrophe site that they were gathering information for Richard Scruggs. The documents were said to have been copied for the purpose of assisting him with his Hurricane Katrina clients. These stated reasons do not appear consistent;

- Initial testimony from the Rigsby sisters indicated that the Company's database accessed in June 2006 was done using an engineer roster. However, the Rigsbys later admitted to the examiners, while under oath, that at least one of them used a Hurricane Katrina client list obtained from Richard Scruggs to assist in accessing the State Farm database. There were other inconsistencies noted surrounding the "data dump" event;
- The examiners interviewed numerous witnesses, including State Farm managers, independent adjusters, former adjusters and engineers, some of whom were cited by the Rigsbys as witnesses to the "fraud." None of these offered testimony to corroborate their allegations. This was further supported by statements made by Mississippi Attorney General Jim Hood when he stated, "...after our prosecutors heard three days of testimony before a Jackson County grand jury, the majority of the prosecutors working on this case determined with a high level of certainty that no fact pattern existed that fell squarely within the insurance fraud statute.";
- The Rigsbys asserted as fact that State Farm shredded documents subpoenaed by the grand jury. When questioned about this under oath, neither could cite any specific evidence that this occurred;
- One of the most puzzling series of events that strained the veracity of those making the allegations was the fact that the Rigsbys repeatedly stated under oath that they had not contacted Scruggs until late February 2006. This notwithstanding, Scruggs appeared before the Commissioner of Insurance for

the State of Mississippi and his Deputy Commissioner on December 15, 2005, stating he had a couple of insiders, high ranking State Farm representatives working with him. There have been no other "insiders" identified other than the Rigsby sisters;

- Another fact the examiners concluded as noteworthy was that the Rigsbys had never appeared before a federal grand jury that was investigating State Farm. As much as the examiners were/are not privy to any information related to the grand jury proceedings, the Rigsbys acknowledged this fact under oath; and,
- It should be noted that even though it was common knowledge nationwide that the MID was investigating State Farm's handling of homeowner claims, no one involved was willing to meet with the examiners to lay out their evidence substantiating these fraud allegations.

As discussed in the "Purpose and Scope" section above, the examiners are not fraud investigators. However, the above inconsistencies and the absence of any corroborating evidence developed to date, lead the examiner's to opine that State Farm and its partners did not develop and carry out a plan to mistreat policyholders to the extent claimed by the "whistleblowers."

COMMENTS

Throughout the course of the examination, the examination team experienced difficulties in receiving information from the Company. Although thousands of documents were produced in a timely fashion, the Company, on several occasions, failed to timely comply with information requests from the examination team and often information was provided that was unresponsive and/or insufficient. This occurred despite a standing order to confer with the examination team on any questions relative to the information being requested.

Requests for information were made to engineer firms and independent adjusting firms who were vendors of State Farm. Most of these vendors never responded until a subpoena was issued and only then was the information provided. This caused significant delays in completing the examination.

Based on the media attention surrounding the documents purloined by the Rigsby sisters, the examination team felt compelled to personally review the documents. It was important, at least initially, for the examiners to see the documents in the context in which they were produced. The MID filed a formal motion in the United States District Court in Alabama seeking permission to review the documents which had been turned over to the Court per the December 8, 2006 injunction entered by Judge William M. Acker, Jr. The MID's motion was opposed by the parties, however, the MID obtained permission from the Court following oral arguments to inspect the documents in chambers. Following a detailed review of the purloined documents, it was decided that the MID either already had access to certain documents or the remaining documents were

insignificant to how claims were handled by the Company. There was no “smoking gun” as previously alleged by the Rigsbys.

The examination team requested that State Farm provide copies of the documents purloined by the Rigsby sisters. State Farm responded by advising the examiners that it had no way of determining what documents were copied. In the later part of 2007, the examiners discovered, indirectly, that State Farm had indeed performed an analysis of the claims that the Rigsbys had accessed and had knowledge of exactly which claims and the specific time they had accessed them. Had the examiners been made aware of this, copies of these files could have been requested and reviewed months before the examiners eventually gained access to the documents through the United States District Court in Alabama.

As referenced throughout this report, the examination team conducted many examinations under oath. These were procedures employed by the examination team designed to gather information from individuals, most of whom were directly involved in the claims handling process. These were accomplished by placing the individuals under oath and questioning them about their involvement in the claims handling process. While the majority of these were beneficial and the individual compliant, there were occasions where the witness appeared less than forthright in their testimony. In comparing the testimony given with the information contained in the claim files, it was apparent to the examination team that contradictions existed. When presented with actual claim files, that in the view of the examination team clearly lacked adequate documentation to support a full investigation, some witnesses refused to acknowledge any errors.

SUBSEQUENT RESOLUTION PROCESS

On or about March 6, 2007, the Commissioner of Insurance reached an agreement with State Farm wherein the Company would re-open and re-adjust all Hurricane Katrina homeowner claims in Hancock, Harrison and Jackson counties along the Mississippi Gulf Coast. This agreement was the result of preliminary findings of the MID examination team as well as the withdrawal of a proposed class action settlement. The initial agreement involved "slab claims" only. However, on March 22, 2007, this was extended to include any policyholder in the three counties who requested that their homeowner claim be re-evaluated.

The MID reviewed sample documents such as letters, offer forms and releases which were to be used by the Company to initiate the re-evaluation program. In May 2007, members of the examination team traveled to State Farm's home office in Bloomington, IL to meet with the management team responsible for the implementation of the re-evaluation process. Following this meeting, members of the examination team monitored the re-evaluation program on a daily basis to ensure the program was functioning properly.

Pursuant to this agreement, State Farm sent notices to all known policyholders in the three coastal counties, beginning with those who had "slab claims", stating that in order to have their claim re-evaluated, the policyholder would need to take the affirmative step of returning a written request for re-valuation. As additional notice to the affected policyholders, State Farm published notice of this agreement in media outlets throughout the coastal area.

MID Special Target Examination of State Farm Insurance Companies –Hurricane Katrina Homeowner Claims

At a minimum, State Farm voluntarily committed to the same payments that were part of the proposed class action settlement in the case of *Woullard v. State Farm Fire & Casualty Company*. Policyholders were given the opportunity to provide additional information they would like considered in the re-evaluation of their claim. The agreement further provided that the re-opening and re-evaluation of the claims would be performed by adjusters who had not been a part of the initial adjustment of the claims and that the entire process would be monitored by members of the MID examination team.

The examination team consisted of experienced catastrophe adjusters. As part of the examination process, these adjusters spent months monitoring every re-evaluation to independently verify that the claims were being re-evaluated according to the terms of the agreement. Part of this process involved the examiners communicating with the policyholders and assisting them in maximizing benefits available through the resolution process.

As of the date of this report, State Farm has provided sworn testimony that it has paid in excess of \$88 million to resolve approximately 5,100 claims. The examination team reviewed approximately 4,900 of these claims during the resolution process. This process is ongoing and continues to be monitored by members of the examination team.

In addition, with respect to the 173 claims files in which the examination team identified as lacking adequate documentation to support a full and thorough investigation, State Farm has provided testimony through a sworn affidavit that 118 of these claims have now been resolved through payments totaling \$11 million, either through re-evaluation, mediation or litigation. Relating to the 64 claims files which contained

indications of wind with no homeowner's payments made, State Farm has provided additional testimony to date that 55 of the claims subsequently received payments in the amount of \$7 million. These payments were made following the initial closing of the file and were made outside of the initial claims handling process.