

MARKET CONDUCT EXAMINATION REPORT OF
UNITED FIRE & CASUALTY COMPANY
CEDAR RAPIDS, IOWA
AS OF DECEMBER 31, 2013

Cedar Rapids, Iowa
March 12, 2014

HONORABLE NICK GERHART
Commissioner of Insurance
State of Iowa
Des Moines, Iowa

Commissioner:

In accordance with your authorization and pursuant to Iowa statutory provisions, a market conduct examination has been made of the records, business affairs and marketing practices of the

UNITED FIRE & CASUALTY COMPANY

CEDAR RAPIDS, IOWA

AS OF DECEMBER 31, 2013

at its Home Office, 118 Second Avenue SE, Cedar Rapids, Iowa.

INTRODUCTION

This market conduct examination report, containing applicable comments, explanations and findings, is presented herein. In general, this is a report by exception. Comments regarding practices and procedures reviewed during the examination have been omitted from the report if no improprieties were found.

SCOPE OF EXAMINATION

United Fire & Casualty Company, hereinafter referred to as the "Company", was last examined as of December 31, 2008. This market conduct examination covers the intervening period from January 1, 2009 to the close of business on December 31, 2013 and was conducted by examiners for the Iowa Insurance Division. A general review and survey was made of the Company's marketing operations and treatment of policyholders for statutory compliance during the stated period. Other supporting evidences have been examined and evaluated to the extent deemed necessary.

Concurrently with the examination of the Company, the Company's subsidiary, Addison Insurance Company, was also examined. As business operations are performed for the companies as a whole, market conduct examination procedures have been performed on the companies as a whole and not on an individual company basis.

HISTORY

The Company was incorporated under a perpetual charter as the United Casualty Company on January 2, 1946. An amendment to the Articles of Incorporation, adopted in January of 1950, changed the corporate name to United Fire & Casualty Company and authorization was obtained to write multiple lines of insurance under the provisions of Chapter 515, Code of Iowa.

On February 1, 2012, a reorganization of United Fire & Casualty Company and all the subsidiary/affiliated companies was completed. United Fire Group, Inc. (UFG), an Iowa corporation, replaced UFC as the publicly held corporation. The holders of UFC common stock were issued the same number of shares and same ownership percentage of UFG as they held immediately prior to the reorganization. On February 2, 2012, shares of UFG common stock commenced trading on the NASDAQ Global Select Market under the symbol "UFCS". The directors and executive officers remained the same.

INSURANCE HOLDING COMPANY SYSTEM

United Fire Group, Inc. (UFG) is the Ultimate Parent member of a Holding Company System as defined by Chapter 521A, Code of Iowa. The authorized capital stock of UFG is 75,000,000 shares of common stock having a par value of \$.001, and 10,000,000 share of serial preferred stock having no par value per share. At December 31, 2013, 25,360,893 common shares were outstanding and stockholders' equity totaled \$782,833,000.

An organizational chart identifying the Holding Company System as of December 31, 2013 follows:

- Dee Ann McIntyre (13.59% Owner of United Fire Group, Inc.)
- United Fire Group, Inc. (Iowa Holding Company)
 - United Fire & Casualty Company (IA)**
 - Addison Insurance Company (IA)
 - American Indemnity Financial Corporation
 - Texas General Indemnity Company (CO)
 - Lafayette Insurance Company (LA)
 - Mercer Insurance Group, Inc.
 - Financial Pacific Insurance Group, Inc.
 - Financial Pacific Insurance Company (CA)
 - Mercer Insurance Company (PA)
 - Franklin Insurance Company (PA)
 - Mercer Insurance Company of New Jersey, Inc. (NJ)
 - BICUS Servicers Corporation
 - United Fire & Indemnity Company (TX)
 - United Fire Lloyds (TX)
 - United Life Insurance Company (IA)
 - United Real Estate Holdings, LLC

In 1962, the United Life Insurance Company was formed to offer life insurance facilities to the Company's fire and casualty agents.

September 1979, the Company purchased all the outstanding common stock shares of the Lafayette Insurance Company of New Orleans, Louisiana.

In June 1990, the Company acquired all of the common stock shares of Addison Farmers' Insurance Company of Lombard, Illinois. March 1997, Addison Farmers' Insurance Company changed its name to Addison Insurance Company.

On August 10, 1999 the Company acquired American Indemnity Financial Corporation (AIFC) as a wholly owned subsidiary. AIFC, domiciled in Delaware and based in Texas, was a holding company that was made up of the following regional property and casualty insurance companies: American Indemnity Company (AIC)

domiciled in Texas, United Fire & Indemnity Company, Texas General Indemnity Company, and United Fire Lloyds.

On May 24, 2006, pursuant to a previously adopted plan of sale, American Indemnity Company conducted an extraordinary dividend distribution of net assets (including ownership of UFI and TGI) to its parent company AIFC. Subsequently, AIFC conducted a dividend distribution of assets (including direct ownership of UFI) to the Company. On May 25, 2006, American Indemnity Company was sold as a 'shell' to a third party.

On March 28, 2011, the Company purchased Mercer Insurance Group (Mercer). Mercer offered commercial and personal lines of insurance to businesses and individuals through its insurance subsidiaries: Mercer Insurance Company, Mercer Insurance Company of New Jersey, Inc., Franklin Insurance Company, and Financial Pacific Insurance Company. The transaction was accounted for as a statutory purchase. With capital infusions made in 2012 and 2013 of \$17,375,000 and \$205,000, respectively, the Company's total cost at December 31, 2013 is \$211,804,939.

AFFILIATED COMPANY AGREEMENT

Intercompany Pooling

With the exception of Texas General Indemnity Company, the United Fire Group property/casualty companies are members of an intercompany reinsurance pooling arrangement, with the Company being the lead pooling insurer. Each of the subsidiary participants cede their net premiums, losses, loss adjustment expenses and other underwriting expenses to the Company. The business is accumulated for pooling with unaffiliated reinsurance ceded on the Company's annual statement Schedule F. Each subsidiary records their allocation from the pool as assumed business. Direct and net pooled premiums totaled \$754 and \$723 million, respectively, for 2013.

Pooling participation at December 31, 2013 is as follows:

United Fire & Casualty Company	65%
Addison Insurance Company	4
Financial Pacific Insurance Company	8
Franklin Insurance Company	1
Lafayette Insurance Company	7
Mercer Insurance Company	9
Mercer Insurance Company of New Jersey, Inc.	3
United Fire & Indemnity Company	2
United Fire Lloyds	1

TERRITORY AND PLAN OF OPERATION

The Company holds certificates of authority and is authorized to transact business in 44 U.S. State jurisdictions excluding Hawaii, Maine, Massachusetts, New Hampshire and Vermont. The Company is a qualified reinsurer in Delaware and Rhode Island.

Property and casualty insurance business for the United Fire Group is produced by approximately 1,200 independent agencies and underwritten through six regional offices:

Denver Regional Office	Westminster, CO
East Coast Regional Office	Pennington, NJ and Lock Haven, PA
Great Lakes Regional Office	Cedar Rapids, IA
Gulf Coast Regional Office	Galveston, TX
Midwest Regional Office	Cedar Rapids, IA
West Coast Regional Office	Rocklin, CA

Each regional office is staffed with administrative, claims, loss control, marketing and underwriting personnel to service the policies written. A claims office is also maintained in New Orleans, Louisiana.

While the Company writes both personal and commercial lines, approximately 90% of the premium volume is written in traditional commercial line products.

COMPLAINT HANDLING

The Company has written processes and best practices for complaint handling procedures. Written complaints received by the Company are primarily administered by the regional underwriting and claims managers with records maintained in a central repository. The Company maintains complaint records in accordance with Iowa Administrative Code 191-15.13 (507B).

MARKETING AND SALES

All Company advertising materials are the responsibility of the Corporate Marketing Department and its communications area. Materials are submitted to Legal Compliance for review to ensure they comply with state regulations. A website is also maintained at www.unitedfiregroup.com.

Products are marketed exclusively through independent insurance agencies. The Group offers a competitive commissions program and a profit-sharing plan as incentives for agents to place high-quality property and casualty insurance business.

POLICYHOLDER SERVICES

In addition to the regional offices, the Company maintains policyholder service centers for direct billing, policy and claim inquiries. Representatives are provided training and are subject to regular quality performance reviews. Registered producers and policyholders may utilize online services for policy, billing and claim information.

CLAIM PRACTICES

The Company maintains written processes and best practices for the adjudication of claims. Loss adjusters are provided training and are subject to regular quality performance reviews.

A study, of claim files from the Group, was conducted for a statutory compliance review of unfair trade practices. The sample included 52 property claim payments. A time study was performed which demonstrated that, with the exception of one claim settled through mediation, all of the property claims were acknowledged

within 15 days of receipt of claim notification and payment was made within 30 days of the liability being confirmed and sufficient information was received, in accordance with Iowa Administrative Code 191-15.41 and 15.42 (507B).

DIRECT UNDERWRITING EXPERIENCE

Direct underwriting experience, as taken from data filed with the N.A.I.C. for each of the years, is as follows:

<u>Classification</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>
Premiums earned	<u>\$ 292,563,929</u>	<u>\$ 285,886,398</u>	<u>\$ 301,997,158</u>
<u>Incurred deductions</u>			
Losses incurred	\$ 178,722,588	\$ 160,613,700	\$ 207,028,637
Defense and cost containment	25,453,623	27,558,838	19,418,245
Adjusting and other expenses	25,462,000	21,348,000	26,774,000
Commission and brokerage	46,745,200	47,359,607	51,172,995
Taxes, licenses and fees	6,360,758	5,886,049	6,938,505
Other acquisition expenses	28,636,000	28,423,000	27,071,000
General expenses incurred	<u>9,849,000</u>	<u>9,886,000</u>	<u>16,821,000</u>
Total deductions	<u>\$ 321,229,169</u>	<u>\$ 301,075,194</u>	<u>\$ 355,224,382</u>
Underwriting gain (loss)	<u>\$ (28,665,240)</u>	<u>\$ (15,188,796)</u>	<u>\$ (53,227,224)</u>
<u>Classification</u>	<u>2012</u>	<u>2013</u>	<u>Total</u>
Premiums earned	<u>\$349,649,547</u>	<u>\$405,083,293</u>	<u>\$1,635,180,325</u>
<u>Incurred deductions</u>			
Losses incurred	\$ 176,595,967	\$ 165,182,323	\$ 888,143,215
Defense and cost containment	20,108,968	17,144,020	109,683,694
Adjusting and other expenses	28,605,000	45,317,000	147,506,000
Commission and brokerage	64,210,610	72,330,124	281,818,536
Taxes, licenses and fees	7,992,515	8,709,311	35,887,138
Other acquisition expenses	34,357,000	38,554,000	157,041,000
General expenses incurred	<u>14,073,000</u>	<u>15,021,000</u>	<u>65,650,000</u>
Total deductions	<u>\$ 345,943,060</u>	<u>\$ 362,257,778</u>	<u>\$ 1,685,729,583</u>
Underwriting gain (loss)	<u>\$ 3,706,487</u>	<u>\$ 42,825,515</u>	<u>\$ (50,549,258)</u>

Expressed as the ratio of incurred deductions to premiums earned the percentages are:

	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>Average</u>
<u>Incurred deductions</u>						
Losses incurred	61.1%	56.2%	68.6%	50.5%	40.8%	54.3%
Defense and cost containment	8.7	9.6	6.4	5.8	4.2	6.7
Adjusting and other expenses	8.7	7.5	8.9	8.2	11.2	9.0
Commission and brokerage	16.0	16.6	16.9	18.4	17.9	17.2
Taxes, licenses and fees	2.2	2.1	2.3	2.3	2.2	2.2
Other acquisition expenses	9.8	9.9	9.0	9.8	9.5	9.6
General expenses incurred	<u>3.4</u>	<u>3.5</u>	<u>5.6</u>	<u>4.0</u>	<u>3.7</u>	<u>4.0</u>
Total deductions	<u>109.8%</u>	<u>105.3%</u>	<u>117.6%</u>	<u>98.9%</u>	<u>89.4%</u>	<u>103.1%</u>
Underwriting gain (loss)	<u>-9.8%</u>	<u>-5.3%</u>	<u>-17.6%</u>	<u>1.1%</u>	<u>10.6%</u>	<u>-3.1%</u>

Direct underwriting experience by state, as taken from data filed with the N.A.I.C. for each of the years, is as follows:

State	Five-Year Average Earned Premium	Five-Year Operating Ratio	2013 Earned Premium	2013 Operating Ratio
Alabama	\$ 6,749,180	114.6%	\$ 8,228,312	133.3%
Alaska	3,856	109.1	15,732	30.4
Arizona	1,093,587	81.39	4,252,209	77.44
Arkansas	9,499,233	106.0	13,960,766	97.1
California	31,557	(553.4)	48,757	111.7
Colorado	16,399,518	81.6	17,776,056	61.3
District of Columbia	1,670	111.7	1,500	136.0
Florida	11,214,418	114.6	13,542,465	132.0
Georgia	33,277	194.9	24,090	(72.5)
Idaho	2,792,437	87.6	2,798,565	213.7
Illinois	27,571,908	91.0	30,710,610	68.9
Indiana	6,745,995	106.1	9,102,202	111.3
Iowa	59,655,679	95.4	70,398,188	79.6
Kansas	13,742,415	95.9	15,311,807	97.1
Kentucky	450,515	54.2	501,721	45.0
Louisiana	9,488,273	175.8	11,309,134	72.1
Maryland	9,091	50.7	10,968	56.4
Michigan	524,928	48.1	544,593	60.1
Minnesota	21,856,653	101.5	27,604,253	87.6
Mississippi	2,789,458	113.4	2,867,953	120.8
Missouri	33,844,860	117.8	36,462,433	48.1
Montana	2,700,365	112.2	5,860,663	79.5
Nebraska	17,826,967	106.4	22,387,748	110.3
Nevada	380,777	62.6	192,541	125.6
New Jersey	1,844	1,269.2	1,242	1,013.9
New Mexico	2,311,466	83.1	2,394,791	8.9
New York	376	91.5	-	-
North Carolina	14,977	66.3	8,601	165.7
North Dakota	5,359,787	78.6	5,735,227	74.4
Ohio	265,803	100.5	194,162	161.5
Oklahoma	879,338	130.8	3,051,091	146.4
Oregon	15,202	29.9	1,000	217.2
Pennsylvania	2,792	224.6	7,705	(504.3)
South Carolina	2,347	157.7	1,042	761.7
South Dakota	17,387,388	107.2	19,474,134	120.7
Tennessee	3,228,662	131.7	4,751,997	50.1
Texas	32,724,149	106.3	50,970,793	103.6
Utah	1,181,188	122.7	1,155,333	26.4
Virginia	4,992	93.8	17,082	43.5
Washington	7,611	65.6	4,743	46.5
West Virginia	12,444	55.6	20,348	31.4
Wisconsin	12,606,399	92.4	17,654,986	109.6
Wyoming	5,622,679	80.3	5,725,750	110.6
Totals	\$ 327,036,064	103.1%	\$ 405,083,293	89.4%

CONCLUSION

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

In addition to the undersigned, Dan Mathis, CFE; Bob Wong, CFE and Bouavan Kha, examiners for the Iowa Insurance Division, participated in the examination and preparation of this report.

Respectfully submitted,

/s/ Virginia West
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