

NORTH CAROLINA DEPARTMENT OF INSURANCE
RALEIGH, NORTH CAROLINA

STATE OF NORTH CAROLINA)	BEFORE THE
COUNTY OF WAKE)	COMMISSIONER OF INSURANCE
)	
)	
IN THE MATTER OF:)	ORDER AND
)	FINAL AGENCY DECISION
THE LICENSURE OF)	
RICHARD KERNODLE)	Docket Number: 1901
NPN #17260140)	
Respondent.)	
)	

THIS MATTER was heard on Wednesday, October 17, 2018, by the undersigned Hearing Officer, as designated by the North Carolina Commissioner of Insurance (“Commissioner”) under N.C. Gen. Stat.§58-2-55, pursuant to a Notice of Hearing that was duly served and issued.

The administrative hearing was held in the Albemarle Building, located at 325 North Salisbury Street, Raleigh, Wake County, North Carolina. Assistant Attorney General Rebecca E. Lem represented the North Carolina Department of Insurance, Agent Services Division (hereinafter “Petitioner”). Richard Kernodle (hereinafter, “Respondent”) did not appear.

At the hearing, Holly Reston from North Carolina Farm Bureau Mutual Insurance Company (“Farm Bureau”) and Peter Joseph Wall of the Agent Services Division (“ASD”) of the Department testified for the Petitioner.

The Petitioner offered into evidence Petitioner’s Exhibits 1 – 16, which were admitted into evidence.

After careful consideration of the evidence and arguments presented, and based on the record as a whole, the undersigned Hearing Officer hereby makes the following Findings of Fact and Conclusions of Law:

FINDINGS OF FACT

1. The Notice of Administrative Hearing was properly served on Respondent pursuant to Rule 4 of the North Carolina Rules of Civil Procedure and

N.C. Gen. Stat. §58-2-69(d), scheduling the hearing for August 23, 2018.

2. On August 13, 2018 Petitioner filed a Motion to Continue the hearing to October 17, 2018, due to the medical unavailability of a key witness for the Petitioner. This motion was granted on August 14, 2018, and an Order rescheduling the hearing to October 17, 2018 was served on the Respondent by certified USPS mail.

3. Respondent formerly held a Producer's license with lines of authority for Accident and Health or Sickness, Casualty, Life, Property, and Medicare Supplement Long-Term Care from June 2014 until it expired in February 2018. Additionally, Respondent held a Broker's license from September 2014 until it expired in March 2017.

Testimony of Holly Reston

4. Holly Reston testified for the Petitioner. Holly Reston is an employee of North Carolina Farm Bureau Mutual Insurance Company ("Farm Bureau"), and has been employed there for 25 years. Her current position, which she has held since October 1, 2018, is Senior Executive of Underwriting. Formerly, she held positions with Farm Bureau as Personal Lines Underwriting Manager, Personal Lines Underwriting Supervisor, Commercial Lines Underwriter, and Personal Lines Underwriter.

5. Respondent was a captive agent for Farm Bureau at the Durham County branch location from approximately July 2014 to January 2017. The Durham County Farm Bureau branch location had approximately 6 agents and a manager during the time the Respondent was employed there. Respondent, like other agents at Farm Bureau, was paid on a strictly commissions basis. Agents do not receive base salaries. Farm Bureau's agents have the opportunity to earn production-based bonuses, awards, and other benefits such as award trips (vacations) based on the volume of policies they write.

6. Ms. Reston testified that prior to the time that Respondent's misconduct was discovered, his production levels were very good and he was considered to be a "rising star" in production, and he was recognized regularly in sales meetings for this.

7. Farm Bureau became aware that there might be an issue regarding Respondent in December 2016, and line underwriter Eric Hughes discovered that during the previous 6 weeks, the Respondent had written 6 homeowners policies that had the wrong credit reports attached to them. Mr. Hughes initially had noted irregularities with auto policy credit reports, which led him to look into Respondent's homeowner policies. These homeowner policy applications, which are done completely electronically ("paperless applications"), had attached credit reports to the

applications for persons who were not applying for these policies. Mr. Hughes made his supervisor, Patricia Cantrell, aware of these issues. Ms. Cantrell reported the issues to Ms. Reston, who was the Personal Lines Manager at that time.

8. Ms. Reston wrote a memo on December 20, 2016 and transmitted it to Bob Tart, who at that time was Senior Executive of Underwriting. Mr. Tart became primarily responsible for overseeing Farm Bureau's investigation into the Respondent's conduct. However, Ms. Reston was kept generally aware of the investigation involving the Respondent, and when Mr. Tart went out on medical leave in late July 2018, Ms. Reston took over the role of overseeing the investigation. Ms. Reston received Mr. Tart's file on the Respondent, and also discussed the matter with Mr. Tart. Mr. Tart did not thereafter return to employment with Farm Bureau and has retired, and Ms. Reston has been promoted to his former position as Senior Executive of Underwriting.

9. Ms. Reston testified regarding two types of misconduct engaged in by Respondent during his employment with Farm Bureau. The first related to homeowners policies, and the second to personal auto insurance policies. Both issues involved manipulation of the policy application process.

Homeowner Policy Application Issue

10. Regarding the homeowners policies, Ms. Reston testified that the homeowners application process at Farm Bureau is electronic – meaning that applications are paperless. In order to qualify for a homeowner's policy, an applicant must have a credit score of 650 or above. Insurance agents utilize a software program to order an applicant's credit score, and they attach this documentation electronically to the homeowner's policy application. This is uploaded to the home office, where the underwriter pulls it into the underwriting queue where the application is subject to underwriting rules. Only applications that did not meet the underwriting rules would be flagged for further review. At the time that Respondent was a Farm Bureau agent, as long as the credit report attached to a homeowner's policy application had a score of 650 or above, that application would not be flagged for further review by underwriting.

11. Counsel for the Petitioner noted that evidence presented at the hearing concerning the homeowner's policies included information that included persons' credit scores. As such, the documentation presented was redacted to show only the first letter of individual's last name, their street address, and other identifying information such as their date of birth and driver's license numbers. The first name and last initial were not redacted.

12. The evidence presented at the hearing showed that Respondent was attaching credit reports for people other than the homeowner's policy applicants to homeowner's policy applications where the applicant's actual credit score would disqualify them from being issued a policy. Ms. Reston testified that the persons' credit reports that were attached to these homeowner's policy applications appear to have no relation to the applicants and were strangers to the applicants, with the one exception of an instance where the Respondent attached his own credit report to an application. Ms. Reston testified that there was no way that Respondent could have attached the wrong people's credit reports to applications accidentally.

13. Evidence admitted at the hearing included documentation in the form of screenshots from Farm Bureau's system showing 39 instances where Respondent attached the wrong credit reports to homeowner's policy applications. Respondent first appears to have done this in February 2015, and evidence presented at the hearing shows that he generally increased the rate at which he attached incorrect credit reports to homeowner's policy applications over time. Evidence presented at the hearing showed that during the period of January through June 2016, over 20% of homeowner's policies written by Respondent had incorrect credit reports attached.

14. Evidence admitted at the hearing included 10 detailed examples of documentation from Farm Bureau's records showing the correct credit reports of homeowner policy applicants, and the credit reports for the persons that were actually attached to the applications. These were also cross-referenced with the screenshots that are retained in Farm Bureau's records. In all ten instances, the actual homeowner's applicants had credit scores that did not qualify for issuance of the policies by Farm Bureau. In all ten instances, the credit reports that were attached to the applications belonged to different people who had credit scores that were over 650 and thus did qualify for issuance of a homeowner's policy.

15. Ms. Reston testified that the reason that Farm Bureau provided the Department with only the ten most recent policies' detailed underlying credit reports is because these documents are only retained in Farm Bureau's system for a certain period of time, and further that after this issue was discovered, Farm Bureau purged the incorrect credit reports from their system as they contained other people's confidential credit information.

16. Ms. Reston testified that since this time, Farm Bureau has changed their online homeowner's policy application process so it is no longer possible to attach someone else's credit report to a homeowner's application. Farm Bureau's system now cross-checks to ensure that the homeowner's policy applicant's credit report matches their names in the system.

17. Ms. Reston testified that Respondent clearly financially benefitted from his practice of attaching incorrect credit reports to what would have otherwise been non-qualifying applications, as Respondent was able to sell more policies and hence gain more commissions and other financial incentives than he would have otherwise.

Personal Auto Policy Application Issue

18. Ms. Reston testified that Respondent took advantage of a change to the way auto policy applications were rated that went into effect in 2015 in order to enter incorrect rating zip codes for auto policy applications, allowing Respondent to sell policies for a lower premium than they actually qualified for. Specifically, Ms. Reston noted that prior to October 2015, auto premiums were determined based on a "territory code". However, effective in October 2015, the North Carolina Rate Bureau ("Rate Bureau") instituted a change in which an auto policy premium was based off of the zip code where a vehicle was garaged, referred to in Farm Bureau's system as the "rating zip code".

19. The affidavits of Farm Bureau employees Richard Phillips and Brian Top were admitted. Richard Phillips, a Product Analysis Manager, attached to his affidavit a list of all personal auto policies written by Respondent. Brian Top, an Operations Division Manager, attached to his affidavit a list of 74 policies with incorrect rating zip codes that could only be explained by Respondent entering incorrect rating zip codes. Brian Top's affidavit also included an attached report showing that he had audited other agents in the same office as Respondent and found no incorrect rating zip codes in the 18 policies he reviewed. Ms. Reston testified that she was familiar with the affidavits and had reviewed these in advance.

20. Ms. Reston noted that after the Rate Bureau's change, a rating zip code would be entered for each vehicle on the policy that is supposed to be where the vehicle is principally garaged. These zip codes corresponded to a territory code, and the territory codes were used to determine how much premium was charged.

21. Ms. Reston noted that on a personal auto policy application, which is entered electronically by Farm Bureau's agents, the agent enters both a mailing address for the policyholder and the rating zip code where each vehicle on the policy is garaged. Ms. Reston noted that there are some legitimate reasons why the mailing address zip code may be different from the rating zip code. The most common reason would be where a policyholder uses a PO Box for their mailing address. Another common reason would be if one of the vehicles on the policy belonged to a college student who was away from home, where the rating zip code would be at the location where the college student primarily keeps their car. Additionally, Ms. Reston noted that there is some address correction software, whereby a mailing address zip code may be auto-corrected in the Farm Bureau system and end up being different than

the rating zip code. Typically, however, an auto policy mailing address and rating address should be the same.

22. Documentary evidence presented at the hearing showed that there were 111 policies written by Respondent that had different mailing address and rating address zip codes. Of these, 74 were determined by Farm Bureau to definitively have different mailing address and rating zip code addresses solely due to the Respondent purposefully entering an incorrect rating zip code. In other words, for 74 of the policies written by Respondent, there was no legitimate reason (such as a PO Box, address correction software, etc.) for there to be different mailing address and rating zip codes.

23. Documentary and testimonial evidence presented at the hearing showed that Respondent systematically entered incorrect rating zip codes in order to be able to quote a lower premium to applicants than they would otherwise have qualified for. This allowed him to sell more policies than he would have otherwise.

24. Documentary evidence presented at the hearing showed that Respondent frequently utilized the same set of zip codes for rating zip codes because these resulted in substantially lower premiums. Ms. Reston testified that the difference in premiums between the mailing address zip codes and the incorrectly utilized rating zip codes was large enough to have allowed Respondent to sell substantially more policies than he would have otherwise.

25. Documentary evidence presented at the hearing showed that Respondent systematically and frequently utilized incorrect rating zip codes for auto policies, and that the frequency at which he utilized incorrect rating zip codes increased over time. Respondent first used an incorrect rating zip code on October 15, 2015, two weeks after it first became possible for him to do so due to the Rate Bureau change. Documentary evidence presented at the hearing showed that Respondent utilized incorrect rating zip codes increasingly between October 2015 and his last month of employment in December 2016. During the period of October through December 2016, Respondent utilized incorrect rating zip codes on 46% of the personal auto policies that he wrote. Ms. Reston testified that this high rate of incorrect rating zip code entry could only have been done intentionally, and not accidentally.

26. Documentary evidence presented at the hearing showed that during the course of its investigation, Farm Bureau employee Brian Top randomly audited the auto policy applications of other agents in the same Durham County office as Respondent for December, 2016. There were no zip code errors noted for any of the other agents' policies sampled, leading Farm Bureau to conclude that this practice of using incorrect rating zip codes appeared to be confined to the Respondent.

27. Meeting minutes from a January 26, 2017 internal Farm Bureau meeting were introduced into evidence identifying the issues regarding the Respondent and the corrective measures being taken by Farm Bureau. Ms. Reston testified that once the Respondent's scheme in utilizing incorrect rating zip codes was discovered, policyholders affected received notification that their premiums would be corrected going forward. However, these policyholders were not back-charged for the difference in the premiums they had already paid. Regarding the homeowner policy credit report issue, the incorrect credit reports were purged from the system and the Farm Bureau homeowner's application system was updated to prevent incorrect credit reports from being attached to applications.

Testimony of Peter Joseph Wall

28. Mr. Peter Joseph Wall testified for the Petitioner.

29. Mr. Wall is a Call Center Supervisor and Complaint Analyst with the Agent Services Division of the North Carolina Department of Insurance. Mr. Wall has been a Complaint Analyst for about three years and a Call Center Supervisor for about a year and a half. Previously, Mr. Wall had private insurance experience from 1999 through 2015 in various positions including claims adjuster, underwriting, underwriting auditing, and reinsurance.

30. Mr. Wall's duties, as they relate to the present matter, include reviewing complaints that come in from insurance companies and the NAIC against agents and adjusters. Mr. Wall has been involved in the matters involving the alleged misconduct by Respondent.

31. Mr. Wall reviewed the license screens showing licenses previously held by Respondent, noting that his Producers license is now expired. Mr. Wall explained that due to the seriousness of the allegations against Respondent, Agent Services Division had determined it was necessary to pursue disciplinary action against Respondent even though his license was expired.

32. Mr. Wall reviewed written correspondence regarding the Respondent. Mr. Wall notes that he first became aware of issues regarding alleged misconduct by Respondent in January 2017, when he was forwarded a complaint received by the Department's Criminal Investigation Division that was lodged by Farm Bureau. Mr. Wall contacted Respondent requesting information. Mr. Wall never received the information after repeated requests, and thereafter issued a notice for an informal conference scheduled for May 30, 2017. Respondent did not appear at the informal conference. Mr. Wall called Respondent on May 30, 2017, and was told by the Respondent that he had forgotten about the informal conference. After a discussion,

Respondent informed Mr. Wall that he wanted to surrender his North Carolina insurance licenses. Mr. Wall thereafter sent Respondent the surrender form, but it was never returned.

33. Mr. Wall testified that he had reviewed all of the exhibits introduced during the hearing in advance, and that these included all of the documents previously received by the Agent Services Division. Mr. Wall stated that he had previously also had the opportunity to discuss the allegations against Respondent with both Mr. Tart and Ms. Reston from Farm Bureau.

34. Mr. Wall expressed the opinion that Respondent's actions regarding both the incorrect credit reports attached to the homeowner's policy applications as well as the use of incorrect rating zip codes on the personal auto policy applications constitute purposeful and fraudulent action on the part of the Respondent. Mr. Wall stated that it was his opinion that Respondent was motivated to do this by personal gain in the form of additional commissions payments and other financial incentives, and that this was not harmless behavior on the part of the Respondent. Mr. Wall explained that the insurance industry depends on accurate actuarial calculations of risk based on multiple factors. The rating zip codes on auto policies and an individual's credit score on a homeowner's policy are examples of such factors. Mr. Wall explained that by introducing incorrect information about these risk factors on applications, this undermined the actuarial foundations of the insurance industry and exposed Farm Bureau to greater financial risk levels than the premiums it received would support. This risks the solvency of Farm Bureau.

CONCLUSIONS OF LAW

1. This matter is properly before the North Carolina Commissioner of Insurance (hereinafter "Commissioner"), and the Commissioner has jurisdiction over the parties and the subject matter pursuant to N. C. Gen. Stat. §§ 58-2-55, 58-33-46, 150B-38 and 150-40, as well as 11 N.C.A.C. 10401 *et seq.* and other applicable statutes and regulations.

2. Pursuant to N.C. Gen. Stat. 58-33-46(f), the Commissioner has the authority to enforce the provisions of Chapter 58 against any person under investigation for violation of Chapter 58, even if the person's license has lapsed. Based on the seriousness of the allegations against the Respondent, it is appropriate to proceed with disciplinary action against the Respondent.

3. Respondent was properly served with the Notice of Hearing and the Motion and Order of Continuance in this matter.

4. Respondent's actions in attaching incorrect credit reports to 39 homeowner's policy applications are violations of N.C. Gen. Stat. § 58-33-46(a)(8), in that Respondent used fraudulent and dishonest practices and demonstrated untrustworthiness and financial irresponsibility in the conduct of this State's business, as this practice allowed Respondent to write homeowner's insurance policies for which the applicants were not qualified.

5. Respondent's actions in attaching incorrect credit reports to 39 homeowner's policy applications are violations of N.C. Gen. Stat. § 58-33-105, as they constituted a false representation on an application for insurance, and this was done for the purpose of Respondent gaining commissions, money or benefits from Farm Bureau.

6. Respondent's actions in attaching incorrect credit reports to 39 homeowner's policy applications are violations of N.C. Gen. Stat. § 58-33-46(a)(4), in that he was paid commissions and other benefits from Farm Bureau to which he was not entitled by selling policies that the applicants should not have qualified for, hence misappropriating or converting monies from Farm Bureau. Furthermore, Respondent misused the credit reports of persons who were not applying for homeowner's policies by improperly attaching them to other people's homeowner policy applications for purposes of Respondent's own financial gain, also in violation of N.C. Gen. Stat. § 58-33-46(a)(4).

7. Respondent's actions in utilizing incorrect rating zip codes on 74 personal auto policy applications are violations of N.C. Gen. Stat. § 58-33-46(a)(8), in that Respondent used fraudulent and dishonest practices and demonstrated untrustworthiness and financial irresponsibility in the conduct of this State's business, as this practice allowed Respondent to quote lower premiums than applicants actually qualified for and thus write more auto insurance business.

8. Respondent's actions in utilizing incorrect rating zip codes on 74 personal auto policy applications are violations of N.C. Gen. Stat. § 58-33-105, as they constituted a false representation on an application for insurance, and this was done for the purpose of Respondent gaining commissions, money or benefits from Farm Bureau by selling more auto policies than he would have otherwise by quoting lower premiums than applicants actually qualified for.

9. Respondent's actions in utilizing incorrect rating zip codes on 74 personal auto policy applications are violations of N.C. Gen. Stat. § 58-33-46(a)(4), in that he was paid commissions and other benefits from Farm Bureau to which he was not entitled by selling policies that the applicants should not have qualified for, hence misappropriating or converting monies from Farm Bureau.

10. Respondent's actions both in attaching incorrect credit reports to homeowner's policy applications and by utilizing incorrect rating zip codes on personal auto policy applications show a pattern of deliberate, systematic behavior intended to personally benefit the Respondent by allowing him to sell more policies than he would have otherwise, which directly resulted in financial benefit to him in the form of commissions. Additionally, Respondent gained additional financial benefits from writing a large volume of business in the form of monetary bonuses.

11. Respondent's violations of N.C. Gen. Stat. §§ 58-33-46(a)(4), 58-33-46(a)(8), and 58-33-105 as described above are violations of the insurance laws pursuant to N.C. Gen. Stat. § 58-33-46(a)(2) for which his license may be revoked.

12. Given the seriousness of Respondent's actions in attaching incorrect credit reports to homeowner's policy applications and utilizing incorrect rating zip codes on personal auto policy applications for his own financial gain, it is appropriate to permanently revoke Respondent's licenses issued by the Department.

ORDER

Based upon the foregoing Findings of Fact and Conclusions of Law, it is ORDERED that the Respondent's licenses issued by the Department be REVOKED.

APPEAL RIGHTS

Under the provisions of N.C. Gen. Stat. § 150B-45, any party wishing to appeal a final decision of the North Carolina Department of Insurance must file a Petition for Judicial Review in the Superior Court of the County where the person aggrieved by the administrative decision resides, or in the case of a person residing outside the State, the county where the contested case which resulted in the final decision was filed. The appealing party must file the petition within 30 days after being served with a written copy of the Order and Final Agency Decision. In conformity with the 11 NCAC 1.0413 and N.C.G.S. § 1A-1, Rule 5, this Order and Final Agency Decision was served on the parties on the date it was placed in the mail as indicated by the date on the Certificate of Service attached to this Order and Final Agency Decision. N.C. Gen. Stat. § 150B-46 describes the contents of the Petition and requires service of the Petition on all parties. The mailing address to be used for service on the Department of Insurance is: **A. John Hoomani, General Counsel, 1201 Mail Service Center, Raleigh, NC 27699-1201.**

This the 29th day of October, 2018.



Meghan Cook
Hearing Officer
N.C. Department of Insurance

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that I have this day served the foregoing **ORDER AND FINAL AGENCY DECISION** by mailing a copy of the same via certified U.S. mail, return receipt requested; via first class U.S. mail to the licensee at the address provided to the Commissioner pursuant to N.C. Gen. Stat. § 58-2-69(b); and via State Courier to Attorney for Petitioner, addressed as follows:

Richard Kernodle
3738 Lindsey Woods Rd
Hillsborough, NC 27278
(Respondent)

Certified Mail Tracking Number: 70170530000073186156

Rebecca E. Lem
Assistant Attorney General
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This the 29th day of October, 2018.


Mary Faulkner
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