

**REPORT OF
MARKET CONDUCT EXAMINATION
OF**

**DONEGAL MUTUAL INSURANCE COMPANY
ATLANTIC STATES INSURANCE COMPANY
Marietta, Pennsylvania**

**AS OF
January 2, 2008**

COMMONWEALTH OF PENNSYLVANIA

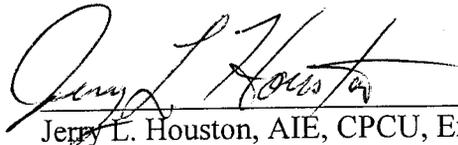


**INSURANCE DEPARTMENT
MARKET CONDUCT DIVISION**

Issued: February 29, 2008

VERIFICATION

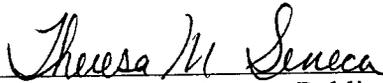
Having been duly sworn, I hereby verify that the statements made in the within document are true and correct to the best of my knowledge, information and belief. I understand that false statements made herein are subject to the penalties of 18 Pa. C.S. §4903 (relating to false swearing).



Jerry L. Houston, AIE, CPCU, Examiner-In-Charge

Sworn to and Subscribed Before me

This *10* Day of *September*, 2007



Notary Public

COMMONWEALTH OF PENNSYLVANIA
NOTARIAL SEAL
THERESA M. SENECA, Notary Public
City of Harrisburg, Dauphin County
My Commission Expires Aug. 15, 2010

**DONEGAL MUTUAL INSURANCE COMPANY
ATLANTIC STATES INSURANCE COMPANY**

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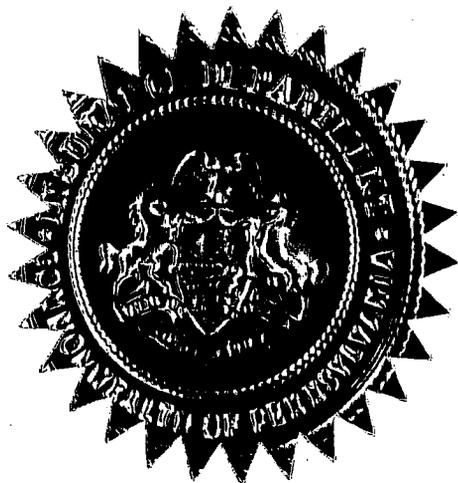
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BEFORE THE INSURANCE COMMISSIONER
OF THE
COMMONWEALTH OF PENNSYLVANIA

ORDER

AND NOW, this 6th day of July, 2007, in accordance with

Section 905(c) of the Pennsylvania Insurance Department Act, Act of May 17, 1921, P.L. 789, as amended, P.S. § 323.5, I hereby designate Randolph L. Rohrbaugh, Deputy Insurance Commissioner, to consider and review all documents relating to the market conduct examination of any company and person who is the subject of a market conduct examination and to have all powers set forth in said statute including the power to enter an Order based on the review of said documents. This designation of authority shall continue in effect until otherwise terminated by a later Order of the Insurance Commissioner.





Joel S. Ario
Insurance Commissioner

BEFORE THE INSURANCE COMMISSIONER
OF THE
COMMONWEALTH OF PENNSYLVANIA

IN RE:	VIOLATIONS:
DONEGAL MUTUAL INSURANCE COMPANY	Sections 641-A and 671-A of Act 147 of 2002 (40 P.S. §§ 310.41 and 310.71)
ATLANTIC STATES INSURANCE COMPANY	Section 903(a) of the Insurance Department Act, Act of May 17, 1921, P.L. 789, No. 285 (40 P.S. § 323.3)
1195 River Road	
Marietta, PA 17547	Sections 4(a) and 4(h) of the Act of June 11, 1947, P.L. 538, No. 246 (40 P.S. §§ 1184)
	Act 1990-6, Section 1793(b) (40 P.S. § 1793)
	Sections 2003(b), 2004, 2006(2) and 2008(b) of Act 68 of 1998 (40 P.S. §§991.2003, 2004, 2006 and 2008)
	Sections 1, 2(1), 3(a)(1), 3(a)(2), 3(a)(3) and 3(a)(5) of the Act of July 3, 1986, P.L. 396, No. 86 (40 P.S. §§ 3401, 3402 and 3403, 3404)
	Sections 5(a)(4) and 5(a)(9) of the Unfair Insurance Practices Act, Act of July 22, 1974, P.L. 589, No. 205 (40 P.S. §§ 1171.5)
	Sections 506.1 and 653 of the Insurance Company Law, Act of May 17, 1921, P.L. 682, No. 284 (40 P.S. §§ 636.1 and 813)
	Title 31, Pennsylvania Code, Sections 113.88, 146.5(b) and (d), 146.6 and 146.7(a)(1)

Respondent. : Title 18, Pennsylvania Consolidated Statutes, Section 4117(k)
: Pennsylvania Assigned Risk Plan Manual, Sections 12(A)(13) and 16.A.4
: Docket No. MC08-01-003

CONSENT ORDER

AND NOW, this 29th day of February, 2008, this Order is hereby issued by the Insurance Department of the Commonwealth of Pennsylvania pursuant to the statutes cited above and in disposition of the matter captioned above.

1. Respondent hereby admits and acknowledges that it has received proper notice of its rights to a formal administrative hearing pursuant to the Administrative Agency Law, 2 Pa.C.S. § 101, et seq., or other applicable law.

2. Respondent hereby waives all rights to a formal administrative hearing in this matter, and agrees that this Consent Order shall have the full force and effect of an order duly entered in accordance with the adjudicatory procedures set forth in the Administrative Agency Law, supra, or other applicable law.

3. Without admitting the allegations of fact and conclusions of law contained herein, Respondent specifically denies that it violated any law or regulation of the Commonwealth.

FINDINGS OF FACT

4. The Insurance Department finds true and correct each of the following

Findings of Fact:

- (a) Respondent is Donegal Mutual Insurance Company and Atlantic States Insurance Company, and maintains its address at 1195 River Road, Marietta, Pennsylvania 17547.
- (b) A market conduct examination of Respondent was conducted by the Insurance Department covering the period from July 1, 2005 through June 30, 2006.
- (c) On January 2, 2008, the Insurance Department issued a Market Conduct Examination Report to Respondent.
- (d) A response to the Examination Report was provided by Respondent on February 1, 2008.
- (e) The Examination Report notes violations of the following:
 - (i) Section 641.1-A of Act 147 of 2002 prohibits any entity or the appointed agent of any entity from transacting the business of insurance through anyone acting without an insurance producer license (40 P.S. § 310.41a);

- (ii) Section 671-A of Act 147 of 2002 prohibits producers from transacting business within this Commonwealth without written appointment as required by the Act (40 P.S. § 310.71).

- (iii) Section 903(a) of the Insurance Department Act, No. 285 (40 P.S. § 323.3), which requires every company subject to examination keep all records and documents relating to its business in such manner as may be required in order that the Department may verify whether the company has complied with the laws of this Commonwealth;

- (iv) Sections 4(a) and 4(h) of the Casualty and Surety Rate Regulatory Act, No. 246 (40 P.S. § 1184), which requires every insurer to file with the Insurance Commissioner every manual of classifications, rules and rates, every rating plan and every modification of any rating plan which it proposes to use in this Commonwealth and prohibits an insurer from making or issuing a contract or policy with rates other than those approved;

- (v) Section 1793(b) of Act 1990-6, Title 75, Pa. C.S. § 1793, which requires the insurer to provide to the insured a surcharge disclosure plan. The insurer providing the surcharge disclosure plan shall detail the provisions of the plan and shall deliver the plan to each insured at least once annually. Additionally, the surcharge information plan shall be given to each

prospective insured at the time application is made for motor vehicle insurance coverage;

(vi) Section 2003(b) of Act 68 of 1998 (40 P.S. § 991.2003), which states that an insurer may not cancel or refuse to renew a policy of automobile insurance on the basis of one accident within the 36 month period prior to the upcoming anniversary date of the policy;

(vii) Section 2004 of Act 68 of 1998 (40 P.S. § 991.2006), which requires that no insurer shall cancel a policy of automobile insurance except for nonpayment of premium, suspension or revocation of the named insured's driver license or motor vehicle registration or a determination that the insured has concealed a material fact or has made a material allegation contrary to fact or has made a misrepresentation of material fact and that such concealment, allegation or misrepresentation was material to the acceptance of the risk by the insurer;

(viii) Section 2006(2) of Act 68 of 1998 (40 P.S. § 991.2006), which requires an insurer to deliver or mail to the named insured a nonrenewal notice and state the date, not less than 60 days after the date of the mailing or delivery, on which cancellation shall become effective. When the policy is being

cancelled for nonpayment of premium, the effective date may be 15 days from the date of mailing or delivery;

(ix) Section 2008(b) of Act 68 of 1998 (40 P.S. § 991.2008), which requires any applicant for a policy who is refused such policy by an insurer shall be given a written notice of refusal to write by the insurer. Such notice shall state the specific reason or reasons of the insurer for refusal to write a policy for the applicant. Within 30 days of the receipt of such reasons, the applicant may request in writing to the Commissioner that he review the action of the insurer in refusing to write a policy for the applicant;

(x) Section 1 of Act 86 (40 P.S. § 3401), which requires a policy of insurance covering property or casualty risks in this Commonwealth shall provide for not less than 30 days advance notice to the named insured of an increase in renewal premium;

(xi) Section 2 of Act 86 (40 P.S. § 3402), which state canceling in midterm a policy of insurance covering commercial property and casualty risks is prohibited for any reason other than the following:

(1) A condition, factor or loss experience material to insurability has changed substantially or a substantial condition, factor or loss experience material to insurability has become known during the policy term.

- (xii) Section 3(a)(1) of Act 86 (40 P.S. § 3403), which requires that a nonrenewal notice be forwarded by registered or first class mail, or delivered by the insurance company directly to the named insured or insureds;
- (xiii) Section 3(a)(2) of Act 86 (40 P.S. § 3403), which requires that a nonrenewal notice be forwarded directly to the named insured or insureds at least 60 days in advance of the effective date of the termination;
- (xiv) Section 3(a)(3) of Act 86 (40 P.S. § 3403), which requires that a cancellation notice shall provide at least 60 days advance notice of the effective date of cancellation, whichever is less;
- (xv) Section 3(a)(5) of Act 86 (40 P.S. § 3403), which requires that a nonrenewal notice state the specific reasons for the nonrenewal, identifying the condition, factor or loss experience which caused the nonrenewal;
- (xvi) Section 5(a)(4) of Act 205 (40 P.S. § 1171.5), which prohibits entering into any agreement to commit, or by a concerted action committing, any act of boycott, coercion or intimidation resulting in or tending to result in unreasonable restraint of or monopoly in the business of insurance;

(xvii) Section 5(a)(9) of Act 205 (40 P.S. §1171.5), which defines an unfair act or practice as: (9) cancelling any policy of insurance covering owner-occupied private residential properties or personal property of individuals that has been in force for 60 days or more or refusing to renew any such policy unless the policy was obtained through material misrepresentation, fraudulent statements, omissions or concealment of fact material to the acceptance of the risk or to the hazard assumed by the company; or there has been a substantial change or increase in hazard in the risk assumed by the company subsequent to the date the policy was issued; or there is a substantial increase in hazards insured against by reason of willful or negligent acts or omissions by the insured; or the insured has failed to pay any premium whether such premium is payable directly to the company or its agent or indirectly under any premium finance plan or extension of credit; or for any other reasons approved by the Commissioner pursuant to rules and regulations promulgated by the Commissioner. No cancellation or refusal to renew by any person shall be effective unless a written notice of the cancellation or refusal to renew is received by the insured whether at the address shown in the policy or at a forwarding address;

(xviii) Section 506.1 of the Insurance Company Law (40 P.S. § 636.1), which requires basic property insurance to be continued 180 days after the death of the named insured, or until the sale of the property;

- (xix) Section 653 of the Insurance Company Law, which states except for non-payment of premium, no policy of insurance issued or renewed against liability under PA Workers Compensation Act may be cancelled or terminated by an insurer during the term of the policy;

- (xx) Title 31, Pennsylvania Code, Section 113.88, which requires the reason given for cancellation shall be clear and complete. It shall be stated so that a person of average intelligence and education can understand it. Phrases such as “losses” or “underwriting reasons” are not sufficiently specific reasons for cancellation.

- (xxi) Title 31, Pennsylvania Code, Section 146.5(b), which requires every insurer, upon receipt of any inquiry from the Department respecting a claim shall, within 15 working days of receipt of such inquiry, furnish the Department with an adequate response to the inquiry;

- (xxii) Title 31, Pennsylvania Code, Section 146.5(d), requires an insurer, upon receiving notification of a claim, shall provide within ten working days necessary claim forms, instructions and reasonable assistance so that first-party claimants can comply with policy conditions and reasonable requirements of the insurer;

(xxiii) Title 31, Pennsylvania Code, Section 146.6, requires that every insurer shall complete investigation of a claim within 30 days after notification of the claim, unless such investigation cannot reasonably be completed within 30 days, and every 45 days thereafter, the insurer shall provide the claimant with a reasonable written explanation for the delay and state when a decision on the claim may be expected;

(xxiv) Title 31, Pennsylvania Code, Section 146.7(a)(1), which requires within 15 working days after receipt by the insurer of properly executed proofs of loss, the first-party claimant shall be advised of the acceptance or denial of the claim by the insurer. No insurer shall deny a claim on the grounds of a specific policy provision, condition or exclusion unless reference to such provision, condition or exclusion is included in the denial. The denial must be given to the claimant in writing and the claim file of the insurer shall contain a copy of the denial;

(xxv) Title 18, Pennsylvania Consolidated Statutes, Section 4117(k), which requires all applications for insurance and all claim forms shall contain or have attached thereto the following notice: "Any person who knowingly and with intent to defraud any insurance company or other person files an application for insurance or statement of claim containing any materially false information or conceals for the purpose of misleading, information

concerning any fact material thereto commits a fraudulent insurance act, which is a crime and subjects such person to criminal and civil penalties.”

(xxvi) The Pennsylvania Assigned Risk Plan Manual, Section 12(A)(13), which states the assigned company shall mail a take-out notice to each insured eligible for take-out and the producer of record at least 45 days, but no more than 60 days, prior to the expiration of the Plan policy to be replaced. The take-out notice shall contain a provisional premium quotation for the voluntary market coverage being offered; and

(xxvii) The Pennsylvania Assigned Risk Plan Manual, Section 16.A.4, which states at least 60 calendar days prior to the expiration date of the final renewal, the Company shall notify the insured that the period of assignment under the Plan will terminate on said expiration date, and a copy of such notice shall be sent to the producer of record.

CONCLUSIONS OF LAW

5. In accord with the above Findings of Fact and applicable provisions of law, the Insurance Department makes the following Conclusions of Law:

(a) Respondent is subject to the jurisdiction of the Pennsylvania Insurance Department.

(b) Respondent's violations of Sections 641-A and 671-A of Act 147 of 2002 are punishable by the following, under Section 691-A of Act 147 of 2002 (40 P.S. § 310.91):

- (i) suspension, revocation or refusal to issue the certificate of qualification or license;
- (ii) imposition of a civil penalty not to exceed five thousand dollars (\$5,000.00) for every violation of the Act;
- (iii) an order to cease and desist; and
- (iv) any other conditions as the Commissioner deems appropriate.

(c) Respondent's violations of Sections 4(a) and (h) of the Casualty and Surety Rate Regulatory Act, No. 246 (40 P.S. § 1184) are punishable under Section 16 of the Casualty and Surety Rate Regulatory Act:

- (i) imposition of a civil penalty not to exceed \$50 for each violation or not more than \$500 for each such wilful violation;
- (ii) suspension of the license of any insurer which fails to comply with an Order of the Commissioner within the time limited by such Order, or any extension thereof which the Commissioner may grant.

(d) Respondent's violations of Sections 2003, 2004, 2006 and 2008 of Act 68 of 1998 are punishable by the following, under Section 2013 of the Act (40 P.S. § 991.2013): Any individual or insurer who violates any of the provisions of this article may be sentenced to pay a fine not to exceed five thousand dollars (\$5,000.00).

(e) Respondent's violations of Sections 1 and 3 of Act 86 (40 P.S. §§ 3401 and 3403) are punishable under Section 8 (40 P.S. § 3408) of this act by one or more of the following causes of action:

- (i) Order that the insurer cease and desist from the violation.
- (ii) Impose a fine or not more than \$5,000 for each violation.

(f) Respondent's violations of Sections 5(a)(4) and 5(a)(9) of the Unfair Insurance Practices Act, No. 205 (40 P.S. §§ 1171.5) are punishable by the following, under Section 9 of the Unfair Insurance Practices Act (40 P.S. § 1171.9):

- (i) cease and desist from engaging in the prohibited activity;
- (ii) suspension or revocation of the license(s) of Respondent.

(g) In addition to any penalties imposed by the Commissioner for Respondent's violations of the Unfair Insurance Practices Act (40 P.S. §§ 1171.1 –

1171.5), the Commissioner may, under Sections 10 and 11 of the Unfair Insurance Practices Act (40 P.S. §§ 1171.10, 1171.11) file an action in which the Commonwealth Court may impose the following civil penalties:

- (i) for each method of competition, act or practice which the company knew or should have known was in violation of the law, a penalty of not more than five thousand dollars (\$5,000.00);
 - (ii) for each method of competition, act or practice which the company did not know nor reasonably should have known was in violation of the law, a penalty of not more than one thousand dollars (\$1,000.00).
- (h) Respondent's violations of Section 506.1 of the Insurance Company Law, No. 284 (40 P.S. § 636.1) are punishable by the following, under 40 Purdon's Statutes, Section 637, by one or more of the following causes of action:
- (i) Suspend or revoke the license of such offending person or entity.
 - (ii) Refuse for a period not to exceed one year, to issue a new license to such offending person or entity.
- (i) Violation of Section 653 of The Insurance Company Law (40 P.S. §813) is punishable by the following, under Section 655 of The Insurance Company

Law (40 P.S. § 815), which states the Commissioner shall have the power to suspend or revoke the license of any insurance company which violates any of the provisions of subdivision (d) of this article.

- (j) Respondent's violations of Title 31, Pennsylvania Code, Section 146.5(b), (d), 146.6 and 146.7(a)(1) are punishable under Section 9 of the Unfair Insurance Practices Act (40 P.S. § 1171.9), as cited above.

ORDER

6. In accord with the above Findings of Fact and Conclusions of Law, the Insurance Department orders and Respondent consents to the following:

- (a) Respondent shall cease and desist from engaging in the activities described herein in the Findings of Fact and Conclusions of Law.
- (b) Respondent shall file an affidavit stating under oath that it will provide each of its directors, at the next scheduled directors meeting, a copy of the adopted Report and related Orders. Such affidavit shall be submitted within thirty (30) days of the date of this Order.
- (c) Respondent shall comply with all recommendations contained in the attached Report.

(d) Respondent shall pay Thirty Thousand Dollars (\$30,000.00) to the Commonwealth of Pennsylvania in settlement of all violations contained in the Report.

(e) Payment of this matter shall be made by check payable to the Commonwealth of Pennsylvania. Payment should be directed to Sharon L. Fraser, Office Manager, Bureau of Enforcement, 1227 Strawberry Square, Harrisburg, Pennsylvania 17120. Payment must be made no later than thirty (30) days after the date of this Order.

7. In the event the Insurance Department finds that there has been a breach of any of the provisions of this Order, based upon the Findings of Fact and Conclusions of Law contained herein may pursue any and all legal remedies available, including but not limited to the following: The Insurance Department may enforce the provisions of this Order in the Commonwealth Court of Pennsylvania or in any other court of law or equity having jurisdiction; or the Department may enforce the provisions of this Order in an administrative action pursuant to the Administrative Agency Law, supra, or other relevant provision of law.

8. Alternatively, in the event the Insurance Department finds that there has been a breach of any of the provisions of this Order, the Department may declare this Order to

be null and void and, thereupon, reopen the entire matter for appropriate action pursuant to the Administrative Agency Law, supra, or other relevant provision of law.

9. In any such enforcement proceeding, Respondent may contest whether a breach of the provisions of this Order has occurred but may not contest the Findings of Fact and Conclusions of Law contained herein.

10. Respondent hereby expressly waives any relevant statute of limitations and application of the doctrine of laches for purposes of any enforcement of this Order.

11. This Order constitutes the entire agreement of the parties with respect to the matters referred to herein, and it may not be amended or modified except by an amended order signed by all the parties hereto.

12. This Order shall be final upon execution by the Insurance Department. Only the Insurance Commissioner or a duly authorized delegate is authorized to bind the Insurance Department with respect to the settlement of the alleged violations of law

contained herein, and this Consent Order is not effective until executed by the Insurance Commissioner or a duly authorized delegee.

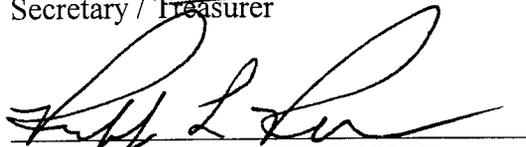
BY: DONEGAL MUTUAL INSURANCE
COMPANY and ATLANTIC STATES
INSURANCE COMPANY, Respondent



President / ~~Vice President~~



Secretary / Treasurer



RANDOLPH L. ROHRBAUGH
Deputy Insurance Commissioner
Commonwealth of Pennsylvania

I. INTRODUCTION

The market conduct examination was conducted at Donegal Mutual Insurance Company and Atlantic States Insurance Company's office located in Marietta, Pennsylvania, from February 28, 2007, through April 6, 2007. Subsequent review and follow-up was conducted in the office of the Pennsylvania Insurance Department.

Pennsylvania Market Conduct Examination Reports generally note only those items to which the Department, after review, takes exception. However, the Examination Report may include management recommendations addressing areas of concern noted by the Department, but for which no statutory violation was identified. This enables Company management to review those areas of concern in order to determine the potential impact upon Company operations or future compliance. A violation is any instance of Company activity that does not comply with an insurance statute or regulation. Violations contained in the Report may result in imposition of penalties.

In certain areas of review listed in this Report, the examiners will refer to "error ratio." This error ratio is calculated by dividing the number of policies with violations by the total number of policies reviewed. For example, if 100 policies are reviewed and it is determined that there are 20 violations on 10 policies, the error ratio would be 10%.

Throughout the course of the examination, Company officials were provided with status memoranda, which referenced specific policy numbers with citation to each section of law violated. Additional information was requested to clarify apparent violations. An exit conference was conducted with Company personnel to discuss

the various types of violations identified during the examination and review written summaries provided on the violations found.

The courtesy and cooperation extended by the officers and employees of the Company during the course of the examination is hereby acknowledged.

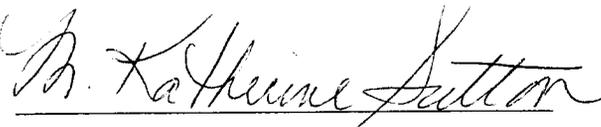
The undersigned participated in this examination and in preparation of this Report.



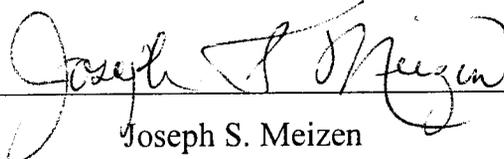
Chester A. Derk, Jr., AIE, HIA
Market Conduct Division Chief



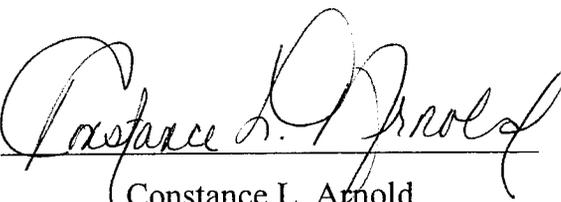
Jerry L. Houston, AIE, CPCU
Market Conduct Examiner



M. Katherine Sutton, AIC
Market Conduct Examiner



Joseph S. Meizen
Market Conduct Examiner



Constance L. Arnold
Market Conduct Examiner

II. SCOPE OF EXAMINATION

The Market Conduct Examination was conducted on Donegal Mutual Insurance Company and Atlantic States Insurance Company, hereinafter referred to as "Company," at their office located in Marietta, Pennsylvania. The examination was conducted pursuant to Sections 903 and 904 (40 P.S. §§323.3 and 323.4) of the Insurance Department Act and covered the experience period of July 1, 2005, through June 30, 2006, unless otherwise noted. The purpose of the examination was to determine the Company's compliance with Pennsylvania insurance laws and regulations.

The examination focused on Company operations in the following areas:

1. Private Passenger Automobile
 - Underwriting – Appropriate and timely notices of nonrenewal, midterm cancellations, 60-day cancellations and declinations.
 - Rating – Proper use of all classification and rating plans and procedures.

2. Assigned Risk Automobile
 - Underwriting – Appropriate and timely notices of nonrenewal and midterm cancellations.
 - Rating – Proper use of all classification and rating plans and procedures.

3. Property
 - Underwriting – Appropriate and timely notices of nonrenewal, midterm cancellations and 60-day cancellations.
 - Rating – Proper use of all classification and rating plans and procedures.

4. Commercial Property

- Underwriting – Appropriate and timely notices of nonrenewal, midterm cancellations, 60-day cancellations, declinations and renewals.

5. Commercial Automobile

- Underwriting – Appropriate and timely notices of nonrenewal, midterm cancellations, 60-day cancellations, declinations and renewals.

6. Workers' Compensation

- Underwriting – Appropriate and timely notices of nonrenewal, midterm cancellations, 60-day cancellations and renewals.

7. Claims

8. Forms

9. Advertising

10. Complaints

11. Licensing

III. COMPANY HISTORY AND LICENSING

Donegal Mutual Insurance Company was incorporated on May 13, 1889, under the laws of Pennsylvania with the title Donegal & Conoy Mutual Fire Insurance Company. The present name was adopted on January 16, 1950. The Company absorbed by merger The Laurel State Mutual Insurance Company and The Reading Mutual Insurance Company, both of Wyomissing, Pennsylvania, as of December 30, 1976.

The Company obtained managerial control of the Southern Mutual Insurance Company of Irvington, Virginia as of September 1, 1984, through the purchase of surplus notes and a management contract. Effective December 31, 1988, Southern Mutual converted to a stock company, was purchased by Donegal Group Inc., and changed its name to Southern Insurance Company of Virginia.

As of March 31, 1993, the Company acquired financial control of Pioneer Insurance Company, formerly Pioneer Mutual Insurance Company. On that date, Pioneer demutualized and the Company acquired 100% of the outstanding stock. The Company had originally assumed managing control of Pioneer Mutual on April 3, 1992, when the Company purchased a surplus note issued by Pioneer Mutual Insurance Company. On March 31, 1997, Pioneer was purchased by Donegal Group, Inc. On May 8, 2002, Pioneer merged into Atlantic States Insurance Company.

As of January 10, 1992, the Company acquired financial control of Delaware Mutual Insurance Company, through the purchase of a surplus note. In conjunction with the purchase of the note, the Company assumed managerial control of Delaware Mutual through a management services agreement. On December 20, 1994, Delaware Mutual Insurance Company demutualized and

adopted the title Delaware American Insurance Company. Upon the demutualization, the Company purchased 100% of the outstanding stock of the Delaware Atlantic. On December 29, 1995, Delaware was purchased by Donegal Group Inc. On August 1, 2001, Delaware merged into Atlantic States Insurance Company.

Effective January 1, 2004, Donegal Group Inc. acquired all of the outstanding stock of Le Mars Insurance Company pursuant to Le Mars' plan of conversion to a stock company from a mutual company.

As of January 1, 2004, Donegal Group Inc. purchased all of the outstanding stock of The Peninsula Insurance Company and its wholly owned subsidiary Peninsula Indemnity Company.

Atlantic States Insurance Company was incorporated under the laws of Pennsylvania on September 26, 1986 and began business on October 1, 1986.

LICENSING

Donegal Mutual Insurance Company's Certificate of Authority to write business in the Commonwealth was issued on May 13, 1889. The Company is licensed in Delaware, Illinois, Indiana, Maryland, New York, North Carolina, Ohio, Pennsylvania, Tennessee and Virginia. The Company's 2006 annual statement reflects Direct Written Premium for all lines of business in the Commonwealth of Pennsylvania as \$169,033,351. Premium volume related to the areas of this review were: Fire \$2,912,067; Farm owner \$2,194,987; Homeowner's Multiple Peril \$39,640,319; Commercial Multiple Peril (non-liability portion) \$19,800,283; Commercial Multiple Peril (liability portion) \$4,950,071; Inland Marine

\$1,594,940; Workers' Compensation \$18,943,584; Private Passenger Automobile Direct Written Premium was reported as Private Passenger Auto No-Fault (personal injury protection) \$5,546,064; Other Private Passenger Auto Liability \$24,027,859 and Private Passenger Auto Physical Damage \$30,450,231; Commercial Automobile Direct Written Premium was reported as Commercial Auto No-Fault (personal injury protection) \$416,364; Other Commercial Auto Liability \$7,866,741 and Commercial Auto Physical Damage \$3,941,312.

Atlantic States Insurance Company's Certificate of Authority to write business in the Commonwealth was issued on October 14, 1986. The Company is licensed in Connecticut, Delaware, Georgia, Indiana, Maryland, New York, Ohio, Pennsylvania, Tennessee and Virginia. The Company's 2006 annual statement reflects Direct Written Premium for all lines of business in the Commonwealth of Pennsylvania as \$57,204,234. Premium volume related to the areas of this review were: Homeowner's Multiple Peril \$1,525,341; Commercial Multiple Peril (non-liability portion) \$7,661,405; Commercial Multiple Peril (liability portion) \$1,915,351; Workers' Compensation \$9,505,513; Private Passenger Automobile Direct Written Premium was reported as Private Passenger Auto No-Fault (personal injury protection) \$2,041,858; Other Private Passenger Auto Liability \$12,942,172 and Private Passenger Auto Physical Damage \$15,797,385; Commercial Automobile Direct Written Premium was reported as Commercial Auto No-Fault (personal injury protection) \$185,678; Other Commercial Auto Liability \$3,699,871 and Commercial Auto Physical Damage \$1,738,534.

IV. UNDERWRITING PRACTICES AND PROCEDURES

As part of the examination, the Company was requested to supply manuals, underwriting guides, bulletins, directives or other forms of underwriting procedure communications for each line of business being reviewed. Agency bulletins and Pennsylvania automobile product guides were furnished for private passenger automobile, homeowners, dwelling fire and commercial lines. The purpose of this review was to identify any inconsistencies which could be considered discriminatory, specifically prohibited by statute or regulation, or unusual in nature.

The following findings were made:

2 Violations Act 205, Section 5(a)(4) [40 P.S. §1171.5(a)(4)]

Unfair Methods of Competition and Unfair or Deceptive Acts or Practices Defined. Entering into any agreement to commit, or by any concerted action committing, any act of boycott, coercion or intimidation resulting in or tending to result in unreasonable restraint of, or monopoly in, the business of insurance. The Company's HO-4 and HO-6 guidelines effective 9/1/04 indicate the following: "We will only write student occupied rentals as an accommodation if Donegal provides coverage on the parent's primary residence (with good experience)". The Company's dwelling fire new business guidelines effective 1/1/02 indicate the following: "Seasonal or secondary dwellings – A Donegal company must write the primary residence with good experience".

V. UNDERWRITING

A. Private Passenger Automobile

1. 60-Day Cancellations

A 60-day cancellation is considered to be any policy, which was cancelled within the first 60 days of the inception date of the policy.

The primary purpose of the review was to determine compliance with Act 68, Section 2003 (40 P.S. §991.2003), which establishes conditions under which action by the insurer is prohibited. These files were also reviewed for compliance with Act 68, Section 2002(b)(3) [40 P.S. §991.2002(b)(3)], which requires an insurer who cancels a policy of automobile insurance in the first 60 days, to supply the insured with a written statement of the reason for cancellation.

Donegal Mutual Insurance Company

From the universe of 326 private passenger automobile files identified as being cancelled in the first 60 days of new business, 25 files were selected for review. All 25 files were received and reviewed. No violations were noted.

Atlantic States Insurance Company

From the universe of 138 private passenger automobile files identified as being cancelled in the first 60 days of new business, 3 files were selected for review. All 3 files were received and reviewed. No violations were noted.

2. Midterm Cancellations

A midterm cancellation is any policy that terminates at any time other than the normal twelve-month policy anniversary date.

The primary purpose of the review was to determine compliance with Act 68, Section 2003 (40 P.S. §991.2003), which establishes conditions under which action by the insurer is prohibited, and Section 2006 (40 P.S. §991.2006), which establishes the requirements which must be met regarding the form and conditions of the cancellation notice.

Donegal Mutual Insurance Company

From the universe of 6,395 private passenger automobile files identified as midterm cancellations by the Company, 59 files were selected for review. All 59 files were received and reviewed. The 4 violations noted were based on 3 files, resulting in an error ratio of 5%.

The following findings were made:

3 Violations Act 68, Section 2004 [40 P.S. §991.2004]

Requires that no insurer shall cancel a policy of automobile insurance except for nonpayment of premium, suspension or revocation of the named insured's driver license or motor vehicle registration or a determination that the insured has concealed a material fact or has made a material allegation contrary to fact or has made a misrepresentation of material fact and that such concealment, allegation or misrepresentation was material to the acceptance of the risk by the insurer. The 3 files noted were cancelled for other than permitted reasons.

1 Violation Act 68, Section 2006(2) [40 P.S. §991.2006(2)]

Requires an insurer to deliver or mail to the named insured a cancellation notice and state the date, not less than sixty (60) days after the date of the mailing or delivery, on which cancellation shall become effective. When the policy is being cancelled for the nonpayment of premium, the effective date may be fifteen (15) days from the date of mailing or delivery. The Company did not provide 60 days notice of cancellation.

Atlantic States Insurance Company

From the universe of 1,941 private passenger automobile files identified as midterm cancellations by the Company, 10 files were selected for review. All 10 files were received and reviewed. No violations were noted.

3. Nonrenewals

A nonrenewal is considered to be any policy that was not renewed, for a specific reason, at the normal twelve-month policy anniversary date.

The purpose of the review was to determine compliance with Act 68, Section 2003 (40 P.S. §991.2003), which establishes conditions under which action by the insurer is prohibited, and Section 2006 (40 P.S. §991.2006), which establishes the requirements which must be met regarding the form and conditions of the cancellation notice.

Donegal Mutual Insurance Company

From the universe of 380 private passenger automobile files identified as nonrenewals by the Company, 100 files were selected for review. All 100 files were received and reviewed. No violations were noted.

Atlantic States Insurance Company

From the universe of 117 private passenger automobile files identified as nonrenewals by the Company, 50 files were selected for review. All 50 files were received and reviewed. No violations were noted.

4. Declinations

A declination is any application that is received by the Company and was declined to be written.

The primary purpose of the review was to determine compliance with Act 68, Section 2003 [40 P.S. §991.2003], which establishes conditions under which action by the insurer is prohibited.

The universe of 2 private passenger automobile files identified as being refused by the Company during the experience period was selected for review. The 2 files were received and reviewed. The 2 violations noted were based on 2 files, resulting in an error ratio of 100%.

The following findings were made:

2 Violations Act 68, Section 2008(b) [40 P.S. §991.2008(b)]

Any applicant for a policy who is refused such policy by an insurer shall be given a written notice of refusal to write by the insurer. Such notice shall state the specific reason or reasons of the insurer for refusal to write a policy for the applicant. Within 30 days of the receipt of such reasons, the applicant may request in writing to the Insurance Commissioner that he review the action of the insurer in refusing to write a policy for the applicant. The Company

failed to issue a notice of refusal to write to inform the applicant of the specific reason or reasons for the refusal and the right of review by the Insurance Commissioner.

B. Private Passenger Automobile – Assigned Risk

Donegal Mutual Insurance Company reports its premium writings for private passenger automobile to the Pennsylvania Assigned Risk Plan. As a result, the Company receives all assignments from the Pennsylvania Assigned Risk Plan.

1. Midterm Cancellations

A midterm cancellation is any policy that terminates at any time other than the normal twelve-month policy anniversary date.

The primary purpose of the review was to determine compliance with Title 75, Pennsylvania Consolidated Statutes, Sections 1742, 1743 and 1744 [75 Pa. C.S. §1742, 1743 an 1744], and all the rules of the Pennsylvania Assigned Risk Plan and Manual.

Donegal Mutual Insurance Company

From the universe of 432 private passenger automobile assigned risk policies cancelled during the experience period, 50 files were selected for review. All 50 files selected were received and reviewed. No violations were noted.

2. Nonrenewal

A nonrenewal is considered to be any policy that was not renewed, for a specific reason, at the normal twelve-month anniversary date.

The purpose of the review was to determine compliance with Title 75, Pennsylvania Consolidated Statutes, Sections 1742, 1743, 1744 [75 Pa. C.S. §1742, 1743 and 1744], and all the rules of the Pennsylvania Assigned Risk Plan and Manual.

Donegal Mutual Insurance Company

The universe of 5 private passenger assigned risk policies nonrenewed during the experience period was selected for review. All 5 files were received and reviewed. The violation noted resulted in an error ratio of 20%.

The following finding was made:

1 Violation Pennsylvania Assigned Risk Plan, Section 16.A.4.

End of Assignment Period. At least 60 calendar days prior to the expiration date of the final renewal, the Company shall notify the insured that the period of assignment under the Plan will terminate on said expiration date. A copy of such notice shall be sent to the producer of record. The Company failed to provide the insured at least 60 calendar days notice of expiration of the assignment period.

C. Property

1. 60-Day Cancellations

A 60-day cancellation is considered to be any policy, which was cancelled within the first 60 days of the inception date of the policy.

The primary purpose of the review was to determine compliance with Act 205, Unfair Insurance Practices Act, Section 5(a)(7)(iii) [40 P.S.

§1171.5(a)(7)(iii)], which prohibits an insurer from canceling a policy for discriminatory reasons and Title 31, Pennsylvania Code, Section 59.9(b), which requires an insurer who cancels a policy in the first 60 days to provide at least 30 days notice of the termination.

Donegal Mutual Insurance Company

From the universe of 371 property policies which were cancelled within the first 60 days of new business, 34 files were selected for review. The policies consisted of homeowner, tenant homeowner, inland marine and dwelling fire. All 34 files were received and reviewed. The violation noted resulted in an error of 3%.

The following finding was made:

1 Violation Act 205, Section 5(a)(4) [40 P.S. §1171.5(a)(4)]

Unfair Methods of Competition and Unfair or Deceptive Acts or Practices Defined. Entering into any agreement to commit, or by any concerted action committing, any act of boycott, coercion or intimidation resulting in or tending to result in unreasonable restraint of, or monopoly in, the business of insurance. The file noted contained a cancellation notice which required supporting business.

Atlantic States Insurance Company

From the universe of 25 homeowner policies which were cancelled within the first 60 days of new business, 10 files were selected for review. All 10 files were received and reviewed. No violations were noted.

2. Midterm Cancellations

A midterm cancellation is any policy termination that occurs at any time other than the twelve-month policy anniversary date.

The primary purpose of the review was to determine personal lines compliance with Act 205, Unfair Insurance Practices Act, Section 5(a)(9) [40 P.S. §1171.5(a)(9)], which establishes the conditions under which cancellation of a policy is permissible along with the form requirements of the cancellation notice.

Donegal Mutual Insurance Company

From the universe of 9,558 property policies which were cancelled midterm during the experience period, 172 files were selected for review. The property policies consisted of homeowners, tenant homeowners, inland marine and dwelling fire. All 172 files were received and reviewed. The 15 violations noted were based on 14 files, resulting in an error ratio of 8%.

The following findings were made:

11 Violations Act 205, Section 5(a)(9) [40 P.S. §1171.5(a)(9)]

Prohibits canceling any policy of insurance covering owner-occupied private residential properties or personal property of individuals that has been in force for sixty days or more or refusing to renew any such policy unless the policy was obtained through material misrepresentation, fraudulent statements, omissions or concealment of fact material to the acceptance of the risk or to the hazard assumed by the company; or there has been a substantial change or increase in hazard in the risk assumed by the company subsequent to

the date the policy was issued; or there is a substantial increase in hazards insured against by reason of willful or negligent acts or omissions by the insured; or the insured has failed to pay any premium when due or for any other reasons approved by the Commissioner. The Company cancelled the 11 files noted for an improper reason. The reasons included unsupported increase in hazard/condition, breed of dog, ineligible mobile home and value of a watercraft.

2 Violations Act 205, Section 5(a)(4) [40 P.S. §1171.5(a)(4)]

Unfair Methods of Competition and Unfair or Deceptive Acts or Practices Defined. Entering into any agreement to commit, or by any concerted action committing, any act of boycott, coercion or intimidation resulting in or tending to result in unreasonable restraint of, or monopoly in, the business of insurance. The 2 files noted contained a cancellation notice which required supporting business.

2 Violations Insurance Company Law, Section 506.1 [40 P.S. §636.1]

Basic property insurance shall be continued one hundred and eighty days after the death of the named insured on the policy or until the sale of the property, whichever event occurs first provided that the premiums for the coverage are paid. The Company failed to provide 180 days of coverage for the 2 files noted.

Atlantic States Insurance Company

From the universe of 73 homeowner policies which were cancelled midterm during the experience period, 10 files were selected for review. All 10 files were received and reviewed. No violations were noted.

3. Nonrenewals

A nonrenewal is considered to be any policy, which was not renewed, for a specific reason, at the normal twelve-month anniversary date.

The primary purpose of the review was to determine personal lines compliance with Act 205, Unfair Insurance Practices Act, Section 5(a)(9) [40 P.S. §1171.5(a)(9)], which establishes the conditions under which cancellation of a policy is permissible along with the form requirements of the nonrenewal notice.

Donegal Mutual Insurance Company

From the universe of 156 property policies which were nonrenewed during the experience period, 98 files were selected for review. The policies consisted of homeowners, tenant homeowners, inland marine and dwelling fire. All 98 files were received and reviewed. The 7 violations noted were based on 7 files, resulting in an error ratio of 7%.

The following findings were made:

4 Violations Act 205, Section 5(a)(9) [40 P.S. §1171.5(a)(9)]

Prohibits canceling any policy of insurance covering owner-occupied private residential properties or personal property of individuals that has been in force for sixty days or more or refusing to renew any such policy unless the policy was

obtained through material misrepresentation, fraudulent statements, omissions or concealment of fact material to the acceptance of the risk or to the hazard assumed by the company; or there has been a substantial change or increase in hazard in the risk assumed by the company subsequent to the date the policy was issued; or there is a substantial increase in hazards insured against by reason of willful or negligent acts or omissions by the insured; or the insured has failed to pay any premium when due or for any other reasons approved by the Commissioner. The Company nonrenewed the 4 files noted for an improper reason.

3 Violations Act 205, Section 5(a)(4) [40 P.S. §1171.5(a)(4)]

Unfair Methods of Competition and Unfair or Deceptive Acts or Practices Defined. Entering into any agreement to commit, or by any concerted action committing, any act of boycott, coercion or intimidation resulting in or tending to result in unreasonable restraint of, or monopoly in, the business of insurance. The 3 files noted contained a nonrenewal notice which required supporting business.

Atlantic States Insurance Company

The universe of 1 homeowner policy which was nonrenewed during the experience period was selected for review. The file was received and reviewed. No violations were noted.

D. Commercial Property

1. 60-Day Cancellations

A 60-day cancellation is considered to be any policy, which was cancelled within the first 60 days of the inception date of the policy.

The primary purpose of the review was to determine compliance with Act 86, Section 7 (40 P.S. §3407), which requires an insurer, who cancels a policy that is in effect less than 60 days, to provide 30 days notice of termination no later than the 60th day unless the policy provides for a longer period of notification.

Donegal Mutual Insurance Company

From the universe of 205 commercial property policies cancelled within the first 60 days of new business, 34 files were selected for review. All 34 files were received and reviewed. The commercial property policies consisted of farm owner, commercial fire, tenant occupied dwelling fire, commercial inland marine and commercial package. No violations were noted.

Atlantic States Insurance Company

The universe of 6 commercial package policies cancelled within the first 60 days of new business was selected for review. All 6 files were received and reviewed. No violations were noted.

2. Midterm Cancellations

A midterm cancellation is any policy termination that occurs at any time other than the twelve-month policy anniversary date.

The purpose of the review was to determine compliance with Act 86, Section 2 (40 P.S. §3402), which prohibits cancellation except for specified reasons and Section 3 (40 P.S. §3403), which establishes the requirements, which must be met regarding the form and condition of the cancellation notice.

Donegal Mutual Insurance Company

From the universe of 3,405 commercial property policies which were cancelled midterm during the experience period, 62 files were selected for review. All 62 files were received and reviewed. The commercial property policies consisted of farm owner, commercial fire, tenant occupied dwelling fire, commercial inland marine and commercial package. The 6 violations noted were based on 5 files, resulting in an error ratio of 8%.

The following findings were made:

1 Violation Act 86, Section 2(1) [40 P.S. §3402(1)]

Canceling in midterm a policy of insurance covering commercial property and casualty risks is prohibited for any reason other than the following: A condition, factor or loss experience material to insurability has changed substantially or a substantial condition, factor or loss experience material to insurability has become known during the policy term. The Company cancelled the policy for an improper reason.

2 Violations Act 86, Section 3(a)(3) [40 P.S. §3403(a)(3)]

Requires that a cancellation notice must be forwarded to the named insured or insureds at least 60 days in advance of the effective date of termination. The Company did not provide

at least 60 days notice of cancellation for the 2 files noted.

3 Violations Act 86, Section 3(a)(5) [40 P.S. §3403(a)(5)]

Requires that a cancellation notice shall state the specific reasons for cancellation. The reasons shall identify the condition, factor or loss experience, which caused the cancellation. The notice shall provide sufficient information or data for the insured to correct the deficiency. The Company did not provide a specific reason for cancellation for the 3 files noted.

Atlantic States Insurance Company

From the universe of 112 commercial package policies which were cancelled midterm during the experience period, 4 files were selected for review. All 4 files were received and reviewed. No violations were noted.

3. Nonrenewals

A nonrenewal is considered to be any policy that was not renewed, for a specific reason, at the normal twelve-month policy anniversary date.

The review was conducted to determine compliance with Act 86, Section 3 (40 P.S. §3403), which establishes the requirements that must be met regarding the form and condition of the nonrenewal notice.

Donegal Mutual Insurance Company

From the universe of 161 commercial property policies identified as nonrenewals, 56 files were selected for review. All 56 files were received and reviewed. The commercial property policies consisted of commercial farm owner, commercial fire, tenant occupied dwelling fire, commercial

inland marine and commercial package. The 6 violations noted were based on 6 files, resulting in an error ratio of 11%.

The following findings were made:

6 Violations Act 86, Section 3(a)(5) [40 P.S. §3403(a)(5)]

Requires that a nonrenewal notice shall state the specific reasons for the nonrenewal. The reasons shall identify the condition, factor or loss experience, which caused the nonrenewal. The notice shall provide sufficient information or data for the insured to correct the deficiency.

AND

Title 31, Pa. Code, Section 113.88

The reason given for nonrenewal shall be clear and complete. It shall be stated so that a person of average intelligence and education can understand it. Phrases such as “losses” or “underwriting reasons” are not sufficiently specific reasons for nonrenewal. The Company did not provide a specific reason for nonrenewal for the 6 files noted.

Atlantic States Insurance Company

From the universe of 26 commercial package policies identified as nonrenewals, 10 files were selected for review. All 10 files were received and reviewed. The 3 violations noted were based on 3 files, resulting in an error ratio of 30%.

The following findings were made:

1 Violation Act 86, Section 3(a)(2) [40 P.S. §3403(a)(2)]

Requires that a nonrenewal notice be forwarded directly to the named insured or insureds at least 60 days in advance of the effective date of the termination. The Company did not provide at least 60 days notice of nonrenewal.

2 Violations Act 86, Section 3(a)(5) [40 P.S. §3403(a)(5)]

Requires that a nonrenewal notice shall state the specific reasons for the nonrenewal. The reasons shall identify the condition, factor or loss experience, which caused the nonrenewal. The notice shall provide sufficient information or data for the insured to correct the deficiency.

AND

Title 31, Pa. Code, Section 113.88

The reason given for nonrenewal shall be clear and complete. It shall be stated so that a person of average intelligence and education can understand it. Phrases such as “losses” or “underwriting reasons” are not sufficiently specific reasons for nonrenewal. The Company did not provide a specific reason for nonrenewal for the 2 files noted.

4. Declinations

A declination is any application that is received and the Company declines to write the coverage.

The primary purpose of the review was to determine compliance with Act 205, Section 5 [40 P.S. §1171.5], which defined unfair methods of competition and unfair or deceptive acts or practices

From the universe of 2,158 commercial property files identified as declinations by the Company during the experience period, 25 files were selected for review. All 25 files were received and reviewed. No violations were noted.

5. Renewals

A renewal is considered to be any policy, which was previously written by the Company and renewed on the normal twelve-month anniversary date.

The purpose of the review was to measure compliance with Act 86, Section 1 (40 P.S. §3401), which requires 30 days advance notice of an increase in renewal premium.

Donegal Mutual Insurance Company

From the universe of 14,180 commercial property policies which were renewed during the experience period, 15 files were selected for review. All 15 files were received and reviewed. The 4 violations noted were based on 4 files, resulting in an error ratio of 27%.

The following findings were made:

4 Violations Act 86, Section 1 [40 P.S. §3401]

This section provides that notwithstanding any other provision of law, a policy of insurance covering commercial property or casualty risks in this Commonwealth shall

provide for not less than 30 days advance notice to the named insured of an increase in renewal premium. This section does not apply to policies written on a retrospective rating plan. The Company did not provide at least 30 days advance notice to the named insured of an increase in renewal premium for the 4 files noted.

Atlantic States Insurance Company

From the universe of 698 commercial property policies which were renewed during the experience period, 15 files were selected for review. All 15 files were received and reviewed. The 3 violations noted were based on 3 files, resulting in an error ratio of 20%.

The following findings were made:

3 Violations Act 86, Section 1 [40 P.S. §3401]

This section provides that notwithstanding any other provision of law, a policy of insurance covering commercial property or casualty risks in this Commonwealth shall provide for not less than 30 days advance notice to the named insured of an increase in renewal premium. This section does not apply to policies written on a retrospective rating plan. The Company did not provide at least 30 days advance notice to the named insured of an increase in renewal premium for the 3 files noted.

E. Commercial Automobile

1. 60-Day Cancellations

A 60-day cancellation is considered to be any policy, which was cancelled within the first 60 days of the inception date of the policy.

The primary purpose of the review was to determine compliance with Act 86, Section 7 (40 P.S. §3407), which requires an insurer, who cancels a policy that is in effect less than 60 days, to provide 30 days notice of termination no later than the 60th day unless the policy provides for a longer period of notification.

Donegal Mutual Insurance Company

From the universe of 41 commercial automobile policies cancelled within the first 60 days of new business, 1 file was selected for review. The file was received and reviewed. No violations were noted.

Atlantic States Insurance Company

The universe of 5 commercial automobile policies which were cancelled within the first 60 days was selected for review. All 5 files were received and reviewed. No violations were noted.

2. Midterm Cancellations

A midterm cancellation is any policy termination that occurs at any time other than the twelve-month policy anniversary date.

The purpose of the review was to determine compliance with Act 86, Section 2 (40 P.S. §3402), which prohibits cancellation except for specified reasons and Section 3 (40 P.S. §3403), which establishes the requirements,

which must be met regarding the form and condition of the cancellation notice.

Donegal Mutual Insurance Company

From the universe of 737 commercial automobile policies identified as midterm cancellations, 22 files were selected for review. All 22 files were received and reviewed. The 3 violations noted were based on 3 files, resulting in an error ratio of 14%.

The following findings were made:

2 Violations Act 86, Section 3(a)(5) [40 P.S. §3403(a)(5)]

Requires that a cancellation notice shall state the specific reasons for the cancellation. The reasons shall identify the condition, factor or loss experience, which caused the nonrenewal. The notice shall provide sufficient information or data for the insured to correct the deficiency.

AND

Title 31, Pa. Code, Section 113.88

The reason given for cancellation shall be clear and complete. It shall be stated so that a person of average intelligence and education can understand it. Phrases such as "losses" or "underwriting reasons" are not sufficiently specific reasons for nonrenewal. The Company did not provide a specific reason for cancellation for the 2 files noted.

1 Violation Act 205, Section 5(a)(4) [40 P.S. §1171.5(a)(4)]

Unfair Methods of Competition and Unfair or Deceptive Acts or Practices Defined. Entering into any agreement to commit,

or by any concerted action committing, any act of boycott, coercion or intimidation resulting in or tending to result in unreasonable restraint of, or monopoly in, the business of insurance. The file noted contained a cancellation notice which required supporting business.

Atlantic States Insurance Company

The Company identified 90 commercial automobile policies that were cancelled during the experience period. No files were selected for review.

3. Nonrenewals

A nonrenewal is considered to be any policy that was not renewed, for a specific reason, at the normal twelve-month policy anniversary date.

The review was conducted to determine compliance with Act 86, Section 3 (40 P.S. §3403), which establishes the requirements that must be met regarding the form and condition of the nonrenewal notice.

Donegal Mutual Insurance Company

From the universe of 52 commercial automobile policies identified as nonrenewals by the Company, 25 files were selected for review. All 25 files were received and reviewed. The 6 violations noted were based on 6 files, resulting in an error ratio of 24%.

The following findings were made:

1 Violation Act 205, Section 5(a)(4) [40 P.S. §1171.5(a)(4)]

Unfair Methods of Competition and Unfair or Deceptive Acts or Practices Defined. Entering into any agreement to commit,

or by any concerted action committing, any act of boycott, coercion or intimidation resulting in or tending to result in unreasonable restraint of, or monopoly in, the business of insurance. The file noted contained a nonrenewal notice which required supporting business.

1 Violation Act 86, Section 3(a)(1) [40 P.S. §3403(a)(1)]

Requires that a nonrenewal notice be forwarded by registered mail or first class mail or delivered by the insurance company directly to the named insured or insureds. The Company did not provide a copy of the notice of nonrenewal so that compliance could be determined for the file noted.

1 Violation Act 86, Section 3(a)(2) [40 P.S. §3403(a)(2)]

Requires that a nonrenewal notice be forwarded directly to the named insured or insureds at least 60 days in advance of the effective date of the termination. The Company did not provide at least 60 days notice of nonrenewal for the file noted.

3 Violations Act 86, Section 3(a)(5) [40 P.S. §3403(a)(5)]

Requires that a nonrenewal notice shall state the specific reasons for the nonrenewal. The reasons shall identify the condition, factor or loss experience, which caused the nonrenewal. The notice shall provide sufficient information or data for the insured to correct the deficiency.

AND

Title 31, Pa. Code, Section 113.88

The reason given for nonrenewal shall be clear and complete.

It shall be stated so that a person of average intelligence and education can understand it. Phrases such as “losses” or “underwriting reasons” are not sufficiently specific reasons for nonrenewal. The Company did not provide a specific reason for nonrenewal for the 3 files noted.

Atlantic States Insurance Company

The universe of 18 commercial automobile policies identified as nonrenewals by the Company was selected for review. All 18 files were received and reviewed. The 2 violations noted were based on 2 files, resulting in an error ratio of 11%.

The following findings were made:

2 Violations Act 86, Section 3(a)(5) [40 P.S. §3403(a)(5)]

Requires that a nonrenewal notice shall state the specific reasons for the nonrenewal. The reasons shall identify the condition, factor or loss experience, which caused the nonrenewal. The notice shall provide sufficient information or data for the insured to correct the deficiency.

AND

Title 31, Pa. Code, Section 113.88

The reason given for nonrenewal shall be clear and complete. It shall be stated so that a person of average intelligence and education can understand it. Phrases such as “losses” or “underwriting reasons” are not sufficiently specific reasons for nonrenewal. The Company did not provide a specific reason for nonrenewal for the 2 files noted.

4. Declinations

A declination is any application that is received and the Company declines to write the coverage.

The primary purpose of the review was to determine compliance with Act 205, Section 5 [40 P.S. §1171.5], which defined unfair methods of competition and unfair or deceptive acts or practices

From the universe of 170 commercial automobile files identified as declinations by the Company during the experience period, 25 files were selected for review. All 25 files were received and reviewed. The 2 violations noted were based on 2 files, resulting in an error ratio of 8%.

The following findings were made:

1 Violation Insurance Department Act, Section 903(a) [40 P.S. §323.3]
Requires every company subject to examination to keep all books, records, accounts, papers, documents and any or all computer or other recordings relating to its business in such manner and for such time as may be required in order that the Department may readily verify whether the Company has complied with the laws of this Commonwealth. The file noted did not reflect the reason for declination.

1 Violation Act 205, Section 5(a)(4) [40 P.S. §1171.5(a)(4)]
Unfair Methods of Competition and Unfair or Deceptive Acts or Practices Defined. Entering into any agreement to commit, or by any concerted action committing, any act of boycott, coercion or intimidation resulting in or tending to result in

unreasonable restraint of, or monopoly in, the business of insurance. The Company declined the applicant due to no supporting business.

5. Renewals

A renewal is considered to be any policy, which was previously written by the Company and renewed on the normal twelve-month anniversary date. The purpose of the review was to measure compliance with Act 86, Section 1 (40 P.S. §3401), which requires 30 days advance notice of an increase in renewal premium.

Donegal Mutual Insurance Company

From the universe of 3,195 commercial automobile policies which were renewed during the experience period, 15 files were selected for review. All 15 files were received and reviewed. The 3 violations noted were based on 3 files, resulting in an error ratio of 20%.

The following findings were made:

3 Violations Act 86, Section 1 [40 P.S. §3401]

This section provides that notwithstanding any other provision of law, a policy of insurance covering commercial property or casualty risks in this Commonwealth shall provide for not less than 30 days advance notice to the named insured of an increase in renewal premium. This section does not apply to policies written on a retrospective rating plan. The Company did not provide at least 30 days advance notice to the named insured of an increase in renewal premium for the 3 files noted.

Atlantic States Insurance Company

From the universe of 537 commercial automobile policies which were renewed during the experience period, 15 files were selected for review. All 15 files were received and reviewed. The 2 violations noted were based on 2 files, resulting in an error ratio of 13%.

The following findings were made:

2 Violations Act 86, Section 1 [40 P.S. §3401]

This section provides that notwithstanding any other provision of law, a policy of insurance covering commercial property or casualty risks in this Commonwealth shall provide for not less than 30 days advance notice to the named insured of an increase in renewal premium. This section does not apply to policies written on a retrospective rating plan. The Company did not provide at least 30 days advance notice to the named insured of an increase in renewal premium for the 2 files noted.

F. Workers' Compensation

1. 60-Day Cancellations

A 60-day cancellation is considered to be any policy, which was cancelled within the first 60 days of the inception date of the policy.

The primary purpose of the review was to determine compliance with Act 86, Section 7 (40 P.S. §3407), which requires an insurer, who cancels a policy that is in effect less than 60 days, to provide 30 days notice of termination no later than the 60th day unless the policy provides for a longer period of notification.

Donegal Mutual Insurance Company

From the universe of 32 workers' compensation policies cancelled within the first 60 days of new business, 1 file was selected for review. The file was received and reviewed. The violation noted resulted in an error ratio of 100%.

The following finding was made:

1 Violation Insurance Company Law, Section 653

Except for nonpayment of premium, no policy of insurance issued or renewed against liability under the Act of June 2, 1915 (P.L. 736, No. 338), known as the Pennsylvania Workers' Compensation Act, may be cancelled or terminated by an insurer during the term of the policy. The Company cancelled the policy due to a prohibited class of business.

Atlantic States Insurance Company

The Company reported 3 workers' compensation policies cancelled within the first 60 days of new business. No files were selected for review.

2. Midterm Cancellations

A midterm cancellation is any policy termination that occurs at any time other than the twelve-month anniversary date.

The purpose of the review was to determine compliance with Insurance Company Law, Section 653 (40 P.S. §813), which prohibits midterm cancellation with exceptions for nonpayment of premium or by request of the insured.

Donegal Mutual Insurance Company

From the universe of 689 workers' compensation policies identified as midterm cancellations, 5 files were selected for review. All 5 files were received and reviewed. The 5 violations noted were based on 5 files, resulting in an error ratio of 100%.

The following findings were made:

5 Violations Insurance Company Law, Section 653

Except for nonpayment of premium, no policy of insurance issued or renewed against liability under the Act of June 2, 1915 (P.L. 736, No. 338), known as the Pennsylvania Workers' Compensation Act, may be cancelled or terminated by an insurer during the term of the policy. The Company cancelled the 5 files noted for reasons other than nonpayment of premium.

Atlantic States Insurance Company

The Company reported 69 workers' compensation policies cancelled midterm during the experience period. No files were selected for review.

3. Nonrenewals

A nonrenewal is considered to be any policy, which was not renewed, for a specific reason, at the normal twelve-month anniversary date.

The review was conducted to determine compliance with Act 86, Section 3 (40 P.S. §3403), which establishes notice requirements for nonrenewals.

Donegal Mutual Insurance Company

From the universe of 58 workers' compensation policies nonrenewed during the experience period, 25 files were selected for review. All 25 files were received and reviewed. The 7 violations noted were based on 7 files, resulting in an error ratio of 28%.

The following findings were made:

2 Violations Act 86, Section 3(a)(2) [40 P.S. §3403(a)(2)]

Requires that a nonrenewal notice be forwarded directly to the named insured or insureds at least 60 days in advance of the effective date of the termination. The Company did not provide at least 60 days notice of nonrenewal for the 2 files noted.

5 Violations Act 86, Section 3(a)(5) [40 P.S. §3403(a)(5)]

Requires that a nonrenewal notice shall state the specific reasons for the nonrenewal. The reasons shall identify the condition, factor or loss experience, which caused the nonrenewal. The notice shall provide sufficient information or data for the insured to correct the deficiency.

AND

Title 31, Pa. Code, Section 113.88

The reason given for nonrenewal shall be clear and complete. It shall be stated so that a person of average intelligence and education can understand it. Phrases such as "losses" or "underwriting reasons" are not sufficiently specific reasons for nonrenewal. The Company did not provide a specific reason for nonrenewal for the 5 files noted.

Atlantic States Insurance Company

From the universe of 23 workers' compensation policies nonrenewed during the experience period, 10 files were selected for review. All 10 files were received and reviewed. The 2 violations noted were based on 2 files, resulting in an error ratio of 20%.

The following findings were made:

2 Violations Act 86, Section 3(a)(5) [40 P.S. §3403(a)(5)]

Requires that a nonrenewal notice shall state the specific reasons for the nonrenewal. The reasons shall identify the condition, factor or loss experience, which caused the nonrenewal. The notice shall provide sufficient information or data for the insured to correct the deficiency.

AND

Title 31, Pa. Code, Section 113.88

The reason given for nonrenewal shall be clear and complete. It shall be stated so that a person of average intelligence and education can understand it. Phrases such as "losses" or "underwriting reasons" are not sufficiently specific reasons for nonrenewal. The Company did not provide a specific reason for nonrenewal for the 2 files noted.

4. Renewals

A renewal is considered to be any policy, which was previously written by the Company and renewed on the normal twelve-month anniversary date.

The purpose of the review was to measure compliance with Act 86, Section 1 (40 P.S. §3401), which requires 30 days advance notice of an increase in renewal premium.

Donegal Mutual Insurance Company

From the universe of 3,554 workers' compensation policies which were renewed during the experience period, 10 files were selected for review. All 10 files were received and reviewed. The 3 violations noted were based on 3 files, resulting in an error ratio of 30%.

The following findings were made:

3 Violations Act 86, Section 1 [40 P.S. §3401]

This section provides that notwithstanding any other provision of law, a policy of insurance covering commercial property or casualty risks in this Commonwealth shall provide for not less than 30 days advance notice to the named insured of an increase in renewal premium. This section does not apply to policies written on a retrospective rating plan. The Company did not provide at least 30 days advance notice to the named insured of an increase in renewal premium for the 3 files noted.

Atlantic States Insurance Company

From the universe of 529 workers' compensation policies which were renewed during the experience period, 10 files were selected for review. All 10 files were received and reviewed. The 3 violations noted were based on 3 files, resulting in an error ratio of 30%.

The following findings were made:

3 Violations Act 86, Section 1 [40 P.S. §3401]

This section provides that notwithstanding any other provision of law, a policy of insurance covering commercial property or casualty risks in this Commonwealth shall provide for not less than 30 days advance notice to the named insured of an increase in renewal premium. This section does not apply to policies written on a retrospective rating plan. The Company did not provide at least 30 days advance notice to the named insured of an increase in renewal premium for the 3 files noted.

VI. RATING

A. Private Passenger Automobile

1. New Business

New business, for the purpose of this examination, is defined as policies written for the first time by the Company during the experience period.

The primary purpose of the review was to measure compliance with Act 246, Sections 4(a) and (h) [40 P.S. §1184], which requires every insurer to file with the Insurance Commissioner every manual of classifications, rules and rates, every rating plan and every modification of any rating plan, which it proposes to use in the Commonwealth. Also, no insurer shall make or issue a contract or policy except in accordance with filings or rates, which are in effect at that time. Files were also reviewed to determine compliance with all provisions of Act 6 of 1990 and Act 68, Section 2005(c) [40 P.S. §991.2005(c)], which requires insurers to provide to insureds a detailed statement of the components of a premium and shall specifically show the amount of surcharge or other additional amount that is charged as a result of a claim having been made under a policy of insurance or as a result of any other factors.

The Company processes and issues personal automobile policies using an automated system. In order to verify the automated system, several policies were manually rated to ensure the computer had been programmed correctly. Once the computer programming had been verified, only the input data needed to be verified. By reviewing base premiums, territory assignments, rating symbols, classifications and surcharge disclosures, the examiners were able to determine compliance with the Company's filed and approved rating plans.

Private Passenger Automobile – New Business Without Surcharges

Donegal Mutual Insurance Company

From the universe of 11,128 private passenger automobile policies identified as new business without surcharges by the Company, 25 files were selected for review. All 25 files were received and reviewed. The 25 violations noted were based on 25 files, resulting in an error ratio of 100%.

The following findings were made:

25 Violations Title 75, Pa. C.S. §1793(b)

Requires the insurer to provide to the insured a copy of their surcharge disclosure plan. The insurer providing the surcharge disclosure plan shall detail the provisions of the plan and the plan shall be delivered to each insured by the insurer at least once annually. Additionally, the surcharge information plan shall be given to each prospective insured at the time application is made for motor vehicle insurance coverage. The Company failed to provide the surcharge disclosure plan to the insured at the time application is made for motor vehicle insurance coverage.

Atlantic States Insurance Company

From the universe of 4,316 private passenger automobile policies identified as new business without surcharges by the Company, 25 files were selected for review. All 25 files were received and reviewed. The 25 violations noted were based on 25 files, resulting in an error ratio of 100%.

The following findings were made:

25 Violations Title 75, Pa. C.S. §1793(b)

Requires the insurer to provide to the insured a copy of their surcharge disclosure plan. The insurer providing the surcharge disclosure plan shall detail the provisions of the plan and the plan shall be delivered to each insured by the insurer at least once annually. Additionally, the surcharge information plan shall be given to each prospective insured at the time application is made for motor vehicle insurance coverage. The Company failed to provide the surcharge disclosure plan to the insured at the time application is made for motor vehicle insurance coverage.

Private Passenger Automobile - New Business With Surcharges

Donegal Mutual Insurance Company

From the universe of 2,836 private passenger automobile policies identified as new business with surcharges by the Company, 50 files were selected for review. All 50 files were received and reviewed. The 50 violations noted were based on 50 files, resulting in an error ratio of 100%.

The following findings were made:

50 Violations Title 75, Pa. C.S. §1793(b)

Requires the insurer to provide to the insured a copy of their surcharge disclosure plan. The insurer providing the surcharge disclosure plan shall detail the provisions of the plan and the plan shall be delivered to each insured by the insurer at least once annually. Additionally, the surcharge

information plan shall be given to each prospective insured at the time application is made for motor vehicle insurance coverage. The Company failed to provide the surcharge disclosure plan to the insured at the time application is made for motor vehicle insurance coverage.

Atlantic States Insurance Company

From the universe of 460 private passenger automobile policies identified as new business with surcharges by the Company, 25 files were selected for review. All 25 files were received and reviewed. The 26 violations noted were based on 25 files, resulting in an error ratio of 100%.

The following findings were made:

25 Violations Title 75, Pa. C.S. §1793(b)

Requires the insurer to provide to the insured a copy of their surcharge disclosure plan. The insurer providing the surcharge disclosure plan shall detail the provisions of the plan and the plan shall be delivered to each insured by the insurer at least once annually. Additionally, the surcharge information plan shall be given to each prospective insured at the time application is made for motor vehicle insurance coverage. The Company failed to provide the surcharge disclosure plan to the insured at the time application is made for motor vehicle insurance coverage.

1 Violation Act 246, The Casualty and Surety Rate Regulatory Act, Section 4 (40 P.S. §1184)

Requires every insurer to file with the Insurance

Commissioner every manual of classifications, rules and rates, every rating plan and every modification of any rating plan, which it proposes to use in the Commonwealth. Also, no insurer shall make or issue a contract or policy except in accordance with filings or rates, which are in effect at the time of issue. The Company rated the policy with an improper territory which resulted in an undercharge of \$35.

2. Renewals

A renewal is considered to be any policy, which was previously written by the Company and renewed on the normal twelve-month anniversary date.

The purpose of the review was to measure compliance with Act 246, Sections 4(a) and (h) (40 P.S. §1184), which requires every insurer to file with the Insurance Commissioner every manual of classifications, rules and rates, every rating plan and every modification of any rating plan, which it proposes to use in the Commonwealth. Also, no insurer shall make or issue a contract or policy except in accordance with filings or rates, which are in effect at the time. Files were also reviewed to determine compliance with Act 68, Section 2005(c) (40 P.S. §991.2005(c)), which requires insurers to provide to insureds a detailed statement of the components of a premium and shall specifically show the amount of surcharge or other additional amount that is charged as a result of a claim having been made under a policy of insurance, or as a result of any other factors.

The Company processes and issues personal automobile policies using an automated system. In order to verify the automated system, several policies were manually rated to ensure the computer had been programmed correctly. Once the computer programming had been verified, only the

input data needed to be verified. By reviewing base premiums, territory assignments, rating symbols, classifications and surcharge disclosures, the examiners were able to determine compliance with the Company's filed and approved rating plans.

Private Passenger Automobile – Renewals Without Surcharges

Donegal Mutual Insurance Company

From the universe of 51,539 private passenger automobile policies renewed without surcharges during the experience period, 25 files were selected for review. All 25 files were received and reviewed. No violations were noted.

Atlantic States Insurance Company

From the universe of 21,550 private passenger automobile policies renewed without surcharges during the experience period, 25 files were selected for review. All 25 files were received and reviewed. The violation noted resulted in an error ratio of 4%.

The following finding was made:

*1 Violation Act 246, The Casualty and Surety Rate Regulatory Act,
Section 4 (40 P.S. §1184)*

Requires every insurer to file with the Insurance Commissioner every manual of classifications, rules and rates, every rating plan and every modification of any rating plan, which it proposes to use in the Commonwealth. Also, no insurer shall make or issue a contract or policy except in accordance with filings or rates, which are in effect at the time of issue. The Company rated the policy with an

improper territory which resulted in an overcharge of \$308.

Private Passenger Automobile – Renewals With Surcharges

Donegal Mutual Insurance Company

From the universe of 5,819 private passenger automobile policies renewed with surcharges during the experience period, 50 files were selected for review. All 50 files were received and reviewed. No violations were noted.

Atlantic States Insurance Company

From the universe of 1,672 private passenger automobile policies renewed with surcharges during the experience period, 50 files were selected for review. All 50 files were received and reviewed. No violations were noted.

Private Passenger Automobile – Renewals In a Higher Plan

Donegal Mutual Insurance Company

The universe of 2 private passenger automobile policies identified as renewals in a higher plan was selected for review. Both files were received and reviewed. No violations were noted.

Atlantic States Insurance Company

This Company did not report any private passenger automobile policies renewed in a higher plan.

B. Private Passenger Automobile – Assigned Risk

Donegal Mutual Insurance Company reports its premium writings for private passenger automobile to the Pennsylvania Assigned Risk Plan. As a result, the Company receives all assignments from the Pennsylvania Assigned Risk Plan.

1. New Business

New business, for the purpose of this examination, was defined as policies written for the first time by the Company during the experience period.

The primary purpose of the review was to determine compliance with Act 246, The Casualty and Surety Rate Regulatory Act, Sections 4(a) and (h) [40 P.S. §1184], which requires every insurer to file with the Insurance Commissioner every manual of classifications, rules and rates, every rating plan and every modification of any rating plan, which it proposes to use in the Commonwealth. Also, no insurer shall make or issue a contract or policy except in accordance with filings or rates, which are in effect at the time. Review was also made of all the rules and rates of the Assigned Risk Plan, compliance with all provisions of Act 6 of 1990, as well as Title 75, Pa. C.S. Sections 1741, 1742, 1743 and 1744 [40 P.S. §1741, 1742, 1743 and 1744], which establishes the Assigned Risk Plan and requires insurers to abide by the rules of the Plan.

Assigned Risk Private Passenger Automobile – New Business – Clean

From the universe of 603 assigned risk private passenger automobile new business policies written as clean during the experience period, 25 files were selected for review. All 25 files selected were received and reviewed. No violations were noted.

Assigned Risk Private Passenger Automobile – New Business – Other Than Clean

From the universe of 402 assigned risk private passenger automobile new business policies written as other than clean during the experience period, 50 files were selected for review. All 50 files selected were received and reviewed. The 2 violations noted were based on 2 files, resulting in an error ratio of 4%.

The following findings were made:

2 Violations Act 246, The Casualty and Surety Rate Regulatory Act, Section 4 (40 P.S. §1184)

Requires every insurer to file with the Insurance Commissioner every manual of classifications, rules and rates, every rating plan and every modification of any rating plan, which it proposes to use in the Commonwealth. Also, no insurer shall make or issue a contract or policy except in accordance with filings or rates, which are in effect at the time of issue. The Company rated the 2 policies with an improper territory which resulted in undercharges of \$333.

Assigned Risk Private Passenger Automobile – Renewals – Clean

From the universe of 147 assigned risk private passenger automobile renewal policies written as clean during the experience period, 25 files were selected for review. All 25 files were received and reviewed. The 2 violations noted were based on 2 files, resulting in an error ratio of 8%.

The following findings were made:

2 Violations Assigned Risk Manual, Section 12(A)(13)

The assigned Company shall mail a take-out notice to each insured eligible for take-out and the producer of record at least 45 days, but no more than 60 days, prior to the expiration of the Plan policy to be replaced. The take-out notice shall contain a provisional premium quotation for the voluntary market coverage being offered. The Company failed to offer a take-out for one policy and failed to offer the take-out within 45 days of expiration of the remaining policy.

Assigned Risk Private Passenger Automobile – Renewals – Other Than Clean

The universe of 54 assigned risk private passenger automobile renewal policies written as other than clean during the experience period was selected for review. All 54 files were received and reviewed. No violations were noted.

C. Homeowners

1. New Business

New business, for the purpose of this examination, was defined as policies written for the first time by the Company during the experience period.

The purpose of the review was to measure compliance with Act 246, Sections 4(a) and (h) (40 P.S. §1184), which require every insurer to file with the Insurance Commissioner every manual of classifications, rules and rates, every rating plan and every modification of any rating plan, which it proposes to use in the Commonwealth. Also, no insurer shall make or issue

a contract or policy except in accordance with filings or rates, which are in effect at the time.

Homeowner Rating – New Business Without Surcharges

Donegal Mutual Insurance Company

From the universe of 9,486 homeowner policies written as new business without surcharges during the experience period, 20 files were selected for review. All 20 files were received and reviewed. No violations were noted.

Atlantic States Insurance Company

From the universe of 1,362 homeowner policies written as new business without surcharges during the experience period, 20 files were selected for review. All 20 files were received and reviewed. No violations were noted.

2. Renewals

A renewal is considered to be any policy, which was previously written by the Company and renewed on the normal twelve-month anniversary date.

The purpose of the review was to determine compliance with Act 246, Sections 4(a) and (h) (40 P.S. §1184), which require every insurer to file with the Insurance Commissioner every manual of classifications, rules and rates, every rating plan and every modification of any rating plan which it proposes to use in the Commonwealth. Also, no insurer shall make or issue a contract or policy except in accordance with filings or rates which are in effect at the time.

Homeowner Rating – Renewals Without Surcharges

Donegal Mutual Insurance Company

From the universe of 63,907 homeowner policies renewed without surcharges during the experience period, 25 files were selected for review. All 25 files were received and reviewed. No violations were noted.

Atlantic States Insurance Company

From the universe of 697 homeowner policies renewed without surcharges during the experience period, 25 files were selected for review. All 25 files were received and reviewed. No violations were noted.

Homeowner Rating – Renewals With Surcharges

Donegal Mutual Insurance Company

From the universe of 557 homeowner policies renewed with surcharges during the experience period, 50 files were selected for review. All 50 files were received and reviewed. The violation noted resulted in an error ratio of 2%.

The following finding was made:

*1 Violation Act 246, The Casualty and Surety Rate Regulatory Act,
Section 4 (40 P.S. §1184)*

Requires every insurer to file with the Insurance Commissioner every manual of classifications, rules and rates, every rating plan and every modification of any rating plan, which it proposes to use in the Commonwealth. Also, no insurer shall make or issue a contract or policy except in accordance with filings or rates, which are in effect at the time of issue. The policy was not rated in accordance with

the Company's filed and approved rating plan. The Company surcharged for only one loss. Surcharging applies for two or more losses. This resulted in an overcharge of \$52.

Atlantic States Insurance Company

This Company did not report any homeowner policies renewed with surcharges during the experience period.

D. Tenant Homeowners

1. New Business

New business, for the purpose of this examination, was defined as policies written for the first time by the Company during the experience period.

The purpose of the review was to measure compliance with Act 246, Sections 4(a) and (h) (40 P.S. §1184), which require every insurer to file with the Insurance Commissioner every manual of classifications, rules and rates, every rating plan and every modification of any rating plan, which it proposes to use in the Commonwealth. Also, no insurer shall make or issue a contract or policy except in accordance with filings or rates, which are in effect at the time.

Tenant Homeowner Rating – New Business Without Surcharges

Donegal Mutual Insurance Company

From the universe of 2,169 tenant homeowner policies written as new business without surcharges during the experience period, 25 files were selected for review. All 25 files were received and reviewed. No violations were noted.

Atlantic States Insurance Company

This Company did not report any tenant homeowner policies written as new business without surcharges during the experience period.

2. Renewals

A renewal is considered to be any policy, which was previously written by the Company and renewed on the normal twelve-month anniversary date.

The purpose of the review was to determine compliance with Act 246, Sections 4(a) and (h) (40 P.S. §1184), which require every insurer to file with the Insurance Commissioner every manual of classifications, rules and rates, every rating plan and every modification of any rating plan which it proposes to use in the Commonwealth. Also, no insurer shall make or issue a contract or policy except in accordance with filings or rates which are in effect at the time.

Tenant Homeowner Rating – Renewals Without Surcharges

Donegal Mutual Insurance Company

From the universe of 8,469 tenant homeowner policies renewed without surcharges during the experience period, 25 files were selected for review. All 25 files were received and reviewed. No violations were noted.

Atlantic States Insurance Company

This Company did not report any tenant homeowner policies renewed without surcharges during the experience period.

Tenant Homeowner Rating – Renewals With Surcharges

Donegal Mutual Insurance Company

The universe of 18 tenant homeowner policies renewed with surcharges during the experience period was selected for review. All 18 files were received and reviewed. The 5 violations noted were based on 5 files, resulting in an error ratio of 28%.

The following findings were made:

*5 Violations Act 246, The Casualty and Surety Rate Regulatory Act,
Section 4 (40 P.S. §1184)*

Requires every insurer to file with the Insurance Commissioner every manual of classifications, rules and rates, every rating plan and every modification of any rating plan, which it proposes to use in the Commonwealth. Also, no insurer shall make or issue a contract or policy except in accordance with filings or rates, which are in effect at the time of issue. The policies were not rated in accordance with the Company's filed and approved rating plan. The 5 files noted were surcharged for one loss. Surcharging applies for two or more losses. This resulted in overcharges of \$183.

Atlantic States Insurance Company

This Company did not report any tenant homeowner policies renewed with surcharges during the experience period.

E. Dwelling Fire

1. New Business

New business, for the purpose of this examination, was defined as policies written for the first time by the Company during the experience period.

The purpose of the review was to measure compliance with Act 246, Sections 4(a) and (h) (40 P.S. §1184), which require every insurer to file with the Insurance Commissioner every manual of classifications, rules and rates, every rating plan and every modification of any rating plan, which it proposes to use in the Commonwealth. Also, no insurer shall make or issue a contract or policy except in accordance with filings or rates, which are in effect at the time.

Dwelling Fire Rating – New Business Without Surcharges

Donegal Mutual Insurance Company

From the universe of 57 dwelling fire policies written as new business without surcharges during the experience period, 10 files were selected for review. All 10 files were received and reviewed. No violations were noted.

Atlantic States Insurance Company

This Company did not report any dwelling fire policies written as new business without surcharges during the experience period.

2. Renewals

A renewal is considered to be any policy, which was previously written by the Company and renewed on the normal twelve-month anniversary date.

The purpose of the review was to determine compliance with Act 246, Sections 4(a) and (h) (40 P.S. §1184), which require every insurer to file with the Insurance Commissioner every manual of classifications, rules and rates, every rating plan and every modification of any rating plan which it proposes to use in the Commonwealth. Also, no insurer shall make or issue a contract or policy except in accordance with filings or rates which are in effect at the time.

Dwelling Fire Rating – Renewals Without Surcharges

Donegal Mutual Insurance Company

From the universe of 528 dwelling fire policies renewed without surcharges during the experience period, 25 files were selected for review. All 25 files were received and reviewed. No violations were noted.

Atlantic States Insurance Company

This Company did not report any dwelling fire policies renewed without surcharges during the experience period.

VII. CLAIMS

The Company was requested to provide copies of all established written claim handling procedures utilized during the experience period. Written claim handling procedures were received and reviewed for any inconsistencies, which could be considered discriminatory, specifically prohibited by statute or regulation, or unusual in nature. No violations were noted.

The Claims review consisted of the following areas of review:

- A. Automobile Property Damage Claims
- B. Automobile Comprehensive Claims
- C. Automobile Collision Claims
- D. Automobile Total Loss Claims
- E. Automobile First Party Medical Claims
- F. Automobile First Party Medical Claims Referred to a PRO
- G. Homeowner Claims
- H. Tenant Homeowner Claims
- I. Dwelling Fire Claims

The primary purpose of the review was to determine compliance with Title 31, Pennsylvania Code, Chapter 146, Unfair Claims Settlement Practices. The files were also reviewed to determine compliance with Act 205, Section 4 (40 P.S. §1171.4) and Section 5(a)(10)(vi) [40 P.S. §1171.5(a)(10)(vi)], Unfair Insurance Practices Act.

A. Automobile Property Damage Claims

Donegal Mutual Insurance Company

From the universe of 3,481 private passenger automobile property damage claims reported during the experience period, 50 files were selected for

review. All 50 files were received and reviewed. No violations were noted.

Atlantic States Insurance Company

From the universe of 145 private passenger automobile property damage claims reported during the experience period, 25 files were selected for review. All 25 files were received and reviewed. No violations were noted.

B. Automobile Comprehensive Claims

Donegal Mutual Insurance Company

From the universe of 2,823 private passenger automobile comprehensive claims reported during the experience period, 28 files were selected for review. All 28 files were received and reviewed. No violations were noted.

Atlantic States Insurance Company

From the universe of 2,108 private passenger automobile comprehensive claims reported during the experience period, 25 files were selected for review. All 25 files were received and reviewed. No violations were noted.

C. Automobile Collision Claims

Donegal Mutual Insurance Company

From the universe of 3,242 private passenger automobile collision claims reported during the experience period, 31 files were selected for review. All 31 files were received and reviewed. No violations were noted.

Atlantic States Insurance Company

From the universe of 1,795 private passenger automobile collision claims reported during the experience period, 25 files were selected for review.

All 25 files were received and reviewed. No violations were noted.

D. Automobile Total Loss Claims

Donegal Mutual Insurance Company

From the universe of 688 private passenger automobile total loss claims reported during the experience period, 32 files were selected for review.

All 32 files were received and reviewed. No violations were noted.

Atlantic States Insurance Company

From the universe of 295 private passenger automobile total loss claims reported during the experience period, 25 files were selected for review.

All 25 files were received and reviewed. No violations were noted.

E. Automobile First Party Medical Claims

Donegal Mutual Insurance Company

From the universe of 2,088 private passenger automobile first party medical claims reported during the experience period, 50 files were selected for review. All 50 files were received and reviewed. The violation noted resulted in an error ratio of 2%.

The following finding was made:

1 Violation Title 31, Pa. Code, Section 146.5(d)

Requires an insurer, upon receiving notification of a claim, shall provide within ten working days necessary claim forms, instructions and reasonable assistance so that first-party

claimants can comply with policy conditions and reasonable requirements of the insurer. The Company did not provide the necessary documents to the claimant within ten working days.

Atlantic States Insurance Company

From the universe of 1,021 private passenger automobile first party medical claims reported during the experience period, 25 files were selected for review. All 25 files were received and reviewed. No violations were noted.

F. Automobile First Party Medical Claims Referred to a PRO

Donegal Mutual Insurance Company

The universe of 5 private passenger automobile first party medical claims referred to a peer review organization was selected for review. All 5 files were received and reviewed. The Company was requested to provide copies of any contracts with the peer review organization it has contracted. The contracts were received and reviewed. No violations were noted.

Atlantic States Insurance Company

The universe of 11 private passenger automobile first party medical claims referred to a peer review organization was selected for review. All 11 files were received and reviewed. The Company was requested to provide copies of any contracts with the peer review organization it has contracted. The contracts were received and reviewed. No violations were noted.

G. Homeowner Claims

Donegal Mutual Insurance Company

From the universe of 4,175 homeowner claims reported during the experience period, 25 files were selected for review. All 25 files were received and reviewed. No violations were noted.

Atlantic States Insurance Company

From the universe of 59 homeowner claims reported during the experience period, 10 files were selected for review. All 10 files were received and reviewed. No violations were noted.

H. Tenant Homeowner Claims

Donegal Mutual Insurance Company

From the universe of 165 tenant homeowner claims reported during the experience period, 20 files were selected for review. All 20 files were received and reviewed. No violations were noted.

Atlantic States Insurance Company

This Company did not report any tenant homeowner claims during the experience period.

I. Dwelling Fire Claims

Donegal Mutual Insurance Company

From the universe of 162 dwelling fire claims reported during the experience period, 20 files were selected for review. All 20 files were received and reviewed. The 3 violations noted were based on 3 files, resulting in an error ratio of 15%.

The following findings were made:

2 Violations Title 31, Pa. Code, Section 146.6

Every insurer shall complete investigation of a claim within 30 days after notification of the claim, unless such investigation cannot reasonably be completed within 30 days, and every 45 days thereafter, the insurer shall provide the claimant with a reasonable written explanation for the delay and state when a decision on the claim may be expected. The Company did not provide timely status letters for the 2 claims noted.

1 Violation Title 31, Pa. Code, Section 146.7(a)(1)

Within 15 working days after receipt by the insurer of properly executed proofs of loss, the first-party claimant shall be advised of the acceptance or denial of the claim by the insurer. The Company failed to deny the portion of the claim that was not covered, in writing.

VIII. FORMS

Throughout the course of the examination, all underwriting files were reviewed to identify the policy forms used in order to verify compliance with Insurance Company Law, Section 354 (40 P.S. §477b), Approval of Policies, Contracts, etc., Prohibiting the Use Thereof Unless Approved. During the experience period of the examination, Section 354 provided that it shall be unlawful for any insurance company to issue, sell, or dispose of any policy contract or certificate covering fire, marine, title and all forms of casualty insurance or use applications, riders, or endorsements in connection therewith, until the forms have been submitted to and formally approved by the Insurance Commissioner. All underwriting and claim files were also reviewed to verify compliance with Act 165 of 1994 [18 Pa. CS §4117(k)(1)] and Title 75, Pa. C.S. §1822, which requires all insurers to provide an insurance fraud notice on all applications for insurance, all claims forms and all renewals of coverage.

The following finding was made:

1 Violation Act 165 of 1994 [18 Pa. C.S. §4117(k)(1)]

Any person who knowingly and with intent to defraud any insurance company or other person files an application for insurance or statement of claim containing any materially false information or conceals for the purpose of misleading, information concerning any fact material thereto, commits a fraudulent insurance act, which is a crime and subjects such person to criminal and civil penalties. The Company failed to provide the fraud warning notice on the insured's statement of claim.

IX. ADVERTISING

The Company was requested to provide copies of all advertising, sales material and internet advertisements in use during the experience period.

The purpose of this review was to determine compliance with Act 205, Section 5 [40 P.S. §1171.5], which defines unfair methods of competition and unfair or deceptive acts or practices in the business of insurance, as well as Title 31, Pennsylvania Code, Section 51.2(c) and Section 51.61.

The Company provided 289 pieces of advertising which included brochures, agent's kits, mail solicitation, billboard, newspaper ad slicks, newspaper inserts, television, radio and newsletters. Internet advertising was also reviewed. No violations were noted.

X. CONSUMER COMPLAINTS

The Company was requested to identify all consumer complaints received during the experience period and provide copies of their consumer complaint logs for the preceding four years. The Company identified 112 consumer complaints received during the experience period and provided all consumer complaint logs requested. Of the 112 complaints reported, 54 complaints were requested, received and reviewed.

The purpose of the review was to determine compliance with the Unfair Insurance Practices Act, No. 205 (40 P.S. §1171). Section 5(a)(11) of the Act requires a Company to maintain a complete record of all complaints received during the preceding four years. This record shall indicate the total number of complaints, their classification by line of insurance, the nature of each complaint, the disposition of these complaints and the time it took to process each complaint.

The following findings were made:

1 Violation Title 31, Pa. Code, Section 146.5(b)

Every insurer, upon receipt of an inquiry from the Department respecting a claim shall, within 15 working days of receipt of such inquiry, furnish the Department with an adequate response to the inquiry. The Company failed to respond to a Department inquiry in a timely manner.

1 Violation Act 86, Section 3(a)(5) [40 P.S. §3403(a)(5)]

Requires that a nonrenewal notice shall state the specific reasons for the nonrenewal. The reasons shall identify the condition, factor or loss experience, which caused the nonrenewal. The notice shall

provide sufficient information or data for the insured to correct the deficiency.

AND

Title 31, Pa. Code, Section 113.88

The reason given for nonrenewal shall be clear and complete. It shall be stated so that a person of average intelligence and education can understand it. Phrases such as “losses” or “underwriting reasons” are not sufficiently specific reasons for nonrenewal. The Company failed to provide a specific reason for nonrenewal.

2 Violations Act 205, Section 5(a)(9) [40 P.S. §1171.5(a)(9)]

Prohibits canceling any policy of insurance covering owner-occupied private residential properties or personal property of individuals that has been in force for sixty days or more or refusing to renew any such policy unless the policy was obtained through material misrepresentation, fraudulent statements, omissions or concealment of fact material to the acceptance of the risk or to the hazard assumed by the company; or there has been a substantial change or increase in hazard in the risk assumed by the company subsequent to the date the policy was issued; or there is a substantial increase in hazards insured against by reason of willful or negligent acts or omissions by the insured; or the insured has failed to pay any premium when due or for any other reasons approved by the Commissioner. The Company failed to provide a proper reason for cancellation for the 2 files noted.

1 Violation Act 86, Section 3(a)(2) [40 P.S. §3403(a)(2)]

Requires that a nonrenewal notice be forwarded directly to the named insured or insureds at least 60 days in advance of the effective

date of the termination. The Company did not provide at least 60 days notice of nonrenewal.

1 Violation Act 68, Section 2003(b) [40 P.S. §991.2003(b)]

States that an insurer may not cancel or refuse to renew a policy of automobile insurance on the basis of one accident within the thirty-six (36) month period prior to the upcoming anniversary date of the policy. The Company nonrenewed the policy on the basis of one paid claim.

The following synopsis reflects the nature of the 54 complaints that were reviewed.

• 17	Cancellations/Nonrenewal	31%
• 28	Claims	52%
• 8	Premium/Accounting	15%
• 1	Miscellaneous	2%
<hr/>		<hr/>
54		100%

XI. LICENSING

In order to determine compliance by the Company and its agency force with the licensing requirements applicable to Section 641.1(a) [40 P.S. §310.41(a) and Section 671-A [40 P.S. §310.71] of the Insurance Department Act No. 147, the Company was requested to furnish a list of all active producers during the experience period and a listing of all producers terminated during the experience period. Underwriting files were checked to verify proper licensing and appointment.

The following findings were made:

Donegal Mutual Insurance Company

2 Violations Insurance Department Act, No. 147, Section 641.1A

[40 P.S. §310.41a]

(a) Any insurance entity or licensee accepting applications or orders for insurance from any person or securing any insurance business that was sold, solicited or negotiated by any person acting without an insurance producer license shall be subject to civil penalty of no more than \$5,000.00 per violation in accordance with this act. This section shall not prohibit an insurer from accepting an insurance application directly from a consumer or prohibit the payment or receipt of referral fees in accordance with this act.

The following producers were found to be writing and /or soliciting policies but were not found in Insurance Department records as holding a Pennsylvania producer license.

Fischer Insurance Agency, Inc.
Thompson Insurance, Inc.

13 Violations Insurance Department Act, No. 147, Section 671-A

(40 P.S. §310.71)

(a) Representative of the insurer – An insurance producer shall not act on behalf of or as a representative of the insurer unless the insurance producer is appointed by the insurer. An insurance producer not acting as a representative of an insurer is not required to be appointed.

(b) Representative of the consumer – An insurance producer acting on behalf of or representing an insurance consumer shall execute a written agreement with the insurance consumer prior to representing or acting on their behalf that:

(1) Delineates the services to be provided; and

(2) Provides full and complete disclosure of the fee to be paid to the insurance producer by the insurance consumer.

(c) Notification to Department – An insurer that appoints an insurance producer shall file with the Department a notice of appointment. The notice shall state for which companies within the insurer's holding company system or group the appointment is made.

(d) Termination of appointment – Once appointed, an insurance producer shall remain appointed by an insurer until such time as the insurer terminates the appointment in writing to the insurance producer or until the insurance producer's license is suspended, revoked or otherwise terminated.

(e) Appointment fee – An appointment fee of \$12.50 will be billed annually to the insurer for each producer appointed by the insurer

during the preceding calendar year regardless of the length of time the producer held the appointment with the insurer. The appointment fee may be modified by regulation.

(f) Reporting – An insurer shall, upon request, certify to the Department the names of all licensees appointed by the insurer.

The following producers were found to be writing policies but were not found in Insurance Department records as having an appointment. The Company failed to file a notice of appointment and submit appointment fees to the Department.

Abraham & Petrini Insurance Agency, Inc.
Benton Insurance Center, Inc.
Carlisle Insurance Services
Ebensburg Insurance Agency
Essick & Barr Insurance
GDK, Inc./T/A Defurio Mongel & Associates
Lancaster Insurance Group LLC
Roitz, R F T/A Norwin Ins Agency
Skier, A M Agency, Inc.
USI Midatlantic
William Agency
William Insurance Agency, Inc.
Pandel Agency

Atlantic States Insurance Company

2 Violations Insurance Department Act, No. 147, Section 641.1A

[40 P.S. §310.41a]

(a) Any insurance entity or licensee accepting applications or orders for insurance from any person or securing any insurance business that was sold, solicited or negotiated by any person acting without an insurance producer license shall be subject to civil penalty of no more than \$5,000.00 per violation in accordance with this act. This

section shall not prohibit an insurer from accepting an insurance application directly from a consumer or prohibit the payment or receipt of referral fees in accordance with this act.

The following producers were found to be writing and /or soliciting policies but were not found in Insurance Department records as holding a Pennsylvania producer license.

Atlantic Group Advantage, Inc.
Miller, Howard S.

*9 Violations Insurance Department Act, No. 147, Section 671-A
(40 P.S. §310.71)*

(a) Representative of the insurer – An insurance producer shall not act on behalf of or as a representative of the insurer unless the insurance producer is appointed by the insurer. An insurance producer not acting as a representative of an insurer is not required to be appointed.

(b) Representative of the consumer – An insurance producer acting on behalf of or representing an insurance consumer shall execute a written agreement with the insurance consumer prior to representing or acting on their behalf that:

(1) Delineates the services to be provided; and

(2) Provides full and complete disclosure of the fee to be paid to the insurance producer by the insurance consumer.

(c) Notification to Department – An insurer that appoints an insurance producer shall file with the Department a notice of appointment. The notice shall state for which companies within the insurer's holding company system or group the appointment is

made.

(d) Termination of appointment – Once appointed, an insurance producer shall remain appointed by an insurer until such time as the insurer terminates the appointment in writing to the insurance producer or until the insurance producer's license is suspended, revoked or otherwise terminated.

(e) Appointment fee – An appointment fee of \$12.50 will be billed annually to the insurer for each producer appointed by the insurer during the preceding calendar year regardless of the length of time the producer held the appointment with the insurer. The appointment fee may be modified by regulation.

(f) Reporting – An insurer shall, upon request, certify to the Department the names of all licensees appointed by the insurer.

The following producers were found to be writing policies but were not found in Insurance Department records as having an appointment. The Company failed to file a notice of appointment and submit appointment fees to the Department.

Aliciene, Joseph R.
BCF Group
Davis Trachtenberg, Inc.
Gray Insurance Group, Inc.
Knowles Associates LLC
National Associates
Retire-Wise Financial Services, Inc.
Strausser Insurance Agency, Inc.
Mechanicsburg Ins. Service

XII. RECOM MENDATIONS

The recommendations made below identify corrective measures the Department finds necessary as a result of the number of some violations, or the nature and severity of other statutory or regulatory violations, noted in the Report.

1. The Company must review and revise internal control procedures to ensure compliance with cancellation notice requirements of Act 68, Sections 2003, 2004, 2006 and 2008 [40 P.S. §§991.2003, 991.2004, 991.2006 and 991.2008], so that the violations noted in the Report do not occur in the future.
2. The Company must review Act 205, Section 5(a)(9) [40 P.S. §1171.5(a)(9)] to ensure that violations regarding the requirements for cancellation and nonrenewal notices, as noted in the Report, do not occur in the future.
3. The Company must review Insurance Company Law, Section 506.1 regarding the cancellation of property insurance after the death of the named insured to ensure that basic property coverage is maintained at least 180 days.
4. The Company must reinforce its internal underwriting controls to ensure that all records and documents are maintained in accordance with Insurance Department Act, Section 903(a) [40 P.S. §323.3], so that violations noted in the Report do not occur in the future.

5. The Company must review and revise internal control procedures to ensure compliance relative to commercial cancellation and nonrenewal requirements of Act 86, Sections 1, 2 and 3 [40 P.S. §§3401, 3402 and 3403], so that the violations noted in the Report do not occur in the future.
6. The Company must review Insurance Company Law, Section 653, to ensure that violations regarding workers' compensation cancellations do not occur in the future.
7. The Company must review Act 205, Section 5(a)(4) [40 P.S. §1171.5(a)(4)] to ensure that the violations relative to supporting coverage noted in the Report does not occur in the future.
8. The Company must review Title 75, Pa. C.S. 1793(b) to ensure that violations regarding the requirement to provide the insured with a surcharge disclosure plan at the time of application, as noted in the Report, do not occur in the future.
9. The Company must review Act 246, Section 4(a) and (h) [40 P.S. §1184] and take appropriate measures to ensure the homeowner rating violations listed in the report do not occur in the future.
10. The premium overcharges noted in the rating section of this report must be refunded to the insureds and proof of such refunds must be provided to the Insurance Department within 30 days of the report issue date.

11. The Company should review and revise internal control procedures to ensure compliance with the claims handling requirements of Title 31, Pennsylvania Code, Chapter 146, Unfair Claims Settlement Practices so that the violations relating to denials, status letters and providing claim forms do not occur in the future.
12. The Company must ensure that all claim forms contain the required fraud warning notice.
13. The Company must review Title 31, Pa. Code, Section 146.5(b) with its claim staff to ensure that all Department inquiries respecting a claim shall furnish the Department with an adequate response to the inquiry within 15 working days of receipt of such inquiry.
14. The Company must ensure all producers are properly licensed and appointed, as required by Section 641.1(a) and Section 671-A [40 P.S. §310.41(a) and 40 P.S. §310.71] of the Insurance Department Act No. 147, prior to accepting any business from any producer.
15. The Company must revise and reissue their underwriting guidelines for use in Pennsylvania to ensure that guidelines do not require supporting primary homeowner coverage in order to bind student occupied rentals and seasonal or secondary dwellings.

XIII. COMPANY RESPONSE



1195 River Road, P.O. Box 302
Marietta, Pennsylvania 17547-0302
(717) 426-1931
www.donegalgroup.com

January 31, 2008

Mr. Chester A. Derk, Jr., AIE, HIA
Market Conduct Division Chief
Commonwealth of Pennsylvania
Insurance Department
Bureau of Enforcement
1227 Strawberry Square
Harrisburg, PA 17120

Re: **Examination Warrant Number: 06-M19-034 Donegal Mutual Insurance Company
Atlantic States Insurance Company**

Dear Mr. Derk:

This letter is in response to the above Examination Report. We appreciate the review conducted by the Department and we welcome the opportunity to use the findings of the report to help us better serve the insurance consumers of Pennsylvania.

As you might expect, there are a number of findings in the report with which we disagree and our comments regarding these findings follow. Since we have previously sent documentation in support of our comments, we will not burden the Department by sending duplicate documentation with this letter, however, we wish to incorporate this documentation by reference. In our response we will refer to the appropriate sections of the report and the particular violations listed in those sections.

IV. Underwriting Practices and Procedures

On Page 8 of the report we are cited for two violations of Act 205, Section 5(a)(4), because our HO4 and HO6 guidelines effective 9/1/04 stated that we would write student-occupied rentals and seasonal or secondary dwellings as long as we were providing the coverage for the primary dwelling. Act 205, Section 5(a)(4) prohibits the entering into of any agreement to commit, or by any concerted action committing, any act of boycott, coercion or intimidation resulting in or tending to result in unreasonable restraint of, or monopoly in, the business of insurance. We believe that requiring supporting coverage in the above two cases did not constitute the entering into of any agreement or any concerted action to commit boycott, coercion or intimidation.

Donegal did not pursue this type of business on a stand-alone basis during the Market Conduct examination experience period. We did, however, consider the writing of this kind

of business on an “accommodation” basis, to round out an account for an existing Homeowners insured. In 2004 the PA Market Conduct Division conducted a review of Personal Lines Homeowners Insurance underwriting guidelines for the period of 1/1/04 through 6/30/04. In compliance with the Department’s letter of 10/22/04, we submitted our Homeowners guidelines, which included the primary residence support requirement for the writing of these types of properties. We received no criticism or indication from the Department that these guidelines were not in compliance with Act 205.

We later amended our guidelines and removed the requirement for supporting coverage for student-occupied rentals and seasonal or secondary dwellings. However, we believe that we were not in violation of Act 205 when these requirements were in our guidelines and we respectfully request that these alleged violations be removed from the report.

V. Underwriting

C. Property

On Page 15 of the report we are cited for violation of Act 205, Section 5(a)(4) because of a cancellation notice citing lack of supporting business as the reason. This involved an application for a Personal Inland Marine Policy covering a diamond ring. At the time of submission it was not the policy of the company to write stand-alone Personal Inland Marine policies. This was considered to be an “accommodation line” to be written for existing Homeowners policyholders. Since the application was submitted on a stand-alone basis and not for an existing policyholder the policy was issued and immediately cancelled. As stated above, we do not believe this constitutes any violation of Act 205 inasmuch as there was no entering into any agreement to commit, or by any concerted action committing, any act of boycott, coercion or intimidation.

Similar to what was stated above, we later amended our guidelines and removed the requirement for supporting coverage for Personal Inland Marine policies. However, we believe that we were not in violation of Act 205 when these requirements were in our guidelines and we respectfully request that these alleged violations be removed from the report.

On Page 16 of the report we are cited for 11 violations of Act 205, Section 5(a)(9), midterm cancellations for improper reasons. However, we disagree with five of these eleven allegations.

In the 3/27/07 summary issued by the examiners, Policy No. HP 5023208 was cited as being in violation because there was “No increase in hazard/condition”, however, the policy was not cancelled for increase in hazard/condition, but rather for material misrepresentation by the insured. The original application indicated “yes” to the question, “Is the property in good and safe condition demonstrating pride of ownership?” The inspection, as stated on the notice of cancellation, clearly showed this to be a false statement. Consequently the policy was cancelled because of material misrepresentation, a cancellation we believe was appropriate. We forwarded an exhibit with our 4/9/07 response to this summary.

Policy No. HP 1132291 was cited for no increase in hazard. Coverage was originally written as new business effective 9/24/04 as a dwelling under construction. As of the issuance of the renewal policy it was determined that the dwelling was not yet completed and occupied. Our underwriting guidelines allow the writing of dwellings under construction but they must be completed within one year. Since the longer a dwelling remains under construction without being completed and occupied the greater the increase in hazard, we believe the cancellation was appropriate. An exhibit was forwarded with our original response.

Policy No. G 1132704 was cited for no increase in hazard. An inspection of the property revealed an elevated deck with no railing to prevent falling from the deck. Recommendations were made to have railings installed. We were advised that the insured would agree to install railings to mitigate this hazardous condition. Despite several follow-ups from the company, the insured failed to remedy this deficiency over the next eight months. In *Smith/Erie*, PO4-10-004 (2005) an insured's failure to comply with an insurer's recommendation constituted an increase in hazard by reason of the insured's failure to act. The insured's failure to comply with our recommendations constituted a willful and negligent act and an increase in hazard and, therefore, we believe the cancellation was appropriate. An exhibit was forwarded with our original response.

Policy No. G 5014590 was cited for no increase in hazard. The policy was cancelled because a deck and steps leading to the front door were not properly protected with railings. The dwelling was originally written as a dwelling under construction and thus when originally written this hazardous condition did not exist. However, upon discovery of the condition the insured was given approximately seven months to correct the deficiency. When the railings were still not installed after this length of time the policy was cancelled because of this increase in hazard. We believe the cancellation was appropriate. An exhibit was forwarded with our original response.

Policy No. G 5015339 was cited for no increase in hazard. Actually this was a nonrenewal, not a midterm cancellation. An inspection revealed several hazardous conditions for which recommendations for correction were made. The insured did not comply with the recommendations and the policy was nonrenewed because of the willful and negligent acts of the insured in failing to comply with the recommendations, thus resulting in an increase in hazard. Therefore, we believe the nonrenewal was appropriate. An exhibit was forwarded with our original response.

On Page 17 of the report we are cited for two violations of Act 205, Section 5(a)(4) for requiring supporting business. For one of these policies, G1133703, the reason for the termination was that the policy covered a seasonal/secondary dwelling and the primary Homeowners policy was no longer in effect. Again, for the reasons stated above we disagree with this allegation and request that this citation be deleted from the report. However, the other policy, BT 0008711, a Boatowners policy, was not cancelled because of lack of support, but rather because of the value of the boat, as stated in our original response to the 3/21/07 summary. We forwarded an exhibit with that response. Thus we would also respectfully request that the allegation that this cancellation violated Act 205, Section 5(a)(4) be removed from the report.

On Page 17 of the report we are cited for two violations for failing to provide 180 days of coverage after the death of a named insured. These cancellations were the result of human error as it is our practice to continue coverage for 180 days following the death of an insured.

On Page 18 of the report we are cited for four violations of Act 205, Section 5(a)(9) for nonrenewing for improper reasons. As stated in our original response of 3/12/07, we disagree with one of these findings. Policy No. HP 5019408 was written new 4/20/05. An inspection developed paint peeling and chipping over the entire house. Recommendation letters requesting that the siding be repainted or replaced to prevent further deterioration were sent three times with no response, so the policy was non-renewed because of a substantial increase in hazard by reason of the insured's willful or negligent acts or omissions. In *Lichter v. State Farm, PH99-12-018 (2000)* it was found that it is unnecessary to establish the pre-inspection condition of the property when the policy termination is for negligent or willful failure of the insured to address a significant hazard discovered in an inspection and communicated to the insured. In another adjudication it was found that when a property policy is terminated for increase in hazard by failure to address a hazard discovered by the insurer which is communicated to the insured, it is not necessary to establish a baseline condition of the property at policy inception when relying on willful or negligent acts to justify policy termination. *Nationwide v. Dundore, PO2-04-036 (2002)* An exhibit was forwarded with our original response.

On Page 19 we are cited for violations of Act 205, Section 5(a)(4) because of nonrenewal for lack of supporting business for secondary/seasonal dwellings. Again we respectfully request that these three alleged violations be removed from the report for the same reasons as explained on earlier pages of this response.

D. Commercial Property

On Pages 25 and 26 of the report we are cited for seven violations of Act 86, Section 1 for failure to provide not less than 30 days advance notice of an increase in commercial renewal premium. As stated in our 3/21/07 original response, for which exhibits were provided, we request that one of these violations be deleted from the report. For Policy No. CF 0122179 the renewal premium did not increase and thus no notification was required.

E. Commercial Automobile

On Page 28 of the report we are cited for two violations of Act 86, Section 3(a)(5) for not providing a specific enough reason for midterm cancellation of a commercial automobile policy. On Policy No. CA 8015764 the reason stated is, "Company has been unable to gain access to premises to conduct loss control survey because insured is in Florida. Donegal is not licensed to write business in Florida." We believe this reason is indeed specific and we would respectfully request that this alleged violation be deleted from the report. An exhibit was forwarded with our original response.

We are also cited on Page 28 for a violation of Act 205, Section 5(a)(4) for cancelling a commercial auto policy because of lack of supporting coverage. Act 205, Section 5(a)(4),

prohibits the entering into of any agreement to commit, or by any concerted action committing, any act of boycott, coercion or intimidation resulting in or tending to result in unreasonable restraint of, or monopoly in, the business of insurance. We believe that requiring supporting coverage in the above case did not constitute the entering into of any agreement or any concerted action to commit boycott, coercion or intimidation.

The writing of commercial lines coverages on an account basis is standard industry practice and is done for valid underwriting reasons. For example, there can be a blurring of coverage applicability between commercial auto and general liability policies. Depending on the nature of the claim, it could be unclear as to whether an insured's commercial auto policy should apply or whether the general liability policy is applicable. If these policies are with different carriers, an insured could be caught between two insurance companies arguing over whose policy should be paying the claim. For this reason it has been our normal underwriting practice to write both of these coverages for an insured, thus removing any potential gaps in coverage that could place the insured at a disadvantage in a claims situation.

This issue was raised by the examiners in our Pennsylvania Market Conduct Exam conducted in 1989, however, in the final settlement the Department allowed the continuation of this requirement for commercial lines.

Additionally, on the policy in question, Policy No. CA 8026293, the reason on the cancellation notice was, "Risk no longer meets minimum underwriting guidelines for insurability by the company." Along with our original response on 3/30/07 we forwarded a copy of a letter from the underwriter to the agent advising that the company did not write monoline commercial auto coverage but that the policy was also being cancelled because of the insured's license suspension and multiple violations. We would request that this violation be deleted from the report.

On Page 29 we are cited for a similar violation of Act 205, Section 5(a)(4) , non-renewal of a commercial auto policy because of lack of supporting coverage, and we would respectfully request the deletion of this violation for the reason outlined above.

On Page 32 we are cited for a similar violation of Act 205, Section 5(a)(4) , declination of a commercial auto policy because of lack of supporting coverage, and we would respectfully request the deletion of this violation for the reason outlined above.

As a matter of information, however, we would like to advise the Department that we do now write monoline commercial automobile policies.

VI. Rating

A. Private Passenger Automobile

On pages 42-44 of the report we are cited for a total of 125 violations of Title 75, Pa C.S. §1793(b) for failure to provide a copy of our surcharge disclosure plan at the time of application. In our original response of 4/20/07, we attached form PLOF 111ax, a sample

Surcharge Disclosure Statement that we provided to every prospective insured during the application process. It is our understanding that we were cited for alleged violations because we were providing this form at the time of policy issuance.

As we stated in our original response, we do not require premium payment when a private passenger auto application is submitted. In order for a contract to be completed there must be offer, acceptance and consideration, i.e. the payment of premium. Until payment is made the transaction is still in the process of application. When the policy is delivered, the applicant can decide whether to pay the premium or not. If the applicant decides not to pay the premium, there has been no consideration and the application process has not been completed.

Thus when we provided the insured with a copy of our Surcharge Disclosure Statement prior to receipt of consideration, it was being provided during the application process and thus was in compliance with Title 75, §1793(b).

Please be advised that, as above, in response to the opinion expressed by the Department during this examination, we have changed our procedures and we now provide our surcharge disclosure notice at the time coverage is quoted. However, we ask that we not be considered to be in violation of Title 75 at the time of the examination and we request that all 125 alleged violations be deleted from the Market Conduct Report.

XII. Recommendations

Our response to each of the numbered recommendations is as follows:

1. The review of our internal control procedures to ensure compliance with the cancellation notice requirements of Act 68 is an ongoing process. We continually review and when necessary revise these procedures as part of our Sarbanes-Oxley compliance.
2. We have reviewed Act 205, Section 5(a)(9) regarding the requirements for cancellation and nonrenewal notices and we will continue to do so on an ongoing basis in an effort to ensure that violations don't occur in the future. As noted previously in this response, we disagree with the Department's findings regarding certain violations alleged in this report, however, it is always our intent to comply with the insurance laws and regulations of the State of Pennsylvania.
3. As stated on Page 5 of this response, it is our practice to continue coverage for 180 days following the death of an insured. The two cancellations that occurred in less than 180 days happened as a result of human error, and one of these errors was a miscounting of the days.
4. It is our company practice to maintain underwriting controls to ensure that all records and documents are maintained in accordance with Insurance Department Act, Section 903(a).

It is noted that the examiners found only one instance where a record was not properly maintained.

5. We have reviewed our internal procedures with regard to commercial cancellations and nonrenewals, especially in the areas of proper notification time frames, specificity of reasons and increases in hazard. In the cases where the notices were cited for lack of specificity it appears the individuals who issued the termination notices thought they were in compliance and that the reasons shown on the notices were specific enough to be understood by the insureds. However, we have re-instructed our commercial staff regarding this provision of Act 86 to make sure that future termination notices contain specific enough information to comply with the Act. Regarding the provision requiring 30 day advance notification of renewal premium increases, it is the policy of the Company to comply with this section of Act 86 by providing the insureds with their renewal policies not less than 30 days before the expiration of the current term. The importance of this provision of the Act has been reinforced to staff and we have redoubled our efforts to ensure compliance.

6. It is the practice of the Company to comply with Insurance Company Law, Section 653 regarding workers' compensation cancellations. The violations cited by the Department occurred as a result of underwriter error. It has been reiterated to staff that workers' compensation policies may not be cancelled during the term of the policy for any reason other than nonpayment of premium.

7. As stated in the body of our response, we do not believe our former requirement of supporting coverage was a violation of Act 205, and that our actions were in compliance with guidelines approved by the Pennsylvania Insurance Department. As noted, however, requirements for supporting primary residence coverage for student-occupied rentals, seasonal/secondary residences and personal inland marine coverages are no longer in our guidelines.

8. We have reviewed Title 75, Pa C.S. §1793 (b) and, as stated in the body of our response, we believe the manner in which we provided notice of our surcharge disclosure plan was in compliance. However, as noted we have changed our procedures in order to comply with the opinion expressed by the Insurance Department during the examination.

9. The report cited ten violations of Act 246. Four of these violations, incorrect rating territories on personal auto policies, were the result of human error. Six of the violations, applying surcharges on Homeowners policies for only one loss, were the result of a system problem. In most cases the surcharges occurred when a claim had more than one feature, e.g. a property and liability claim arising out of the same incident. The system was reading this as two separate claims. This was corrected and is no longer occurring. In the cases where overcharges were inadvertently made, premiums were returned to the insureds.

10. Any premium overcharges noted in the rating section of this report were refunded to the insureds and proof of such refunds have been provided to the Insurance Department.

11. Similar to 1 above, the review of our internal control procedures to ensure compliance with the claims handling requirements of Title 31, Pennsylvania Code, Chapter 146, is an

ongoing process. We continually review and when necessary revise these procedures as part of our Sarbanes-Oxley compliance. The report lists only four instances of noncompliance and, in fact, the examiners commented favorably during the examination about the minimal number of claims violations they found.

12. We have checked our claims forms to make sure they contain the required fraud warning notice. The examiners found one older form that did not have this notice and this was the only violation found.

13. It is the practice of our Claims Department that all Department inquiries respecting claims shall be responded to within 15 working days. The one violation that was found by the examiners was the result of human error.

14. It is Company practice to accept business only from producers who are properly licensed and appointed. We are now processing all appointments electronically through SIRCON.

15. As noted in 7 above, our guidelines have been changed and no longer require supporting primary Homeowners coverage in order to bind student-occupied rentals and seasonal or secondary dwellings.

Before closing, we would like to thank the examiners for their efforts and for their conduct throughout the examination process. They were friendly, courteous and made every effort to conduct the examination efficiently and with minimal disruption to the daily functioning of the Company. Our staff was very impressed by their professionalism.

Sincerely,



Cyril J. Greenya, CPCU
Senior Vice president
Chief Underwriting Officer

cc: Randolph Rohrbaugh
Donald Nikolaus

Enclosures