

REPORT OF MARKET CONDUCT EXAMINATION OF

**NAZARETH MUTUAL INSURANCE COMPANY
Nazareth, Pennsylvania**

**AS OF
May 2, 2008**

COMMONWEALTH OF PENNSYLVANIA

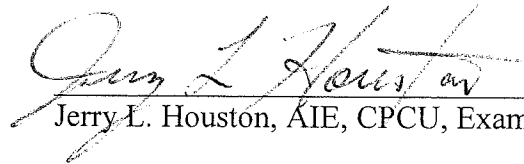


**INSURANCE DEPARTMENT
MARKET CONDUCT DIVISION**

Issued: June 5, 2008


VERIFICATION

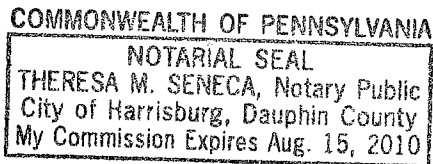
Having been duly sworn, I hereby verify that the statements made in the within document are true and correct to the best of my knowledge, information and belief. I understand that false statements made herein are subject to the penalties of 18 Pa. C.S. §4903 (relating to false swearing).


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

Sworn to and Subscribed Before me

This 28 Day of April, 2008


Notary Public



NAZARETH MUTUAL INSURANCE COMPANY

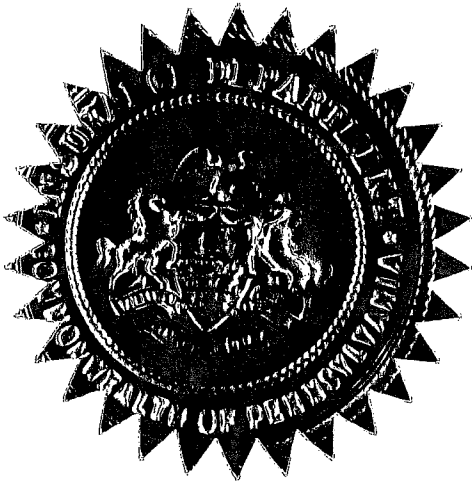
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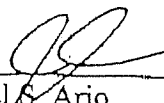
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BEFORE THE INSURANCE COMMISSIONER
OF THE
COMMONWEALTH OF PENNSYLVANIA

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

Nazareth Mutual Insurance Company
Market Conduct Examination as of the
close of business on May 2, 2008

Docket No.
MC08-05-010

ORDER

A market conduct examination of Nazareth Mutual Insurance Company (referred to herein as "Respondent") was conducted in accordance with Article IX of the Insurance Department Act, 40 P.S. § 323.1, et seq., for the period July 1, 2006 through June 30, 2007. The Market Conduct Examination Report disclosed exceptions to acceptable company operations and practices. Based on the documentation and information submitted by Respondent, the Department is satisfied that Respondent has taken corrective measures pursuant to the recommendations of the Examination Report.

It is hereby ordered as follows:

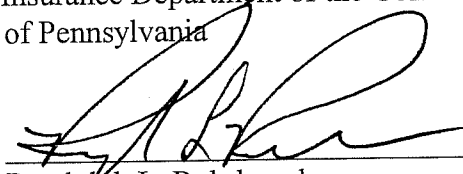
1. The attached Examination Report will be adopted and filed as an official record of this Department. All findings and conclusions resulting from the review of the Examination Report and related documents are contained in the attached Examination Report.
2. Respondent shall comply with Pennsylvania statutes and regulations.

3. Respondent shall comply with the recommendations contained in the attached Report.

4. 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.

The Department, pursuant to Section 905(e)(1) of the Insurance Department Act (40 P.S. § 323.5), will continue to hold the content of the Examination Report as private and confidential information for a period of thirty (30) days from the date of this Order.

BY: Insurance Department of the Commonwealth
of Pennsylvania



Randolph L. Rohrbaugh
Deputy Insurance Commissioner

(June 5, 2008)

I. INTRODUCTION

The market conduct examination was conducted at Nazareth Mutual Insurance Company's office located in Nazareth, Pennsylvania, from February 4, 2008, through February 15, 2008. Subsequent review and follow-up was conducted in the office of the Pennsylvania Insurance Department.

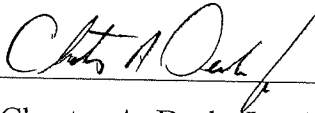
Pennsylvania Market Conduct Examination Reports generally note only those items to which the Department, after review, takes exception. However, the Examination Report may include management recommendations addressing areas of concern noted by the Department, but for which no statutory violation was 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%.

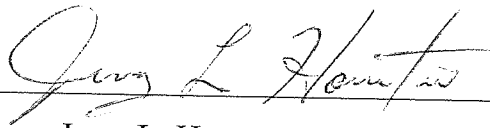
Throughout the course of the examination, Company officials were provided with status memoranda, which referenced specific policy numbers with citation to each section of law violated. Additional information was requested to clarify apparent violations. An exit conference was conducted with Company personnel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

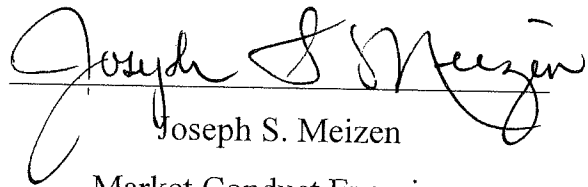
The undersigned participated in this examination and in preparation of this Report.



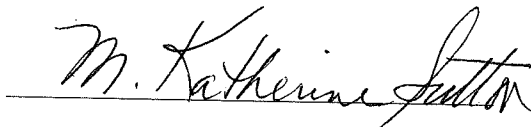
Chester A. Derk, Jr., AIE, HIA
Market Conduct Division Chief



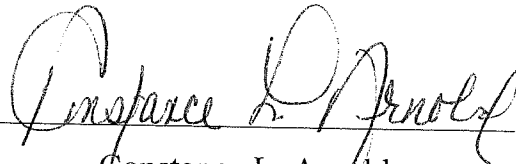
Jerry L. Houston, AIE, CPCU
Market Conduct Examiner



Joseph S. Meizen
Market Conduct Examiner



M. Katherine Sutton
Market Conduct Examiner



Constance L. Arnold
Market Conduct Examiner

II. SCOPE OF EXAMINATION

The Market Conduct Examination was conducted on Nazareth Mutual Insurance Company, hereinafter referred to as “Company,” at their office located in Nazareth, 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, 2006, through June 30, 2007, 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. Property
 - 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. Commercial Property
 - Underwriting – Appropriate and timely notices of nonrenewal, midterm cancellations, 60-day cancellations, declinations and renewals.
3. Claims
4. Forms
5. Advertising
6. Complaints
7. Licensing

III. COMPANY HISTORY AND LICENSING

Nazareth Mutual Insurance Company was formed by the consolidation on July 1, 1957, of the Citizens' Mutual Fire Insurance Company of Northampton County, Farmers' Mutual Fire Insurance Company of Northampton County and Nazareth Mutual Fire Insurance Company, all of Nazareth, Pennsylvania. The three carriers had limited their solicitation of business to three counties in Pennsylvania. Operations are now state-wide.

LICENSING

Nazareth Mutual Insurance Company's Certificate of Authority to write business in the Commonwealth was issued on May 3, 1957. The Company is licensed in Pennsylvania. The Company's 2006 annual statement reflects Direct Written Premium for all lines of business in the Commonwealth of Pennsylvania as \$8,222,759. Premium volume related to the areas of this review were: Fire \$1,343,909; Homeowners Multiple Peril \$5,153,316; Commercial Multiple Peril (Non-liability portion) \$742,447 and Inland Marine \$14,210.

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 underwriting guides were furnished for homeowners, dwelling fire, commercial fire and business owners. 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:

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's underwriting guidelines required supporting business on unusual type risks, some commercial risks or risks of low value.

1 Violation Act 205, Section 5(a)(7)(iii) [40 P.S. §1171.5(a)(7)(iii)]

Unfair Methods of Competition and Unfair or Deceptive Acts or Practices Defined. "Unfair Methods of Competition" and "Unfair or Deceptive Practices" in the business of insurance means: Unfairly discriminating by means of: Making or permitting any unfair discrimination between individuals of the same class and essentially the same hazard with regard to underwriting standards and practices or eligibility requirements by reason of race, religion, nationality or

ethnic group, age, sex, family size, occupation, place of residence or marital status. The terms “underwriting standards and practices” or “eligibility rules” do not include the promulgation of rates if made or promulgated in accordance with the appropriate rate regulatory act of this Commonwealth and regulations promulgated by the Commissioner pursuant to such act. The Company’s underwriting guidelines prohibit writing risks with student housing exposures.

V. UNDERWRITING

A. 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.

The universe of 22 property policies which were cancelled within the first 60 days of new business was selected for review. The policies consisted of homeowner and owner occupied dwelling fire. All 22 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.

From the universe of 1,986 property policies which were cancelled midterm during the experience period, 88 files were selected for review. The property policies consisted of homeowners and owner occupied dwelling fire. All 88 files were received and reviewed. The 2 violations noted were based on 2 files, resulting in an error ratio of 2%.

The following findings were made:

1 Violation 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 policy for an improper reason.

1 Violation Act 205, Section 5(a)(9)(iii) [40 P.S. §1171.5(a)(9)(iii)]

Requires that a cancellation notice shall state the specific reason or reasons of the insurer for cancellation.

The Company did not provide a specific reason for cancellation for the file 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.

From the universe of 96 property policies which were nonrenewed during the experience period, 34 files were selected for review. The property policies consisted of homeowner and owner occupied dwelling fire. All 34 files were received and reviewed. The 2 violations noted were based on 2 files, resulting in an error ratio of 6%.

The following findings were made:

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 nonrenewed the 2 files noted for an improper reason.

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, Unfair Insurance Practices Act, Section 5(a)(7)(iii) [40 P.S. §1171.5(a)(7)(iii)], discriminatory reasons.

From the universe of 148 personal property applications declined during the experience period, 50 files were selected for review. The files consisted of homeowner and owner occupied dwelling fire applications. All 50 files 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 205, Section 5(a)(7)(iii) [40 P.S. §1171.5(a)(7)(iii)]

Unfair Methods of Competition and Unfair or Deceptive Acts or Practices Defined. “Unfair Methods of Competition” and “Unfair or Deceptive Practices” in the business of insurance

means: Unfairly discriminating by means of: Making or permitting any unfair discrimination between individuals of the same class and essentially the same hazard with regard to underwriting standards and practices or eligibility requirements by reason of race, religion, nationality or ethnic group, age, sex, family size, occupation, place of residence or marital status. The terms “underwriting standards and practices” or “eligibility rules” do not include the promulgation of rates if made or promulgated in accordance with the appropriate rate regulatory act of this Commonwealth and regulations promulgated by the Commissioner pursuant to such act. The Company declined the two applicants based on place of residence.

B. 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.

The universe of 4 tenant occupied dwelling fire policies that were identified by the Company as being cancelled in the first 60 days of new business was selected for review. All 4 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.

From the universe of 274 commercial property policies cancelled midterm during the experience period, 9 files were selected for review. The commercial property files consisted of commercial package and tenant occupied dwelling fire. All 9 files were received and reviewed. The 68 violations noted were based on 62 files within the universe, resulting in an error ratio of 23%.

The following findings were made:

2 Violations Act 86, Section 2 [40 P.S. §3402]

Grounds for cancellation. Canceling in midterm a policy of insurance covering commercial property and casualty risks is prohibited for any reason other than those enumerated under this section. The 2 files noted were cancelled for other than permitted reasons.

4 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 4 files noted.

6 Violations Act 86, Section 4(a) [40 P.S. §3404(a)]

Requires that unearned premium be returned to the insured not later than 10 business days after the effective date of termination where commercial property or casualty risks are cancelled in mid-term by the insurer. The Company did not return the unearned premium to the insured within 10 business days after the effective date of termination for the 6 files noted.

56 Violations Act 86, Section 4(b) [40 P.S. §3404(b)]

Requires that unearned premium be returned to the insured not later than 30 days after the effective date of termination where commercial property or casualty risks are cancelled in mid-term by the insured. The Company did not return the unearned premium to the insured within 30 days after the effective date of termination for the 56 files 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.

From the universe of 56 commercial property policies nonrenewed during the experience period, 36 files were selected for review. The commercial property policies consisted of tenant occupied dwelling fire, commercial fire and commercial package. All 36 files were received and reviewed. No violations were 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.

From the universe of 3,511 commercial property policies renewed during the experience period, 80 files were selected for review. The commercial property policies consisted of tenant occupied dwelling fire, commercial fire, commercial inland marine and commercial package. All 80 files were received and reviewed. The 13 violations noted were based on 13 files, resulting in an error ratio of 16%.

The following findings were made:

13 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 13 files noted.

5. 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.

The universe of 9 commercial property declinations reported by the Company during the experience period was selected for review. No violations were noted.

VI. RATING

A. 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

From the universe of 902 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.

The following concern was noted:

Concern: Homeowner policies are eligible for a rate credit from 2% to 5% for various protective devices. The Company's application does not ask the questions regarding premises alarm systems and protective devices.

Inspections usually involve external viewing and would not detect internal alarm systems. The concern is some policyholders might be eligible for a rate credit and not receiving it because the question is not asked and the

inspection is not necessarily detecting protective devices.

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

From the universe of 10,868 homeowner policies renewed without surcharges during the experience period, 50 files were selected for review. All 50 files were received and reviewed. No violations were noted.

The following concern was noted:

Concern: Homeowner policies are eligible for a rate credit from 2% to 5% for various protective devices. The Company's application does not ask the questions regarding premises alarm systems and protective devices. Inspections usually involve external viewing and would not detect internal alarm systems. The concern is some policyholders might be eligible for a rate credit and not receiving it because the question is not asked and the inspection is not necessarily detecting protective devices.

Homeowner Rating – Renewals With Surcharges

The universe of 15 homeowner policies renewed with surcharges during the experience period was selected for review. All 15 files were received and reviewed. The violation noted resulted in an error ratio of 7%.

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 did not rate the policy in accordance with their filed and approved rating plan which resulted in an overcharge of \$154.

B. 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

The universe of 7 tenant homeowner policies written as new business without surcharges during the experience period was selected for review. All 7 files were received and reviewed. No violations were noted.

The following concern was noted:

Concern: Homeowner policies are eligible for a rate credit from 2% to 5% for various protective devices. The Company's application does not ask the questions regarding premises alarm systems and protective devices.

Inspections usually involve external viewing and would not detect internal alarm systems. The concern is some policyholders might be eligible for a rate credit and not receiving it because the question is not asked and the inspection is not necessarily detecting protective devices.

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

From the universe of 118 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.

The following concern was noted:

Concern: Homeowner policies are eligible for a rate credit from 2% to 5% for various protective devices. The Company's application does not ask the questions regarding premises alarm systems and protective devices.

Inspections usually involve external viewing and would not detect internal alarm systems. The concern is some policyholders might be eligible for a rate credit and not receiving it because the question is not asked and the inspection is not necessarily detecting protective devices.

C. 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

The universe of 14 dwelling fire policies written as new business without surcharges was selected for review. All 14 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.

Dwelling Fire Rating – Renewals Without Surcharges

From the universe of 92 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.

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. Homeowner Claims
- B. 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. Homeowner Claims

From the universe of 330 homeowner claims reported during the experience period, 50 files were selected for review. All 50 files were received and reviewed. The 6 violations noted were based on 6 files, resulting in an error ratio of 12%.

The following findings were made:

6 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 6 claims noted.

B. Dwelling Fire Claims

From the universe of 118 dwelling fire claims reported during the experience period, 25 files were selected for review. All 25 files were received and reviewed. The 4 violations noted were based on 4 files, resulting in an error ratio of 16%.

The following findings were made:

4 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 4 claims noted.

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)], 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 findings were made:

3 Violations 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 did not provide the fraud warning on an application for business owners insurance, an application for homeowners insurance and a sworn statement in proof of loss claim form.

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 9 pieces of advertising in use during the experience period, which was local media advertisements involving their agents. The Company's website 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 7 consumer complaints received during the experience period and provided all consumer complaint logs requested. All 7 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:

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

Requires an insurer to maintain a complete record of all the complaints, which it has 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 time it took to process each complaint. The Company's complaint logs for 2002, 2003, 2004 and 2005, failed to display the total number of complaints or the time it took to process each complaint.

The following synopsis reflects the nature of the 7 complaints that were reviewed.

•	5	Underwriting Cancellations/Nonrenewals	72%
•	1	Claims	14%
•	1	Refund	14%
	<hr/> 7		<hr/> 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:

*6 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.

Adam Ryan Barton
Doreen M. Bassett
Timothy C. Benckini
William L. Bookwalter
Dryfoos Insurance Agency, Inc.
Sheeley Insurance Agency, Inc.

XII. RECOMMENDATIONS

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 Act 205, Section 5(a)(9) [40 P.S. §1171.5(a)(9)] to ensure that the violations regarding the requirement for cancellation and nonrenewal notices, as noted in the Report, do not occur in the future.
2. The Company must review and revise internal control procedures to ensure compliance relative to commercial cancellation and nonrenewal requirements of Act 86, Sections 2, 3 and 4 [40 P.S. §§3402, 3403 and 3404], so that the violations noted in the Report do not occur in the future.
3. The Company must review Act 86, Section 1 [40 P.S. §3401], to ensure that violations regarding notification to the insured of an increase in premium do not occur in the future.
4. The Company must review Act 246, Section 4(a) and (h) [40 P.S. §1184] and take appropriate measures to ensure the homeowner rating violation listed in the report does not occur in the future.
5. The premium overcharge noted in the rating section of this report must be refunded to the insured and proof of such refund must be provided to the Insurance Department within 30 days of the report issue date.

6. 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 status letters, as noted in the Report, do not occur in the future.
7. The Company must ensure all producers are properly appointed, as required by Section 671-A [40 P.S. §310.71] of the Insurance Department Act No. 147, prior to accepting any business from any producer.
8. The Company must revise and reissue their underwriting guidelines for use in Pennsylvania to ensure that guidelines do not require supporting coverage.
9. The Company must revise and reissue their underwriting guidelines for use in Pennsylvania to ensure that the guidelines do not exclude applicants from being eligible to obtain insurance for reasons established in Act 205, Section 5(a)(7)(iii) [40 P.S. §1171.5(a)(7)(iii)].
10. The Company must review Act 205, Section 5(a)(11) [40 P.S. §1171.5(a)(11)], to ensure that the violations relative to complaint records noted in the Report do not occur in the future.
11. The Company must ensure that all claim forms contain the required fraud warning notice.

XIII. COMPANY RESPONSE



NAZARETH MUTUAL INSURANCE COMPANY

P.O. BOX 209, NAZARETH, PENNSYLVANIA 18064-0209 PHONE: 610/759-3020

FAX: 610/759-7320

1-800-321-6783

information@nazarethmutual.com

May 13, 2008

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

RE: Response to the Report of Examination Warrant Number: 07-M19-067

Dear Mr. Derk;

The following are the responses to the above report dated May 2, 2008.

Recommendations:

- 1. The Company must review Act 205, Section 5 (a) (9) [40 P.S. 1171.5 (a) (9)] to ensure that the violations regarding the requirement for cancellation and nonrenewal notices, as noted in the Report, do not occur in the future.**

The nonrenewal requirements per the above section of Act 205 have been reviewed with the underwriting staff to insure that only allowable reasons are used and to ensure that the specific reasons for cancellation are included.

- 2. The Company must review and revise internal control procedures to ensure compliance relative to commercial cancellation and nonrenewal requirements of Act 86, Section 2, 3 and 4 [40 P.S. 3402, 3403 and 3404], so that the violations noted in the Report do not occur in the future.**

The above requirements of Act 86 have been reviewed with the Underwriting staff as well as reviewing the internal control procedures. The company converted to a new processing system effective June 1, 2006. This had an impact to the timely processing of policies and refunds for several months. The majority of the violations occurred during this time frame.

- 3. The Company must review Act 86, Section 1 [40 P.S. 3401] to ensure that violations regarding notification to the insured of an increase in premium do not occur in the future.**

Education on the proper timeframes for notice of increased premium has been reinforced with the staff. As noted above, the Company implemented a new processing system effective June 1, 2006 which adversely impacted the timely processing. Several months in 2006 were impacted by this conversion.

- 4. The Company must review Act 246, Section 4(a) and (h) [40 P.S. 1184] and take appropriate measures to ensure the homeowner rating violation listed in the Report does not occur in the future.**

The one violation was a clerical error and the refund has been returned to the insured.

- 5. The premium overcharge noted in the rating section of this report must be refunded to the insured and proof of such refund must be provided to the Insurance Department within 30 days of the report issue date.**

As noted above, this was returned to the insured on March 7, 2008 and confirmed with the Department on April 18, 2008.

- 6. The Company should review and revise internal control procedures to insure compliance with the claim handling requirements of Title 31, Pennsylvania Code, Chapter 146, Unfair Claims Settlement Practices so that the violations relation to status letters, as noted in the Report, do not occur in the future.**

Internal controls have been reviewed with the staff as well as outside adjusters to insure that the timely notifications of status letters are sent according to Title 31.

- 7. The Company must ensure all procedures are properly appointed, as required by Section 671-A [40 P.S. 310.71] of the Insurance Department Act No. 147, prior to accepting any business from any procedure.**

The Company has begun to use SIRCOM to process all agency licensing. The oversights noted in the Report have been corrected.

- 8. The Company must revise and reissue their underwriting guidelines for use in Pennsylvania to ensure that the guidelines do not require supporting coverage.**

The underwriting guidelines have been revised and are being reissued.

- 9. The Company must revise and reissue their underwriting guidelines for use in Pennsylvania to ensure that the guidelines do not exclude applicants from being eligible to obtain insurance for reasons established in Act 205, Section 5(a)(7)(iii) [P.S. 1171.5(a)(7)(iii)].**

The underwriting guidelines have been revised and are being reissued to ensure compliance with Act 205.

- 10. The Company must review Act 205, Section 5(a) (11) [40 P.S. 1171.5(a) (11)], to ensure that the violations relative to complaint records noted in the Report do not occur in the future.**

Act 205 was reviewed and a column added to the existing complaint logs to indicate the number of days to complete the handling of the complaint. In addition, the total number of complaints for the year was added to the bottom of our existing complaint logs.

- 11. The Company must ensure that all claim forms contain the required fraud warning notice.**

The required fraud warning was added to all claim forms.

Concerns:

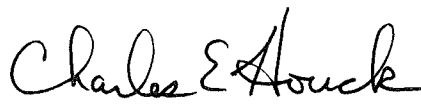
- 1. Homeowner policies are eligible for a rate credit from 2% to 5% for various protective devices. The Company's application does not ask the questions regarding premises alarms and protective devices. Inspections usually involve external viewing and would not detect internal alarm systems. The concern is some policyholders might be eligible for a rate credit and not receiving it because the question is not asked and the inspection is not necessarily detecting protective devices.**

The application has been modified to include questions about the protective devices. Agents have the new applications and were instructed to begin using them immediately.

The issues raised in the examination have been addressed. We want to thank the examiners for their professionalism and helpfulness that was exhibited during the examination. We feel we gained a better insight to bring us in compliance with all the Pennsylvania Insurance Department laws and regulations.

Sincerely,
Nazareth Mutual Insurance Company


Justin A. Kelly
President & CEO


Charles E. Houck
Chairman