

**REPORT OF  
MARKET CONDUCT EXAMINATION  
OF**

**MERCHANTS MUTUAL INSURANCE COMPANY**

**Buffalo, New York**

**AS OF  
February 29, 2008  
COMMONWEALTH OF PENNSYLVANIA**

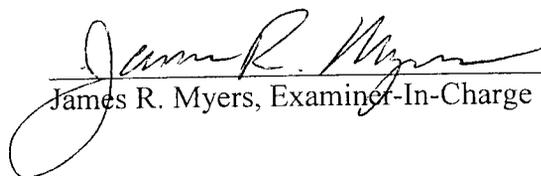


**INSURANCE DEPARTMENT  
MARKET CONDUCT DIVISION**

**Issued: April 17, 2008**

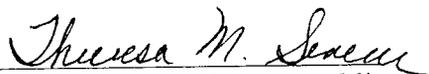
VERIFICATION

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).

  
James R. Myers, Examiner-In-Charge

Sworn to and Subscribed Before me

This 19 Day of February, 2008



Notary Public  
COMMONWEALTH OF PENNSYLVANIA

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

# MERCHANTS MUTUAL INSURANCE COMPANY

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BEFORE THE INSURANCE COMMISSIONER  
OF THE  
COMMONWEALTH OF PENNSYLVANIA

ORDER

AND NOW, this 6<sup>th</sup> 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:
	:	
MERCHANTS MUTUAL	:	Sections 641.1-A and 671-A of
INSURANCE COMPANY	:	Act 147 of 2002 (40 P.S. §§ 310.41
250 Main Street	:	and 310.71)
Buffalo, NY 14240	:	
	:	Act 1990-6, Sections 1711(b),
	:	1731(b)(c), 1791.1(a) and (b), and
	:	1793(b) (Title 75 Pa.C.S. §§ 1711,
	:	1731, 1791 and 1793)
	:	
	:	Sections 1, 3(a)(2), 3(a)(5), 3(a)(6),
	:	and 7(c) of the Act of July 3, 1986,
	:	P.L. 396, No. 86 (40 P.S. §§3401,
	:	3403 and 3407)
	:	
	:	Sections 4(a) and 4(h) of the Act of
	:	June 11, 1947, P.L. 538, No. 246
	:	(40 P.S. §§ 1184)
	:	
	:	Sections 2003(a)(1), (13) and (14) of
	:	Act 68 of 1998 (40 P.S. §§991.2003)
	:	
	:	Sections 5(a)(4), 5(a)(9), and
	:	5(a)(9)(iii) of the Unfair Insurance
	:	Practices Act, Act of July 22, 1974,
	:	P.L. 589, No. 205 (40 P.S. §§ 1171.5)
	:	
	:	Section 506.1 of the Insurance
	:	Company Law, Act of May 17, 1921,
	:	P.L. 682, No. 284 (40 P.S. § 636.1)
	:	
	:	Title 31, Pennsylvania Code, Sections
	:	59.6(6), 69.53(a), 113.88 and 146.6
	:	
Respondent.	:	Docket No. MC08-03-023

CONSENT ORDER

AND NOW, this 17<sup>th</sup> day of April, 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.

FINDINGS OF FACT

3. The Insurance Department finds true and correct each of the following Findings of Fact:

- (a) Respondent is Merchants Mutual Insurance Company, and maintains its address at 250 Main Street, Buffalo, New York 14240.

- (b) A market conduct examination of Respondent was conducted by the Insurance Department covering the experience periods from January 1, 2006 through December 31, 2006.
- (c) On February 29, 2008, the Insurance Department issued a Market Conduct Examination Report to Respondent.
- (d) A response to the Examination Report was provided by Respondent on March 27, 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 (40 P.S. § 310.71), which prohibits producers from transacting business within this Commonwealth without written appointment as required by the Act;

- (iii) Section 1711(b) of Act 1990-6, Title 75, Pa.C.S. § 1171(b), which requires all insurers to make available for purchase a motor vehicle insurance policy which contains only the minimum requirements of financial responsibility and medical benefits;
- (iv) Section 1731(b) and (c) of Act 1990-6, Title 75, Pa.C.S. § 1731(b) and (c), which requires the named insured to be informed that he may reject uninsured and underinsured motorist coverage by signing a written rejection form;
- (v) Section 1791.1(a) of Act 1990-6, Title 75, Pa.C.S. § 1791, which requires that at the time of application for original coverage and every renewal thereafter, an insurer must provide to an insured an itemized invoice listing the minimum motor vehicle insurance coverage levels mandated by the Commonwealth and the premium charge for the insured to purchase the minimum mandated coverages. The invoice must contain the following notice in print of no less than ten-point type: “The laws of the Commonwealth of Pennsylvania, as enacted by the General Assembly, only require you to purchase liability and first-party medical benefit coverages. Any additional coverage in excess of the limits required by law are provided only at your request as enhancements to basic coverages.” The insurer shall provide the itemized invoice to the insured in conjunction with

the declaration of coverage limits and premiums for the insured's existing coverages;

(vi) Section 1791.1(b) of Act 1990-6, Title 75, Pa.C.S. § 1791, which requires an insurer to provide an insured a notice of the availability of two alternatives of full tort insurance and limited tort insurance;

(vii) 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 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;

(viii) 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;

(ix) 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;

- (x) Section 3(a)(5) of Act 86 (40 P.S. § 3403), which requires that a midterm cancellation or nonrenewal notice shall state the specific reasons for the cancellation or nonrenewal. The reasons shall identify the condition, factor or loss experience which caused the midterm cancellation or nonrenewal. The notice shall provide sufficient information or data for the insured to correct the deficiency;
  
- (xi) Section 3(a)(6) of Act 86 (40 P.S. § 3403), which requires the mid-term cancellation notice state that, at the insured's request, the insurer shall provide loss information to the insured for at least three years or the period of time during which the insurer has provided coverage to the insured, whichever is less;
  
- (xii) Section 7(c) of Act 86 (40 P.S. § 3407), which states this act does not apply to commercial property and casualty insurance policies that are in effect less than 60 days, unless they are renewals. An insurer may cancel the policy provided it gives at least 30 days' notice of the termination and provided it gives notice no later than the 60<sup>th</sup> day , unless the policy provides for a longer period of notification;
  
- (xiii) 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;

- (xiv) Section 2003(a)(1) 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 due to age;
- (xv) Section 2003(a)(13) 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 due to not at-fault accidents;
- (xvi) Section 2003(a)(14) 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 for any claim under the comprehensive portion of the policy unless such loss was intentionally caused by the insured;
- (xvii) Section 5(a)(4) of the Unfair Insurance Practices Act, No. 205 (40 P.S. §1171.5(a)(4)), which prohibits entering into any agreement to commit, or by any concerted action committing, any act of boycott, coercion or intimidation resulting in unreasonable restraint of, or monopoly in, the business of insurance;

(xviii) 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;

(xix) Section 5(a)(9)(iii) of Act 205 (40 P.S. § 1171.5), which requires that a cancellation notice shall state the specific reason or reasons of the insurer for cancellation;

- (xx) 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 on the policy or until the sale of the property, whichever occurs first, provided that the premiums are paid;
- (xxi) Title 31, Pennsylvania Code, Section 59.6(6), which states notices of cancellation or refusal to renew shall specify any changes or increased hazards it has relied on. If the reason is failure to pay a premium, the insurer shall specify the amount due, and the date that it was due;
- (xxii) Title 31, Pennsylvania Code, Section 69.53(a), which states a Peer Review Organization shall contract, in writing, jointly or separately with an insurer for the provision of peer review services as authorized by Act 1990-6 and this chapter;
- (xxiii) Title 31, Pennsylvania Code, Section 113.88, which states 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; and
- (xxiv) 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.

#### CONCLUSIONS OF LAW

4. 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 641.1-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 Act 86, Sections 1, 3 and 7 (40 P.S. §§ 3401, 3403 and 3407) 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.

(d) 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.

(e) Respondent's violations of Section 2003 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).

(f) Respondent's violations of Sections 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) Respondent's violations of Title 31, Pennsylvania Code, Section 146.6 are punishable under Sections 9, 10 and 11 of the Unfair Insurance Practices Act, (40 P.S. §§ 1171.9, 1171.10 and 1171.11), as stated above.

#### ORDER

5. 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-Five Thousand Dollars (\$35,000.00) 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 Ginny Marquart, Administrative Assistant, 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.

6. 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.

7. 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.

8. 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.

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

10. 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.

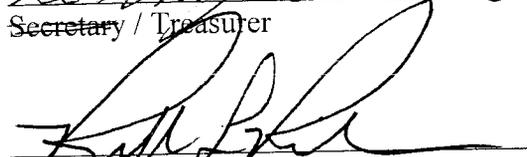
11. This Order shall be final upon execution by the Insurance Department. Only the Insurance Commissioner or a duly authorized delegee is authorized to bind the Insurance Department with respect to the settlement of the alleged violations of law

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

BY: MERCHANTS MUTUAL 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 Merchants Mutual Insurance Company's office located in Buffalo, New York, from October 16, 2007, through December 4, 2007. Subsequent review and follow-up was conducted in the office of the Pennsylvania Insurance Department.

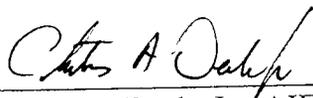
Pennsylvania Market Conduct Examination Reports generally note only those items to which the Department, after review, takes exception. However, the Examination Report may include management recommendations addressing areas of concern noted by the Department, but for which no statutory violation was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

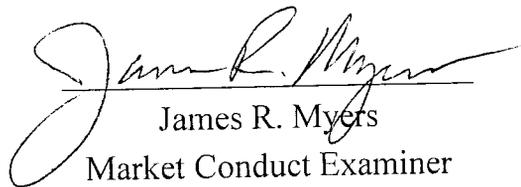
Throughout the course of the examination, Company officials were provided with status memoranda, which referenced specific policy numbers with citation to each section of law violated. Additional information was requested to clarify apparent violations. An exit conference was conducted with Company personnel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

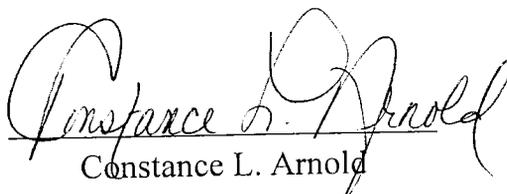
The undersigned participated in this examination and in preparation of this Report.



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



James R. Myers  
Market Conduct Examiner



Constance L. Arnold  
Market Conduct Examiner

## II. SCOPE OF EXAMINATION

The Market Conduct Examination was conducted on Merchants Mutual Insurance Company, hereinafter referred to as "Company," at their office located in Buffalo, New York. 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 January 1, 2006, through December 31, 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. 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.
  
3. Commercial Property
  - Underwriting – Appropriate and timely notices of nonrenewal, midterm cancellations, 60-day cancellations, declinations and renewals.
  
4. Commercial Automobile
  - Underwriting – Appropriate and timely notices of nonrenewal, midterm cancellations, 60-day cancellations, declinations and renewals.

5. Workers' Compensation

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

6. Claims

7. Forms

8. Advertising

9. Complaints

10. Licensing

### III. COMPANY HISTORY AND LICENSING

Merchants Mutual Insurance Company was incorporated April 10, 1917, under the laws of New York as the Merchants Mutual Automobile Liability Insurance Company. It was licensed and commenced business March 5, 1918. The title was changed to Merchants Mutual Casualty Company in 1923 and to its present title on March 1, 1957.

#### LICENSING

Merchants Mutual Insurance Company's Certificate of Authority to write business in the Commonwealth was last issued on April 1, 2007. The Company is licensed in Delaware, Indiana, Maine, Maryland, Massachusetts, Michigan, New Hampshire, New Jersey, New York, Ohio, Pennsylvania, Rhode Island, Vermont and Virginia. The Company's 2006 annual statement reflects Direct Written Premium for all lines of business in the Commonwealth of Pennsylvania as \$9,013,782. Premium volume related to the areas of this review were: Fire \$65,072; Homeowners Multiple Peril \$798,557; Commercial Multiple Peril (Non-liability portion) \$1,010,271; Commercial Multiple Peril (Liability portion) \$2,562,278; Inland Marine \$28,981; Workers' Compensation \$1,316,470; Private Passenger Automobile Direct Written Premium was reported as Private Passenger Auto No-Fault (personal injury protection) \$39,434; Other Private Passenger Auto Liability \$147,072 and Private Passenger Auto Physical Damage \$169,873; Commercial Automobile Direct Written Premium was reported as Commercial Auto No-Fault (personal injury protection) \$63,529; Other Commercial Auto Liability \$1,606,040 and Commercial Auto Physical Damage \$573,310.

#### *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 and tenant occupied dwelling fire. 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:

*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 Company's workers' compensation guidelines stated the following: "It is our intent to write workers' compensation coverage in conjunction with our other lines of business". The dwelling fire and homeowner guidelines indicated the primary coverage was required in order to write seasonal or secondary coverage.

*3 Violations Act 68, Section 2003(a)(1) [40 P.S. §991.2003(a)(1)]*

Discrimination Prohibited – (a) An insurer may not cancel or refuse to write or renew a policy of automobile insurance for any of the following reasons: Age. The Company made 3 different references

in their automobile guidelines using age as criteria for refusal to write a policy of automobile insurance.

*2 Violations Act 68, Section 2003(a)(13) [40 P.S. §991.2003(a)(13)]*

Discrimination Prohibited – (a) An insurer may not cancel or refuse to write or renew a policy of automobile insurance for any of the reasons specified in 2003(a)(13). The Company's automobile guidelines reference 2 separate instances using not at-fault accidents as criteria for refusal to write a policy of automobile insurance.

*3 Violations Act 68, Section 2003(a)(14) [40 P.S. §991.2003(a)(14)]*

Discrimination Prohibited – (a) An insurer may not cancel or refuse to write or renew a policy of automobile insurance for the following reason: Any claim under the comprehensive portion of the policy unless such loss was intentionally caused by the insured. The Company's automobile guidelines referenced 3 separate instances of using comprehensive losses as criteria for refusal to write a policy of automobile insurance.

*1 Violation Title 75, Pa. C.S. §1711(b)*

All insurers shall make available for purchase a motor vehicle insurance policy which contains only the minimum requirements of financial responsibility and medical benefits. The Company's minimum liability limits offered are 50/100/25 or \$100,000 for combined single limit.

## 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.

The universe of 5 private passenger automobile files identified as being cancelled in the first 60 days of new business 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 Act 68, Section 2003(a)(1) [40 P.S. §991.2003(a)(1)]*

Discrimination Prohibited – (a) An insurer may not cancel or refuse to write or renew a policy of automobile insurance for any of the following reasons: Age. The Company used driving experience as a reason for cancellation.

## 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.

The universe of 58 private passenger automobile files identified as midterm cancellations by the Company was selected for review. All 58 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.

The universe of 13 private passenger automobile files identified as nonrenewals by the Company was selected for review. All 13 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 5 private passenger automobile applications declined by the Company was selected for review. All 5 files were received and reviewed. The violation resulted in an error ratio of 20%.

The following finding was made:

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

An insurer may not cancel or refuse to write or renew a policy of automobile insurance due to age. The Company cannot use driving experience which constitutes a per se unlawful criteria based upon age.

#### **B. Private Passenger Automobile – Assigned Risk**

Merchants 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. During the experience period, the Company did not have any private passenger assigned risk policies in force.

## 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.

The universe of 14 property policies which were cancelled within the first 60 days of new business was selected for review. The policies consisted of homeowner and tenant homeowner. All 14 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 563 property policies which were cancelled midterm during the experience period, 31 files were selected for review. The

property policies consisted of homeowners and tenant homeowners. All 31 files were received and reviewed. The 377 violations noted were based on the universe of 563, resulting in an error ratio of 67%.

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 cancelled the 4 files noted for an improper reason.

*6 Violations 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.

*AND*

*Title 31, Pa. Code, Section 59.6(6)*

If the reason is a substantial change or increase in the hazard, the insurer shall specify the changes or increased hazards it relied on for its actions. The Company did not provide a specific reason for cancellation for the 6 files noted.

*367 Violations Title 31, Pa. Code, Section 59.6(6)*

If the reason is a substantial change or increase in the hazard, the insurer shall specify the changes or increased hazards it relied on for its actions. If the reason is the failure to pay a premium, the insurer shall specify the amount due, and the date that it was due. The Company failed to specify the date when the premium was due on the cancellation notice. The 367 violations represent the number of policies that were cancelled for nonpayment of premium.

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.

The universe of 36 property policies which were nonrenewed during the experience period was selected for review. The property policies consisted of homeowner and tenant homeowner. All 36 files were received and

reviewed. Of the 36 files reviewed, 10 were found to be duplicate nonrenewals, reducing the universe to 26. The 19 violations noted were based on 19 files, resulting in an error ratio of 73%.

The following findings were made:

*19 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 19 files noted for an improper reason. The reason for nonrenewal for all 19 files was: "Producing agent no longer represents the Company".

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.

The universe of 27 personal property applications declined during the experience period was selected for review. All 27 files were received and reviewed. Of the 27 files reviewed, 20 were identified as 60-day cancellations, 4 were identified as midterm cancellations and 3 were duplicate files, reducing the universe to 24. The 6 violations noted were based on 4 files, resulting in an error ratio of 17%.

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 cancelled the 4 files noted for an improper reason.

*2 Violations 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 2 files 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 60<sup>th</sup> day unless the policy provides for a longer period of notification.

The universe of 3 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 3 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 58 commercial property policies cancelled midterm during the experience period, 28 files were selected for review. The commercial property files consisted of commercial package, commercial inland marine, commercial fire and tenant occupied dwelling fire. All 28 files were received and reviewed. The 2 violations noted were based on 2 files, resulting in an error ratio of 7%.

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 cancellation. 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 cancellation. The Company failed to provide a specific reason for cancellation for the 2 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 49 commercial property policies nonrenewed during the experience period, 24 files were selected for review. The commercial property policies consisted of tenant occupied dwelling fire, commercial fire, commercial inland marine and commercial package. All 24 files were received and reviewed. The 17 violations noted were based on 12 files, resulting in an error ratio of 50%.

The following findings were made:

#### *11 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 11 files noted.

#### *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 did not provide a specific reason for nonrenewal.

*5 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 5 files noted contained a nonrenewal notice which required supporting business, which is prohibited.

#### 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 411 commercial property policies renewed during the experience period, 55 files were selected for review. The commercial property policies consisted of tenant occupied dwelling fire, commercial fire, commercial inland marine and commercial package. All 55 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 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.

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.

From the universe of 381 commercial property declinations reported by the Company during the experience period, 28 files were selected for review. The commercial property files consisted of commercial fire, commercial package and commercial inland marine. Of the 28 files requested, 4 files were received and reviewed. No violations were noted.

The following concern was made:

**Concern:** The Company does not retain declinations for an extended period of time. It is a concern that the Department cannot determine whether the declinations are in compliance. The Company should retain declinations for at least 3 years.

## **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 60<sup>th</sup> day unless the policy provides for a longer period of notification.

The universe of 2 commercial automobile policies cancelled within the first 60 days of new business was selected for review. Both files were received and reviewed. The violation noted resulted in an error ratio of 50%.

The following finding was made:

*1 Violation Act 86, Section 7(c) [40 P.S. §3407(c)]*

This act does not apply to commercial property and casualty insurance policies that are in effect less than 60 days, unless they are renewals. An insurer may cancel the policy provided it gives at least 30 days' notice of the termination and provided it gives notice no later than the 60<sup>th</sup> day, unless the policy provides for a longer period of notification.

*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 cancellation. The Company failed to provide a specific reason for cancellation.

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 70 commercial automobile policies cancelled midterm during the experience period, 20 files were selected for review. All 20 files were received and reviewed. Of the 20 files reviewed, 2 files were identified as 60-day cancellations. 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.

The universe of 21 commercial automobile policies nonrenewed during the experience period was selected for review. All 21 files were received and reviewed. The 3 violations noted was based on 3 files, resulting in an error ratio of 14%.

The following findings were made:

#### *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.

#### 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 506 commercial automobile policies renewed 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 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.

## 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.

From the universe of 186 commercial automobile declinations reported by the Company during the experience period, 25 files were selected for review. Of the 25 files requested, 4 files were received and reviewed. No violations were noted.

The following concern was made:

**Concern:** The Company does not retain declinations for an extended period of time. It is a concern that the Department cannot determine whether the declinations are in compliance. The Company should retain declinations for at least 3 years.

## F. **Workers' Compensation**

### 1. 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.

The universe of 24 workers' compensation policies identified as midterm cancellations was selected for review. All 24 files were received and reviewed. No violations were noted.

## 2. 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.

From the universe of 251 workers' compensation policies nonrenewed during the experience period, 30 files were selected for review. All 30 files were received and reviewed. The 271 violations noted were based on the universe of 251 files, resulting in an error ratio of 100%.

The following findings were made:

### *12 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 12 files noted.

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

Requires that a nonrenewal notice shall state that at the insured’s request, the insurer shall provide loss information to the insured for at least three years or the period of time during which the insurer has provided coverage to the insured, whichever is less. The 251 files noted contained a nonrenewal notice which did not provide the required information.

*8 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 8 files noted contained a nonrenewal notice which required supporting business.

3. 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 359 workers' compensation policies which were renewed during the experience period, 25 files were selected for review. All 25 files were received and reviewed. No violations were 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

From the universe of 32 private passenger automobile policies identified as new business without surcharges, 15 files were selected for review. All 15 files were received and reviewed. The 98 violations noted were based on the universe of 32, resulting in an error ratio of 100%.

The following findings were made:

*1 Violation Title 75, Pa. C.S. §1711(b)*

All insurers subject to this chapter shall make available for purchase a motor vehicle insurance policy which contains only the minimum requirements of financial responsibility and medical benefits as provided for in this chapter. The Company failed to honor the request of the insured for a policy with minimum liability limits.

*1 Violation Title 75, Pa. C.S. §1731(b) & (c)*

The named insured shall be informed that he may reject uninsured and underinsured motorist coverage by signing a written rejection form. The Company failed to provide signed written rejection forms for uninsured and underinsured motorist coverage.

*32 Violations Title 75, Pa. C.S. §1791.1(a)*

Requires that at the time of application for original coverage and every renewal thereafter, an insurer must provide to an insured an itemized invoice listing the minimum motor vehicle insurance coverage levels mandated by the Commonwealth and the premium charge for the insured to

purchase the minimum mandated coverages. The invoice must contain the following notice in print of no less than ten-point type: "The laws of the Commonwealth of Pennsylvania, as enacted by the General Assembly, only require you to purchase liability and first-party medical benefit coverages. Any additional coverage or coverages in excess of the limits required by law are provided only at your request as enhancements to basic coverages." The insurer shall provide the itemized invoice to the insured in conjunction with the declaration of coverage limits and premiums for the insured's existing coverages. The Company failed to provide the required notice at the time of application.

*32 Violations Title 75, Pa. C.S §1791.1(b)*

Requires an insurer to provide an insured a notice of the availability of two alternatives of full tort insurance and limited tort insurance. The Company did not provide the notice of tort options to the insured at the time of application.

*32 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 did not provide the surcharge disclosure plan to the insured at the time of application.

Private Passenger Automobile - New Business With Surcharges

The universe of 1 private passenger automobile policy identified as new business with surcharges by the Company was selected for review. The file was received and reviewed. The 3 violations noted were based on one file, resulting in an error ratio of 100%.

The following findings were made:

*1 Violation Title 75, Pa. C.S. §1791.1(a)*

Requires that at the time of application for original coverage and every renewal thereafter, an insurer must provide to an insured an itemized invoice listing the minimum motor vehicle insurance coverage levels mandated by the Commonwealth and the premium charge for the insured to purchase the minimum mandated coverages. The invoice must contain the following notice in print of no less than ten-point type: "The laws of the Commonwealth of Pennsylvania, as enacted by the General Assembly, only require you to purchase liability and first-party medical benefit coverages. Any additional coverage or coverages in excess of the limits required by law are provided only at your request as enhancements to basic coverages." The insurer shall provide the itemized invoice to the insured in conjunction with the declaration of coverage limits and premiums for the insured's existing coverages. The Company failed to provide the required notice at the time of application.

*1 Violation Title 75, Pa. C.S §1791.1(b)*

Requires an insurer to provide an insured a notice of the availability of two alternatives of full tort insurance and limited tort insurance. The Company did not provide the notice of tort options to the insured at the time of application.

*1 Violation 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 did not provide the surcharge disclosure plan to the insured at the time of application.

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

From the universe of 305 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.

The following concern was made:

**Concern:** The Company provides a notice listing the minimum mandated coverages at renewal along with the premium cost. Hereafter, the Company should implement an invoice at renewal that itemizes the premium charge for the insured to purchase the minimum mandated coverages.

### Private Passenger Automobile – Renewals With Surcharges

The universe of 21 private passenger automobile policies renewed with surcharges during the experience period was selected for review. All 21 files were received and reviewed. No violations were noted.

The following concern was made:

**Concern:** The Company provides a notice listing the minimum mandated coverages at renewal along with the premium cost. Hereafter, the Company should implement an invoice at renewal that itemizes the premium charge for the insured to purchase the minimum mandated coverages.

### **B. Private Passenger Automobile – Assigned Risk**

Merchants 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. During the experience period, the Company did not have any private passenger assigned risk policies in force.

### **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

From the universe of 172 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.

#### Homeowner Rating – New Business With Surcharges

The Company was asked to provide a list of homeowner policies written as new business with surcharges during the experience period. The Company originally identified 108 policies. A review of a sample of 20 files revealed that none of the policies contained a surcharge for losses. A new data run was ordered and it was determined that the Company did not have any new business policies with 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.

#### Homeowner Rating – Renewals Without Surcharges

From the universe of 1,068 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

The universe of 7 homeowner policies renewed with surcharges during the experience period was selected for review. All 7 files were received and reviewed. No violations were noted.

### **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

From the universe of 47 tenant homeowner policies written as new business without surcharges during the experience period, 15 files were selected for review. All 15 files were received and reviewed. No violations were noted.

### Tenant Homeowner Rating – New Business With Surcharges

The Company was asked to provide a list of tenant homeowner policies written as new business with surcharges during the experience period. The Company originally identified 14 policies. A review of the 14 files revealed that none of the policies contained a surcharge for losses. A new data run was ordered and it was determined that the Company did not have any new business policies with 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

From the universe of 314 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.

### Tenant Homeowner Rating – Renewals With Surcharges

The universe of 2 tenant homeowner policies renewed with surcharges by the Company during the experience period was selected for review. Both files were received and reviewed. No violations were noted.

## **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**

The universe of 1 dwelling fire policy written as new business without surcharges was selected for review. The file was 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

The universe of 14 dwelling fire policies renewed without surcharges was selected for review. All 14 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 rated the policy incorrectly, resulting in an overcharge of \$11.

## 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 First Party Medical Claims
- E. Automobile First Party Medical Claims Referred to a PRO
- F. Homeowner Claims
- G. Tenant Homeowner 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**

From the universe of 29 private passenger automobile property damage claims reported during the experience period, 15 files were selected for review. All 15 files were received and reviewed. No violations were noted.

**B. Automobile Comprehensive Claims**

From the universe of 27 private passenger automobile comprehensive claims reported during the experience period, 15 files were selected for review. All 15 files were received and reviewed. No violations were noted.

**C. Automobile Collision Claims**

From the universe of 27 private passenger automobile collision claims reported during the experience period, 15 files were selected for review. All 15 files were received and reviewed. No violations were noted.

**D. Automobile First Party Medical Claims**

The universe of 12 private passenger automobile first party medical claims reported during the experience period was selected for review. All 12 files were received and reviewed. No violations were noted.

**E. Automobile First Party Medical Claims Referred to a PRO**

The Company was asked to provide a list of all private passenger automobile first party medical claims that were referred to a peer review organization during the experience period. The Company did not report any claims. The Company was also asked to provide copies of any written contracts with the peer review organization it has contracted. The Company advised that they did not have any written contracts in place with a peer review organization.

The following finding was made:

*1 Violation Title 31, Pa. Code, Section 69.53(a)*

A Peer Review Organization shall contract, in writing, jointly or separately with an insurer for the provision of peer review services as authorized by Act 1990-6 and this chapter. The Company failed to have a written contract in place with a peer review organization.

**F. Homeowner Claims**

From the universe of 86 homeowner claims reported 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:

*7 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 7 claims noted.

**G. Tenant Homeowner Claims**

The universe of 6 tenant homeowner claims reported during the experience period was selected for review. All 6 files were received and reviewed.

The 2 violations noted were based on 2 files, resulting in an error ratio of 33%.

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.

### 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.

No violations were noted.

## *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 60 pieces of advertising in use during the experience period, which included brochures, agent's kits and agent sales aides. Internet advertising for agents 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 10 consumer complaints received during the experience period and provided all consumer complaint logs requested. All 10 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 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.

*1 Violation Insurance Company Law, Section 506.1 [40 P.S. §636.1]*

Requires that 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 cancelled the policy within the 180 days of the death of the named insured.

The following synopsis reflects the nature of the 10 complaints that were reviewed.

•	6	Claims Related	60%
•	2	Billing	20%
•	1	Customer Service	10%
•	1	Cancellation	10%
	<hr/>		<hr/>
	10		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:

*1 Violation 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 producer was found to be writing and/or soliciting policies but was not found in Insurance Department records as holding a Pennsylvania producer license.

Simon Cohen Levin

*18 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.

H. Dean Allison Agency/T/A MBV, Inc.  
Barnes Financial Group, Inc.  
BRS Services, Inc.  
George Burkle, inc.  
Francis J. Craig Agency, Inc.  
Gallina & Sons  
Edward F. Haldeman & Associates, Inc.  
Thomas H. Heist Insurance Agency, Inc.  
Hopwood Insurance Agency, Inc.  
Insurance Agency Alliance, Inc.  
Kelly Insurance Group, Inc.  
Robert McIntyre Insurance, Inc.  
Peebly Insurance, Inc.  
Howard R. Peterman Company  
Snyder Moore Agencies, Inc.  
Paul Sprowls Agency, Inc.  
Yardley Insurance Services, Inc.  
Richard A. Zuber Insurance Agency

## *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 and revise internal control procedures to ensure compliance with cancellation notice requirements of Act 68, Section 2003 [40 P.S. §§991.2003], 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 the violation regarding the requirement for cancellation and nonrenewal notices, as noted in the Report, does 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 review and revise internal control procedures to ensure compliance relative to commercial cancellation and nonrenewal requirements of Act 86, Sections 3 and 7 [40 P.S. §§3403 and 3407], so that the violations noted in the Report do not occur in the future.
5. 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.

6. The Company must review Title 75, Pa. C.S. §1791.1(a) and (b) to ensure that an itemized invoice listing minimum coverages and tort options is provided at the time of application, as noted in the Report, and does not occur in the future.
7. 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.
8. The Company must review Act 205, Section 5(a)(4) [40 P.S. §1171.5(a)(4)] to ensure that the violation relative to supporting coverage noted in the Report does not occur in the future.
9. The Company must revise its underwriting procedures to ensure that each applicant for private passenger automobile liability insurance is provided an opportunity to exercise the waiver for uninsured and underinsured motorist coverage forms are obtained and retained with the underwriting file. This is to ensure that violations noted under Title 75, Pa. C.S. §1731(b) & (c) do not occur in the future.
10. The Company must review Act 246, Section 4(a) and (h) [40 P.S. §1184] and take appropriate measures to ensure the dwelling fire rating violation listed in the report does not occur in the future.
11. 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.

12. The Company must review Title 75, Pa. C.S. §1711(b) and make available for purchase a motor vehicle insurance policy which contains only the minimum requirements of financial responsibility and medical benefits.
13. 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.
14. The Company must review Title 31, Pa. Code, Section 69.53(a) with its claim staff to ensure that a written contract is in place with an approved peer review organization established for the purpose of evaluating treatment, health care services, products or accommodations provided to any injured person. Such evaluation shall be for the purpose of confirming that such treatment, products, services or accommodations conform to the professional standards of performance and are medically necessary.
15. 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.
16. The Company must revise and reissue their underwriting guidelines for use in Pennsylvania to ensure that guidelines do not require supporting coverage.

17. 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 Section 2003 of Act 68 [40 P.S. §991.2003].

**XIII. COMPANY RESPONSE**



**Thomas B. Harris, CPCU**  
Vice President, Underwriting and Product Development

March 26, 2008

**VIA OVERNIGHT MAIL**

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: **Merchants Mutual Insurance Company**  
**Market Conduct Examination Warrant Number: 07-M29-024**

Dear Mr. Derk:

Please accept this letter in response to the Department's Report of Examination of Merchants Mutual Insurance Company covering the period January 1, 2006, through December 31, 2006. We have specifically addressed each of the Department's 17 recommendations.

Our response outlines the corrective actions we have implemented in Underwriting, Claims, and Sales & Marketing to achieve compliance with Pennsylvania laws and regulations. We will monitor adherence to proper procedures via quarterly quality review audits.

Merchants greatly appreciates the professionalism and understanding you, Ms. Arnold, and Mr. Myers extended to us throughout the exam process.

Please do not hesitate to contact me should you have any questions regarding this response.

Sincerely,

Thomas B. Harris, CPCU  
Vice President, Underwriting and Product Development

Enclosures

**MERCHANTS INSURANCE GROUP**

250 Main Street P.O. Box 903 Buffalo, New York 14240 (716)849-3333

### **XIII. COMPANY RESPONSE**

#### **Recommendation #1**

**The Company must review and revise internal control procedures to ensure compliance with cancellation notice requirements of Act 68, Section 2003 [40 P.S. §§991.2003], so that the violations noted in the Report do not occur in the future.**

Merchants has provided a copy of 40 P.S. §§991.2003 to all Personal Lines Underwriting personnel, and clarified in writing the prohibition of using age and/or driving experience as a reason for cancellation, non-renewal, or declination of a Private Passenger Auto policy. Further, Merchants has revised and republished our Personal Auto underwriting guidelines to remove all criteria relating to age or driving experience.

Adherence to proper cancellation, nonrenewal, and declination procedures is included in our quarterly quality review audits.

#### **Recommendation #2**

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

With respect to blank cancellation and/or non-renewal reasons, Merchants has revised our policy processing system to require the entry of free-form text when an underwriter decides to cancel or non-renew a Homeowners Policy. Therefore, it is no longer possible to issue a cancellation or non-renewal without the addition of this text.

With respect to vague cancellation notice reasons, we have provided a copy of 40 P.S. §1171.5(a)(9) to all Personal Lines Underwriting personnel, and clarified in writing the requirement that reasons for cancellation or nonrenewal be specific and identify the change or increased hazard that was relied on for the action. Notices will state the specific reason(s) for the cancellation or nonrenewal.

With respect to non-payment cancellation notices, we are making programming changes to print the date when the premium was due on the cancellation notice.

Adherence to proper cancellation, nonrenewal, and declination procedures is included in our quarterly quality review audits.

#### **Recommendation #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.**

With respect to the cancellation due to the death of the named insured, Merchants has clarified in writing to all Personal Lines Underwriting personnel the requirement that basic property insurance must be continued for at least 180 days after the death of the named insured or until the sale of the property, whichever event occurs first, provided that the premiums for the coverage are paid.

#### **Recommendation #4**

**The Company must review and revise internal control procedures to ensure compliance relative to commercial cancellation and nonrenewal requirements of Act 86, Sections 3 and 7 [40 P.S. §§ 3403 and 3407], so that the violations noted in the Report do not occur in the future.**

With respect to blank cancellation and/or non-renewal reasons, Merchants has revised our policy processing system to require the entry of free-form text when an underwriter decides to cancel or non-renew a Commercial Insurance Policy. Therefore, it is no longer possible to issue a cancellation or non-renewal without the addition of this text.

With respect to vague cancellation and/or non-renewal reasons, Merchants has provided a copy of 40 P.S. §§3403 and 3407 to all Commercial Lines Underwriting personnel, and clarified in writing the requirement that reasons for cancellation and non-renewal be specific and identify the condition, factor or loss experience that caused the cancellation or nonrenewal. Notices will provide sufficient information or data for the insured to correct the deficiency.

With respect to the eleven violations for failure to provide 60 days notice of nonrenewal, please note these were all Dwelling Fire policies, to which we were mistakenly applying the Personal Lines notice standard of 30 days. Within Merchants, our Personal Lines Underwriting unit handles all Dwelling Fire policies. Therefore, we have clarified in writing to all Personal Lines underwriting staff the requirement that Dwelling Fire nonrenewals require a minimum of 60 days notice to the insured. In addition, we are making programming changes to increase the minimum number of days allowed by our policy processing system for Dwelling Fire nonrenewals to 60 days.

With respect to notification to the insured of the availability of loss information on Workers' Compensation nonrenewal notices, Merchants has added the required verbiage to the notice. Our nonrenewal notices for the other Commercial Lines of business did already include the required loss information verbiage.

Adherence to proper cancellation, nonrenewal, and declination procedures is included in our quarterly quality review audits.

#### **Recommendation #5**

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

With respect to notice of renewal premiums, Merchants has provided a copy of 40 P.S. §3401 to all Commercial Lines Underwriting personnel, and clarified in writing the requirement that any increase in renewal premium for any reason requires 30 days notice to the insured.

Adherence to proper renewal notification procedures is included in our quarterly quality review audits.

#### **Recommendation #6**

**The Company must review Title 75, Pa. C.S. §1791.1(a) and (b) to ensure that an itemized invoice listing minimum coverages and tort options is provided at the time of application, as noted in the Report, and does not occur in the future.**

Merchants is making programming changes to produce the required notification at the time of application. The notice will specifically identify minimum coverages and the associated premium breakdown and will identify the insured's existing coverage limits and premium breakdown.

#### **Recommendation #7**

**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.**

Merchants is making programming changes to produce the Surcharge Disclosure notice (form MU 08 47 07 05) at the time of application.

#### **Recommendation #8**

**The Company must review Act 205, Section 5(a)(4) [40 P.S. Section §1171.5(a)(4)] to ensure that the violation relative to supporting coverage noted in the Report does not occur in the future.**

Merchants has provided a copy of 40 P.S. Section §1171.5(a)(4) to all Personal Lines and Commercial Lines underwriting staff, and clarified in writing, that under no circumstances may lack of supporting business be a deciding factor in a decision to decline new business or non-renew or cancel existing business.

In addition, we have revised and republished our Homeowners, Dwelling Fire, and Workers' Compensation underwriting guidelines to remove all criteria relating to supporting business.

Adherence to proper cancellation, nonrenewal, and declination procedures is included in our quarterly quality review audits.

#### **Recommendation #9**

**The Company must revise its underwriting procedures to ensure that each applicant for private passenger automobile liability insurance is provided an opportunity to exercise the waiver for uninsured and underinsured motorist coverage forms are obtained and retained with the underwriting file. This is to ensure that violations noted under Title 75, Pa. C.S. §1731(b) & (c) do not occur in the future.**

Merchants has a procedure in place to automatically generate Coverage Selection Forms with all new business. The one file found in the examination was the result of human error in that a generic Coverage Selection Form was used rather than our automatically generated form. We believe this was an extremely isolated incident, however we have clarified in writing the need to use our system generated Coverage Selection Form with all new business.

In addition, we are making programming changes to further enhance our Coverage Selection Form by printing "Rejected" whenever the insured rejects Uninsured and Underinsured Motorist Coverage on the ACORD application.

#### **Recommendation #10**

**The Company must review Act 246, Section 4(a) and (h) (40 P.S. § 1184) and take appropriate measures to ensure the dwelling fire rating violation listed in the report does not occur in the future.**

Merchants is making programming changes to correct the Dwelling Fire rating algorithm to exactly match our filed and approved manual rules. We have refunded the \$11 overcharge for the one file found in the examination. We have previously provided documentation of the refund to the Pennsylvania Insurance Department, which Ms. Constance Arnold has acknowledged.

#### **Recommendation #11**

**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.**

We have refunded the \$11 overcharge for the one file found in the examination. We have previously provided documentation of the refund to the Pennsylvania Insurance Department, which Ms. Constance Arnold has acknowledged.

#### **Recommendation #12**

**The Company must review Title 75, Pa. C.S. § 1711(b) and make available for purchase a motor vehicle insurance policy which contains only the minimum requirements of financial responsibility and medical benefits.**

Merchants has provided a copy of Pa. C.S. §1711(b) to all Personal Lines Underwriting personnel, and clarified in writing the requirement to allow minimum financial responsibility limits. In addition, we have revised and republished our guidelines to reflect the availability of minimum financial responsibility limits. Lastly, we are making programming changes to reflect the minimum limits in the application of the guidelines and the preferred driver discount.

#### **Recommendation #13**

**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.**

Merchants will conduct monthly audits of all Pennsylvania Homeowner and Tenant Homeowner claims to ensure that the required status letters are sent to policyholders in accordance with the statutory requirements as outlined in Title 31, Pennsylvania Code, Chapter 146, Unfair Claims Settlement Practices. We will retain records of all monthly claims audits.

#### **Recommendation #14**

**The Company must review Title 31, Pa. Code, Section 69.53(a) with its claim staff to ensure that a written contract is in place with an approved peer review organization established for the purpose of evaluating treatment, health care services, products or accommodations provided to any injured person. Such evaluation shall be for the purpose of confirming that such treatment, products, services or accommodations conform to the professional standards of performance and are medically necessary.**

Merchants has a formal signed agreement in place with Concentra Integrated Services, Inc. (now known as Coventry). A copy of the services agreement is available upon request. We have confirmed with Coventry that they are an approved Peer Review Organization (PRO) pursuant to Title 31, Pa. Code, Section 69.53(a).

#### **Recommendation #15**

**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.**

Merchants has filed a notice of appointment to the Department for the 18 producers that were not found as having a Merchants appointment. These errors resulted from an old, manual process by which we notified the Insurance Department of agency appointments.

Since late 2004 Merchants has employed an automated Agency Appointment process by which the Pennsylvania Insurance Department is electronically notified of new agency appointments in real-time via our vendor, Sircon. In addition, under our Agency Agreement, Merchants agents are contractually obligated to maintain a valid license in all applicable jurisdictions.

Given our formalized and automated Agency Appointment process, we are confident errors such as those found in the exam will not occur in the future.

#### **Recommendation #16**

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

Merchants has revised and republished our Homeowners, Dwelling Fire, and Workers' Compensation underwriting guidelines to remove all criteria relating to supporting business.

#### **Recommendation #17**

**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 Section 2003 of Act 68 (40 P.S. § 991.2003).**

Merchants has revised and republished our Personal Auto eligibility criteria with all references to driver age, not at-fault accidents, and comprehensive claims removed.