

2002 PROPERTY AND CASUALTY TARGET MARKET CONDUCT EXAMINATION

OF

**STATE NATIONAL SPECIALTY INSURANCE COMPANY
(STATE NATIONAL COMPANIES)**

BY

THE FLORIDA DEPARTMENT OF INSURANCE

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EXECUTIVE SUMMARY

State National Specialty Insurance Company (“Company”) is a foreign property and casualty insurer licensed to conduct business in the State of Florida during the scope of this property and casualty market conduct examination. The scope of this examination was January 2001 through January 2002. The examination began February 24, 2002 and ended April 20, 2002. This is the first examination for this insurer.

The purpose of this examination was to review the issues behind the volume of consumer complaints received by the Department of Insurance. From a review of the consumer complaints filed against the Company, the Department focused on rating issues and claim delays.

A total of three hundred and eighty (380) files were examined for this Company with twenty-five (25) errors being identified. The following represents general findings; however, specific details are found in each section of the report.

Fifty (50) complaint files were examined with no errors.

Fifty (50) private passenger automobile policies were examined. Fifteen (15) errors were identified. The errors were the result of human clerical errors in calculating individual rates. No consistent or system errors were found.

Fifty (50) cancellations and nonrenewals were examined with ten (10) errors being identified. The errors include the failure to give proper notice of cancellation. No errors involved nonrenewals.

One hundred (100) claim files were examined with no errors noted. Fifty-four claim files involved files with independent medical examinations requested by the Company concerning PIP coverage.

Thirty (30) files were examined for the agents/MGA/advertising review with no errors identified.

The Company terminated its agreement with Assurance Managing General Agents, Inc., and began the nonrenewal of all of its policies prior to advising the Florida Department of Insurance. The Company has been advised to discontinue nonrenewal until it has complied with governing law and properly notified the Florida Department of Insurance of its intent to discontinue writing this line of business.

The Company has been requested to return all overcharges that resulted from incorrect rating of private passenger automobile policies. Those overcharges have been returned accompanied by MC-1 letters.

As a result of the findings of this examination, \$43.00 was returned to Florida consumers due to overcharges of premium.

CERTIFICATE OF AUTHORITY – AUTHORIZED LINES

GENERAL COMMENTS

The Certificate of Authority and Renewal Invoices were reviewed for all years within the scope of the examination.

EXAM FINDINGS

The review included verification of the lines of business the Company was authorized to write during the scope of the examination versus those lines actually being written. The review verified that notification requirements to discontinue writing private passenger automobile lines were not met. The Company did not meet those requirements until after they had discontinued renewal of policies. Prior to the examination conclusion, the Company had begun the notification process with the Florida Department of Insurance.

Examination Findings

One (1) error was found.

The error is described as follows:

1. One (1) error was due to failure to notify the Department of a line of business discontinuance. This constitutes a violation of Section 624.430, Florida Statutes.

The Company ceased writing new and renewal private passenger automobile lines effective December 31, 2001. Notice was mailed from the Company dated March 21, 2002 to the Department of Insurance and received on March 22, 2002.

The Company was requested to cease all withdrawal actions March 27, 2002, until the withdrawal plan was approved by the Department of Insurance.

COMPANY OPERATIONS/MANAGEMENT

HISTORY/MANAGEMENT

The Company is a wholly-owned insurance company subsidiary of State National Companies (“SNC”). The Company, State National Insurance Company, Inc., and State and County Mutual Fire Insurance Company are the three insurance companies owned by SNC.

The Company is a stock fire and casualty insurance company organized under the laws of Florida in April 1963. The Company is admitted to write insurance in 30 jurisdictions. The Company writes primarily private passenger automobile business which is produced by unaffiliated managing general agencies. The Company was acquired by SNC in 1999. The Company was re-domesticated to Texas in 2001.

SNC is family owned. Lonnie, Terry and Garry Ledbetter began the parent company in 1973. Management has not had substantive changes in officers during the scope of the examination.

The principal administrative office of State National is in Fort Worth, Texas. Claim servicing for Florida is by Superior Adjusting of Ft. Lauderdale, Florida.

COMPANY PROCESSES/STATISTICAL AFFILIATIONS

Computer System

The Company maintains personal automobile information on a proprietary system of the managing general agent (MGA), Assurance Managing General Agents, utilizing an IBM AS400 with remote access via network workstations.

The Company and MGA allow email access for insured, agent, regulator and vendor customers. The Company and MGA systems are protected by firewalls.

The MGA maintains an agency network for franchise agents of Assurance Managing General Agents. These agents can submit applications and underwriting information through the internet.

The Company and the MGA maintain independent sites on the internet for informational purposes only. Neither website is used for agent solicitations or claims settling.

Anti-Fraud Plan

The Company has filed a Plan with the Florida Department of Insurance as required by Section 626.9891, Florida Statutes.

The Plan does meet the requirements and has established a Special Investigation Unit (SIU) that services business written in the State of Florida. The investigative activities include inquiry into suspicious property and casualty claims and questionable underwriting submissions.

Disaster Recovery Plan

The Company has developed a Disaster Recovery Plan for use with Florida business. The plan includes relocation of staff to predetermined sites and utilization of alternate computer facilities.

Internal Audit Procedures

The Company has developed Internal Audit Procedures for use in reviewing Florida business. An independent auditor performed two audits annually during the scope of the examination.

Privacy Plan

The Company has developed a Plan to meet the requirements of Emergency Rule 4ER-01. The Company does not use credit reports or credit rating in the underwriting process.

The Company sent its Privacy Policy to all policyholders by July 1, 2001 providing an opportunity for policyholders to opt-out from having information regarding the policyholder shared.

Statistical Affiliations

The Company reports statistical information to the National Association of Independent Insurers (NAII).

Credit Reports

The Company does not use Credit Reports as an underwriting tool.

OPERATIONS/MARKETING

Marketing

The Company only marketed private passenger automobile insurance through one managing general agent in Florida during the scope of the examination. The Company has discontinued marketing in Florida and advised the Department of Insurance.

Agents/Agencies/MGA/Exchange of Business/Direct Response/Internet/Adjusters and Claims Handling

An agency agreement between the Company, Assurance Managing General Agents and Transatlantic Reinsurance Company existed during the scope of the examination. Assurance Managing General Agents contracted to perform all functions necessary for production, service and management of policies issued. The MGA is licensed and appointed in the State of Florida.

The Company used registered agents for all production. The Company does not appoint agents. Policies were stamped with the correct wording and numbered as registered policies.

The Company does sponsor an internet web site for informational purposes only. The internet is not used for solicitations or claim handling.

Lines of Business

The Company wrote private passenger automobile during the scope of the examination in all areas of Florida. The Company ceased writing business December 31, 2001. The Company and the MGA have terminated their contract. All business is being non-renewed. No agents are being registered in 2002.

REVIEW OF POLICIES

PRIVATE PASSENGER AUTOMOBILE

Description of Product/Lines of Business

The Company writes private passenger automobile through a managing general agent. Private passenger automobile policies can include bodily injury, property damage, collision, comprehensive, personal injury protection, uninsured motorist and towing. The Company uses tier rating to differentiate between groups of coverage. Each renewal is underwritten as if it were a new submission. Each renewal has a new motor vehicle record reviewed and the insured is placed in the appropriate tier. The Company does write policies that only include property damage liability and personal injury protection coverage. The Company does not use credit reports or credit rating in the underwriting process.

Premium and Policy Counts

Direct Premiums Written and in-force policy counts for the scope of the examination are as follows:

<u>Year</u>	<u>DPW</u>	<u>Policy Count</u>
2000	\$13,011,988	29,631
2001	\$13,787,559	28,591

This program was written for only two years, January 1, 2000 to December 31, 2001.

Examination Findings

Fifty (50) policy files were examined.

Fifteen (15) errors were found.

Errors affecting premium resulted in six (6) overcharges totaling \$106.00 and three (3) undercharges totaling \$183.00.

The errors are broken down as follows:

1. Fifteen (15) errors were due to failure to follow the filed rate, rating schedule, rating rule, or underwriting guideline. This constitutes a violation of Section 627.0651, Florida Statutes. These errors were due to failure to use the correct symbol for vehicles, failure to use correct vehicle identification number and failure to use the correct model year of the vehicle. These errors resulted in two (2) overcharges totaling \$43.00, which have been refunded by the Company. Other overcharges were offset by undercharges or were less than \$5.00.

CANCELLATIONS/NONRENEWALS REVIEW

DESCRIPTION OF CANCELLATION/NONRENEWAL PROCEDURES

For the files reviewed notices of cancellation and nonrenewal are issued in compliance with Florida Statutes. Nonrenewal notices are issued thirty-five days in advance for private passenger automobile. Notices provide specific reasons for the action. Return premiums are calculated on both a short-rate and pro-rata basis. Notices are sent by certificate of mailing to the named insured and mortgage holders.

CANCELLATION REVIEW

Forty (40) cancelled policies were examined.

One (1) error was found.

The error is described as follows:

1. One (1) error was due to failure to provide timely notice of cancellation. This constitutes a violation of Section 627.728, Florida Statutes. This error was due to providing twenty-nine (29) days notice.

NONRENEWAL REVIEW

Ten (10) nonrenewed policies were examined.

No errors were found.

COMPLAINTS/INVESTIGATION REVIEW

The reason for this target examination was the number of consumer complaints received by the Florida Department of Insurance. The Company was the subject of 165 complaints received by the Department during the scope of the examination. Review of the consumer complaints received by the Florida Department of Insurance did not establish an indication of improper business practices.

The Company has an established complaint procedure that involves the participation of both the Company and the MGA.

A complete record of all the complaints received by the Company during the scope of the examination has been maintained as is required by Section 626.9541(1) (j), Florida Statutes. Procedures for handling these complaints have been established by the Company.

Fifty (50) consumer complaints received during the scope of examination were reviewed and findings are as follows:

COMPLAINTS RECEIVED FROM DOI

Consumer Services Ref. No.	Alleged Violation	Violation Found	Comments
s0001 0034600	Premium Cancellation	None	Premium Finance Co. cancelled
s0001 0020826	Underwriting Cancellation	None	Lack of documentation with application
s0001 0028082	Underwriting Cancellation	None	Duplicate coverage
s0001 0049885	Incorrect Premium	None	Wrong symbol
s0001 0056814	Underwriting Cancellation	None	Other resident driver & medical
n/a	Refund of premium	None	Bureau of Agents & Agency complaints, auto cancellation and refund
s0001 0060362	Underwriting Cancellation	None	No documentation of coverage
s0001 0062228	Underwriting Cancellation	None	Cancel – incorrect application
s0001 0068689	Underwriting Cancellation	None	Cancel - non driver question
s0001 0063778	Denial of coverage	None	No record of policy
s0102 0005894	Underwriting Cancellation	None	Cancel - < 2yr license
s0102 0009847	Premium	None	Cancel - non-pay
s0103 0010966	Premium	None	Cancel - short-rate
s0102 0011082	Underwriting Cancellation	None	Misrepresentation - incorrect application
s0102 0011771	Underwriting Cancellation	None	Misrepresentation - incorrect application
s0102 0015482	Underwriting Cancellation	None	Misrepresentation - incorrect application
s0102 0021482	Underwriting Cancellation	None	Misrepresentation - incorrect application
s0102 00194667	Premium	None	Misrepresentation - incorrect application
s0102 0022852	Premium	None	Misrepresentation - incorrect application
s0102 0018991	Underwriting Cancellation	None	Duplicate policy
s0102 0019394	Premium	None	Nonpay
s0102 0023478	Underwriting Cancellation	None	Misrepresentation - incorrect application
s0102 0024658	Premium	None	Cancel - return premium

s102 0029756	Premium	None	Nonpay
s102 0030252	Incorrect Premium	None	Misrepresentation - incorrect application
s0102 0038402	Premium Cancellation	None	Nonpay
s0102 0036626	Premium Cancellation	None	Nonpay
s0102 0040297	Underwriting Cancellation	None	Incorrect application
s001 0039983	Claims – delay	None	Total loss disputed by insured. Appraiser confirmed total.
s001 0039551	Claims – delay	None	Repair check mailed 1/20/01
s0001 0037790	Claims – delay	None	Rental bill paid slow
s0001 0042182	Claims - refused to provide policy info to an attorney	None	Coverage limits sent on two occasions
s0001 0044982	Claims – denial	None	Company reversed denial and paid
s0001 0052213	Claims – delay	None	Company offered compromise liability settlement
s0001 0050059	Claims - settlement amount	None	Company paid additional rental
s0001 0061320	Claims – delay	None	Company provided coverage
s0001 0059384	Claims – delay	None	Insured did not have physical damage coverage
s0001 0062725	Claims – delay	None	Insured did not have coverage for PD claim. Denied in writing
s0001 0062747	Claims – delay	None	Agent/binder question, claim denied
s0001 00633022	Claims - handling	None	Insured did not submit towing bill
s0001 0064975	Claims - denial	None	Insured denied coverage, no cooperation
s0001 0065521	Claims - settlement amount	None	Total loss disputed by insured. Appraiser confirmed total.
s0102 0004271	Premium	None	Misrepresentation - incorrect application
s0102 0011956	Claims -settlement amount	None	Ab-initio cancellation, premium to finance company
s0102 0020785	Claims	None	Comprehensive loss - car into water
s0102 0021779	Claims - handling	None	Check mailed to wrong address
s0102 0025190	Claims - settlement amount	None	Claimant used collision coverage due to disagreement on value of total loss
s0102 0023930	Claims -denial	None	Ab-initio cancellation, premium to finance company
s102 0030912	Claims	None	Total loss disputed by insured. Appraiser confirmed total.
s0102 0029433	Claims - handling	None	Insured late reported claim d/l 6/6/00, reported 11/14/01

No errors were found.

COMPLAINTS COMPANY RECEIVED FROM CONSUMERS

No complaints received directly from consumers were contained in the Company's complaint records for the scope of the examination.

CLAIMS REVIEW

DESCRIPTION OF CLAIMS REVIEWED – NON-PPA/MEDICAL REVIEWS

The types of private passenger automobile claims reviewed include: bodily injury; property damage; collision; comprehensive; uninsured motorists; underinsured motorist; medical payments; and personal injury protection (PIP).

Examination Findings

Forty-five (45) claims were examined. Fifteen (15) claims were collision, twelve (12) claims were comprehensive and eighteen (18) claims were property damage.

No errors were found.

DESCRIPTION OF CLAIMS REVIEWED – PPA/MEDICAL REVIEWS

Private passenger automobile claims reviewed included: bodily injury; uninsured motorist; underinsured motorists; and personal injury protection (PIP).

Examination Findings

Fifty-five (55) claims were examined. Fifty-four (54) claims were PIP and one (1) was bodily injury.

No errors were found.

AGENTS/MGA REVIEW/ADVERTISING/MARKETING

DESCRIPTION OF MGA ARRANGEMENTS

The Company appointed Assurance Managing General Agents, Inc., a licensed, managing general agent during the scope of the examination. The agreement provided that the MGA had sole authority to market, produce, underwrite, rate and issue policies. The MGA is responsible for adjusting claims for policies written in Florida. The policies were reinsured on a 100% quota share with Transatlantic Reinsurance Company. The agreement between the Company and the MGA terminated December 31, 2001. All policies are being nonrenewed.

Neither the Company nor the MGA advertised during the scope of the examination.

The MGA does charge a policy fee for each policy. No errors were found concerning policy fees.

The review disclosed that the Company and the MGA do not appoint agents. One hundred and twenty-five agents were registered to the Company during the scope of the examination.

The standard operating procedure is to not appoint agents because they do not have binding authority.

Examination Findings

Ten (10) applications written during the scope of examination were examined. Each agent was licensed in Florida but not appointed by the Company. Each agent was registered by the Company.

No errors were found.

Twenty (20) agencies were selected from agencies that produced over \$25,000 in premium. The licensed agents of the agencies are registered by the Company. The Company does not appoint Primary Agents.

No errors were found.