

2001 PROPERTY AND CASUALTY TARGET MARKET CONDUCT EXAMINATION

OF

AMERICAN ALTERNATIVE INSURANCE CORPORATION
(MUNICH RE)

BY

THE FLORIDA DEPARTMENT OF INSURANCE

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I. INTRODUCTION

American Alternative Insurance Corporation (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 the examination was January 1999 through May 2001. The examination began July 15, 2001 and ended September 1, 2001. This is the first property and casualty market conduct examination of this insurer by the Florida Department of Insurance.

The purpose of the current examination was to verify whether the Company is conducting business in compliance with Florida Statutes and Rules since it started writing business July 1, 1997 in the State of Florida.

During this examination, records reviewed included policies, audits, agent/MGA licensing, cancellations/nonrenewals, and consumer complaints for the period of January 1999 through May 2001, as reflected in the report.

This report contains examination results addressing all areas of noncompliance found during the course of the examination. In all instances, the Company was to take corrective action as required, issue appropriate refunds, make all necessary filings with the Department and immediately cease any activity that continues to place the Company in noncompliance with Florida Statutes/Rules.

As a result of the findings of this examination, \$236,292.75 was returned to Florida consumers due to overcharges of premium and/or inappropriately charged fees.

Additionally, agents may have collected and retained unauthorized inspection fees of \$75.00 in connection with some of the applications for 122 policies. The Company shall cause the return of any such fees to the affected insureds acknowledging no prior receipt of a refund. (See Pending Issues Section.)

II. PRE-EXAM REVIEW OF COMPANY WRITINGS

A. CERTIFICATE OF AUTHORITY - AUTHORIZED LINES

1. General Comments

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

2. Exam Findings

The review included verification of the lines of business the Company was authorized to write during the scope of examination versus those lines actually being written. It also included verification that notification requirements were met for any line of business that was discontinued.

No errors were found.

III. COMPANY OPERATIONS/MANAGEMENT

A. PROFILE

American Alternative Insurance Corporation was incorporated in New York on April 26, 1923, under the original name of American Union Insurance Company of New York. The name was changed in 1987 to American Union Reinsurance Company. American Union Reinsurance Company was acquired from American States Insurance Company by American Re Corporation on January 1, 1994.

American Re Corporation and its subsidiaries were acquired by Munich Re, a reinsurer domiciled in Germany on November 25, 1996. Munich Re is the ultimate controlling entity of American Alternative Insurance Corporation pursuant to insurance holding company laws.

Effective July 31, 1998, American Alternative Insurance Corporation changed its domicile from New York to Delaware through a merger with American Alternative Insurance Corporation of Delaware, a shell company established for the sole purpose of this transaction. As a result of the merger, all prior financial information was restated to reflect the collective information of the merged entities. The change of domicile of American Alternative Insurance Corporation was approved by the Florida Department of Insurance on December 1, 1998.

At this time, only the MGA, Inserve, is actively soliciting business in Florida. The Company requires that all producing agents be licensed and appointed by the Company and does not accept business under the exchange of business statute.

The Company does not have any current plans for conducting direct response workers' compensation marketing in Florida. There are also no current plans for conducting Internet marketing in Florida.

Claims are handled by licensed adjusters who are employees of the MGA, Inserve. When circumstances of a particular claim dictate, the claim is assigned to an adjusting company for assistance in handling.

The business of the Company is conducted by employees of Insurance Company Operations, a division of American Re. American Alternative Insurance Corporation does not have any employees.

B. MANAGEMENT

The Company does not have its own computer system at this time. The facilities and systems of American Re are utilized. Computer communications between the Company and the program administrators is conducted by means of the American Re website at www.amre.com. In order to minimize the impact of an unexpected loss of Vital Business Processes, American Re has contracted with IBM on behalf of American Re and American Alternative Insurance Corporation to provide its Disaster Recovery Plan and/or Technical Recovery guides in the event of a catastrophic disaster. The Company also has an IT-NT Server Recovery Plan in place as well as an Apollo System Technology Disaster Recovery Plan.

The Company contracted with a vendor specializing in fraud claims to utilize its Special Investigations Unit Services to handle anti-fraud activities relating to claims handling. The contract was revised on August 22, 1996 and again on June 2, 1999. The plan and subsequent revisions were filed with the Department of Insurance, Division of Fraud, under Section 626.9891(1)(b), Florida Statutes. Exhibit I.

The Company has a Manual of Operational and Internal Audit Procedures describing the philosophy and techniques regarding the monitoring and improvement of operations performed for the Company by MGA's, Program Administrators and TPA's. The manual provides directions on all aspects of an

operational unit, from when to conduct an audit to how to use the findings of an audit to improve performance. The Insurance Company Operations Department conducts audits to assure compliance with regulations and conformance to Company standards.

The Company has a privacy plan in place which complies with Emergency Rule 4ER01. Exhibit II.

C. OPERATIONS

The Company's MGA, Inserve, has specific marketing plans, which include dividing the State into four geographical areas with a limited number of independent agencies in each area. The agencies are trained for Company marketing and underwriting, as well as required to meet production goals. The target markets are retail, restaurants and light manufacturing.

IV. REVIEW OF POLICIES

A. WORKERS' COMPENSATION

1. Application of Rules, Rates and Forms

a. General Comments

American Alternative Insurance Corporation is a National Council on Compensation Insurance (NCCI) company and as such uses this organization's rules, rates and forms. In addition, the Company does make some independent filings. The NCCI acts as statistical agent for this line of business.

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>
1999	\$16,578,547	2,073
2000	\$ 9,131,461	1,324
2001	\$ 3,153,572	277

The decrease in both direct premium written and policy count was due to the Company changing its marketing strategy. The MGA was placing business with the Company under the exchange of business statute by accepting submissions from all agents. This was changed to accept business only from agents licensed and appointed with the Company. The underwriting guidelines were also changed and a large number of policies were nonrenewed.

b. Error Percentages

One hundred (100) policies and audits were examined.

Ninety-three (93) errors were found.

Errors affecting premium resulted in ten (10) overcharges totaling \$4,678.00 and twelve (12) undercharges totaling \$12,507.00. An additional estimated \$9,150.00 is also being refunded to 122 insureds as a result of the refund of inspection fees.

The errors are broken down as follows:

1. Twenty-five (25) errors were due to failure to audit the policy and/or return the premium in a timely manner. This constitutes a violation of Section 627.191, Florida Statutes. The final audit was not completed and or billed within ninety days.
2. Seventeen (17) errors were due to failure to provide a notice of renewal, nonrenewal or cancellation in a timely manner. This constitutes a violation of Section 627.4133, Florida Statutes. A notice of renewal or nonrenewal was not issued forty-five days prior to expiration.
3. Seventeen (17) errors were due to failure to follow the filed rate, rating schedule, rating rule or underwriting guideline. This constitutes a violation of Section 627.191, Florida Statutes. The insured was not notified of a possible FCCPAP credit.

4. Eight (8) errors were due to failure to follow the filed rate, rating schedule, rating rule or underwriting guideline. This constitutes a violation of Section 627.191, Florida Statutes. The minimum premium for Classification 8810 was not charged when no premium was developed at audit , as required by NCCI rule. These errors resulted in eight (8) overcharges totaling \$4,216.00, which have been refunded by the Company.
5. Seven (7) errors were due to failure to follow the filed rate, rating schedule, rating rule or underwriting guideline. This constitutes a violation of Section 627.191, Florida Statutes. The incorrect employers liability increased limits factor was charged or the minimum premium was not charged. These errors resulted in six (6) undercharges totaling \$205.00 and one (1) overcharge which was combined with an undercharge for an experience modification factor error shown in item eight.
6. Three (3) errors were due to failure to follow the filed rate, rating schedule, rating rule or underwriting guideline. This constitutes a violation of Section 627.191, Florida Statutes. Credit for a drug free workplace was given without insured certification. These errors resulted in three (3) undercharges totaling \$6,826.00.
7. Two (2) errors were due to failure to follow the filed rate, rating schedule, rating rule or underwriting guideline. This constitutes a violation of Section 627.191, Florida Statutes. An incorrect classification was assigned to the insured's business. These errors resulted in one (1) overcharge totaling \$53.00, which has been refunded by the Company and one (1) undercharge totaling \$380.00.

8. One (1) error was due to failure to follow the filed rate, rating schedule, rating rule or underwriting guideline. This constitutes a violation of Section 627.191, Florida Statutes. The applicable premium discount was not allowed.
This error resulted in an overcharge totaling \$409.00, which has been refunded by the Company.
9. Three (3) errors were due to failure to follow the filed rate, rating schedule, rating rule or underwriting guideline. This constitutes a violation of Section 627.191, Florida Statutes. The incorrect experience modification factor was used. These errors resulted in three (3) undercharges totaling \$5,096.00.
10. One (1) error was due to failure to follow the filed rate, rating schedule, rating rule or underwriting guideline. This constitutes a violation of Section 627.191, Florida Statutes. A credit was allowed for the \$2,500 Mandatory Offer of Deductible. The undercharge for this error was combined with an undercharge for an experience modification factor error shown in Item eight.
11. One (1) error was due to failure to attach a mandatory endorsement. This constitutes a violation of Section 627.412, Florida Statutes. The Benefits Deductible Endorsement WC 09 06 05 was not attached when a \$500 deductible was chosen by the insured.
12. Two (2) errors were due to failure to comply with unfair trade practice requirements. This constitutes a violation of Section 626.9541(1)(n)(2)(a), Florida Statutes. A charge was not made for the attachment of Waiver of Right to Recover From Others as required by NCCI Florida exceptions.

13. Six (6) errors were due to failure to follow the filed rate, rating schedule, rating rule or underwriting guidelines. This constitutes a violation of Section 626.9541(1)(0)(1), Florida Statutes. The Company was charging inspection fees on policies produced through the Braishfield agency. The Company was requested to identify the affected insureds and refund any monies charged to the insureds. See Pending Issues Section.

V. AGENTS/MGA REVIEW

Ten (10) applications/policies written during the scope of examination were examined.

Twenty-nine (29) errors were found.

None of the errors affected policy fees.

The errors are broken down as follows:

1. Five (5) errors were due to failure to comply with workers' compensation application requirements. This constitutes a violation of Rule 4-189.003, Florida Administrative Code. The required Florida application was not used.
2. Six (6) errors were due to use of an unlicensed nonresident agent. This constitutes a violation of Section 626.741, Florida Statutes.
3. Nine (9) errors were due to failure to display the agent's name/license identification number or insurer name on the application. This constitutes a violation of Section 627.4085, Florida Statutes.
4. One (1) error was due to failure to maintain records. This constitutes a violation of Section 627.318, Florida Statutes. The policy file did not contain an application.
5. Four (4) errors were due to use of unlicensed/unappointed agent. This constitutes a violation of Section 626.112, Florida Statutes.
6. Four (4) errors were due to failure to properly countersign/obtain power of attorney. This constitutes a violation of Section 624.425, Florida Statutes.

VI. CANCELLATIONS/NONRENEWALS REVIEW

Fifty (50) cancelled/nonrenewed policies were examined.

Forty-eight (48) errors were found.

One (1) error resulted in an underreturn totaling \$732.00.

The errors are broken down as follows:

1. Twenty-three (23) errors were due to failure to audit policy and return premium in a timely manner. This constitutes a violation of Section 627.191, Florida Statutes.
2. Twenty-three (23) errors were due to failure to provide a specific reason for cancellation or nonrenewal. This constitutes a violation of Section 627.4091, Florida Statutes.
3. One (1) error was due to failure to follow the filed rate, rating schedule, rating rule or underwriting guideline. This constitutes a violation of Section 627.191, Florida Statutes. No premium was developed at audit so minimum premium for Classification Code 8810 applies. The cancellation was calculated on a short rate basis instead of pro rata when the insured closed the business. This error resulted in an underreturn totaling \$732.00, which has been refunded by the Company.
4. One (1) error was due to failure to provide timely notice of renewal, nonrenewal or cancellation. This constitutes a violation of Section 627.4133, Florida Statutes. A notice of cancellation was not issued.

VII. COMPLAINTS REVIEW

A complete record of all the complaints received by the Company since the date of the last 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. Complaint handling procedures are described in Exhibit III.

Consumer complaints received during the scope of examination were reviewed, and the findings are as follows:

A. DOI REFERRALS

INVESTIGATION REPORT CASE # 1428

CONSENT ORDER / CASE NO.: 33511-99-CO

American Alternative was directed by Consent Order 33511-99-CO to cease the practice of charging a managed care fee to its insureds, and within (60) days of the execution of the Consent Order, to refund \$48,420.00 in managed care fees assessed by Managed Care USA to the insureds identified by the Company.

The policy/audit rate review being conducted as a part of this market conduct examination revealed that the list of insureds initially furnished to the Department of Insurance was not all inclusive. This constitutes a violation of Section 626.9541(1)(0)(1), Florida Statutes.

The Company was requested to conduct a thorough search of all records to identify all insureds who have paid a managed care fee and refund such fee to the affected insureds.

The Company was further requested to furnish a list to the Department of Insurance of affected insureds and confirmation of the refunds being made. Exhibit IV.

The Company has advised that an additional 655 insureds who paid a managed care fee were identified and a total of \$230,882.75 has been refunded by the Company. Exhibit IV-c.

VIII. PENDING ISSUES

The following issues were pending at the conclusion of the examination:

There was a list of insureds identified in accordance with the Consent Order Case NO.: 33511-99-CO of June 22, 2001 as having paid and were being refunded a managed care fee. The policy review of this examination revealed that the list may not have been all inclusive. Some of the files reviewed indicated a fee had been charged to insureds not appearing on the list. The Company, with the cooperation of Inserve (f/k/a Occucare), was requested to conduct a thorough search of all records (1997-2001) to identify all insureds who have paid a managed care fee and refund any amount that was not identified under the Consent Order. Exhibit IV. The Company advised that checks totaling \$230,882.75 have been mailed to 655 insureds in addition to the refunds and insureds set forth on the list attached to the Consent Order. The Company has been directed to furnish a list of these insureds to the Department of Insurance, along with confirmation that the refunds have been made.

The policy rate review revealed that an inspection fee of \$75.00 was being charged on some business produced by Braishfield of Florida, Inc. without the knowledge of Company. An advisory was issued requesting that the Company review all business produced by Braishfield of Florida, Inc., identify any insureds charged an inspection fee, and make the necessary refunds. The Company was advised to complete the process within ninety (90) days following the issuance of any Consent Order by the Florida Department of Insurance subsequent to the conclusion of this examination. Exhibit V. The Company responded that a search of Braishfield files had identified 122 incidents in which a \$75 inspection fee could have been collected from and not previously refunded to insureds. The Company shall cause the return of any such fees collected and retained by any agent to the affected insured acknowledging no prior receipt of those refunds.

IX. EXHIBITS

<u>SUBJECT</u>	<u>EXHIBIT NUMBER</u>
REVISED ANTI-FRAUD PLAN FILING	I
COMPANY PRIVACY POLICY	II
COMPANY COMPLAINT PROCEDURES & LOG	III
ADVISORY DIRECTING COMPANY TO REFUND MANAGED CARE FEES (CONSENT ORDER)	IV
COMPANY RESPONSE TO MANAGED CARE FEES ADVISORY (CONSENT ORDER)	IV-a-c
ADVISORY DIRECTING COMPANY TO REFUND INSPECTION FEES	V
COMPANY RESPONSE TO INSPECTION FEES ADVISORY	V-a