

2001 PROPERTY AND CASUALTY TARGET MARKET CONDUCT EXAMINATION

OF

**COTTON STATES MUTUAL INSURANCE COMPANY
(COTTON STATES GROUP)**

BY

THE FLORIDA DEPARTMENT OF INSURANCE



DATE FILED: 12/18/02

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INTRODUCTION

Cotton States Mutual 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 1999 through September 2001. The examination began September 30, 2001 and ended December 1, 2001. The last property and casualty market conduct examination of this insurer by the Florida Department of Insurance was concluded in December 1997.

The prior examination report included the review of private passenger automobile, commercial automobile, dwelling fire, homeowners, farmowners, businessowners, personal umbrella, and personal inland marine. Violations cited included use of unfiled uninsured motorist selection forms, incorrect application of multi-car discounts, use of unfiled declaration pages, incorrect classification codes, failure to provide anti-lock brake discounts, incorrect automobile symbols, incorrect protection classes, incorrect territory zones, failure to provide timely notices of the renewal premium, failure to attach required endorsements, failure to display the agent's name and license identification number legibly on applications, and failure to affix the fraud statement on proof of loss forms.

The purpose of the current examination was to address consumer complaints and verify compliance with Florida Statutes and Administrative Rules.

During this examination, records reviewed included private passenger automobile and homeowners policies, cancellations/nonrenewals, agent/MGA licensing, claims and consumer complaints for the period of January 1999 through September 30, 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 requested 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, \$2,223.59 was returned to Florida consumers due to overcharges of premium and underpayments of claims. An estimated additional refund of \$154,200 will be made by the Company due to the rerate of private passenger automobile policies, homeowners policies, and claims readjustments. In addition, \$380 will be remitted to the Florida Department of Insurance for appointment fees due to the use of unappointed agents and customer service representatives. See Pending Issues Section.

CERTIFICATE OF AUTHORITY – AUTHORIZED LINES

GENERAL COMMENTS

The Certificate of Authority/Renewal Invoices was 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. It also included verification that notification requirements were met for any lines of business that were discontinued.

No errors were found.

COMPANY OPERATIONS/MANAGEMENT

HISTORY/MANAGEMENT

Cotton States Mutual Insurance Company was formed in 1941, under the name of Cotton Farmers Mutual Insurance Association. The present name was adopted in 1951. The Company, along with Shield Insurance Company, forms the Cotton States Insurance Group, and operates from the home office located in Atlanta, Georgia. All operations are performed at this location. The Company is a mutual company owned by its policyholders. The corporate officers are: Mr. J. Ridley Howard, Chairman, President & CEO, Mr. Robert L. Fischer, Senior Vice President, Mr. Harry V. Scott Jr., Senior Vice President, and since the prior examination, Mr. Roger W. Fisher, Senior Vice President CFO & Treasurer.

COMPANY PROCESSES/STATISTICAL AFFILIATIONS

Computer System

The Company utilizes an IBM 9672 mainframe as the primary computer system.

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 by establishing a Special Investigation Unit.

Disaster Recovery Plan

The Company has developed a Disaster Recovery Plan for use with Florida business.

Internal Audit Procedures

The Company has not developed Internal Audit Procedures for use in reviewing Florida business, however, the claims department does maintain internal auditing functions. The Company was requested to develop an Internal Audit Procedure and provide same to the Department within 90 days of receipt of this examination report. See Pending Issues Section.

Privacy Plan

The Company has developed a Plan to meet the requirements of Emergency Rule 4ER-01.

Statistical Affiliations

The Company is a member of Insurance Services Office (ISO). In addition, the National Association of Independent Insurers (NAII) acts as the Company's official statistical agent.

Credit Reports

The Company only uses credit reports with homeowners business as an underwriting tool, however, it is not the sole underwriting factor, but is used along with other factors weighted equally. This is an area that may be revisited by the Department.

OPERATIONS/MARKETING

Marketing

There have been no changes in business practices since the last examination. There is no emphasis or de-emphasis on any particular product or line of business. The Company targets preferred personal lines risks. Business is written in all areas of the State, however, the majority of business is written in the Northern and Central regions of the State.

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

The Company utilizes a network of multi-line appointed agents to market products in the State. The majority of claims are handled by Company adjusters, and in some cases by independent adjusters. The Company does maintain a web site, www.cottonstates.com however, it is not used for active solicitation of business. Direct response is not utilized.

Lines of Business

The lines of business currently written by the Company include private passenger automobile, commercial automobile, dwelling fire, homeowners, farmowners, businessowners, commercial multi-peril, crop multi-peril, personal umbrella, and personal inland marine.

REVIEW OF POLICIES

PRIVATE PASSENGER AUTOMOBILE

Description of Product/Lines of Business

This is a monoline program for preferred risks. Credit reports are not utilized in the underwriting process, however, driving history, prior insurance, usage of vehicle, age of driver, etc., are among the underwriting criteria. If the risk does not qualify for Cotton States Mutual Insurance Company, which is the preferred market, business might qualify for Shield Insurance Company, which is the standard market. Rating tiers are not used.

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>
1999	\$15,436,737	16,313
2000	\$15,192,555	15,867
**	\$10,596,165	16,249

**As of September 30, 2001

Examination Findings

One hundred (100) policy files were examined.

Twenty-nine (29) errors were found.

Errors affecting premium resulted in sixteen (16) overcharges totaling \$977.06 and ten (10) undercharges totaling \$1,137.20. In addition, an estimated \$52,200 will be returned to insureds.

The errors are broken down as follows:

1. Thirteen (13) errors were due to failure to follow the filed rates. This constitutes a violation of Section 627.0651, Florida Statutes, and is considered a business practice of the Company. These errors were due to failure to give the filed 10% preferred transfer discount when eligible. These errors resulted in twelve (12) overcharges totaling \$868.40, which have been refunded by the Company. The remaining error did not result in an overcharge due to the policy having multiple errors resulting in a net undercharge recorded in Item 2. In addition, the Company was directed to rerate all policies in effect during the scope of this examination based on the aforementioned error. Exhibit I. Refunds will go to approximately nine hundred (900) insureds with an estimated total of \$52,200. See Pending Issues Section.
2. Eight (8) errors were due to failure to follow the filed rates. This constitutes a violation of Section 627.0651, Florida Statutes. These errors were due to the use

of incorrect territory codes. These errors resulted in seven (7) undercharges totaling \$923. The remaining error did not affect premium.

3. Three (3) errors were due to failure to follow the filed rates. This constitutes a violation of Section 627.0651, Florida Statutes. These errors were due to the use of incorrect automobile symbols on physical damage coverage. These errors resulted in three (3) overcharges totaling \$100.16, which have been refunded by the Company.
4. Two (2) errors were due to failure to follow the filed rates. This constitutes a violation of Section 627.0651, Florida Statutes. These errors were due to failure to apply appropriate safety device discounts where eligible. These errors resulted in one (1) overcharge totaling \$8.50, which has been refunded by the Company. The remaining error did not result in an overcharge due to the policy having multiple errors resulting in a net undercharge recorded in Item 2.
5. Three (3) errors were due to failure to follow the filed rates. This constitutes a violation of Section 627.0651, Florida Statutes. These errors were due to applying a non-eligible multi-car discount. These errors resulted in three (3) undercharges totaling \$214.20. This error occurred in the 1997 Examination, Page 4, Item 2. Exhibit II.

HOMEOWNERS

Description of Product/Lines of Business

This is a monoline program for preferred business. The Company uses basic homeowners HO-3, HO-4, and HO-6 forms. Credit reports are utilized as an underwriting criteria along with other criteria such as loss history, prior insurance, etc. Rating tiers are not used.

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>
1999	\$7,244,703	20,641
2000	\$7,756,797	22,374
**	\$6,579,139	24,520

**As of September 30, 2001

Examination Findings

One hundred (100) policy files were examined.

Twenty-five (25) errors were found.

Errors affecting premium resulted in eighteen (18) overcharges totaling \$547.52 and two (2) undercharges totaling \$1,534.81. In addition, an estimated \$99,000 will be returned to insureds.

The errors are broken down as follows:

1. Fourteen (14) errors were due to failure to follow the filed rates. This constitutes a violation of Section 627.062, Florida Statutes, and is considered a business practice of the company. These errors were due to failure to apply the Building Code Effectiveness Grading (BCEG) factors to eligible risks. These errors resulted in fourteen (14) overcharges totaling \$409.88, which have been refunded by the Company. In addition, the Company was directed to re-rate all policies in effect during the scope of this examination based on the aforementioned error. Exhibit III. Refunds will go to approximately three thousand (3,000) insureds with an estimated total refund of \$99,000. See Pending Issues Section.
2. Six (6) errors were due to failure to follow the filed rates. This constitutes a violation of Section 627.062, Florida Statutes. These errors were due to the use of incorrect territory codes. These errors resulted in four (4) overcharges totaling \$137.64, which have been refunded by the Company and two (2) undercharges totaling \$1,534.81.
3. Six (5) errors were due to failure to follow the filed rates. This constitutes a violation of Section 627.062, Florida Statutes. These errors were due to the use of

incorrect protection classes. These errors were in the same protection class group, which did not affect premium.

CANCELLATIONS/NONRENEWALS REVIEW

DESCRIPTION OF CANCELLATION/NONRENEWAL PROCEDURES

The Company mails cancellation/nonrenewal notices to insureds, agents, and lienholders. Unearned premium is calculated pro-rata. Unearned premium is computer-generated and the date of return to the insured is documented in the computer. A register for proof-of-mailing verification is maintained.

CANCELLATION REVIEW

Forty (40) cancelled policies were examined.

One (1) error was found.

The error did not affect premium calculations.

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 giving the insured 14 days notice of cancellation in lieu of the required 45 days notice of cancellation for a private passenger automobile policy.

NONRENEWAL REVIEW

Ten (10) nonrenewed policies were examined.

No errors were found.

COMPLAINTS/INVESTIGATION 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.

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

DOI RECEIVED COMPLAINTS/INVESTIGATIONS REFERRAL

Consumer Services Ref. Number	Consumer's Last Name	Alleged Violation	Violation Found	Corrective Action Requested
Company Received	Spencer Jr.	Questioning nonrenewal reason	None	None

COMPANY RECEIVED COMPLAINTS

Consumer Services Ref. Number	Consumer's Last Name	Alleged Violation	Violation Found	Corrective Action Requested
S0001-0013961	Hobby	Questioning pol canc	None	None
Company received	Davis	Questioning non-ren	None	None
Company received	Roman	Policy surcharge	None	None
S9899-0067493	Cox	Premium issue	None	None
Company received	Weijers	Premium issue	None	None
S9900-0005192	North	Collateral Business	None	None
S9899-0059532	Ayen	Questioning non-ren	None	None
S9899-0058089	Devine	Questioning non-ren	None	None
Company received	Desmond	Questioning pol canc	None	None
S9899-0045937	Shelton	Possible redlining	None	None
Company received	Ham	Cancellation dispute	None	None
Company received	Scully	Cancellation dispute	None	None
Company received	Geoghegan	Cancellation dispute	None	None
Company received	Schirber	Questioning pol canc	None	None
S0001-0024535	Prough	Non-renewal inquiry	None	None
Company received	Callas	Questioning pol canc	None	None
Company received	Gruver	Questioning pol canc	None	None
S9900-0064769	Henry	Questioning pol canc	None	None
Company received	Tucker	Questioning non-ren	None	None
Company received	Pippin	Questioning pol canc	None	None
Company received	Class	Questioning non-ren	None	None
S0001-0025222	Lindboe	Agent handling	None	None
S0001-0011623	Kull	Premium refund	None	None
Company received	Smith	Questioning pol canc	None	None
Company received	Flannery	Title inquiry	None	None
S9900-0019917	Bernard	Refusal to insure HO	None	None
S9900-0021884	Miller	Additional premium	None	None
S9900-0016609	Fleetwood	Questioning non-ren	None	None
S9900-0060969	Lanier	Claim inquiry	None	None
S9900-0065576	Bell	Cancellation notice	None	None
Company received	Scholden III	Claim denial	None	None
Company received	Chizanskos	Claim dispute	None	None
Company received	Wilson	Claim dispute	None	None
Company received	Calhoun	Questioning non-ren	None	None
S0001-0064665	Tompkins	Questioning non-ren	None	None
S0001-0028728	Hamrick	Questioning non-ren	None	None
Company received	Carnes	Questioning non-ren	None	None

S0001-0048206	Searles	Questioning pol canc	None	None
Company received	Ball	Questioning non-ren	None	None
Company received	Wetterer	Claim settlement	None	None
S0001-0054202	Mistry	Pemium issue	None	None
Company received	Lange	Claim handling delay	None	None
Company received	Danzy	Claim delay	None	None
Company received	Beggs	Claim dispute	None	None
S0001-0065560	Joanos	Cancellation inquiry	None	None
S0001-0069096	Raynes	Claim denial	None	None
Company received	Otley	Claim dispute	None	None
Company received	Leibow	Agent handling	None	None
S9900-0026504	Neel	Refusal to insure	None	None
S9900-0020455	Miller	Additional premium	None	None

Fifty (50) consumer received complaints were reviewed.

No errors were found.

The purpose of this examination was due to consumer complaints. The complaints reviewed were not indicative of improper business practices.

CLAIMS REVIEW

DESCRIPTION OF CLAIMS REVIEWED – NON-PPA/MEDICAL REVIEWS

The types of claims reviewed included private passenger automobile and homeowners. The types of losses included total losses, PIP, comprehensive, collision, property damage, bodily injury liability, fire, water, theft, and vandalism.

Examination Findings

Fifty (50) claims were examined. Twenty-five (25) claims were private passenger automobile and twenty-five (25) claims were homeowners.

Fifteen (15) errors were found.

Ten (10) errors resulted in underpayments totaling \$699.01 and (3) errors resulted in overpayments totaling \$101.00. In addition, an estimated \$12,000 will be returned to insureds.

The errors are broken down as follows:

1. Thirteen (13) errors were due to failure to properly adjust claims. This constitutes a violation of Section 626.877, Florida Statutes, and is considered a business practice of the Company. These errors were due to incorrect sales tax applied to private passenger automobile total losses directly caused by the incorrect application of the discretionary sales surtax to the base sales tax by county. These errors resulted in ten (10) underpayments totaling \$699.01, which have been paid by the Company, and three (3) overpayments totaling \$101. In addition, the Company was directed to readjust all private passenger automobile total losses during the scope of this examination. Exhibit IV. Refunds will go to approximately three hundred (300) insureds with an estimated total of \$12,000. See Pending Issues Section.
2. Two (2) errors were due to failure to properly forward the motor vehicle title. This constitutes a violation of Section 319.30, Florida Statutes. These errors were due to failure to forward the motor vehicle title on total losses to the Division of Highway Safety and Motor Vehicles within 72 hours upon receipt of same by the Company.

DESCRIPTION OF CLAIMS REVIEWED – PPA/MEDICAL REVIEWS

The review included a PIP claim referred to an independent medical examiner (IME) for medical review.

Examination Findings

One (1) claim was examined. One (1) claim was a PIP claim.

No errors were found.

AGENTS/MGA REVIEW/ADVERTISING/MARKETING

DESCRIPTION OF MGA ARRANGEMENTS

The Company does not utilize MGAs. The Company utilizes appointed independent agents.

Examination Findings

Forty (40) applications/policies written during the scope of examination were examined.

Eight (8) errors were found.

None of the errors affected policy fees.

The errors are broken down as follows:

1. Two (2) errors were due to failure to display the agent's name and/or license identification number on the applications. This constitutes a violation of Section 627.4085, Florida Statutes. This error occurred in the 1997 Examination, Page 22, Item 1. Exhibit V.
2. Six (6) errors were due to failure to appoint agency employees. This constitutes a violation of Section 626.733, Florida Statutes. The primary agent of agencies maintaining a premium volume in excess of \$25,000 failed to appoint all agents or customer service representatives employed. Three hundred eighty dollars (\$380) will be remitted to the Florida Department of Insurance for appointment fees due to use of unappointed agents and customer service representatives during the scope of this examination. See Pending Issues Section.

PENDING ISSUES

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

MONETARY ISSUES

1. In the Private Passenger Automobile Section, Item 1, the Company was advised on October 24, 2001 to rerate all private passenger automobile policies during the scope of this examination due to failure to give the filed 10% preferred transfer discount when eligible. Exhibit I. Per Company estimate, refunds will go to approximately nine hundred (900) insureds with an estimated total of \$52,200. The Company was directed to provide documentation of the refunds to the Florida Department of Insurance within ninety 90 days of the receipt of this examination report. Exhibit VI.
2. In the Homeowners Section, Item 1, the Company was advised on October 29, 2001 to rerate all homeowners policies during the scope of this examination due to failure to apply the Building Code Effectiveness Grading (BCEG) factors to eligible risks. Exhibit III. Per Company estimate, refunds will go to approximately three thousand (3,000) insureds with an estimated total of \$90,000. The Company was directed to provide documentation of the refunds to the Florida Department of Insurance within ninety 90 days of the receipt of this examination report. Exhibit VI.
3. In the Claims Review Section, Item 1, the Company was advised on November 1, 2001 to readjust all automobile total loss claims during the scope of this examination due to the incorrect application of discretionary sales surtax to the base sales tax. Exhibit IV. Per Company estimate, refunds will go to approximately three hundred (300) insureds with an estimated total of \$12,000. The Company was directed to provide documentation of the refunds to the Florida Department of Insurance within ninety 90 days of the receipt of this examination report. Exhibit VI.
4. In the Agent Review Section, Item 2, the Company is to remit \$380 to the Department for appointment fees due to use of unappointed agents and customer service representatives.

CORRECTIVE ACTIONS

1. Company Operations/Management – The Company should develop an internal audit program and file it with the Department.
2. Private Passenger Automobile – The Company is in violation of Section 627.0651, Florida Statutes, and must give the 10% preferred transfer discount when an insured is eligible per filed rates. The Company should review applications closely for eligibility, along with directing agents to monitor same.
3. Homeowners – The Company is in violation of Section 627.062, Florida Statutes, and must apply the Building Code Effectiveness Grading factors (BCEG) to all eligible risks per filed rates.
4. Claims Review – The Company is in violation of Section 626.877, Florida Statutes, and must correct their application of discretionary sales surtax to the

base sales tax by applying this percentage to the first \$5,000 of the loss only and not the entire amount.

5. Agency Review – The Company is in violation of Section 626.112, Florida Statutes, and must appoint those agents and customer service representatives found to be unappointed and remit \$380 in appointment fees owed to the Florida Department of Insurance.

The Company is requested to complete all corrective actions within ninety 90 days of the receipt of this examination report. Exhibit VI.

EXHIBITS

<u>SUBJECT</u>	<u>EXHIBIT NUMBER</u>
PPA RERATE WITH COMPANY RESPONSE	I
1997 MARKET CONDUCT EXAM REPORT PAGE #4	II
HOMEOWNERS RERATE WITH COMPANY RESPONSE	III
CLAIMS RERATE WITH COMPANY RESPONSE	IV
1997 MARKET CONDUCT EXAM REPORT PAGE #22	V
TIME DOCUMENTATION FOR RERATE WITH- COMPANY RESPONSE	VI