FINANCIAL SERVICES COMMISSION

FLORIDA OFFICE OF INSURANCE REGULATION
MARKET INVESTIGATIONS

TARGET MARKET CONDUCT FINAL EXAMINATION REPORT

OF

FIRST COMMERCIAL INSURANCE COMPANY

AS OF

September 3, 2004

NAIC COMPANY CODE: 10347

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PURPOSE AND SCOPE OF EXAMINATION

Under authorization of the Financial Services Commission, Florida Office of Insurance Regulation (Office), Market Investigations, pursuant to Section 624.3161, Florida Statutes, a target market conduct examination of First Commercial Insurance Company (Company) was performed by Examination Resources, LLC. The scope of this examination was January 1, 2002 through August 27, 2004. The examination began July 26, 2004 and ended September 3, 2004.

The purpose of this examination was to review the Company's practices in handling workers' compensation business from Professional Employer Organizations (PEOs), review of premiums and classifications, review of complaints and cancellations related to PEOs business, and to verify compliance with Florida Statutes and the Florida Administrative Code. The Company records were examined at its home office located at 7900 NW 155th Street, Miami Lakes, Florida.

This Final Report is based upon information from the examiner's draft report, additional research conducted by the Office, and additional information provided by the Company. The files examined were selected systematically from data files provided by the Company using Microsoft Excel's "random sample" selection process. Procedures and conduct of the examination were in accordance with the Market Conduct Examiner's Handbook produced by the National Association of Insurance Commissioners.

Error tolerance levels applied are as follows: monetary returns under $5.00 were waived; zero tolerance levels were applied to all improprieties by the Company which were in violation of Florida Statutes and Rules.

POLICY AND CERTIFICATE REVIEW

First Commercial Insurance Company is a domestic property and casualty insurer licensed to conduct business in the State of Florida. The Company provides workers' compensation insurance mainly for Professional Employer Organizations. A PEO, also referred to as an employee leasing company or staff leasing company, provides human resources and administrative services to businesses that elect to outsource functions, such as human resources support, benefits administration, payroll, and federal and state employment tax filings. Additionally, a PEO provides workers' compensation coverage for all leased employees.

Total written premiums, rounded to the nearest million, during the scope of the examination are broken down as follows:

Year	Total Written Premium	PEO Business Written Premium	Percentage of PEO Premium to Total Premium
2002	$69 million	$54 million	78%
2003	$109 million	$77 million	71%
2004*	$55 million	$42 million	76%

* as of 6/30/04

Policies and certificates of insurance are issued by the Company. The PEOs have web access to the Company server for the ability to print certificates as evidence of insurance. The PEOs cannot edit the contents of a certificate; however, it can add third party certificateholder information. Proof of coverage is forwarded by the PEOs to the Division of Workers' Compensation. The Company does not have any process in place to verify accuracy or timeliness of submissions. See "Findings" under this section.

The Company is only licensed in the State of Florida and there was no evidence of coverage provided in other states in the policies reviewed.

The Company uses AM Best underwriting classification of hazard codes to determine acceptability.

The Company requires within its acceptance criteria a history of the PEO, audited financials, client employer list with class codes, payroll history, current business plan, background checks, marketing materials, prior insurance information and loss runs. A loss forecast report is prepared by the Underwriting Manager to determine if the premium is adequate for the risk and a recommendation is made to management for acceptance or declination of the risk. If the premium is not adequate, the Company obtains a consent-to-rate (excess rates) authorization form from the insured. With the exception of large deductible policies, the Company now utilizes excess rates for all PEO business. The Company is in compliance with the ten percent (10%) limitation of policies with excess rates set forth by Section 627.171(2), Florida Statutes, as the number of policies with excess rates is less than 10%. However, the Company was not in compliance with the reporting requirements of Rule 69O-137.008, Florida Administrative Code. See "Findings" under this section.

Premium payment schedules are set on a monthly basis and all policies reviewed showed that payments by PEOs were made timely. Payroll and classification codes are submitted on a weekly basis. The experience modification factors were all documented in the files reviewed.

Financial guarantees are required for all large deductible accounts. The Company is the beneficiary of letters of credit issued on behalf of the PEOs.

Claims are handled by UniSource Administrators. Loss results are monitored by the Company on a monthly basis. Claim frequency reviews are performed by the Company on a monthly basis, and the Company advised that the PEOs and UniSource Administrators conduct quarterly reviews. Claims reporting issues are reviewed monthly by the Company, and the Company advised that the PEOs and UniSource Administrators conduct quarterly reviews.

Safety issue reviews are also performed by the Company on a monthly basis, and the Company advised that a PEOs safety team performs reviews.

Classification reviews are conducted by the Company on an annual basis as required by Section 627.192, Florida Statutes. Classification reviews are also conducted at the final audit of each policy. The Company advises that monthly reviews are being conducted by each PEO and by UniSource Administrators. However, the Company does not have any process in place to verify that the reviews are being conducted, therefore, this could not be verified.

Corrective Action: The Company should establish procedures for periodic audits of the classification reviews performed by the PEOs and UniSource Administrators to verify that they are being performed and are knowledgeable and aware of the results of the reviews. The Company should conduct an audit of each PEO and of UniSource Administrators to review the monthly classification reviews they conduct, produce a written report of findings and provide a copy of the report to the Office within (60) days of receipt of the examination report.

The Company has a risk management department that provides services to insureds on a requested basis. The Company advised that PEOs have safety professionals that work directly with client employers. However, the Company does not routinely audit the PEOs operations for verification that the PEO has a properly implemented program. See "Findings" under this section.

The review included verification of proper premiums being applied and proper risk classifications. See "Findings" under this section.

Findings

The Company issued fifty-eight (58) new and renewal policies to PEOs during the scope of the examination. These policies provided coverage to 23,964 client employers. Policies issued are broken down as follows:

Year	New Business	Renewals
2002	16	6
2003	7	10
2004*	2	17

* as of 6/30/2004

Ten policies were reviewed. These policies provided coverage to 3,753 client employers. One hundred client employers with 191 class codes were reviewed.

Twenty-one errors were found involving all 10 policies. Seven errors resulted in overcharges totaling $103,700.30, and 6 errors resulted in undercharges totaling $22,185.58. In addition, a re-rate of certain policies was requested that resulted in 9 overcharges totaling $308,797.77. The Company has refunded all overcharges or credits have been applied to the insured's account.

The errors are broken down as follows:

1. Three errors were due to failure to follow the filed rate. This constitutes a violation of Section 627.191, Florida Statutes. The Company did not apply the Terrorism Risk Insurance Act 3% rate applicable to all policies without large deductibles effective April 1, 2003. These errors resulted in undercharges totaling $15,555.58.

   Corrective Action: The Company began applying this rate on May 1, 2004. The Company should correct these errors at the next audit.

2. Three errors were due to failure to obtain a notarized signature of the insured on the application. This constitutes a violation of Rule 69O-189.003, Florida Administrative Code.
   Corrective Action: The Company should remind its agents of this requirement.

3. Three errors were due to failure to follow the filed rate. This constitutes a violation of Section 627.191, Florida Statutes. The Company calculated the premium discount incorrectly. These errors resulted in 2 overcharges totaling $18,970.04 and an undercharge of $2,215.00.

   Corrective Action: The Company has refunded both overcharges. The Company should review all PEOs policies that had been audited for verification that the premium discount was applied correctly. Twenty-three policies were re-rated and 1 policy was found with an incorrect premium discount. This error resulted in an overcharge of $3,959.80, which has been refunded to the insured.

4. Two errors were due to the use of an unfiled rate. This constitutes a violation of Section 627.091, Florida Statutes. The Company used a large deductible program without prior approval from the Office.

   Corrective Action: The large deductible program filing was approved by the Office on January 16, 2004.

5. Two errors were due to failure to follow the filed rate. This constitutes a violation of Section 627.191, Florida Statutes. These errors were due to the use of an incorrect classification code. These errors resulted in 2 overcharges totaling $621.00.

   Corrective Action: The Company advised that they would correct both errors at final audit.

6. Three errors were due to failure to follow the filed rate. This constitutes a violation of Section 627.191, Florida Statutes. These errors were due to incorrect premium calculations. There were 2 undercharges totaling $5,181.67 and an overcharge of $5,333.22.

   Corrective Action: The Company has refunded the overcharge to the insured.

7. One error was due to the use of an unfiled rate. This constitutes a violation of Section 627.091, Florida Statutes. The Company used August 2002 rates in lieu of the applicable January 2001 rates when developing the final audit premium. This error resulted in an overcharge of $73,304.50.

   Corrective Action: The Company has refunded the overcharge to the insured.

8. One error was due to the use of an unfiled rate. This constitutes a violation of Section 627.091, Florida Statutes. The Company used outdated increased limit factors. This error resulted in an overcharge of $5,471.54, which has been refunded to the insured. It was determined that the Company used outdated factors for the period from August 1,

2002 through December 31, 2002. The Company was requested to re-rate all PEOs policies issued during this period.

Corrective Action: The Company re-rated 8 policies issued during the affected period and overcharges totaling $304,837.97 have been credited or refunded to insureds.

9. One error, applicable to eight excess rated policies, was due to failure to file quarterly reports for excess rates. This constitutes a violation of Rule 69O-137.008, Florida Administrative Code. The Company advised that it was unaware of the reporting requirements. The Company was requested to file the required reports.

   Corrective Action: The Company has filed all quarterly reports beginning with the period from 2001 to present.

10. One error was due to failure to conduct routine audits of PEOs safety programs. This constitutes a violation of Section 627.0915, Florida Statutes. The Company relies on the PEOs to conduct loss control services, however, the Company does not routinely audit the PEOs operations for verification that the PEO has a properly implemented program.

    Corrective Action: To assure acceptability of the PEOs risk management services, the Company should monitor and conduct routine audits of the PEOs operations and make recommendations and issue directives, as appropriate, to assure a properly implemented program and to ensure that employers are eligible for premium discounts. The Company advised that it would begin routinely auditing each PEOs safety program. The Company should conduct an audit of each PEO to review the safety program audits they conduct, produce a written report of findings and provide a copy of the report to the Office within 60 days of receipt of the examination report.

11. One error was due to failure to conduct periodic audits of proof of coverage submissions to the Division of Workers' Compensation by the PEOs on the Company's behalf.

    Corrective Action: To assure the accuracy and timeliness of PEOs submissions to the Division of Workers' Compensation, the Company should monitor and conduct periodic audits of submissions made by the PEO on the Company's behalf. The Company advised that it would begin random audits of submissions to verify accuracy and timeliness of submissions.

COMPLAINTS REVIEW

The examination encompassed a review of all complaints received by the Company that were related to PEO business. The Company received a total of 53 complaints during the scope of the examination. One complaint was identified as a PEO related complaint.

Of the 53 complaints, 48 were Workers' Compensation related. The Company advised that it began using the services of First Commercial Claim Services, LLC, in addition to UniSource Administrators, as of October 1, 2004.

Corrective Action: The Company should submit to the Office revised procedures implemented to address claims related complaints.

Sample Findings

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

One complaint related to PEOs was reviewed.

One error related to PEOs was found.

The error is described as follows:

1. One error was due to failure to notify the certificateholder of coverage termination within 30 days. This constitutes a violation of Section 440.42, Florida Statutes. A third party certificateholder was not notified timely of the termination of coverage of a client employer. The Company relies on the insurance agency that produced the business to provide notice of terminations. Notice was sent 5 months after termination to the certificateholder. The Company does not have a mechanism in place to monitor timely and accurate notice of terminations.

   Corrective Action: Refer to Cancellation/Nonrenewal section below.

CANCELLATION/NONRENEWAL REVIEW

There were 2 policies cancelled during the scope of the examination. In addition, there were 3,353 client employer certificates terminated. Cancelled policies were reviewed to determine if cancellations were made in accordance with Florida Statutes. Certificates of insurance were reviewed to determine if proper notice of termination to the insurer was provided by the PEOs and to determine if certificateholders were notified of terminations within 30 days, as stated on the certificates of insurance.

Sample Findings

Two cancelled policies were reviewed. No errors were found.

Fifty certificates of insurance were reviewed. Fifty-three errors were found, involving 29 certificates of insurance.

The errors are broken down as follows:

1. Twenty-seven errors were due to failure to notify certificateholders of coverage termination within 30 days. This constitutes a violation of Section 440.42, Florida Statutes. The Company relies on the insurance agency that produced the business to provide termination notices. The Company does not have procedures in place to monitor compliance with timely notices.

2. Twenty-six errors were due to failure of the PEO's to timely notify the insurer of client employer terminations. This constitutes a violation of Section 627.192, Florida Statutes. This statute requires the PEOs to issue termination notices directly to the client employer within a certain timeframe. The timeframes were not being met. The Company does not have procedures in place to monitor compliance with timely notices.

   Corrective Action: The Company should establish procedures to perform periodic audits of each PEO and agency related to terminations to assure compliance with both issues. The Company sent memorandums to the PEOs regarding termination requirements. In addition, the Company advised that it would immediately begin random audits of policy and certificate termination notices to monitor compliance with timely notice requirements.

   Company Response: The Company implemented procedures for random audits of PEO's to assure compliance.

REPORT SUMMARIZATION

A sample review of 163 policy, complaint, and cancellation files was conducted for this Company. Seventy-seven errors were found. The following represents general findings, however, specific details are found in each section of the report.

Sample Files Reviewed -- 163

- 10 workers' compensation policies
- 100 certificates of insurance
- 52 cancellations
- 1 complaint file

Findings

- Policy and Certificates – 23 errors – pages 3 to 5 of the report
    - Failure to follow the filed rate by not applying the Terrorism Insurance Act premium, use of incorrect premium discount, use of incorrect classification codes and incorrect premium calculations.
    - Failure to obtain a notarized signature of the insured on the application.
    - Use of an unfiled rate by the use of incorrect set of rates and use of an unfiled deductible plan.
    - Failure to file quarterly reports for excess rates.
    - Failure to conduct periodic audits of PEOs safety programs.
    - Failure to conduct periodic audits of proof of coverage submissions to the Division of Workers' Compensation by the PEOs.
- Complaints – 1 error – page 6 of the report
    - Failure to notify certificateholder of coverage termination within 30 days.
- Cancellations – 53 errors – page 6 of the report
    - Failure to notify certificateholder of coverage termination within 30 days.

- Failure of PEOs to timely notify the insurer of client employer terminations.

Company Response

The Company will begin to provide the necessary certification and report of findings as required.

EXAMINATION FINAL REPORT

The Office hereby issues this report as the Final Report, which is based upon information from the examiner's draft report, additional research conducted by the Office, and additional information provided by the Company.