FLORIDA DEPARTMENT OF INSURANCE

TARGET MARKET CONDUCT REPORT

OF

PENN TREATY NETWORK AMERICA INSURANCE COMPANY

AS OF

June 30, 2000

DIVISION OF INSURER SERVICES
BUREAU OF LIFE AND HEALTH
INSURER SOLVENCY & MARKET CONDUCT
MARKET CONDUCT SECTION

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January 17, 2001

Honorable Tom Gallagher
Treasurer and Insurance Commissioner
State of Florida
The Capitol, Plaza Level Eleven
Tallahassee, Florida 32390-0300

Dear Commissioner Gallagher:

Pursuant to the provisions of Section 624.3161, Florida Statutes, and in accordance with the Agreement for Market Conduct Services dated May 10, 2000 a Target Market Conduct Examination has been performed on:

Penn Treaty Network America Insurance Company
3440 Lehigh Street
P. O. Box 7066
Allentown, Pennsylvania
18105-7066

The report of such examination is herein respectfully submitted.

Sincerely,

Robert D. Flege
CIE, CFE, FLMI, ALHC, ASF
Independent Contract Analyst

***Certified Insurance Examiner (CIE) Certified Fraud Examiner (CFE)**
Fellow Life Management Institute (FLMI) Associate Life & Health Claims (ALHC)
Associate in State Filings (ASF)
Past President – Insurance Regulatory Examiners Society (IRES)

INTRODUCTION

Penn Treaty Network America Insurance Company hereinafter is generally referred to as "the Company" when not otherwise qualified.

This Target Market Conduct Examination was conducted by Robert D. Flege, CIE, CFE, FLMI, ALHC, ASF, pursuant to Section 624.3161, Florida Statutes.

This Target Market Conduct Examination commenced on May 11, 2000, and concluded on August 18, 2000.

SCOPE OF EXAMINATION

This examination covers various phases of the Company's operations in the State of Florida from January 1, 1997 through June 30, 2000, and subsequent information when required.

The purpose of this Target Market Conduct Examination was to determine if the Company's practices and procedures conform to the Florida Statutes and the Florida Administrative Code.

Procedures and conduct of the examination were in accordance with the Department's Field Examination Guidelines and the Market Conduct Examiner's Handbook produced

by the National Association of Insurance Commissioners (NAIC). The handbook standards of a seven percent (7%) error factor for claim resolution procedures and a ten percent (10%) error factor for other procedures were given consideration and applied where applicable.

The examination included, but was not limited to, the following areas of the Company's operation involving accident and health insurance policies covering principally long-term skilled, intermediate and custodial nursing home care and home health care written by the Company or assumed and reinsured under Assumption Reinsurance Agreements:

Billing and Waiver of Premiums
Notices of Cancellation
Claims Handling
Complaint Handling
Form Filings

Files were examined on the basis of file content at the time of examination. Comments and recommendations were made in those areas in need of correction and improvement.

DESCRIPTION OF COMPANY

History

The Company is owned by Penn Treaty American Corporation, a publicly-traded holding company (NYSE: PTA). Penn Treaty Network American (PTNA) is the principal company within the Penn Treaty Group concentrating on underwriting, marketing and sale of individual and group accident and health products, principally covering long-term nursing home and home health care. The group is a leading writer of individual long-term care insurance in the country and is licensed to conduct business in fifty (50) states and the District of Columbia.

Through common stock offerings and issuance of convertible debt securities, as well as the company's high-quality investment portfolio, Penn Treaty Network America Insurance Company and their parent, Penn Treaty American Corporation, have raised additional capital to fund premium expansion. The Company entered into a reinsurance agreement with Cologne Life Re during 1998 to address the capital requirements for premium expansion.

CERTIFICATE OF AUTHORITY

The Company is authorized to write the following lines of business in the State of Florida, subject to compliance with all applicable laws and regulations of Florida:

Life
Group Life and Annuities
Accident and Health

The original Certificate of Authority was issued on June 7, 1954 and was re-issued under No. 98-23-3603386, January 1, 1998.

The scope of the examination included all health products. Life and Annuities were excluded.

POLICY FORM FILINGS

The Company was requested to provide a listing of all forms filed and in use in Florida as well as a listing of all forms that had been discontinued during the scope of the examination. Review by the Company determined that twenty-four (24) policy forms had been discontinued and written notice had not been provided to the Department as required by Section 627.410(6)(e)(1), Florida Statutes.

The Company was advised to provide a sample of all health policies in use during the time frame of the examination period. A review of these policies determined that four (4)

forms, approved by the Department, contained prohibited language. Company executives agreed that this language should not have been included in the filed forms and that it was prohibited in Florida. Consequently, the Company had in use an approved non-complying form.

These forms contained the following clause,

"**Cancellation:** We cannot cancel this Policy at any time. Once this Policy's thirty (30) day examination period has expired, you may only cancel this Policy on its renewal date ... If you request We cancel this policy, the termination of this policy will take effect on the first renewal date following Our receipt of Your request." The effect of this wording is that all premium becomes fully earned one day following the free look period which is contrary to the provisions of Section 627.6043(2), Florida Statutes."

CLAIM PROCEDURES

The Company provided a Claims Processing Protocol directive which outlines time frames for supplying claim forms, claims acknowledgment, payment or denial of claims, delay notifications, additional delay letters, responding to written inquiries, responding to telephone calls and final disposition of a claim.

The Company stated that these time frames were “guidelines” and were not necessarily being followed.

The Company does not appear to have an internal audit program to assure compliance with statutes and standards in the handling of claims.

DENIED CLAIMS

A random sample of fifty (50) denied claims files, from a population of one thousand sixty (1,060), were selected for review.

In the review of denied claims the company has agreed to violations in four (4) instances involving failure to promptly pay or deny claims and failure to notify an insured that the claim is being contested within forty-five (45) days as required by Section 627.613(2), Florida Statutes.

This would indicate an error factor of eight percent (8%) which is above the acceptable ratio set forth by the National Association of Insurance Commissioners (NAIC).

PAID CLAIMS

A random sample of fifty (50) paid claims files, from a population of four thousand eight hundred and four (4,804) Home Health Care, Long Term Care, Cancer and Hospital Indemnity claims, were selected for review.

The following data was for claims paid from January 1, 1997 through June 30, 2000.

The following data represents the number of days between the date that complete Proof of Loss was received and payment was made.

Calendar Days	Number of Claims	Percentage
0 – 30	46	92
30 – 60	3	6
Over 60	1	2
TOTALS	50	100%

In the review of these fifty (50) files the following violations were documented:

1. Six (6) violations of Section 627.613(6), Florida Statutes. The Company failed to include interest in the payment of overdue claims. In each instance, the Company was instructed to forward a check to the insured and/or provider in payment of the required interest. These checks totaled ninety-four dollars and forty-three cents ($94.43)

2. One (1) violation of Section 626.9541(1)(i)(3)(b), Florida Statutes. A company claims representative misrepresented insurance policy provisions relating to coverage. The insured was advised that an elimination period applied to their claim when in fact the policy required payment at 80% for non-case managed claims.
3. Four (4) violations of Section 626.9541(1)(i)(3)(a), Florida Statutes. The Company failed to adopt and implement standards for the proper investigation of claims. The Company failed to comply with the time frames set forth in their claim procedures.
4. Four (4) violations of Section 626.9541(1)(i)(3)(c), Florida Statutes. The Company failed to acknowledge and act promptly upon communications. The Company failed to acknowledge and process claim payments in a timely manner once Proof of Loss was received.
5. One (1) violation of Section 627.613(1), Florida Statutes. Benefits were not paid within thirty (30) days after Proof of Loss was received. This is within the acceptable error ratio as established by the NAIC.

POLICIES CANCELLED

The Company advised that they had not cancelled any policies mid-term during the time frame of the examination inasmuch as their policies do not provide a right to cancel. They did rescind five (5) policies that involved misrepresentation of material facts on an application.

COMPLAINT PROCEDURES

The Company has Complaint Procedures in place. The Company maintains Complaint Logs for both complaints received from the Department of Insurance and from consumers. The following time study indicates compliance with adopted procedures.

Calendar Days	Number of Complaints	Percentage
0 – 30	25	100
30 – 60	0	0
Over 60	0	0
TOTALS	25	100%

In reviewing these twenty-five (25) files the following violations were documented:

1. One (1) violation of Section 627.613(6), Florida Statutes. The Company failed to include interest in the payment of an overdue claim. The Company has been instructed to forward a check in the amount of one thousand seven hundred ninety-one dollars and ninety-five cents ($1,791.95) to the insured which represents interest due on a claim in the amount of $39,955 which was unreasonably delayed from May 1999 to October 1999. This is within the acceptable error ratio as established by the NAIC.
2. One (1) violation of Section 626.9541(1)(o)(2), Florida Statutes. Company agent, Lenny Zanello, Sr., knowingly collected a premium that was less than the premium filed and approved by the Department. The agent was terminated by the Company effective June 16, 1999.

BILLING PROCEDURES

The Company provided premium billing notices utilized in monthly, quarterly, semi-annual and annual billing of policies. They advised that the only notice relative to cancellation for non-payment of premium is the "Lapse Notice" to which they attach an Application for Reinstatement. The "Lapse Notice" does not contain language sufficient to comply with Section 627.6043(1), Florida Statutes, inasmuch as it does not specifically provide the reason as required. The Company's practice is to send a "Late Notice" issued fifteen (15) days after the current due date which would be fifteen (15) days prior to the lapse date. This would comply with the requirement that at least ten (10) days written notice be given, however, the "Late Notice" does not provide specific language to the effect that the policy would be cancelled as of a certain date for non-payment of premium.

REFUND UNEARNED PREMIUM

Section 627.6043(2), Florida Statutes provides, "In the event of cancellation, the insurer will return promptly the unearned portion of any premium paid."

The Company executed a Consent Agreement for Final Order in Case No. 93-6223, dated December 13, 1995. This order provided in part, "...Penn Treaty shall henceforth make

refunds to their customers consistent with the statutory requirements of Section 627.6043, Florida Statutes, ..."

It has been determined in the course of this examination that the Company has failed to comply with the provisions of the above statute and the referenced Consent Agreement for Final Order.

The Company, for at least a period of three (3) years beginning in May 1997 to May 2000, routinely forwarded to insureds that had requested cancellation of their policy a form letter that read in part, *"Your policies do provide a right to cancel. It is not, however, the practice of our company to refund other than when the request for cancellation is made during the free look period, as stated on the front page of your policies. Your request is past the free look period and we must decline it."*

In other instances, the Company failed to refund the unearned premium upon request for cancellation and did not forward the above referenced form letter.

In response to a request for all policies that were cancelled and did not include a refund for unearned premium, the Company provided a listing of nine hundred thirty-one (931) policies.

The Company provided a listing of one thousand five hundred sixty-one (1,561) policies that were allowed to lapse at the expiration of the grace period. Further review indicated that some policies were incorrectly listed.

The Company is currently in the process of reviewing the two thousand four hundred ninety-two (2,492) policies involved to determine the appropriate amount of unearned premium and the amount of refund due to policyholders.

The Company has advised that this review will not be completed until September 7, 2000 and checks for any premium refunds would not be mailed until September 20, 2000.

The Company was advised that it would be reasonable to include interest at the rate of eight percent (8%) per annum in the refunds. They provided the Department with a copy of each check issued as well as the letter of explanation forwarded to the insured.

The Company sent the Department documentation dated September 7, 11, and 13, 2000. Total Consumer Recoveries equaled $37,477.34. The amount is distributed as follows:

Refunddue	$33,244.81
Interest due	$ 4,232.53
TOTAL	$37,477.34

CONSUMER RECOVERY

As a result of this Target Market Conduct Examination payments have been made, to date, to residents of the State of Florida in the amount of; two hundred twenty-four dollars and twenty-eight cents ($224.28) refunded due to a return of unearned premium and one thousand eight hundred seventy-six dollars and thirty-eight cents ($1,876.38) in interest not included in overdue claim payments.

The total amount of unearned premium and interest to be refunded to upon completion of the Company's review of the two thousand four hundred ninety-two (2,492) policies was thirty seven thousand four hundred seventy seven dollars and thirty four cents ($37,477.34). The total recovery is an amount of thirty nine thousand five hundred seventy eight dollars ($39,578.00).

"ALLRISK HEALTHCARE"

Penn Treaty Network America Insurance Company markets memberships in a plan that provides access to discounts and various Senior Healthcare Services such as;

Prescriptions,
Mail Order Prescription Programs,
Vision and Eyework Network,
Chiropractic Network,
Dental Network,
Medical Equipment,
and,
Podiatry, etc.

Titled, "AllRisk Healthcare" these plans are marketed through their licensed and appointed insurance agents, who are paid commissions, and are primarily targeted for;

- Uninsurables never submitted for long term care insurance due to poor health or age, and
- Long term care prospects that cannot afford long term care.

The company acknowledged these memberships are available and are sold to persons who may have coverage for benefits under Home Health Care, Long Term Care, Assisted Living policies and are covered under Medicare.

The annual fee for a Member in a Household, including their spouse, is $1,042 for persons up to age 65 and $2,242 for age 81+.

There are no discounts or coordination of benefits for persons who have coverage for benefits under various insurance plans.

The Company reports that 248 memberships have been sold in Florida, since February 1, 2000, generating a sales volume of $288,446. There have been 130 memberships sold in eight (8) other states; AZ, IL, KY, MI, OH, OR, PA and TX.

Fifty-five (55) of these persons were also covered by Penn Treaty insurance policies providing various benefits.

Brochures state, “PENN TREATY NETWORK AMERICA INSURANCE COMPANY”, immediately followed by (In much smaller but bold type) “**This is not an insurance plan**” as well as asserting,

> *“Penn Treaty Long Term Care policies are considered some of the best in the industry. In 1998, their comprehensive Long Term Care Policy (PF2600) was selected #1, out of more than 100 other company’s policies, by a leading consumer magazine. Penn Treaty is expanding its business into non-insurance products through offering AllRisk Healthcare....”*

This constitutes a violation of Section 626.9541(1)(b)(4), Florida Statutes, because these statements are deceptive and misleading. This product is clearly unrelated to their long-term care product and uses terminology which is generally associated with insurance products.

This product was not filed for informational purposes with the Pennsylvania Department of Insurance or with any other Department of Insurance.

The Company reports that expenses from the sale, marketing, administration and development of the "AllRisk Healthcare" product were kept separate from their "insurance" products. The Company advised, "All revenue and expense related to the AllRisk non-insurance product are recorded separately on our general ledger. Revenue from annual fees is recorded as other income. Commissions to agents are maintained separately, but are reported as commission expense. Printing costs, our main expense, and any other related-costs are maintained separately and are reported as general and administrative expenses."

This response does not provide in sufficient detail an accounting for executive salaries, development expenses, various handling charges, marketing expenses, etc., which could be charged to their "insurance" products and therefore reflected in their premium projections and calculations. Failure to account for these additional expenses could result in premium increases for "regulated" insurance products.

UNFAIR INSURANCE TRADE PRACTICES

During the course of this examination, the examiner reviewed a file involving policies in-force and cancelled for John and Mary Welty, Dunedin, Florida.

From 1989 to 2000 the Company processed twenty-two (22) applications for Long Term Care, Home Health Care, Medicare Supplement and Life Insurance. Eleven (11) of the policies were cancelled and refunds made prior to the effective date of the policy. Five (5) of the six (6) policies which were in force as of August 21, 1997 were still in force as of August 15, 2000.

In July of 1997, Penn Treaty agents advised Mary L. Welty that she did not need a Penn Treaty Life Insurance Policy, No. 195357, and that she should cancel the policy and utilize the Cash Value of the policy to pay premiums to be incurred on policies being written at that time.

The following agents were involved:

1. Gordon Bachmann, Fl. License No. A010910, was an agent for Penn Treaty from May 17, 1993 to July 2, 1999. He has been licensed by Florida since February 15, 1993 and as of June 14, 2000 held appointments from twenty (20) companies.

2. Agent Scott Mednick, Fl. License No. A175443, was an agent for Penn Treaty from February 10, 1995 to July 21, 1999. He has been licensed by Florida since April 27, 1992 and as of June 14, 2000 held appointments from forty-three (43) companies.

This activity represents a violation of Section 626.9521(1), Florida Statutes, which prohibits unfair or deceptive acts or practices involving the business of insurance and Section 626.9541(1)(a)(1), Florida Statutes, involving an Unfair Insurance Trade Practice.

The Company agreed with this assertion relative to the aforementioned agents, however, the Company did not terminate these agents for cause.

The Company is directed to audit the policies written by the aforementioned agents to determine any unfair and deceptive marketing practices.

The Company is directed to implement a protocol for detecting and monitoring replacement activities to insure a demonstrable benefit to the policyholder.

CONCLUSION

The customary practices and procedures promulgated by the National Association of Insurance Commissioners (NAIC) were followed in performing this Target Market Conduct Examination of Penn Treaty Network America Insurance Company as of June 30, 2000, with due regard to the Insurance Laws of the State of Florida.

Respectfully submitted,

Robert D. Flege
CIE, CFE, FLMI, ALHC, ASF
Independent Contract Analyst

FINDINGS AND RECOMMENDATIONS

The following findings were made in the preceding pages of this report. The Company is directed to:

Page 7 Comply with Section 627.410(6)(e)(1), Florida Statutes, by providing notice to the DOI in writing of its decision to discontinue the availability of a policy form or certificate within thirty (30) days.

Page 8 The Company is directed to file revisions in the following forms to comply with Section 627.6043(2), Florida Statutes, to eliminate wording relative to cancellation which reads, "Once this Policy's thirty (30) day examination period has expired, you may only cancel this Policy on its renewal date ... If you request we cancel this policy, the termination of this policy will take effect on the first renewal date following our receipt of your request":

1. Personal Freedom II, PF2600-2(FL)
2. Assisted Living Plus, ALP(FL)-P
3. Assisted Living Plus, ALP(FL)-TQ-P
4. Independent Living IV, IL-4-TQ-P(FL)

The Company is directed to issue an endorsement to each policy in effect advising that this wording is not applicable and provide the Department with a listing of the policies involved and the date that the endorsement was issued.

Page 9	Comply with Section 627.613(2), Florida Statutes. Adopt and implement standards to assure that an insured is notified that their claim is being contested within forty-five (45) days following receipt of the claim.
Page 11	Comply with Section 627.613(6), Florida Statutes. Establish claim handling procedures to assure that interest is paid on all overdue claim payments.
Page 12	Comply with Section 626.9541(1)(i)(3)(b), Florida Statutes. Adopt and implement standards to assure that insurance policy provisions are not misrepresented.
Page 12	Comply with Section 626.9541(1)(i)(3)(a), Florida Statutes. Implement standards for the proper investigation of claims.
Page 12	Comply with Section 626.9541(1)(i)(3)(c), Florida Statutes. Adopt and implement standards to assure that communications with respect to claims are acknowledged and acted upon promptly.
Page 13	Comply with Section 626.9541(1)(o)(2), Florida Statutes. Adopt and implement standards and provide adequate agency training to assure that premiums disclosed to prospective policyholders are in accordance with premiums filed and approved.
Page 14	Comply with Section 627.6043(1), Florida Statutes. Provide required notice and reason of cancellation when policies are cancelled/lapsed for nonpayment of premium.

Page 16	The Company is directed to complete the review of the two thousand four hundred ninety two (2,492) policies to determine the appropriate amount of unearned premium to be refunded to policyholders in accordance with Section 627.6043(2), Florida Statutes Forward checks to those policyholders, including interest at the rate of eight percent (8%) per annum, and provide the Department of Insurance with copies of the checks and letter of explanation sent to each policyholder.
Page 19	Comply with Section 626.9541(1)(b)(4), Florida Statutes. Discontinue use of statements that are deceptive and misleading in the sale and marketing of “All Risk Healthcare” a non-insurance product.
Page 21	The Company is directed to implement a protocol for detecting and monitoring replacement activities to insure a demonstrable benefit to the policyholder.
Page 21	Comply with Section 626.9541(1)(a)(1), Florida Statutes, which prohibits a practice known as “misrepresentation”.
Page 21	The Company is directed to audit the policies written by the aforementioned agents to determine any unfair and deceptive marketing practices.