

**FLORIDA DEPARTMENT
OF
FINANCIAL SERVICES**

**OFFICE OF INSURANCE REGULATION
BUREAU OF MARKET CONDUCT**

TARGET MARKET CONDUCT EXAMINATION REPORT

**OF
U.S. SECURITY INSURANCE COMPANY**

AS OF

SEPTEMBER 3, 2003

**NAIC COMPANY CODE: 21300
NAIC GROUP: KINGSWAY FINANCIAL SERVICES, INC.,**

EXAMINER:

WILLIAM A. DOW, III, AIE, FLMI

FILED DATE: 6/4/04



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PURPOSE AND SCOPE OF EXAMINATION

Under authorization of the Florida Department of Financial Services, Office of Insurance Regulation, Bureau of Market Conduct, pursuant to Section 624.3161, Florida Statutes, a property and casualty target market conduct examination of U.S. Security Insurance Company (Company) was performed by William A. Dow, III, AIE, FLMI, an independent contractor. The scope of this examination was January 1, 2002 through August 29, 2003. The examination began May 11, 2003 and ended September 3, 2003. The last property and casualty market conduct examination of this insurer by the Florida Office of Insurance Regulation (OIR) was concluded February 23, 2001.

The purpose of this examination was to review the issues leading to the high volume of consumer complaints received by the Florida Department of Financial Services, to analyze open and closed claims with regard to claims handling procedures and to verify the Company's compliance with Florida Statutes and Rules. From a review of the consumer complaints filed against the Company, the OIR focused on claims delays, untimely return of unearned premium due to cancellation and rating issues.

In reviewing materials for this report, the examiner relied primarily on records maintained by the Company. The examination included, but was not limited to, a review of company operations/management, private passenger automobile policies, cancellations/non-renewals, claims, consumer complaints and complaint handling. The files examined were selected systematically from data files provided by the Company using Microsoft Excel's "random number" selection process. Some audits normally done using sampling techniques were performed instead by the use of electronic means for sorting, filtering and calculating the total population of review areas during the scope of the examination. The examination report is a report by exception. As a result, files or material reviewed containing no improprieties by the Company have been omitted from the examination report. 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.

COMPANY OPERATIONS/MANAGEMENT

U. S. Security Insurance Company (Company) is a domestic property and casualty insurer licensed to conduct business in the State of Florida. The Certificate of Authority and Renewal Invoices were reviewed for all years within the scope of this examination. The review included a verification of the lines of business the Company was authorized to write versus the lines actually written.

The Company was originally incorporated in the State of Florida in December of 1985 and is corporately-owned by Hamilton Risk Management Company. In January of 1999, Hamilton Risk Management Company was purchased by Kingsway Financial Services, Inc.

The Company's home office is located at 3915 Biscayne Boulevard, Miami, Florida. The Company previously maintained a branch office located at 222 South Westmont Drive, Altamonte Springs, Florida, but closed that office earlier this year.

The Company is currently affiliated with APPCO Premium Finance Company, Auto Body Tech, Insurance Management Services, Inc. and Corporate Claims Services, which are all subsidiaries of Hamilton Risk Management Company.

The following is a list of the Company's corporate officers:

Roberto Espin, Jr.	Chief Executive Officer/President/Chairman of the Board
Kevin T. Walton	Executive Vice President/General Manager
Rachel Aldulaimi	Secretary/Treasurer
Alberto Naon	Vice President of Insurance Operations

There have been no substantive changes in the officers of the Company since the prior examination.

COMPANY PROCESSES/STATISTICAL AFFILIATIONS

Phone System

In February 2002, the Company contracted with Mitel Networks to install new technological equipment to provide increased capacity for handling the large volume of incoming and outgoing phone calls the Company is currently receiving.

Computer System

The Company utilizes a Windows based operating system designed by Kingsway America for the management of policy and claim information. This system also allows the Company's agents to generate "point of sale" policies and other supporting policy documentation through the Company's website.

Anti-Fraud Plan

The Company has filed a Plan with the Florida Department of Financial Services as required by Section 626.9891, Florida Statutes. The Plan does meet the requirements by establishing a Special Investigation Unit (SIU). The SIU is comprised of five (5) investigators and one (1) technical support person. An average of one hundred (100) claims per months are referred by Company adjusters to the SIU for investigation. Red flags or triggers (i.e., a vehicle reported stolen and found burned with no sign of forced entry, a vehicle found in a canal with none of the insured's belongings inside or conflicting stories regarding the facts of a loss) initiate the referrals. Only ten percent (10%) result in the suspicion of fraud. The SIU investigates all suspected fraud cases. Any case suspected of fraud is then referred to the Florida Department of Financial Services, Division of Fraud. From January 2003 through June 2003, sixty-seven (67) suspected cases of fraud have been referred by the Company to the Florida Department of Financial Services, Division of Fraud.

The Company has been involved during the past year in an "anti-fraud" campaign. From the end of December 2002 until the end of March 2003, the Company rented sixty (60) bench signs encouraging people who suspected insurance fraud to call a toll-free number shown on the sign. Approximately one hundred (100) calls have been received from this advertisement. To date, the Company has not been the insurer involved in any of the suspected cases of fraud related to this campaign. The Company has referred each call to either the Florida Division of Fraud, the National Insurance Crime Bureau or the insurance company involved depending upon the circumstances. In addition, the Company has joined a group of other insurance companies in placing video cameras in locations where several cases of fraud have been known to occur (i.e., particular canal locations).

Disaster Recovery Plan

The Company has developed a Disaster Recovery Plan for use with Florida business. The Company has contracted with Compaq, Inc., to provide new computers in the event the Company computers are destroyed or unusable due to any disaster. The Company backs up its records on a daily basis, and the backup copy is kept off-site.

Internal Audit Procedures

The Company has developed Internal Audit Procedures for use in reviewing Florida business. The Company uses an external auditor to randomly check policies and claims for accuracy, payments and reserves. The Company has various balancing procedures to identify errors in the financial statement that may be caused by system error.

Privacy Plan

The Company has developed a Plan to meet the requirements of Rule 4-128, Florida Administrative Code. The Company provides a letter to each new insured advising that it will not disclose any non-public information.

Statistical Affiliations

The National Association of Independent Insurers acts as the Company's official statistical agent for its private passenger automobile program, and Insurance Services Office acts as the Company's official statistical agent for its commercial programs.

Credit Reports

The Company does not use credit reports as an underwriting tool.

Tiering

The Company has three (3) tiers (Elite, Preferred and Standard) for the placement of its insureds for rating purposes. The qualifying factors determining tier placement are limits of bodily injury liability coverage, prior insurance with or without lapse in coverage, age of the driver(s), driving experience, proof of financial responsibility (SR-22) requirement (if any) and driving records. All risks are re-rated prior to renewal by the Company's computer rating program. If a risk qualifies for a lower premium tier, it is automatically moved to the proper tier.

TIER FACTORS (PERCENTAGE OF BASE RATES)

Coverages	Bodily Injury	Property Damage	PIP	Comprehensive	Collision
Elite	0.70	0.70	0.70	0.70	0.70
Preferred	0.80	0.80	0.80	0.80	0.80
Standard	1.00	1.00	1.00	1.00	1.00

OPERATIONS/MARKETING

Marketing

The Company writes non-standard private passenger automobile insurance coverages in the State of Florida, as well as commercial automobile, garage liability, general liability and flood insurance. The Company has written private passenger automobile insurance since its inception and became part of FEMA's Write your Own Program (flood insurance) in 1991. The Company began writing commercial automobile, garage liability and general liability insurance in 2000.

The Company experienced substantial growth as a direct result of the cessation of new and renewal business in South Florida by many non-standard personal automobile insurance companies leaving agencies with a limited number of companies in which to place business. To decrease its volume of business, the Company has reduced its agency force from a total of 492 agencies as of December 31, 2002, to 425 agencies as of May 31, 2003 (a decrease of 19%). Each of the Company's current agents has been assigned a "new policy" quota to limit production. In addition, all existing policies written through the canceled agents have been non-renewed.

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

The Company uses a captive managing general agency, Insurance Management Services, Inc., corporately-owned by Hamilton Risk Management Company, for developing new business in the State of Florida. Insurance Management Services, Inc. is licensed and appointed by the Company and appoints licensed independent agents throughout the State of Florida to market the Company's insurance products to the general public.

The Company's website can be accessed at www.hamiltonrisk.com.

The Company uses a captive adjusting company, Corporate Claims Services, Inc., for the processing of its claims. Corporate Claims Services, Inc., is corporately-owned by Hamilton Risk Management Company and uses licensed and appointed staff adjusters and appraisers as well as independent appraisers when needed.

Lines of Business

During the scope of this examination, the Company wrote the following lines of business: non-standard private passenger automobile insurance, flood insurance, commercial automobile insurance, garage liability insurance and general liability insurance.

REVIEW OF POLICIES

PRIVATE PASSENGER AUTOMOBILE

The current examination encompassed a complete review of private passenger automobile coverages including bodily injury liability, property damage liability, personal injury protection, uninsured motorist, comprehensive, collision, towing and rental reimbursement.

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>
2002	\$90,821,402	138,637
2003	\$56,557,233	82,405

The premiums and policy count for 2003 reflect only the policies written through June 30, 2003. The increase from 2002 to 2003 in both the premium and policy counts is a direct result of the cessation of new business in South Florida by a number of non-standard personal automobile insurance carriers and a Company rate increase effective May 1, 2003.

Sample Review Findings

Fifty (50) policy files were examined.

No errors were found.

CANCELLATIONS/NONRENEWALS REVIEW

DESCRIPTION OF CANCELLATION/NONRENEWAL PROCEDURES

The cancellation/nonrenewal procedures followed by the Company for its private passenger automobile insurance policies do comply with laws regarding the timely issuance of notices of cancellation/nonrenewal. The notices of cancellation/nonrenewal are mailed to the policyholder and lienholder, when applicable, and proper dates are used for calculating unearned premiums.

Sample Review Findings- Cancellation Review

One hundred (100) cancelled policies were examined.

No errors were found.

Sample Review Findings – Nonrenewal Review

Fifty (50) non-renewed policies were examined.

Eight (8) errors were found.

The errors are broken down as follows:

1. Eight (8) errors were due to failure of the Company to identify specific reasons for the non-renewal of private passenger automobile insurance policies. This constitutes a violation of Section 627.4091, Florida Statutes. The errors resulted from the use of a generic phrase on the non-renewal notices to encompass various reasons for non-renewal of policies. For example, the Company used the reason “Incomplete App/Missing Information” when the reason for non-renewal was the insured’s failure to select a different PIP option at the Company’s request. The Company also used “Incomplete App/FL Driver’s License” when the actual reason for non-renewal was a suspended driver’s license.

Sample Size	Number of Errors	Percentage to Sample
50	8	16%

Corrective Action: The Company has been requested to immediately implement changes to insure that all future notices of non-renewal identify the specific reason(s) for non-renewal. The Company disagrees with these findings. See Pending Issues Section.

COMPLAINT HANDLING

Total Population Findings

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

CLAIMS REVIEW

DESCRIPTION OF CLAIMS REVIEWED

This examination included the review of claims made under private passenger automobile insurance policies and included the following types of coverage: bodily injury and property damage liability, personal injury protection benefits, uninsured motorist, physical damage including comprehensive and collision, towing and rental.

Sample Review Findings

One hundred (100) private passenger automobile claim files were reviewed. The Company provided a list of all claim files closed during the scope of the examination. The claim files reviewed were selected systematically from this list using Microsoft Excel's "random number" selection process and included claims closed with payment and claims closed without payment.

Thirty-one (31) errors were found.

The errors are broken down as follows:

1. Twenty (20) errors were due to failure to adopt and implement standards for the proper investigation of claims. These errors constitute a violation of Section 626.9541(1)(i)(3)(a), Florida Statutes. These errors were due to failure by the Company to handle many aspects of the claims in a timely manner resulting in settlement delays.

Sample Size	Number of Errors	Percentage to Sample
100	20	20%

Corrective Action: The Company has been requested to re-evaluate all areas of its claim handling process and to implement procedures for proper investigation and timely processing of claims. The Company has responded by implementing an on-going process of reviewing and changing procedures to properly investigate and handle claims and to reduce the time to close claims.

2. Six (6) errors were due to failure to communicate timely. This constitutes a violation of Rule 4-166.024, Florida Administrative Code. These errors were due to failure of the Company to respond to claims communications within fourteen (14) days.

Sample Size	Number of Errors	Percentage to Sample
100	6	6%

Corrective Action: The Company has been requested to implement procedures for the proper investigation of claims to include, but not limited to, timely communication with regard to phone calls and written correspondence. The Company has responded by implementing a tracking system for incoming complaint calls to ensure response in a timely manner. In addition, the Company has implemented procedures for the training of new employees and on-going training of its present staff, as well as increased its supervisory staff and established random audit procedures for the purpose of reviewing claim files.

3. Four (4) errors were due to failure to disclose policy information. This constitutes a violation of Section 627.4137, Florida Statutes. These errors were due to failure of the Company to disclose policy information within thirty (30) days of receipt of a written request from the claimant for such information.

Sample Size	Number of Errors	Percentage to Sample
100	4	4%

Corrective Action: The Company has been requested to implement procedures to respond to written requests for policy information by the claimant within thirty (30) days. The Company has responded by establishing audit procedures for the purpose of reviewing claim files to ensure that all communications are responded to in a timely manner.

4. One (1) error was due to the misrepresentation of pertinent facts or insurance policy provisions relating to coverages at issue. This constitutes a violation of Section 626.9541(1)(i)(2), Florida Statutes. This error was due to a declination of coverage to the claimant by the Company's adjuster when, in fact, the policy contract provided coverage.

Sample Size	Number of Errors	Percentage to Sample
100	1	1%

Corrective Action: This error was an isolated incident. The Company has advised that the adjuster involved is no longer employed.

The following chart, provided by the Company, provides monthly itemizations for the total population of claims from January 2002 through June 2003. The Company assigns claims to adjusters on a line of coverage basis (i.e., bodily injury, property damage, personal injury protection, etc.) according to the adjuster's area of expertise.

CLAIMS TABLE

Category	Jan-02	Feb-02	Mar-02	Apr-02	May-02	Jun-02	Jul-02	Aug-02	Sep-02	Oct-02	Nov-02	Dec-02	Jan-03	Feb-03	Mar-03	Apr-03	May-03	Jun-03
Claims open beginning of month	9,874	10,748	11,592	12,579	13,048	13,824	14,004	13,645	13,524	12,924	12,729	12,435	12,535	12,164	12,259	12,150	12,364	12,399
New claims reported	2,543	2,273	2,757	3,346	3,234	2,753	2,622	2,797	2,412	2,724	2,082	2,623	2,507	2,445	2,598	3,102	3,118	3,011
Claim pmts. made	1,920	1,948	2,369	3,111	3,053	3,291	3,466	3,431	3,470	3,670	3,430	3,290	3,610	3,182	3,396	3,806	3,641	4,119
Claims closed w/o pmt	778	548	704	1,334	945	1,136	1,260	1,129	1,297	1,170	896	1,003	1,097	802	1,004	1,011	1,105	1,158
Total Claims closed	1,669	1,429	1,770	2,877	2,458	2,573	2,981	2,918	3,012	2,919	2,376	2,525	2,878	2,350	2,707	2,888	3,083	3,233
Claims pending end of the month	10,748	11,592	12,579	13,048	13,824	14,004	13,645	13,524	12,924	12,729	12,435	12,533	12,164	12,259	12,150	12,364	12,399	12,177
Total # of adjusters	23	29	31	30	32	36	39	44	47	48	49	50	52	54	51	51	58	62
Claims Complaints	47	38	81	69	81	67	70	41	46	47	36	39	51	45	61	67	109	52

During 2002, the Company's Direct Premium Written (DPW) increased due to the insolvency of one company and the discontinuance or drastic reduction in non-standard premium writings in South Florida by many other companies. This increase in DPW continued through May 2003. As a direct result of the increased DPW, the number of claims filed also escalated, and the Company's pending claims continued to increase. During this time, claims were not always handled in a timely manner, consumer claim calls were not being answered and adjusters were not responding to messages left by consumers. This resulted in a large number of consumer complaints being filed against the Company.

In order to combat the increase in DPW, the Company began reducing its agency force early in 2003. As of December 31, 2002, there were 492 agencies representing the Company, mainly in South Florida. This figure was reduced to 425 as of May 31, 2003. In addition, the Company placed production quotas on its remaining agency force to further limit production. At this time, the Company has indicated it has placed a priority on providing superior claims service and substantially reducing the number of consumer complaints. To achieve this goal, the Company has implemented the following changes:

1. The Company has developed a new training unit. An experienced senior adjuster is in charge. Seven (7) college graduates have been hired and began training July 21, 2003. It is the Company's goal to have these adjuster trainees obtain temporary licenses enabling them to start handling claims under heavy supervision within six (6) to eight (8) weeks. The Company plans to have these employees take the Florida adjuster's examination within ninety (90) days of employment. The new training unit will be maintained and used for training new adjusters as needed. In addition, it will also be used for on-going training of current claims personnel employed by the Company.
2. A Fast Trac system has been developed to handle new property damage and physical damage claims where coverage and liability are clear. In these cases, it is the Company's intent to close these claims within five (5) working days from date of report. This system has been in place since July 7, 2003.
3. On May 26, 2003, the Company hired an experienced call center manager to monitor all calls received by the Company's customer service representatives (CSR's). This monitoring process is achieved by the use of computer software which keeps track of many aspects of incoming calls including the number of calls received, the hold time on each call, the average hold time for all calls, the length of each call, the average length of all calls, the number of unanswered calls due to hang ups by the consumer and the percentage of calls answered. As of July 7, 2003, the answer rate for calls was ninety-nine percent (99%). The answer rate in the middle of May, before the call center was enhanced, was thirty-eight percent (38%). The call center manager has implemented a "flex lunch" system, which allows more CSR's to be available during standard lunch periods. The CSR's have been instructed to postpone non-call activity during peak periods of call time.
4. A "complaint call" follow-up procedure has been implemented. The call center manager monitors all complaint calls to ensure return calls are made. This procedure is accomplished with e-mails to the appropriate adjuster and, if needed, to the adjuster's supervisor. This monitoring continues until the call center manager confirms the call has been returned within a twenty-four (24) hour period.

5. The Company has created an internal claims auditor position. This person will provide an on-going analysis of the Company's claims handling procedures as reflected in the claim files and will implement changes as needed. The primary focus of the claims auditor will be on timely responses to both consumers and regulatory agencies.

Since the implementation of the above procedures, the number of complaints filed against the Company has decreased. The Company received sixty (60) complaints in June 2003 compared to one hundred twelve (112) complaints received in May 2003. The number of complaints filed in June 2003 is the lowest filed against the Company since February 2003.

CLAIMS ANALYSIS

An in depth review of the total population of claims, which was obtained from computer runs, was conducted. Both open and closed claims during the scope of the examination were reviewed to determine if the number of open claims at the end of each month was increasing. Based on the analysis of claims by month, it appears open claims at the end of each month was increasing from January 2002, through October of 2002. Starting in November of 2002, the volume of open claims leveled off and continues to remain level due to changes implemented by the Company to improve claims handling.

The in-force policy count for each month from January through June of 2003, has increased thirteen percent (13%). However, the total number of open claims at the end of each month has only increased three percent (3%) during this same time period indicating more claims processing capacity.

REPORT SUMMARIZATION

A sample review of three hundred (300) files was examined for this Company. Thirty-nine (39) errors were found. The following represents general findings; however, specific details are found in each section of the report.

Sample Files Reviewed -- 300

- Fifty (50) private passenger automobile files
- One hundred (100) cancellation files
- Fifty (50) non-renewal files
- One hundred (100) claim files

Findings

- Non-renewals – eight (8) errors – page 7 of the report
 - Failure to identify a specific reason for non-renewal
- Claims – thirty-one (31) errors – pages 9 and 10 of the report
 - Failure to adopt and implement standards for the proper investigation of claims-claims delays
 - Failure to communicate timely
 - Failure to timely disclose policy information
 - Misrepresentation of pertinent facts or insurance policy provisions

Corrective Actions

- Implement changes to insure that all future notices of non-renewal identify the specific reason(s) for such non-renewal. See Pending Issues Section.
- Re-evaluate all areas of claim handling and implement procedures for proper investigation and timely processing of claims, including timely communication with claimants.
- Implement procedures to respond to written requests for policy information by the claimant within thirty (30) days.

As a result of the findings of this examination, the Company has implemented procedures for the training of new employees and on-going training of its present staff, as well as increased its supervisory staff, established procedures to monitor responses to incoming telephone calls and established random audit procedures for the purpose of reviewing claim files. The Company has further established procedures to maintain an on-going process of reviewing and changing procedures to properly investigate and handle claims and to reduce the time to close claims.

PENDING ISSUES

The following issue was pending at the conclusion of the examination field work:

CORRECTIVE ACTION

1. Due to violations of Section 627.4091, Florida Statutes, the Company should implement changes to insure that all future notices of non-renewal identify the specific reason(s) for non-renewal.

EXAMINATION REPORT SUBMISSION

The courtesy and cooperation of the officers and employees of the Company during the examination are acknowledged.

The undersigned examiner conducted the examination and prepared the draft report.

Respectfully submitted,

William A. Dow, III, AIE, FLMI
Independent Market Conduct Examiner