



LOUISIANA DEPARTMENT OF INSURANCE

JAMES J. DONELON, COMMISSIONER

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**OCTOBER 1, 2008**

**ORDER ADOPTING REPORT OF EXAMINATION**

**AS OF NOVEMBER 30, 2007**

**OF**

**LEXINGTON INSURANCE COMPANY**

The above report was completed by an examiner of the Louisiana Department of Insurance.

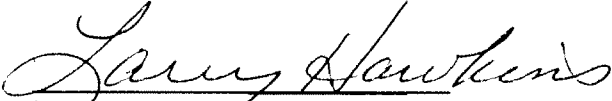
The findings and conclusions of the Department regarding the status of the Company result from consideration of the review of the report, relevant examiner workpapers and any written submissions or rebuttals of the Company.

Prior to and during the course of this examination, the position of Lexington Insurance Company ("Lexington") was that as a surplus lines insurer it was not subject to examination by the Louisiana Department of Insurance (the "Department"). Ultimately, Lexington consented to a targeted market conduct examination concerning how Lexington handled claims arising out of Hurricane Katrina and Hurricane Rita with the express reservation that such consent would not be construed as an admission by Lexington that Lexington was subject to such examination. Although the Department is of the opinion that Lexington is subject to market conduct examinations, the Department and Lexington have agreed that Lexington's consent to this examination will not be used in any future proceeding as an admission against Lexington. Accordingly, both the Department and Lexington reserve their rights concerning whether Lexington is subject to market conduct examination in the event that the Department seeks to conduct any future such examination of Lexington.

**IT IS HEREBY ORDERED** that the examination report is re-adopted by this Department and is now public record.

Should you have any questions, please do not hesitate to contact me at (225) 342-9173.

James J. Donelon  
Commissioner of Insurance  
State of Louisiana

BY:   
Larry Hawkins, MCM, Director  
Market Conduct Division  
Louisiana Insurance Department

DATED THIS FIRST DAY OF OCTOBER, 2008.

**REPORT OF EXAMINATION**  
**OF THE**  
**MARKET CONDUCT AFFAIRS**  
**OF**  
**LEXINGTON INSURANCE COMPANY**

**BOSTON, MASSACHUSETTS**

**AS OF**

**November 30, 2007**

**NAIC CODE 19437**

**NAIC ETS EXAM NO. LA071-M73**

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February 28, 2008

Honorable James J. Donelon  
Commissioner of Insurance  
P O Box 94214  
Baton Rouge, Louisiana 70804-9214

Sir:

Pursuant to statutory provisions and in compliance with your instructions, a targeted market conduct examination has been made of the affairs of

**LEXINGTON INSURANCE COMPANY**  
**100 SUMMER STREET**  
**BOSTON, MASSACHUSETTS 02110**

as of November 30, 2007 and the report of examination is herewith submitted.

## **FOREWORD**

A targeted market conduct examination was performed of the activities of Lexington Insurance Company from August 28, 2005 through November 30, 2007. The examination was performed by test and all tests applied during the examination are included in this report.

### **PURPOSE AND SCOPE OF MARKET CONDUCT EXAMINATION**

In accordance with **LRS 22:1301 et. seq.**, the market conduct examination of Lexington Insurance Company, hereinafter referred to as ("Company"), was a targeted market conduct examination authorized by the Louisiana Department of Insurance ("Department") to examine the handling of homeowner's insurance claims resulting from Hurricanes Katrina and Rita.

The purpose of this examination was to review compliance by the Company with Louisiana Insurance Laws, Regulations, Directives and the National Association of Insurance Commissioners ("NAIC") Guidelines.

The ACL Program, a data manipulation program, provided by the Department was utilized in this examination. Samplings were utilized to test the Company's records and procedures. The ACL Program was used to automatically generate a random sampling of claims records. "Random" is a theoretical concept meaning that all items in a population or file (before selection) have an equal chance of appearing in the sampling.

Generally, a random or systematic sampling size of sixty (60) records will be selected for review. A minimum confidence level of ninety-five percent (95%) with a maximum error rate of five percent (5%) will be used for all samples.

## **COMPANY OPERATIONS**

### ***Company History***

Lexington Insurance Company is a member of the American International Group, Inc. companies. Lexington was incorporated under the laws of the State of Delaware on March 31, 1965 and began business on April 1, 1965. The Company is a wholly-owned indirect subsidiary of American International Group, Inc.

Lexington is licensed to transact multiple lines of insurance in Delaware, and is an eligible surplus lines insurer in each of the remaining 49 states, the District of Columbia, Puerto Rico, and the U.S. Virgin Islands. The Company writes substantially all lines of property and casualty insurance with an emphasis on commercial business. As a surplus lines insurer, Lexington focuses on insuring those risks for which admitted or licensed insurers do not readily provide coverage, whether because of the complexity of the risk, because the unique nature of a particular risk does not lend itself to conventional insurance contracts, because the risk requires high limits of insurance that may exceed an admitted or licensed insurer's underwriting criteria, or because the risk presents characteristics or attributes that make it unacceptable to admitted or licensed insurers.

In 2005, Lexington's written premiums for Louisiana business totaled \$98.9 million. This amount increased to \$148.6 million for 2006. Lexington has had 6,907 total claims resulting from Hurricane Katrina, and an additional 473 claims resulting from Hurricane Rita. More than ninety-six percent (96%) of these claims have been closed, with total indemnification payments in excess of \$1.3 billion (includes homeowner's and commercial claims). Indemnity payments for homeowner's claims resulting from Hurricane Katrina are in excess of \$384.7

million, and are in excess of \$10.0 million for claims resulting from Hurricane Rita (through January 11, 2008).

### ***Hurricane Claims Handling***

The Company provided the following write-up detailing its handling of the hurricane claims:

“The extreme nature of Hurricanes Katrina and Rita necessitated extraordinary efforts on Lexington’s part to respond to homeowner’s claims resulting from these storms. Factors such as the sheer number of claims; the fact that as a surplus lines insurer Lexington cannot have claims employees on site in the various states in which an insured property is situated , and therefore must rely upon independent adjusters to adjust claims; the fact the offices of the principal adjustment company utilized by Lexington in New Orleans were flooded, thus requiring that entity to subcontract this work to other firms; the inability to locate or contact insureds, many of whom were forced to evacuate New Orleans; access to segments of New Orleans being denied to adjusters due to flooding; and the need to retain sufficient staff in Lexington’s Boston office to examine and process adjustment reports were some of the many challenges that Lexington faced as a result of Katrina and Rita.”

“Lexington responded to these issues by implementing measures that included the following:

1. Establishing a 24-hour call center to receive calls from insureds.
2. Opening and funding an account with Western Union on September 2, 2005 to provide ALE payments to any individual who contacted the Company and stated that he or she was a Lexington insured. Payments initially were made in the amount of \$1000; this was increased on September 10<sup>th</sup> to \$1500, and again later that month to \$2500. These payments were made without confirming whether the individual contacting the Company was a Lexington insured, and without regard to determining whether that individual’s property was damaged or whether any damage asserted was covered by a Lexington homeowner’s insurance policy. Each payee was informed by letter that the Company

would not seek reimbursement if Lexington subsequently determined that the property damage sustained was due to a non-covered peril.

3. Retaining claims adjusters on a consulting basis as examiners in the Company's Boston office to review and process adjustment reports as received. This effort commenced in advance of Hurricane Katrina making landfall. A consulting staff of 25 examiners was retained by the end of October 2005, and a staff of 55 examiners was in place by January 2006. The sole responsibility of these individuals was to administer homeowner's claims resulting from Hurricanes Katrina and Rita.
4. Anticipating the potential volume of claims and the inability of insureds to contact their agents and the Company in order to submit claims, Lexington commenced the claims process prior to actually receiving any claims by identifying the geographical areas that were impacted by Hurricane Katrina; identifying the Company's in-force insurance policies in the affected areas; setting up claims files on the basis of that information; assigning an examiner to each claims file; forwarding photocopies of policies to the independent adjustment firm retained by the Company; directing the adjustment firm to contact insureds and begin the adjustment process; and, where insureds could not be located, directing the adjustment firm to perform "drive-bys" of insured properties.
5. Establishing an arrangement in September 2005 with an accounting firm having an office situated in Baton Rouge to issue claims payments to insureds where damage assessments were less than \$25,000.
6. Implementing an arrangement with an accounting firm in Boston to process claims payments from a trust account funded by the Company.
7. Waiving proof of loss requirements up to \$100,000 for recoverable losses.
8. Waiving up to \$50,000 the depreciation provisions in Lexington's homeowner's insurance policy for both structural losses and contents losses.
9. Waiving indefinitely the 180-day requirement in Lexington's homeowner's insurance policy for release of holdbacks.

By virtue of these efforts, Lexington issued approximately \$6.4 million in homeowner's insurance claims payments within the first 60 days after Hurricane Katrina made landfall."

## CLAIMS REVIEW

The Company provided a file of all claims for Hurricanes Katrina and Rita from August 28, 2005 through November 30, 2007. The file was analyzed using ACL and the following categories and amounts were found:

<u>Type of Claim</u>	<u>No. of Payments</u>	<u>No. of Claims</u>	<u>Paid Amount</u>
Closed with Payment	46,879	6,604	\$197,078,987
Open	4,031	344	\$ 28,168,521
Closed without Payment	<u>0</u>	<u>70</u>	<u>\$ 0</u>
Total	50,910	7,018	\$225,247,508

### *Closed Claims Review*

A random sample of sixty (60) closed paid claims was selected from a listing provided by the Company for the period of August 28, 2005 through November 30, 2007. The files were reviewed to determine the time taken to pay the claims and to determine if the files contained adequate documentation. Also, the files were reviewed to determine if the adjustment of the claims was conducted in accordance with the statutes and regulations.

It was found that twelve (12) claims in the sample had no payments made within thirty (30) days after receipt of the estimate as required by the statutes. This is not in compliance with

**LRS 22:658 A.(1)** which states:

**"All insurers issuing any type of contract, other than those specified in R.S.22:656, R.S. 22:657, and Chapter 10 of Title 23 of the Louisiana Revised Statutes of 1950, shall pay the amount of any claim due any insured within thirty days after receipt of satisfactory proofs of loss from the insured or any party in interest..."**

It is recommended that the Company implement procedures to ensure that all claims are paid in accordance with the above statute.

All of the claims in this sample were paid in an average of twenty-five (25) days after receipt of proof of loss from the adjuster.

It was found that the initiation of the loss adjustment for all of the claims in the sample was started within thirty (30) days after notification of the loss as required by the statutes. The initiation of the loss adjustment of the claims in the sample was started in an average of nine (9) days after notification of the loss.

### ***Open Claims Review***

A random sample of sixty (60) open paid claims was selected from a listing provided by the Company for the period of August 28, 2005 through November 30, 2007. The files were reviewed to determine the time taken to pay the claims and to determine if the files contained adequate documentation. Also, the files were reviewed to determine if the adjustment of the claims was conducted in accordance with the statutes and regulations.

It was found that six (6) claims in the sample had no payments made within thirty (30) days after receipt of the estimate as required by the statutes. This is not in compliance with **LRS 22:658 A.(1)** which states:

**"All insurers issuing any type of contract, other than those specified in R.S.22:656, R.S. 22:657, and Chapter 10 of Title 23 of the Louisiana Revised Statutes of 1950, shall pay the amount of any claim due any insured within thirty days after receipt of satisfactory proofs of loss from the insured or any party in interest..."**

It is recommended that the Company implement procedures to ensure that all claims are paid in accordance with the above statute.

All of the claims in this sample were paid in an average of twenty (20) days after receipt of proof of loss from the adjuster.

It was found that the initiation of the loss adjustment for all of the claims in the sample was started within thirty (30) days after notification of the loss as required by the statutes. The

initiation of the loss adjustment of the claims in the sample was started in an average of eleven (11) days after notification of the loss.

It was found that fifty-two (52) of the sixty (60) open claims in the sample (87%) were in litigation at the time of the examination.

The Company issued the following response to the exceptions listed above:

“Lexington implemented appropriate measures for the timely payment of claims resulting from Hurricanes Katrina and Rita. These efforts were complicated by the unique and extraordinary circumstances arising from these catastrophes – including the substantial number of claims submitted to the Company; the fact that the offices of the principal adjustment firm utilized by Lexington were flooded; the flooding within New Orleans that prevented timely adjustment of claims; the evacuation of many of the Company’s insureds from New Orleans; and communication problems that made it difficult to communicate with insureds. Notwithstanding these challenges and problems, Lexington submits that it addressed claims in an efficient and timely manner.”

“To ensure payment of catastrophe-related claims within the thirty (30) day time period required by LRS 22:658 A(1), Lexington has partnered with two (2) national independent adjustment firms that have the capability to provide immediate resources for the investigation and adjustment of homeowner property claims, and to provide the resources needed by Lexington at its offices in Boston to process adjustment reports and effect claims payments. These entities have demonstrated to the Company’s satisfaction that they have implemented contingency plans for continued service in the event of a catastrophe should their offices be directly impacted by that situation in a manner similar to that which Lexington’s principal independent adjustment firm experienced as a result of Hurricane Katrina. The two (2) firms

have, in addition, effected “real time” reporting procedures allowing Lexington’s claims examiners internet access to adjustment reports as prepared; this will permit immediate receipt by the Company of claims information, and thus will permit efficient and expeditious claims administration. These measures were implemented by Lexington independent of the current examination: they were put in effect in 2006 as a result of the Company’s experience responding to the claims resulting from Hurricanes Katrina and Rita.”

***Denied Claims Review***

The Company provided a listing of seventy (70) claims that were either denied or closed without payment during the period of August 28, 2005 through November 30, 2007. A systematic sample of sixty (60) claims was selected from this listing. The claims were reviewed to determine the reason for denial or closure. A summary of the reasons is presented in the following table:

<b><u>Reason for Closure or Denial</u></b>	<b><u>Number of Claims</u></b>
Claim below deductible	16
Duplicate claim	11
Insured withdrew claim	10
Claim opened for anticipated loss but no claim filed	10
Not a denied claim; paid but not entered in system	4
Looting claim; insured has not responded	3
No damage	2
No coverage for wind; only for contents	1
Insured has insurance with another company	1
Company could never make contact with insured	1
All damage is from flood	<u>1</u>
Total	60

The denied claims review was completed without any exceptions.

### ***Additional Living Expense***

The Company provided the following explanation of the Additional Living Expense (ALE) payments provided to the insureds:

“ALE payments are governed by the terms of Lexington’s homeowner’s insurance policy. Appropriate proof of incurred expenses in the form of leases, rental records, and non-recoverable documents must be provided to the Company before any ALE payment will be made. Payments do not exceed the limit of liability under the policy at issue.”

“Though ALE payments typically cover the shortest period of time required to repair or replace the damaged residence, consideration under the circumstances resulting from Hurricanes Katrina and Rita was given by Lexington to delays in effecting repairs because damaged property at times was inaccessible due to flooding; many insureds were unavailable because of required property evacuations; and contractors often were unavailable due to work volume or were hindered by the lack of necessary construction materials. Accordingly, if repairs to a home that was damaged by a covered peril could not be commenced by an insured for an extended period of time by reason of any of these factors, consideration would be given for such delay and ALE payments would be provided to that insured during such period.”

### ***General Comments***

In some cases, the received date of the claim is not accurate as many claims were opened by the Company as "Anticipated Louisiana losses" and not from a claim presented by the insured or the producer. Therefore, the date in the file is a "claim create date" and not a "claim received date." The received date is used in the evaluation of the initiation of the loss adjustment. Even though this date may have been inaccurate in some cases, no exceptions were found in the evaluation of the initiation of the loss adjustment.

In some cases, the paid date is not accurate because some checks were issued in the field or outside the normal payment system and were not entered into the payment system until several days later. Although this procedure expedited the payment process, it introduced an error of a few days in the reflected payment date that was recorded in the payment system. Therefore, the date in the system was the date when the payment was entered and not the date on the check. The only dates presented to the examiner were the dates recorded in the payment system. This was taken into account when the number of exceptions was calculated.

In some cases, there was not enough information in the files to accurately determine when the adjustment of the claim actually started. These claims were not included in the above calculations.

In some cases, it was difficult to determine when the estimates had been received at the Company as these estimates were not date stamped when received and there were no notes in the file to show when the estimates were received. In these cases, the date of the estimate was used as the received date. Failure to date stamp documentation or record the date received does not allow the Department to determine whether claims payments were made within the statutory time limits. It is recommended that the Company implement procedures to date stamp the received date on all documentation relating to payment of the claims or record the receipt dates in the notes.

While the Louisiana Insurance Code is silent concerning the time elapsed from the initial inspection of the property until the time the estimate of damages is prepared and sent to the Company, it should be noted that during the examination there were indications that much time had elapsed between the date of the inspection of the property and the date the estimate was prepared by the adjuster. The average time between the inspection and estimate date was found

to be 42 days for the closed claims and 54 days for the open claims. This had no adverse effect on the timeliness of claims payments by the Company after receipt of the estimate. This is mentioned only as it could explain some customer complaints relating to delays in the conclusion of the handling of their claims.

## COMMENTS AND RECOMMENDATIONS

### CLAIMS REVIEW

It was found that twelve (12) claims in the closed claims sample were not paid within the thirty (30) day time period as required by the statutes. This is not in compliance with **LRS 22:658 A.(1)**. It is recommended that the Company implement procedures to ensure that all claims are paid in accordance with the above statute.

It was found that six (6) claims in the open claims sample were not paid within the thirty (30) day time period as required by the statutes. This is not in compliance with **LRS 22:658 A.(1)**. It is recommended that the Company implement procedures to ensure that all claims are paid in accordance with the above statute.

In some cases, it was difficult to determine when the estimates had been received at the Company as these estimates were not date stamped when received and there were no notes in the file to show when the estimates were received. It is recommended that the Company implement procedures to date stamp the received date on all documentation relating to payment of the claims or record the receipt dates in the notes.

The Company issued the following response to the exceptions listed above:

“To ensure payment of catastrophe-related claims within the thirty (30) day time period required by LRS 22:658 A(1), Lexington has partnered with two (2) national independent adjustment firms that have the capability to provide immediate resources for the investigation and adjustment of homeowner property claims, and to provide the resources needed by Lexington at its offices in Boston to process adjustment reports and effect claims payments. These entities have demonstrated to the Company’s satisfaction that they have implemented contingency plans for continued service in the event of a catastrophe should their offices be

directly impacted by that situation in a manner similar to that which Lexington's principal independent adjustment firm experienced as a result of Hurricane Katrina. The two (2) firms have, in addition, effected "real time" reporting procedures allowing Lexington's claims examiners internet access to adjustment reports as prepared; this will permit immediate receipt by the Company of claims information, and thus will permit efficient and expeditious claims administration. These measures were implemented by Lexington independent of the current examination: they were put in effect in 2006 as a result of the Company's experience responding to the claims resulting from Hurricanes Katrina and Rita."

## **CONCLUSION**

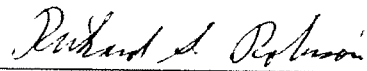
I, Richard S. Robison, do solemnly swear and affirm that I am an examiner for the Commissioner of Insurance of the State of Louisiana and that, as such, I was assigned to conduct a targeted examination of the market conduct activities of

**LEXINGTON INSURANCE COMPANY**  
**BOSTON, MASSACHUSETTS**

That I made such examination and the above and foregoing is a true and correct copy of my report of such company and the same is true and correct to the best of my knowledge, information and belief.

I would like to acknowledge the courteous cooperation of the Company's Officers and Employees.

Respectfully submitted,



**Richard S. Robison**  
**Louisiana Department of Insurance**