

REPORT OF EXAMINATION
OF THE
MARKET CONDUCT AFFAIRS
OF
PROGRESSIVE SECURITY INSURANCE COMPANY

METAIRIE, LOUISIANA

AS OF

December 31, 1999

NAIC CODE 10050

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February 15, 2001

Honorable J. Robert Wooley
Acting Commissioner of Insurance
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Sir:

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

PROGRESSIVE SECURITY INSURANCE COMPANY

METAIRIE, LOUISIANA

as of December 31, 1999 and the report of examination is herewith submitted.

FOREWORD

A market conduct examination was performed of the activities of PROGRESSIVE SECURITY INSURANCE COMPANY from January 1, 1996 through December 31, 1999.

The market conduct examination is, in general, a report by exception. This means that references in the examination report to procedures and/or files subject to review may be omitted if no improprieties or errors were noted. Unless otherwise stated, the NAIC Market Conduct Examiners' Handbook, Volume II was used as a measure of compliance.

PURPOSE AND SCOPE OF MARKET CONDUCT EXAMINATION

The market conduct examination of PROGRESSIVE SECURITY INSURANCE COMPANY, hereinafter referred to as ("Progressive") or ("Company"), was a routine market conduct examination conducted in conjunction with the financial examination with both being authorized by the Louisiana Department of Insurance.

The examination included, but was not limited to, the following areas of the Company's operation:

- Company Overview,
- Complaint and Grievance Review,
- Producer Review,
- Marketing and Sales Review,
- Underwriting and Rating Review and
- Claims Review.

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 NAIC Guidelines set the standards of conduct for a property and casualty insurer and promote a program of fair treatment of policyholders.

COMPANY OVERVIEW

Company History

The Company was organized and the Articles of Incorporation were recorded on May 11, 1994 and commenced business on December 27, 1994. The purpose of the corporation is to engage in the business of writing property and casualty insurance, inland marine and such other types or lines of insurance permitted by the laws of the State of Louisiana.

Territory and Plan of Operations

The Company is licensed to transact vehicle, liability and inland marine insurance in the State of Louisiana. Marketing is conducted through an independent agency system. During the period under examination the daily operations of the Company were performed in various states.

Although the Company contracts with independent agents throughout Louisiana, 800 numbers are available to assist the consumer to purchase automobile, boat, motorcycle and recreational vehicle coverage. The 800 callers are first directed to Tempe, Arizona with backup locations in Austin, Texas and Cleveland, Ohio. Non-resident Louisiana agents will assist the caller with selecting the appropriate coverage. Also, Louisiana consumers have Internet access to purchase auto coverage.

Underwriting of new policies, policy renewals and cancellations are performed in Tampa, Florida while customary service for policy changes and/or questions is directed to Austin, Texas. The Company maintains ten claim offices located throughout the state

of Louisiana. The Progressive Corporation, the Company's parent located in Ohio, handles the Company's investments.

Antifraud Policy

The Company responded that it employs four individuals with extensive law enforcement experience whose role is to investigate and pursue claims that indicate evidence of fraud. In addition, these special investigators provide extensive training to the Company's claim personnel on the aspects of detecting potentially fraudulent claims.

The Company did not provided any written antifraud procedures or guidelines that would enable employees to perform their daily functions in accordance with the goals and direction of management.

Certificate of Authority

The Company's Certificate of Authority was issued with an effective date of December 20, 1994 and authorized the Company to transact property and casualty insurance in the State of Louisiana.

Comments and Recommendations from Previous Reports

There were no recommendations relating to the Company's market conduct activities in the previous financial examination report as of December 31, 1995.

Affiliated Companies

The Company is wholly owned and controlled by The Progressive Corporation, an Ohio corporation. The Company is a member of a very large holding company system

that includes over 80 companies. The complete organizational chart is shown in detail in the Company's annual statement.

COMPLAINT REVIEW

This review was conducted in accordance with the provisions of Louisiana Revised Statute 22:1214(17) which states as follows:

"Failure to maintain adequate complaint handling procedures. Failure of any insurer to maintain a complete record of all the complaints that it received since the date of its last examination. This record shall indicate the total number of complaints, their classification by line of insurance, the nature of each complaint, the disposition of each complaint, and the time it took to process each complaint. For purposes of this Paragraph, "complaint" shall mean any written communication primarily expressing a grievance received by the insurer from the Department of Insurance."

A sample of 50 complaints filed with the Department between 1997 and 1999 were reviewed and generally consisted of complaints due to the insured's misunderstanding of the policy provisions, delays in handling insured's requests, delays in claim payments or dissatisfaction with the insurer's claims practices.

The Company's complaint register was reviewed and compared to the Department's listing of complaints. The Company used a Lotus Notes database to maintain its complaint register. The Company's register did not contain 12 complaints from 1998 and 1999. Also, the Company did not have complaint files for five of the 50 complaints files sampled. The Company was advised of the missing complaint files not contained in its complaint register. No complaint trends or patterns were detected during the review.

PRODUCER REVIEW

The Company's agent listing as of December 31, 1999 contained approximately 1,800 active agent appointments. A sample of 50 of the Company's appointed agents was compared to the Department's list to determine if the agents have been properly appointed. No discrepancies were found.

Although the Company indicated that background checks were instituted in 2000, the Company had no formal procedure for the investigation of its agent recruits during the period under examination. The Company was reminded of the DOI's Bulletin #99-01 dated June 1, 1999 referencing "Consent for Prohibited Person to engage in Insurance Business". This Bulletin was a notification to all persons and entities engaged in or contemplating being engaged in the business of insurance in this state, that the Louisiana Department of Insurance has enacted guidelines and requirements for granting written consent to engage in the business of insurance for individuals who are considered "prohibited persons" under The Violent Crime Control and Law Enforcement Act of 1994, Title 18 U.S. Code, Sections 1033 and 1034. The Company's President stated that investigation of agents was now in compliance with the Department's guidelines and requirements.

A sample of 50 agent files was selected for review in order to determine the type of documentation in files. The files did not contain a copy of the agent's Louisiana license. The Company has a large number of non-resident agents in Louisiana. Most of these agents reside in Arizona, Florida and Ohio and according to their files had numerous non-resident licenses with other states. These agents are responsible for quoting and selling insurance products through the Company's direct call centers.

The Company has a website for agents titled ForAgentsOnly.com. The Company indicated that this website will be a future site for agent commission statements and related documentation. The Company stated this website was controlled by passwords assigned by the agents, and consequently, could not be reviewed by the examiners.

The Company was asked to provide commissions statements for a sampling of 50 agents. The Company could only provide a statement of commissions paid to each agency and not to each agent at the agency. A review of these commission statements revealed that different commissions were paid to different groups of agents during the examination period.

In the last quarter of 1997 the Company offered an exclusive contract to its agency force that offered an additional 2% in commissions while the contract was in force. Although the contract required the agent to quote only Progressive insurance rates on new business, the agent was permitted to maintain existing contracts with other auto carriers. The Vanguard Program later replaced this program.

In January and February 1998 the Company offered an additional 2 percent commissions to *all* agents. The Company explained this offer was made to stimulate new business sales. However, the Company could not provide any copies of emails or bulletins provided to the agency force introducing this bonus commission offer.

The Company offered a Vanguard Program in May 1998 whereby agents could qualify by producing a certain amount of new business each month and by maintaining at least a 70% violation disclosure on applicants. The agents who qualified were allowed to choose their commission rates: either 12% for new business and 10% for renewals, or 10% for new business and 8% for renewals.

Those agents who chose the 12%/10% commission rates offered the same standard premium rates to applicants as offered by all non-Vanguard agents (remaining agents not under the Vanguard Program). The only difference was that the Vanguard Agent was paid a higher commission than the non-Vanguard agent.

Those Vanguard Agents who chose the 10%/8% commission rates received the same commission rate as the non-Vanguard agent but was able to market a discounted premium referred to as *Supersaver Premium Rates*. These rates provided applicants a 2% premium discount if rated in the middle and standard markets, and a 6% premium discount if rated in the preferred and ultra-preferred markets.

Once an agent selected a Vanguard commission rate schedule, he or she must market the same premium rates associated with that commission rate schedule to all applicants. An agent cannot market a *Supersaver Premium Rate* to one applicant and the standard premium rates to another applicant.

MARKETING AND SALES REVIEW

The Company advertises through radio, television and the telephone book. The main theme of these advertisements is to inform a prospective customer of the Company rates plus a comparison of rates from up to three other insurers. This is available through a toll free number or on the Company's website. These figures are derived from a premium study of other insurers conducted by the Company. Other advertisements suggest potential savings by requesting a rate quote from the Company.

The Company's Internet website, *Progressive.Com*, provides information about the Company, allows a prospective customer to find an agent's business location, to ~~obtain a quote for auto coverage and to submit an application online.~~

UNDERWRITING AND RATING REVIEW

The agents submit all applications electronically. The Company does not accept paper applications. The original copy of the application is maintained at the agent's office and the agent is to provide a copy of the application to the applicant. In addition, the applicant can apply for all types of coverage via a toll free number and for auto coverage through the Company's website, *Progressive.com*. After completion of the phone application, the Company mails the application to the applicant for review and signature.

A random sampling of 48 new business cases for automobile coverage was selected from the 5th and 15th issue day of each month for the years 1997, 1998 and 1999. This review revealed that the underwriting department received new applications and generated new policies for mailing in approximately a 19-day turnaround time.

A review of the applications from this new business sampling revealed that ten of the applications (approximately 20%) were not signed by the applicants: seven of these applications were on policies issued directly by the Company and the remaining three were on policies issued by agents. Four applications from the sampling (approximately 8%) were not provided: the agents could not find three of the applications and the Company was unable to provide the remaining one.

Because of the electronic processing of applications, the agent is expected to provide a copy of the paper application to the applicant and keep the original at his or her office. As noted earlier, the agents did not provide three of the applications from this new business review. Also, it does not appear the Company performs any meaningful audits to evaluate the agents' record keeping procedures.

When asked, the Company acknowledged it does not attempt to retrieve applications that customers do not mail back for policies sold directly by phone via the Progressive Call Centers. The Company does not consider this cost effective to pursue these applications. However, if the Uninsured Motorist (UM) Rejection Form is not received, the Company sends a follow-up request to the applicant. If the applicant does not respond, U M Coverage is added with limits matching the bodily injury coverage.

A sample of ten policies was selected from the original new business sampling. A comparison was made of the rates utilized by the Company against the rates filed with the Louisiana Rating Commission. Because the Company does not use rate manuals, the examiners were unable to include this item in this review. Therefore, the examiners relied on the declaration page for the policy premium and a computer printout of rate calculations provided by the Company illustrating how the premiums were calculated. Premiums charged to sampled policies were verified to the Company's rate filings without exception.

Base premium rates are determined for each market tier. The market tier is determined by three factors: financial responsibility rating (credit reports), the limits of prior bodily injury liability insurance coverage and any prior lapse in insurance coverage.

A small sampling of applications from the original new business sampling was selected to verify that the writing agent was properly licensed and appointed. One agent was found to be unlicensed and not appointed during the period in which he wrote one of the sampled applications.

Upon further review, it was found that this agent wrote 44 policies during the five-month period in 1999 in which he was unlicensed and not appointed. The Department was notified of this finding.

A judgmental sampling of 96 cases of policy cancellations and non-renewals of automobile coverage was selected from copies of notices provided by the Company. The reasons for cancellation and non-renewal were reviewed in order to verify that these practices were not unfairly discriminatory. No exceptions were detected.

The quoting process for automobile coverage of the Company's Internet site was reviewed and quotes were obtained for various customer profiles as determined by the examiners, and in some cases, comparison rates from other companies were provided. It was noted that the system ranks applicants based on a financial responsibility score that is obtained from a credit vendor. There is a programming error that prevents the offering of comparison quotes when a "no match" condition occurs on the applicant credit history. The Company stated this error was corrected during the course of the examination.

The Company's Internet site is designed for a user to input personal information such as name, address, social security number, birth date, and prior insurance history. All of this information is necessary to obtain the *lowest quote* for auto coverage. The examiners were hampered by such personal requirements and as regulators were not able to accurately check the rates since entering only basic test data would generate inaccurate quotes.

Progressive uses a secure server implementing the Secure Sockets Layer protocol to interact with the user when personal information is provided during the purchase or payment process. The server encrypts information so a third party cannot read the data

while in transit. The Company's website, *Progressive.com*, has been secured with a digital certificate by RSA Data Security/Secure Server CA that transmits via 128-bit encryption.

A review of policy forms currently used by the Company revealed that all had been filed and approved by the Department.

CLAIMS REVIEW

Claims are usually reported to the Company by telephone. Claims are first routed by 800 numbers to Austin, Texas. Based on the Louisiana area and zip codes provided by the claim caller, the call is forwarded to the nearest Louisiana claim office. The Company maintains ten claims offices in Louisiana that are located in Metairie, Harvey, Houma, Chalmette, Mandeville, Baton Rouge, Lafayette, Lake Charles, Shreveport and Monroe.

When the claim call is transferred to a Louisiana claims office a computer screen is available to the Louisiana claims adjuster in order to verify coverage and make arrangements with the insured/caller to inspect the damaged vehicle. The date of the phone call and the date of the loss once entered into the computer are permanent data. A new claim number must be assigned in order to correct the date of the phone call and/or date of the loss.

A systematic random sampling of 54 open and closed litigated claim files was selected for review from listings provided by the Company for the years 1997, 1998 and 1999. There were no indications that the Company's claim handling of these files encouraged litigation.

A systematic sampling of 21 pended claims as of December 31, 1999 was selected for review from a listing provided by the Company. This review revealed that claims were usually delayed due to the length of time required to determine the extent of bodily injury sustained as the result of a collision and/or the threat of litigation.

The Company does not maintain any computer records of denied claims. However, it was determined that the Company maintained a copy of denied claim letters. A listing of these denied claim letters for 1999 was prepared by the Company and provided to the examiners. From this listing a judgmental sampling of 50 claim denials was selected for review. These denials appeared to be in accordance with policy provisions and regulations.

The Company was asked to provide its 1999 paid claims as reported in its annual statement as of December 31, 1999. The ACL Program provided by the Department was utilized to analyze this claim data.

The Company did not provide the claim file as requested by the examiners. The 1999 paid claim file provided by the Company contained payments made in 2000 and could not be reconciled to the total claims reported in the Company's 1999 annual statement. Also, the claim payments were totaled by line of business under the earliest date of claim payment for each claim number. Apparently the purpose of this program was to reduce the number of claim lines in the report. Due to the characteristics of the claim file provided by the Company, ACL could not be used to accurately measure the time lag for bodily injury and medical payments because such payments usually are paid over a period of time. However, it should be noted that the review of a sample of paid

claims *with bodily injury* indicated that these claims were settled promptly upon receipt of the required medical records.

ACL generated the following paid property damage claims for 1999. These reports are based on the actual number of claims processed.

COLLISION CLAIMS

92%	<i>PAID WITHIN 30 DAYS</i>
4%	<i>PAID WITHIN 60 DAYS</i>
2%	<i>PAID WITHIN 90 DAYS</i>
2%	<i>PAID 91 DAYS OR LATER</i>

PROPERTY DAMAGE CLAIMS

82%	<i>PAID WITHIN 30 DAYS</i>
8%	<i>PAID WITHIN 60 DAYS</i>
3%	<i>PAID WITHIN 90 DAYS</i>
7%	<i>PAID 91 DAYS OR LATER</i>

COMPREHENSIVE CLAIMS

87%	<i>PAID WITHIN 30 DAYS</i>
8%	<i>PAID WITHIN 60 DAYS</i>
3%	<i>PAID WITHIN 90 DAYS</i>
2%	<i>PAID 91 DAYS OR LATER</i>

The ACL Program generated a random sampling of 60 paid claims in 1999. The review of this sampling indicated that claims were paid promptly and in accordance with policy provision and regulations.

The Metairie claims office supervised the gathering of requested claim files from the other Louisiana claims offices. The Company had difficulty securing the claim files on a timely basis from the Louisiana claims offices. In addition, a small part of the claim sampling contained comprehensive glass claims that were maintained in Austin, Texas which were not provided on a timely basis.

The Company contracts with various repair facilities in order to provide a program called "TotalPro Service". The purpose of this program is to expedite the repair of the vehicle by allowing the Company to work closely with the repair facility. In addition, if the Company's insured or other party involved in an accident select a TotalPro-approved collision repair facility, the Company offers a limited lifetime warranty for the repair for as long as the insured or other party owns or leases the vehicle. Even though the Company does offer the "TotalPro Service", the insured or other party is not discouraged from selecting a different repair facility.

COMMENTS AND RECOMMENDATIONS

The Ohio Parent provided its Market Conduct Manager as the contact person for this examination. Examination requests and questions were communicated by email and telephone to the Ohio contact person. Based on the nature of the request it was delegated to the responsible personnel in the appropriate state. This method of gathering data for the examination proved slow and cumbersome, as apparently it was difficult for the contact person to oversee the timely development of the requested data. The Company is not in compliance with **LSA-R.S. 22: 39** which states as follows:

“The books and records of every domestic and redomesticated insurer shall be located within the state of Louisiana.”

It is recommended that the Company maintain its complaint register in accordance with LSA-R.S. 22:1214(17).

The Underwriting and Claims Review indicate that the Company has been successful in providing its policyholders with prompt service in the issuance of policies and the payment of claims. The Company’s prompt issuance of policies appears to be the result of applications submitted electronically by field underwriters, applications completed via toll free numbers and the increasing use of a website in which an applicant can submit an application to the Company via the Internet.

The usage of electronic applications has resulted in a decreased usage of paper creating a “paperless environment”. With the advent of this “paperless environment”, it is imperative that the Company be mindful of its statutory obligations as addressed in LSA-R.S. 22:1214 (16) which states as follows:

“Failure to maintain marketing and performance records. Failure of an insurer to maintain its books, records, documents and other business records in such an order that data regarding complains, claims, rating, underwriting, and marketing are accessible and retrievable for examination by the insurance commissioner. Data for at least the current calendar year and the two preceding years shall be maintained.”

Specifically, commission statements provided to the agents under its website *Foragentsonly.com* should be programmed so that the examiners will have access to these statements. Also, the Company should provide a “test site” so that the examiners could, with greater flexibility, verify rate calculations on its website, *Progressive. Com*.

Based on the findings from the Producer Review, it is recommended that the Company review its recruiting procedures in order to determine that procedures are in

place to verify that all agents contracted by the Company are properly licensed and appointed by the Louisiana Department of Insurance.

Based on the documentation provided to the examiners, it appears that the Company has classified its agency force into two separate classes: Vanguard agents and agents not qualified for the Vanguard Program, referred to in this report as non-Vanguard agents. The main criteria for qualifications as a Vanguard agent as determined by the Company are as follows: maintain at least a 70% violation disclosure on private auto applications, produce a minimum number of private auto applications and quote only Vanguard rates to all new applicants.

Once qualified, the Vanguard agent must chose between receiving a higher commission rate on first year and renewal auto premiums or continuing his or her current commission rates as previously detailed in this report. However, if the newly qualified Vanguard agent elects to continue receiving his current commission compensation, he or she is qualified to market (and must market) Supersaver Premium Rates, discounted rates, to all applicants.

The Vanguard Program could result in an applicant receiving a different premium quote for the same auto coverage based *only* upon his agent selection because all agents of the Company use the same underwriting guidelines. The Company's practice of establishing a group of agents to market a discounted premium to *some* applicants but not to *all* applicants with similar risk factors appears to be in conflict with LSA-R.S.-22: 652.

The liberal qualifications determined by the Company for the Vanguard Program do not appear to legitimize a separate class of agents. See PRODUCER REVIEW, page 7.

It is recommended that the Company take corrective action to ensure its Vanguard Program is in compliance with statutory requirements.

It is recommended that the Company consider developing a form for use by the agent in which the applicant can sign attesting to receipt of a copy of the application. In addition, audits should be conducted of the agent's office to verify that the agent is adequately maintaining the original applications. Audit findings should be in written form. See PRODUCER REVIEW, page 7 and UNDERWRITING AND RATING REVIEW, page 10.

The Company is reminded that uninsured motorist coverage shall be added to all automobile liability insurance issued in this state unless rejected or lower limits are requested. The following statute addresses the issuance of uninsured motorist coverage in detail. **LSA-R. S. 22:1406 D. (1)(a)(i)** states in part as follows:

"The following provisions shall govern the issuance of uninsured motorist coverage in this state:

(1)(a)(i) No automobile liability insurance covering liability arising out of the ownership, maintenance, or use of any motor vehicle shall be delivered or issued for delivery in this state with respect to any motor vehicle designed for use on public highways and required to be registered in this state or as provided in this Subsection unless coverage is provided therein or supplemental thereto, in not less than the limits of bodily injury liability provided by the policy, under provisions filed with and approved by the commissioner of insurance, for the protection of persons insured thereunder who are legally entitled to recover nonpunitive damages from owners or operators of uninsured or underinsured motor vehicles because of bodily injury, sickness, or disease, including death resulting therefrom: however, the coverage required under this Subsection is not applicable when any insured named in the policy either rejects coverage, selects lower limits, or selects economic-only coverage, in the manner provided in Item D(1) (a) (ii) of this Subsection. In no event shall the policy limits of an uninsured motorist policy be less than the minimum liability limits required under R.S. 32:900, unless economic-only coverage is selected as authorized herein..."

See UNDERWRITING AND RATING REVIEW, page 10.

The ACL claims data was requested on October 10, 2000 and was provided to the examiners in two stages on November 22, 2000 and December 11, 2000. The ACL sampling request for paid claims was dated on November 30, 2000 and the Company provided this documentation over a period of time with the remainder of this request received by the examiners on January 22, 2001. It is recommended that the Company give full consideration to its record retention requirements for future examinations in order that requested examination data can be timely provided. See CLAIMS REVIEW, page 13.

It is recommended that the Company develop an antifraud policy that would enable employees to perform their duties in accordance with the goals and direction of management. It is also recommended that the antifraud policy for employees along with the Company's guidelines to detect and investigate claim fraud should be in written form. See COMPANY OVERVIEW, page 4.

CONCLUSION

I, Richard A. Spong, 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 an examination of the market conduct activities of

PROGRESSIVE SECURITY INSURANCE COMPANY

METAIRIE, LOUISIANA

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.

Richard S. Robison, Louisiana Insurance Compliance Examiner, also participated in this examination and joins the undersigned in acknowledging the courteous cooperation of the Company's Officers and Employees.

Respectfully submitted,



Richard A. Spong, CIE, CFE
Louisiana Department of Insurance