

REPORT ON

MARKET CONDUCT EXAMINATION

OF THE

PROVIDENCE WASHINGTON INSURANCE COMPANY
ONE OLD STONE SQUARE
PROVIDENCE, RHODE ISLAND 02901
NAIC CODE #01562

AS OF

JUNE 1, 1992

DEPARTMENT OF BUSINESS REGULATION
INSURANCE DIVISION
STATE OF RHODE ISLAND

Table of Contents

SALUTATION	1
FOREWORD	3
SCOPE OF EXAMINATION	2
HISTORY	2
COMPANY OPERATIONS AND MANAGEMENT	8
CERTIFICATE OF AUTHORITY	11
CONSUMER OR OTHER RELATED COMPLAINTS	12
LICENSING OF AGENTS, AGENCIES AND BROKERS	13
UNDERWRITING	15
CANCELLATIONS & NON-RENEWALS	16
SUMMARY OF RECOMMENDATIONS	18
CONCLUSION	20

February 2, 1993

Honorable Sheldon Whitehouse
Insurance Commissioner
State of Rhode Island
Providence, Rhode Island 02903

Sir:

In compliance with your instructions, and pursuant to Section 27-1-11 of the insurance laws of the State of Rhode Island, a Market Conduct Examination has been performed of the Rhode Island business of:

Providence Washington Insurance Company
One Old Stone Square
Providence, Rhode Island 02901

hereinafter referred to as "the Company" and the following report is respectfully submitted.

FOREWORD

The Report on the Market Conduct Examination is, in general, a report by exception. Any additional practices, procedures and/or files subject to review during the examination may have been omitted from the report if no errors and/or improprieties were indicated.

SCOPE OF EXAMINATION

The examination, as stated in the salutation, was conducted in accordance with Section 27-1-11 of the insurance laws of the State of Rhode Island. The examination commenced on May 13, 1992 and covered the period from January 1, 1990 to June 1, 1992.

The primary purpose of the examination was to determine the company's compliance with the statutes, rules, regulations and policy provisions relative to the Company's insurance business activities within the State of Rhode Island.

The examination was performed in conformance with the procedures as prescribed by the National Association of Insurance Commissioners. Accordingly, certain schedules, reviews and analyses were prepared and evaluations performed of principle segments of the company. These segments included Consumer Complaints, Agents Licensing, Certificates of Authority, Sales and Advertising, Underwriting, Rating, Cancellations/Non-renewals and Claims. The results of the evaluations satisfied the primary purpose of the examination and formed the bases of the findings, recommendations and conclusions presented in the report.

HISTORY

The Company is the outgrowth of two companies; namely, the

Providence Insurance Company and the Washington Insurance Company, which were incorporated by Acts of the General Assembly of the State of Rhode Island on January 5, 1799 and January 10, 1800, respectively.

On May 18, 1815, the two companies entered into an agreement whereby they would consolidate into one company, under the name, "Providence Washington Insurance Company", but legislative action necessary to effectuate the agreement was not taken at that time.

The Act to incorporate the stockholders of the Providence Insurance Company and the Washington Insurance Company into the one company, Providence Washington Insurance Company, was passed by the General Assembly of the State of Rhode Island at its February Session, 1820.

The capital of the consolidated companies amounted to \$132,000, represented by 4,200 shares.

The Charter provided for a minimum capital of \$132,000 which could be increased from time to time by a vote of at least two-thirds of all the stockholders to an amount not to exceed \$500,000. The authorized capital stock was changed by charter amendments in the following years:

- 1872 - Par Value reduced to five dollars per share.
 - 1875 - Par Value increased to fifty dollars per share.
 - 1899 - Authorized capital increased to seven hundred and fifty thousand dollars.
 - 1902 - Authorized capital increased to one million dollars.
 - 1923 - Authorized capital increased to ten million dollars.
- Preferred stock may be issued by a two-thirds vote of all the stockholders. The par value of the capital stock may be fixed from time to time by a two-thirds vote of all the stockholders entitled to vote thereon.

The charter was also amended by Acts of the General Assembly in the years 1947, 1953, 1966, 1968 and 1971.

The original capital of the united companies was \$132,000 which was increased during 1827 to \$200,000, divided into 6,250 shares of stock. The par value of the stock was fixed at \$5 per share in 1872, decreasing the capital to \$31,250. During 1875, the capital was increased to \$400,000 and the par value was changed to \$50 per share. Stock dividends in the years 1898, 1911 and 1912 increased the capital to \$500,000, \$750,000 and \$1,000,000, respectively. The par value was increased to \$100 per share in 1924, resulting in a capital of \$2,000,000. A stock dividend of 50% and a reduction in the par value of \$10 per share in 1926 resulted in capital of \$3,000,000, divided into 300,000 shares of stock. The sales of

80,000 shares at \$10 a share of the \$10 par value convertible preferred stock and 100,000 shares of common stock at \$10 in December, 1950 increased capital to \$4,800,000. The conversion of 60 shares of the \$10 preferred stock for 87 shares of the \$10 common stock in 1955 increased capital to \$4,800,270.

Subsequent conversion and redemption of the preferred stock resulted in the following changes:

	Shares <u>Preferred Stock</u>	Shares <u>Common Stock</u>	<u>Capital</u>
1955 Balance	79,940	400,087	\$ 4,800,270
1966	(300)	390	900
1967	(100)	130	300
1968	(5,130)	6,668	15,380
1969	(72,958)	94,845	218,870
1969	<u>(1,452)</u>	<u>*</u>	<u>(14,520)</u>
Balance 12-31-69	<u>- 0 -</u>	<u>502,120</u>	\$ <u>5,021,200</u>

*Company exercised callable feature of the preferred stock.

At December 31, 1981, the Company's outstanding stock was directly owned by Providence Capitol Investment Company, an indirect wholly-owned subsidiary of Gulf & Western Industries, Inc.

In July 1982, Richfield Holdings, Ltd., a newly formed Bermuda corporation, acquired the Company through the purchase of Providence Capitol Investment Company from Gulf & Western Industries, Inc.

On December 10, 1986 PW Investors, Inc., an affiliate of AEA Investors, Inc., acquired the Company from Providence Capitol Investment Ltd., formerly Richfield Holdings, Ltd.

In June 1987, the Company's Board of Directors approved the sale of Motor Vehicle Casualty Company. On October 28, 1987 the sale was completed for approximately \$10.5 million. Pursuant to terms of the Purchase Agreement, the new assets of Motor Vehicle as of September 30, 1987, except for licenses, cash and securities, were transferred via a dividend to the Company. In addition, the Company agreed to reinsure all outstanding insurance liabilities and assume all non-insurance liabilities as of September 30, 1987.

In September 1987, the Company entered into a joint venture agreement to form PW Reinsurance Management Company and invested \$700,000 in February 1988, representing a 70% share in the new venture.

In April 1989, an Agreement and Plan of Merger was consummated among Baloise Holdings, a Swiss Corporation, PW Group, Inc., a newly formed Rhode Island Corporation, PW Investment, Inc. and PW

Investors, Inc. As a result of the Agreement and Plan of Merger, PW Investors, Inc. was merged in PW Group, Inc. PW Group, Inc. became the holding company for the Company and Subsidiaries ("The Company") and various affiliates. The majority of PW Group, Inc. outstanding common stock was acquired by Baloise United States Holding Company, an indirectly wholly-owned subsidiary of Baloise Holdings. The Plan of Merger relative to the Rhode Island corporations was approved by the Rhode Island Department of Business Regulation, Insurance Division on April 6, 1989.

Effective January 1, 1991, PW Group, Inc. merged into PW Holdings, Inc., a newly formed Delaware Corporation. Such merger was granted an exception by the Rhode Island Department of Business Regulation, Insurance Division, since there was no actual change of control.

Certain sales of various subsidiaries of the Company were proposed by the Company's Board of Directors during the latter part of 1992. As of the final coverage date of the examination, however, no such sales occurred and, therefore, none were reported.

The company owns all the outstanding capital stock of the Western Alliance Insurance Company and Providence Lloyds of Austin, Texas, the York Insurance Company, of Elmhurst, Illinois and the Providence Washington Insurance Company of Alaska and the preferred General Agency of Alaska, both of Anchorage, Alaska, Colorado Casualty Insurance Company of Englewood, Colorado and American

Concept Insurance Company of Rapid City, South Dakota.

COMPANY OPERATIONS AND MANAGEMENT

The company, under its charter, was authorized to write insurance on all vessels, and the property laden therein; upon houses and other buildings, and the furniture and other goods therein; to become principal, surety, indemnitor, endorser or otherwise to bind itself on, or upon any bond recognizance, undertaking, guaranty, contract of indemnity, agreement or writing obligatory in the nature thereof, and on or upon, every obligation whatsoever, and to write insurance against any other casualty or risk which now or hereafter may lawfully be the subject of liability, casualty, burglary, fidelity, indemnity or surety business; and to write insurance of all other types permitted by any general law or public law of Rhode Island or special law now or hereafter in effect, insofar as the same may be applicable to the Company.

Direct written premiums for the Company for calendar year 1991 were \$287,848,418. Rhode Island's production for the same period was \$16,392,999, which represents 5.7 percent of the Company's total direct written premium. The following schedule outlines the Company's mix of insurance business in the State of Rhode Island. The source of all figures presented in the schedule is the 1991 Annual Statement.

Schedule of Rhode Island Direct Written Premiums
1991

<u>Line of Business</u>	<u>Direct Written Premiums</u>
Fire	\$676,957.00
Allied Lines	72,925.00
Homeowners	528,111.00
Commercial Multi Peril	1,778,865.00
Ocean Marine	34,706.00
Inland Marine	41,230.00
Earthquake	7,002.00
Workers' Compensation	8,748,411.00
Other Liability	617,537.00
Private Passenger Automobile	1,844,487.00
Commercial Automobile	2,024,767.00
Fidelity	6,673.00
Surety	20.00
Burglary & Theft	142.00
Boiler & Machinery	<u>\$11,166.00</u>
 Total Direct Written Premiums	 <u>\$16,392,999.00</u>

During the year 1990 the Company's senior management decided not to accept any more Voluntary Workers' Compensation Business. Therefore, according to the Company's senior management, the Workers' Compensation Direct Written Premiums, as reported in the prior schedule, pertain to Involuntary Workers' Compensation business assigned to the Company by the National Council on Compensation Insurance ("the Council"). The Council administrates both the National Workers' Compensation Reinsurance Pool and the Workers' Compensation Assigned Risk Pool in the State of Rhode Island. The Company, as a member and a servicing carrier of both Pools, is subject to the Council's administrative decrees. As such, the Company is required to account for and cede all Council assigned Workers Compensation Direct Written Premiums less

Servicing Carrier Fees to the Council. In addition, the Company issues the appropriate policies, provides the necessary services to the policy holders and/or claimants, and is provided reimbursement for all losses less certain loss Adjustment Expenses by the Council. On quarterly, semi-annual and annual bases, the Council reconciles both of the Pools and assesses each member according to a formula established and agreed upon by the members and promulgated by the Council.

In addition, although not pertinent to the prior schedule but relevant to subsequent events, as of April 1, 1992, the Company's senior management decided that the Company no longer write Private Passenger Automobile Insurance in the State of Rhode Island.

At the time of the examination, the Company was licensed to transact insurance business in the District of Columbia, all states of the United States (except Hawaii), the Canadian provinces of Alberta, British Columbia, New Brunswick, Ontario and Quebec.

Relative to the handling of the Company's insurance business in the State of Rhode Island, the operations took place in the following manner and geographic location (s):

- 1) Policy Holder Service - The Underwriting rating and processing of all policies was administrated through the Company's branch location at 88 Boyd Avenue, East Providence, Rhode Island

02914. However, all business was obtained from duly appointed agents through the Independent Agency System with the exception of the following:

- a) Involuntary Workers' Compensation Insurance policies assigned to the Company by the Council and
- b) Assigned Risk Automobile Insurance policies assigned to the Company by the Rhode Island Automobile Plan ("the Plan").

2) Claims Processing - All Rhode Island claims were processed through the Company's East Providence office at the same address noted in 1) above. The initial notices of loss were reported to the Company by the appointed agents, the Council or the Plan. Company staff and/or independent adjusters provided the necessary info/data for the intermediate and finish disposition of the loss claim. However, The Company issued all drafts and made all final resolution of the claim.

CERTIFICATE OF AUTHORITY

The Company's Certificates of Authority were reviewed for the

periods under examination. The Company's writings are in conformance with the authority granted by their Certificates.

CONSUMER OR OTHER RELATED COMPLAINTS

The Company's procedures for handling consumer or other related complaints were examined to verify the Company's compliance with Rhode Island Statutes 27-29-3 & 4 - "Unfair and Deceptive Acts".

During the examination, the resident vice president was interviewed. The results of the interview indicated that complaint handling procedures appear to adequately provide the necessary internal administrative controls to ensure compliance to the Rhode Island Statutes referenced above.

Although all complaints reviewed were responded to by the Company in a professional manner and in accordance with the Rhode Island statutes, two complaint files were not logged in the complaint register (Company uses NAIC's recommended format) as required by company procedures. These omissions were determined by the examiner upon reconciliation of the Company's complaint register with a list of consumer complaints from the Insurance Division of the Rhode Island Department of Business Regulation.

Therefore, it is recommended that:

- 1) All appropriate personnel should be reissued a copy of the written consumer or other related complaint handling procedures.

- 2) All appropriate personnel should verify in writing that they have received their reissued copy, are aware of its contents and are presently implementing and/or reinforcing adherence.

LICENSING OF AGENTS, AGENCIES AND BROKERS

The Company's internal system for the handling of agents, agencies, and brokers' licensing was reviewed to verify the Company's compliance with the statutes and regulations of the State of Rhode Island relative to such licensing. (See R.I. Insurance Law Section 27-3-1 thru 4P.5)

During the examination, the Branch Sales Manager was interviewed. The results of the interview produced a verbally communicated narrative of the Company's procedures for obtaining or terminating the license of an agent, agency or broker. The narrated procedures appeared to adequately provide all internal administrative controls necessary to insure that the Company was in compliance with the

statutes and regulations referred to above.

Upon performing a reconciliation of the Company's records with a list of active agents from the Insurance Division of the Rhode Island Department of Business Regulation, an exception was identified. The exception, as noted, involved three (3) separate agencies acting on the Company's behalf in violation of Rhode Island Insurance Law Section 27-3-2, License Requirements. The three (3) agencies, at the time of the reconciliation, were not properly authorized by the Company or the Insurance Commissioner to act as the Company's agent (see R.I. Insurance Law Section 27-3-1, Agent defined).

Therefore, it is recommended that:

- 1) Licensing and termination procedures for agents, agencies, and brokers be put in writing and become part of the Company's procedures manual.
- 2) The department responsible for licensing and termination of agents, agencies, and brokers be given a copy of the written procedures for immediate implementation.

- 3) Licensing manager/coordinator should verify in writing that the written procedures have been implemented.

UNDERWRITING

For the period under examination, the Company's underwriting procedures for all lines of business within the State of Rhode Island were reviewed. The review was conducted to determine the Company's compliance with the statutes and regulations of the State of Rhode Island, especially as they relate to collusive underwriting practices and discriminatory risk selection.

Although the examination procedures performed showed no evidence of collusive and/or discriminatory activity in the underwriting division of the Company, certain weaknesses in the internal procedures relative to the declination of coverage were noted. Of those weaknesses, only three (3) deserve mention in this report.

The first weakness dealt with the Company's decision to decline a risk and yet provide no evidence of informing the submitting agent. Second, of the 52 files selected, thirty-three percent (33%) failed to contain evidence of the specific reason for the underwriter's declination. Finally, approximately fifteen percent (15%) of the selected sample of the 52 files failed to provide documentation of the date of receipt and/or declination of the risk.

As a result of the above it is recommended that the Company implement guidelines for underwriters to follow when reviewing files for potential coverage or possible declination. The following procedure should be included with the proposed guidelines: Upon reviewing and declining coverage of an insured or potential insured, the underwriter should enter in the file both the date of receipt and declination of the request for coverage, as well as, evidence that the declination has been conveyed to the agent.

CANCELLATIONS & NON-RENEWALS

As a result of the testing performed, an exception was noted, as well as, certain internal procedural weaknesses. The exception dealt with Private Passenger Automobile Policies issued by the Company through one of its licensed Agents. The agent requested that the Company not send non-renewal notices to the clients, even though, the Company had documented its intent not to renew the coverages upon their respective renewal dates. A letter from the agent, as well as, the test results verified the company's honoring of the agent's request. By so doing, the Company came in direct violation of Insurance Regulation XVI, Automobile Insurance Policies; Cancellations and Renewal Provisions, Section 4 notice of nonrenewal, as well as, the Company's own Private Passenger Automobile Coverage provisions. The internal procedural weaknesses

referred to above, involved lack of documentation within various policy files upon cancellation or non-renewal by either the Company or the policy - holder.

It is recommended that the Company comply with the Insurance regulations of the State of Rhode Island as they relate to cancellations and nonrenewal of all lines of business handled by the Company. Procedures for the handling of Cancellations and Nonrenewals should be established, implemented and strictly adhered to. One of the recommended procedures to be included above is the complete documentation within the policy file of the cancellation or nonrenewal proceedings, as well as, all correspondence between the parties involved. In addition, all policy files should be fully documented to evidence compliance with such procedures.

In conclusion, for the period under examination, the Company was not fully in compliance with the Insurance Regulations of the State of Rhode Island relative to Cancellation or Nonrenewals.

SUMMARY OF RECOMMENDATIONS

Page

It is recommended that:

- 13 1) All appropriate personnel should be reissued a copy of the written consumer or related complaint handling procedures.
- 13 2) All appropriate personnel should verify in writing that they have received their reissued copy, are aware of its contents and are presently implementing and/or reinforcing adherence.

It is recommended that:

- 14 1) Licensing and termination procedures for agents, agencies, and brokers be put in writing and become part of the Company's procedures manual.
- 14 2) The department responsible for licensing and termination of agents, agencies and brokers be given a copy of the written procedures for immediate implementation.
- 15 3) Licensing manager/coordinator should verify in writing that the written procedures have been implemented.
- 16 It is recommended that the company implement guidelines

for underwriters to follow when reviewing files for potential coverage of possible declination. The following procedure should be included with the proposed guidelines: Upon reviewing and declining coverage of an insured or potential insured, the underwriter should enter in the file both the date of receipt and declination of the request for coverage, as well as, evidence that the declination has been conveyed to the agent.

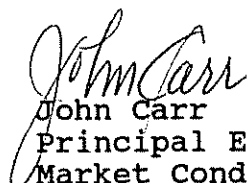
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CONCLUSION

Acknowledgement is made of the courteous cooperation extended by the Company's officers and employees during the course of the examination.

In addition to the undersigned, Robert Arrow, Senior Examiner participated in the examination, as well as, the preparation of this report.

Respectfully submitted,


John Carr
Principal Examiner
Market Conduct
State of Rhode Island