Market Conduct Examination

UNITED SERVICES AUTOMOBILE ASSOCIATION
AND
USAA CASUALTY INSURANCE COMPANY

San Antonio, Texas

STATE OF NEW JERSEY
DEPARTMENT OF BANKING AND INSURANCE
Office of Consumer Protection Services

Market Conduct Examination Section

Date Report Adopted: March 6, 2007

MARKET CONDUCT EXAMINATION

of the

UNITED SERVICES AUTOMOBILE ASSOCIATION

USAA CASUALTY INSURANCE COMPANY

located in

San Antonio Texas

as of

April 27, 2005

BY EXAMINERS

of the

STATE OF NEW JERSEY
DEPARTMENT OF BANKING AND INSURANCE

OFFICE OF CONSUMER PROTECTION SERVICES
MARKET CONDUCT EXAMINATION SECTION

DATE REPORT ADOPTED: MARCH 6, 2007

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I. INTRODUCTION

A. SCOPE OF EXAMINATION

This is a report of the Market Conduct and Anti-Fraud Compliance activities of the United Services Automobile Association and USAA Casualty Insurance Companies (hereinafter referred to as “USAA” and “CIC” respectively, or collectively as the Companies). In this report, examiners of the New Jersey Department of Banking and Insurance (NJDOBI) present their findings, conclusions and recommendations as a result of their examination. The Market Conduct Examiners were Robert Greenfield Examiner-in-Charge, Thomas H. Goehrig and John Sivon.

The scope of the examination included private passenger automobile insurance sold by the Company in New Jersey. The examiners evaluated the Companies’ compliance with the regulations and statutes pertaining to automobile underwriting, prompt handling of claim files and anti-fraud compliance. The review period for the examination was January 1, 2003 to April 27, 2005. Review of database records included the period January 1, 2003 to December 31, 2003. The examiners conducted their fieldwork at the United States Automobile Association in San Antonio, Texas between November 29, 2004 and February 4, 2005. On various dates thereafter, the examiners completed additional review work and report writing in Trenton, New Jersey.

The examiners randomly selected files and records from computer listings and documents provided by the Company. The random selection process is in accordance with the National Association of Insurance Commissioner’s (NAIC) Market Conduct Examiners’ Handbook. In addition, the examiners used the NAIC Handbook, Chapter VIII Conducting the Property and Casualty Examination as a guide to examine the Company and to write this report.

B. ERROR RATIOS

Error ratios are the percentage of files reviewed which an insurer handles in error. A file is counted as an error when it is mishandled or the insured is treated unfairly, even if no statute or regulation is applicable. If a file contains multiple errors, the examiners will count the file only once in calculating error ratios. However, any file which contains more than one error will be cited more than once in the report. In the event that the insurer corrects an error as a result of a consumer complaint or due to the examiners’ findings, the error will be included in the error

ratio. If the insurer corrects an error independent of a complaint or NJDOBI intervention, the error is not included in the error ratios.

For the purpose of the database computer analyses conducted during this review period, the examiners define an exception as a file or record in a database that does not meet specified criteria as set forth in electronic queries. The file or record has not been reviewed in depth by an examiner. However, the frequency, type or severity of these exceptions may result in the examiners extracting sub-populations and review samples for further, detailed analysis.

Whenever the examiners find that a company commits a type of error with sufficient frequency, they will cite the errors as an improper general business practice. Whenever the examiners identified errors that constitute an improper general business practice, they have stated this in the report that follows.

The examiners sometimes find improper general business practices of an insurer that may be technical in nature or which did not have an impact on a consumer. Even though such a practice would not be in compliance with applicable law, the examiners do not count each of these files as an error in determining error ratios. Whenever such business practices do have an impact on the consumer, each of the files in error will be counted in the error ratio. The examiners indicate in the report that follows whenever they did not count any particular files in the error ratio.

The examiners submitted written inquiries to Company representatives on the errors cited in this report. This provided the opportunity to respond to the examiners' findings and to provide exception to the statutory and/or regulatory errors or mishandling of files reported herein. In response to these inquiries, USAA and CIC agreed with some of the errors cited in this report. On those errors with which the Company disagreed, the examiners evaluated the individual merits of each response and gave due consideration to all comments. In some instances, the examiners did not cite the files due to the Companies' explanatory responses. In others, the errors remained as cited in the examiners' inquiries.

C. COMPANY PROFILE

United Services Automobile Association (USAA) is organized as a reciprocal inter-insurance exchange. This Company began conducting business in June, 1922 as the “United States Army Automobile Insurance Association” with offices at Kelly Field, Texas. The present title was adopted at the same time that its headquarters was established at Fort Sam Houston, Texas. USAA is licensed in all states, the District of Columbia, Guam, Puerto Rico, and the Virgin Islands.

Subscribers of the exchange (members) are limited to active and former commissioned, non-commissioned and warrant officers of the regular forces and reserve components of the United States Armed Services. The Companies also write private passenger business for its non-military employees.

USAA Casualty Insurance Company (CIC) was incorporated and licensed in the State of Texas under the name United Services Casualty Insurance Company in September 1968. The current name was adopted in December 1970. In July 1990, CIC was redomesticated to Florida. In January 2000, CIC was redomesticated back to Texas. All outstanding capital stock is owned by United Services Automobile Association. The company is licensed in all states and the District of Columbia. CIC specializes in writing personal lines property and casualty insurance for active duty enlisted personnel other than non-commissioned officers (NCOs), and ex-dependents of USAA members. USAA specializes in writing personal lines property and casualty insurance.

USAA and CIC are direct writers in the State of New Jersey. Operations are conducted on a direct basis by mail and telephone from the Home and Regional Offices. Regional offices are maintained in Colorado Springs, Colorado, Norfolk, Virginia, Sacramento, California, Phoenix, Arizona, and Tampa, Florida. The majority of claims are handled through the regional and home office staff. Claims requiring additional handling are referred to staff field adjusters.

II. CLAIMS REVIEW

A. INTRODUCTION

This review covers Personal Injury Protection (PIP), collision, comprehensive and property damage claims submitted under private passenger automobile insurance. In reviewing each claim, the examiners checked for compliance with all applicable statutes and regulations that govern timeliness requirements in settling first and third party claims. The examiners conducted specific reviews placing particular emphasis on **N.J.S.A. 17:29B-4(9)** and **N.J.A.C. 11:2-17** (Unfair claim and settlement practices), **N.J.A.C. 11:3-10.5** and **N.J.A.C. 11:2-17.7** (timeliness of settlement and notification of delay) and **N.J.S.A. 39:6A-5** (timely payment of Personal Injury Protection Benefits). These requirements relate to NAIC Market Conduct standards outlined in Chapter VIII of the Property and Casualty Insurance Examinations section of the NAIC Handbook.

B. ERROR RATIOS

The examiners calculated the error ratios by applying the procedure outlined in the introduction of this report. Error ratios are itemized separately based on the review samples as indicated in the following charts. The PIP review consisted of reviewing one randomly selected bill from each file.

Chart 1 below, identified as Random Sample Paid Claims Review, is a summary of the examiners' random review of claim files which yielded an overall error ratio of 7% with respect to timely claim payment. Chart 2 below, identified as Database Exception Prompt Pay Claims Review, is a summary of the examiners' population-wide database review of claim files, which yielded an overall error ratio of less than 1% with respect to timely claim payment. It should be noted that the examiners could not include an electronic, systems-wide PIP review because the Companies' databases did not retain date fields necessary to measure timeliness.

Chart 3 below, identified as Random Sample Denied Claims Review, is a summary of the examiners' random review of denied property damage files which yielded an error ratio of 0%. The examiners did not review randomly selected denied collision or comprehensive claims because the database review outlined in Chart 4, Database Exception Denied Claims Prompt Settlement Review, revealed no potential errors. Chart 4 is a summary of the examiners' population-wide review of denied claims that yielded an overall exception ratio of less than 1%. The examiners could not review denied PIP claims on a population-wide basis because of the systems limitations described above. A summary of these charts and the examiners' overall findings are addressed below.

1. Random Sample Paid Claims Review

Random Sample	Files Reviewed	Files in Error	Error Ratio
PIP Claims			
USAA	**25**	**1**	**4%**
CIC	**25**	**0**	**0**
Subtotal	**50**	**1**	**2%**
Collision Claims			
USAA	**20**	**0**	**0%**
CIC	**20**	**8**	**40%**
Subtotal	**40**	**8**	**20%**
Comprehensive Claims			
USAA	**18**	**2**	**11%**
CIC	**16**	**0**	**0**
Subtotal	**34**	**2**	**6%**
Property Damage			
USAA	**20**	**0**	**0**
CIC	**19**	**0**	**0**
Subtotals	**39**	**0**	**0**
Random Totals	**163**	**11**	**7%**

2. Database Exception Prompt Pay Claims Review

Claim Review Category	Claims Paid	Number of Exceptions	Exception Ratio
Collision			
USAA	**3,782**	**16**	**<1%**
CIC	**4,484**	**16**	**<1%**
Subtotal	**8,266**	**32**	**<1%**
Comprehensive			
USAA	**967**	**18**	**1.86%**
CIC	**1,263**	**15**	**1.19%**
Subtotal	**2,230**	**33**	**1.48%**
Property Damage			
USAA	**2,314**	**14**	**<1%**
CIC	**2,911**	**15**	**<1%**
Subtotal	**5,225**	**29**	**<1%**
Overall Totals	**15,721**	**94**	**<1%**

3. Random Sample Denied Claims Review

Review Category	Files Reviewed	Files in Error	Error Ratio
Property Damage Claims			
USAA	**4**	**0**	**0%**
CIC	**7**	**0**	**0%**
Subtotal	**11**	**0**	**0%**
Random Totals	**11**	**0**	**0%**

4. Database Exception Denied Claims Prompt Settlement Review

Claim Review Category	Claims Denied	Number of Exceptions	Exception Ratio
Collision			
USAA	**1,845**	**0**	**0%**
CIC	**2,258**	**0**	**0%**
Subtotal	**4,103**	**0**	**0%**
Comprehensive			
USAA	**255**	**0**	**0%**
CIC	**372**	**0**	**0%**
Subtotal	**627**	**0**	**0%**
Property Damage			
USAA	**1.080**	**1**	**<1%**
CIC	**1,331**	**3**	**<1%**
Subtotal	**2,411**	**4**	**<1%**
Overall Totals	**7,141**	**4**	**<1%**

C. PERSONAL INJURY PROTECTION CLAIMS – RANDOM SAMPLE

1. Failure to Pay PIP Claim Timely – 1 File in Error

N.J.S.A. 39:6A-5g states that a claim "shall be overdue if not paid within 60 days after the insurer is furnished written notice of the fact of a covered loss…" **N.J.A.C. 11:2-17.7(b)** states that, "The maximum period for all personal injury protection (PIP) claims shall be 60 calendar days after the insurer is furnished written notice of the fact of a covered loss…; provided however that an insurer may secure a 45-day extension in accordance with **N.J.S.A. 39:6A-5**." In addition, the examiners checked for compliance with Chapter VIII, paragraph G, Standard 3 in the Claims section of the NAIC Market Conduct Examination Handbook which states that the examiners should verify that claims are resolved in a timely manner.

The examiners reviewed 50 paid PIP claims and found that USAA failed to settle claim number **2056425-33** within the maximum 60-calendar day time frame without securing additional time to investigate, contrary to the above statutes and regulation. The Company received notice of a PIP claim on January 9, 2003 from AHS Hospital in the amount of $311.00 but did not issue payment until April 23, 2003, a period of 44 days beyond the required time frame of 60 days.

2. Failure to Pay Interest on Delayed PIP Payment – 1 File in Error

N.J.S.A. 39:6A-5(h) requires the payment of interest on all overdue benefits. This is relative to Standard Number 6 in the claims section of the NAIC Market Conduct Handbook, which states that "Claims (should be) properly handled in accordance with policy provisions and applicable statutes, rules and regulations." The examiners also found that the Company failed to pay the required interest on PIP claim **2056425-33** cited above. The Company agreed with the examiners' finding on this claim.

D. PHYSICAL DAMAGE CLAIMS – RANDOM SAMPLE

1. Failure to Settle Physical Damage Claims Within Maximum 30-Day Period and Failure to Issue Delay Notices on Physical Damage Claims (10 Files in Error) - Improper General Business Practice Regarding Delay Notices

N.J.A.C. 11:3-10.5(a) states that unless clear justification exists, or unless provided by law, the maximum payment period for physical damage claims shall be 30 calendar days. This is relative to Standard Number 6 in the claims section of the NAIC Market Conduct Handbook, which states that "Claims (should be) properly handled in accordance with policy provisions and applicable statutes, rules, and regulations.

Contrary to **N.J.A.C. 11:3-10.5(a)** as referenced above, the Companies failed to pay eight collision and two comprehensive claims within the required 30-day period.

PLEASE SEE APPENDIX A-1 FOR LIST OF FILES IN ERROR

The examiners also noted that the Companies did not send a delay notice to any of the insureds listed in Appendix A-1. This is contrary to **N.J.A.C. 11:3-10.5(b)**. This regulation states that, "...if any element of a claim remains unresolved for more than 30 days for physical damage claims from the date of the loss notice by the insured, the insurer shall provide the insured with a written explanation of the specific reasons for delay in the claim settlement. Updated written notices shall be sent every 30 days thereafter until all elements of the claim are either honored or rejected." Since this error occurred with a frequency of 100%, the examiners cited

this error as an improper general business practice. The examiners note that these files reflected several different settlement characteristics. Some were repaired at a direct repair shop, others were repaired at a shop selected by the insured and others were total losses where the vehicle was not repaired. In each case, delays in the settlement process can adversely affect the insured, e.g., exceeding rental limits or maximums, as well as difficulties in selecting shops other than the DRP and incurring additional expenses where the insured in not happy with DRP settlement progress. In such cases, a delay notice is warranted.

2. Results of Population-Wide Paid Claim Database Review

The examiners conducted database time study reviews on the Companies' entire population of paid collision, comprehensive and property damage claims as stated previously. The examiners could not review paid PIP claims in this manner because the Companies' systems did not retain relevant data required for this review.

The examiners queried this data by measuring claim receipt date and file feature closure date. It should be noted that the Companies' systems could not capture the actual payment date, thus requiring analysis based on the claim feature closure date. Since the claim feature closure date always occurred after the actual payment, the results of the time study were biased against the Companies. To offset this skew, the examiners added an additional five days (average lag between payment date and file closure date) to the maximum settlement periods (30 calendar days for first party claims pursuant to N.J.A.C. 11:3-10.5(a) and 45 calendar days pursuant to N.J.A.C. 11:2-17.7(c)2) and developed database queries that identified settlements beyond 35 days for physical damage claims and 50 days for property damage claims.

As noted in Chart 2 above, the examiners found exception ratios of less than one percent on collision and property damage claims. On paid property damage claims, the examiners found an exception ratio of less than two percent. On denied claims as noted in Chart 4 above, the examiners reported a zero percent exception ratio on collision and comprehensive claims, and an exception ratio of less than one percent on property damage claims. Regarding the latter, the Company identified the four claims that comprised the property damage exception ratio; since dates were known on these files, the examiners were able to calculate the exact number of days to settle these claims (see Appendix A-2).

III. UNDERWRITING REVIEW

A. INTRODUCTION

The examiners checked for compliance with applicable statutes and regulations including N.J.S.A. **17:29A-6, 15, 36 and 38** (filed and approved rating methods), N.J.A.C. **11:3-39** (premium discounts), N.J.A.C. **11:3-19A** (Tier rating plans and underwriting rules) and **Bulletins 00-02** and **03-33** (congruence between rating territory and vehicle garaging location). These statutory and administrative requirements relate to the NAIC Standards of Chapter VIII – Conducting the Property and Casualty Insurance Examination of the Market Conduct Examiners' Handbook.

B. ERROR RATIOS

Company	Files Reviewed	Files in Error	Error Ratios
CIC	109	0	0%
USAA	92	0	0%
Total	201	0	0%

C. EXAMINERS' FINDINGS

1. Approved Rating, Premium Discounts, Tier Placement and Territory Assignment Review

The random samples for both companies were reviewed for conformity with approved tier underwriting plans that USAA and CIC filed with the Department. This review also included the Companies' adherence to Department **Bulletin No.00-02** and **03-33**, which specifies that the proper territory rating is to be based on the automobile garage location rather than the insured's mailing address zip code. Finally, the examiners checked for compliance with senior citizen discount mandates specified in N.J.S.A. **17:29A-38**, as well as application of passive restraint discounts for vehicles equipped with such devices, including airbags and automatic seat belts.

The examiners reviewed a random sample of 201 files and found that the Companies provided all applicable discounts and properly placed the insured drivers in the correct tiers and assigned insureds to the appropriate territory.

2. Improper Nonrenewal Notices Found in Underwriting Files – 2 Files in Error

N.J.A.C. 11:3-8.3(e)1 states that no notice of nonrenewal shall be valid unless it includes the designated provision(s) of this subchapter under which action is being taken. This regulation is related to NAIC Market Conduct Examination Standard 23: Termination Practices in the underwriting and rating section of the NAIC Handbook, which states that termination notices must comply with policy provisions, state laws and company guidelines. On terminated policy numbers **10515094** and **10368525**, which were discovered during the underwriting review, the Company relied on its underwriting guidelines to justify its decision to terminate these policies. Although **N.J.A.C. 11:3-8.3(e)1ii** permits an insurer to nonrenew a policy when an insured does not meet the insurer's underwriting guidelines, **N.J.A.C. 11:3-8.3(e)1** requires that insurers specify the authority for such terminations. In response to the examiners' inquiries, the Company agreed that, contrary to **N.J.A.C. 11:3-8.3(e)1,** the termination notices did not specify that these policies were terminated pursuant to authority specified in **N.J.A.C. 11:3-8.3(e)1ii.** Since this error was caused by programming statements in the Company's automated notice system, this error occurred on all termination notices. However, the examiners did not consider this error to be an improper general business practice because of the relatively benign impact on the consumer.

IV. ANTI-FRAUD COMPLIANCE REVIEW

A. INTRODUCTION

Pursuant to **<u>N.J.S.A.</u> 17:33A-8** and **<u>N.J.A.C.</u> 11:16-6** **<u>et seq</u>**., insurers are required to file for approval a fraud prevention plan in accordance with the specifications outlined in **<u>N.J.S.A</u>. 17:33A-15**. In addition, **<u>N.J.A.C</u>. 11:16-6.4(a)** requires the establishment of a full-time Special Investigative Unit (SIU) whenever the insurer exceeds 2,500 policies. SIU personnel are required to meet qualifications established by **<u>N.J.A.C.</u>** 11:16-6.4(d) 1&2. The SIU unit is to be comprised of staff with a minimum amount of education and experience. In addition to investigating suspected claim and underwriting fraud and referrals to the New Jersey Office of the Insurance Fraud Prosecutor, the SIU is responsible for providing annual in-house fraud detection and prevention training to claims and underwriting personnel. The Company is also required to provide an annual report to the New Jersey Department of Banking and Insurance.

B. EXAMINERS FINDINGS

The examiners reviewed USAA's implementation of its claim and underwriting fraud prevention and detection plan and its fraud detection and prevention training records and found that plan implementation and training are in compliance with the above statute and regulation. The examiners submitted several inquiries to the Companies, requesting the approved fraud manual, procedures for collection and preservation of evidence, SIU and OIFP referral methodology and measures for sharing information between SIU and the Underwriting department. The companies' response to these inquiries indicated compliance.

The examiners randomly selected and reviewed 27 closed SIU claim files and 32 SIU underwriting files for compliance with **<u>N.J.A.C.</u> 11:16-6 et seq.**, and found no errors.

V. RECOMMENDATIONS

USAA and CIC should inform all responsible personnel and third party entities who handle the files and records cited as errors in this report of the examiners' recommendations and remedial measures that follow in the report sections indicated. The examiners also recommend that the companies establish procedures to monitor compliance with these measures.

Throughout this report, the examiners cite and/or discuss all errors found. If the report cites a single error, the examiners often include a "reminder" recommendation because if a single error is found, more errors may have occurred.

The examiners acknowledge that during the examination, the companies have agreed and had already complied with, either in whole or in part, some of the recommendations. For the purpose of obtaining proof of compliance and for the Companies to provide its personnel with a document they can use for future reference, the examiners have listed all recommendations below.

A. GENERAL INSTRUCTIONS

All items requested for the Commissioner and copies of all written instructions, procedures, recommended forms, etc. should be sent to the Commissioner, c/o Clifton J. Day, Manager of the Market Conduct Examinations and Anti-fraud Compliance Unit, Mary Roebling Building, 20 West State Street, PO Box 329, Trenton, N.J. 08625, within thirty (30) days of the date of the adopted report.

B. CLAIMS

1. The Company should remind all appropriate personnel, including outside vendors when applicable, that when they are handling first party claims, they must:

   a. Pay all PIP claims within 60 days unless an extension of 45 days is requested in writing pursuant to **N.J.S.A. 39:6A-5g** and **N.J.A.C. 11:2-17.7(b)**.

   b. Pay interest on PIP claims paid beyond the required time frames pursuant to **N.J.S.A. 39:6A-5h**. USAA and CIC must reopen and review the 1 PIP claim the examiners cited for failure to pay interest listed in Appendix A.2 of this report. The Company should calculate and pay the interest for the period of delay as required by the statute.

c. The Companies should issue instructions to all claim personnel stating that, pursuant to **N.J.A.C. 11:3-10.5(a)**, insurers are required to settle first party claims within 30 calendar days from receipt.

d. Pursuant to **N.J.A.C. 11:3-10.5(b)** if an insurer is unable to settle claims within the time periods specified, the insurer must send written notices of delay every 30 days as appropriate, until settlement.

2. The Company should remind all appropriate personnel that that the maximum payment period for property liability claims shall be 45 calendar days from receipt by the insurer of notification of claim. If the insurer is unable to settle the property damage claim within the time period specified, the insurer must send to the claimant a written notice of delay after the initial notice of loss and every 45 days thereafter until all elements of the claim are either honored or rejected pursuant to **N.J.A.C. 11:2-17.7(C)2** and **N.J.A.C. 11:2-17.7(e)**.

C. UNDERWRITING

3. Pursuant to **N.J.A.C. 11:3-8.3(e)l**, the Companies must issue written instructions to all appropriate personnel stating that notices of non-renewal shall not be valid unless they include the designated provision(s) of the non-renewal regulation.

APPENDIX A – CLAIM ERRORS

1. Failure to Settle Physical Damage Within 30 days - 10 Files in Error (Average 24 Day Delay)

Member Number*	Claim Number	Claim Type	Notice Date	Date Paid	Days to Pay	Days beyond 30
1	5	Coll	01/07/03	05/05/03	118	88
2	2	Coll	05/02/03	07/06/03	65	35
3	24	Coll	12/01/02	01/20/03	50	20
4	1	Coll	02/12/03	03/25/03	41	11
5	1	Coll	01/15/03	03/03/03	47	17
6	1	Coll	05/16/03	06/17/03	32	2
7	5	Coll	12/04/02	01/17/03	44	14
8	1	Coll	02/11/03	04/04/03	52	22
9	7	Comp	03/31/03	05/27/03	57	27
10	20	Comp	01/29/03	03/03/03	33	3

2. Failure to Settle Denied Property Damage Claims within 45 Days– Database Exceptions Review (Average 53 Day Delay)

Member Number*	Claim Number	Claim Type	Notice Date	Date Denied	Days to Deny	Days beyond 45
11	1	PD	9/27/02	1/10/03	105	60
12	4	PD	11/20/02	1/30/03	71	26
13	18	PD	3/17/03	7/23/03	128	83
14	11	PD	10/18/02	1/13/03	87	42

*Actual member number is personal information and confidentially retained by DOBI in its official files. This number is provided merely to differentiate one claim from the next.

VERIFICATION PAGE

I, Robert Greenfield, am the Examiner-in-Charge of the Market Conduct Examination of the United Services Automobile Association and USAA Casualty Insurance Companies conducted by examiners of the New Jersey Department of Banking and Insurance. This verification is based on my personal knowledge as acquired in my official capacity.

The findings, conclusions and recommendations contained in the foregoing report represent, to the best of my knowledge, a full and true statement of the Market Conduct examination of United Services Automobile Association and USAA Casualty Insurance Companies as of April 27, 2005.

I certify that the foregoing statements are true. I am aware that if any of the foregoing statements made by me is willfully false, I am subject to punishment.

______________________________	______________________________
Date	Robert Greenfield Examiner-In-Charge New Jersey Department of Banking and Insurance