

REPORT ON

MARKET CONDUCT EXAMINATION

of the

PIEDMONT MUTUAL INSURANCE COMPANY

Statesville, North Carolina

BY REPRESENTATIVES OF THE

NORTH CAROLINA DEPARTMENT OF INSURANCE

as of

August 27, 2012

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Raleigh, North Carolina
August 27, 2012

Honorable Wayne Goodwin
Commissioner of Insurance
Department of Insurance
State of North Carolina
Dobbs Building
430 N. Salisbury Street
Raleigh, North Carolina 27603

Honorable Commissioner:

Pursuant to your instructions and in accordance with the provisions of North Carolina General Statute (NCGS) 58-2-131, a general examination has been made of the market conduct activities of

**PIEDMONT MUTUAL INSURANCE COMPANY
(NAIC #17335)**

NAIC Exam Tracking System Exam Number: NC094-M50
Statesville, North Carolina

hereinafter generally referred to as the Company, at the North Carolina Department of Insurance (Department) office located at 11 S. Boylan Avenue, Raleigh, North Carolina. A report thereon is respectfully submitted.

FOREWORD

This examination reflects the North Carolina insurance activities of Piedmont Mutual Insurance Company. The examination is, in general, a report by exception. Therefore, much of the material reviewed will not be contained in this written report, as reference to any practices, procedures, or files that manifested no improprieties were omitted.

SCOPE OF EXAMINATION

This examination commenced on April 23, 2012 and covered the period of January 1, 2008 through December 31, 2010 with analyses of certain operations of the Company being conducted through August 2, 2012. All comments made in this report reflect conditions observed during the period of the examination.

The examination was arranged and conducted by the Department. It was made in accordance with Market Regulation standards established by the Department and procedures established by the National Association of Insurance Commissioners (NAIC) and accordingly included tests of policyholder treatment, marketing, underwriting practices, terminations and claims practices.

It is the Department's practice to cite companies in apparent violation of a statute or rule when the results of a sample show errors/noncompliance at or above the following levels: 0 percent for consumer complaints, sales and advertising, producers who were not appointed and/or licensed, and the use of forms and rates/rules that were neither filed with nor approved by the Department; 7 percent for claims; and 10 percent for all other areas reviewed. When errors are detected in a sample, but the error rate is below the applicable threshold for citing an apparent violation, the Department issues a reminder to the company.

EXECUTIVE SUMMARY

This market conduct examination revealed concerns with Company procedures and practices in the following areas:

Underwriting Practices: Commercial General Liability – producers not properly appointed by the Company. Commercial Fire – producers not properly appointed by the Company.

Specific violations related to each area of concern are noted in the appropriate section of this report. All North Carolina General Statutes and rules of the North Carolina Administrative Code cited in this report may be viewed on the North Carolina Department of Insurance Web site www.ncdoi.com by clicking “INSURANCE DIVISIONS” then “LEGISLATIVE SERVICES”.

This examination identified various non-compliant practices. The Company is directed to take immediate corrective action to demonstrate its ability and intention to conduct business in North Carolina according to its insurance laws and regulations.

All unacceptable or non-compliant practices may not have been discovered or noted in this report. Failure to identify or criticize improper or non-compliant business practices in North Carolina or in other jurisdictions does not constitute acceptance of such practices. Examination report findings that do not reference specific insurance laws, regulations, or bulletins are presented to improve the Company’s practices and ensure consumer protection.

COMPANY OVERVIEW

History and Profile

Piedmont Mutual Insurance Company was incorporated in 1992 as a non-assessable mutual insurance company operating in North Carolina. Effective January 1, 2006, the Company amended its charter and became a limited assessable multiple lines insurance company. Piedmont Mutual Insurance Company is the successor to the Iredell, Alexander and Davie County branch of the Farmers Mutual Fire Insurance Association of North Carolina, which predecessor dates to 1893.

Company Operations and Management

The Company is a writer of personal and commercial coverages. The Company is licensed only in North Carolina.

Direct written premium for the Company in 2010 was \$3,076,227. Premium writings in North Carolina between 2008 and 2010 increased approximately 78.1 percent. The charts below outline the Company's mix of business for selected lines in 2010 and loss ratios for the examination period.

Line of Business	Written Premium	Percentage
Homeowners	\$ 1,809,457	58.8
Fire and Allied Lines	\$ 899,663	29.2
Commercial	\$ 132,189	4.3
Other Liability	\$ 113,303	3.7
Farmowners	\$ 108,543	3.6
Inland Marine	\$ 13,072	0.4
Total	\$ 3,076,227	100.0

Year	Written Premium	Earned Premium	Incurred Losses	Loss Ratio
2008	\$1,727,045	\$1,690,110	\$ 445,843	26.4
2009	\$2,274,713	\$1,956,103	\$ 807,527	41.3
2010	\$3,076,227	\$2,720,715	\$1,248,917	45.9

Certificate of Authority

The Certificates of Authority issued to the Company were reviewed for the period under examination. These certificates were reviewed to determine compliance with the provisions of NCGS 58-7-15. The Company's writings in North Carolina were deemed to be in compliance with the authority granted.

Disaster Recovery Procedures

Piedmont Mutual management has developed a basic disaster recovery plan that will protect the organization and its clients in the event that all or part of its operation and/or

computer services are rendered unusable. The plan is designed to minimize the disruption of operations and ensure some level of organizational stability and an orderly recovery after a disaster. Disasters taken into consideration are theft, fire and catastrophic storm.

POLICYHOLDER TREATMENT

Consumer Complaints

The Company's complaint handling procedures were reviewed to determine compliance with applicable North Carolina statutes and rules. The Company's complaint register was reconciled with a listing furnished by the Consumer Services Division of the Department.

All 12 complaints contained in the Department's listing were selected and received for review. The distribution of complaints requiring a response to the Department is shown in the chart below.

Type of Complaint	Total
Claims	9
Underwriting	3
Total	12

The Company's response to each complaint was deemed to be appropriate to the circumstances.

The average service time to respond to a Departmental complaint was 5.0 calendar days. A chart of the Company's response time follows:

Service Days	Number of Files	Percentage of Total
1 - 7	12	100.0
Total	12	100.0

Privacy of Financial and Health Information

The Company provided privacy of financial and health information documentation for the examiners' review. The Company exhibited policies and procedures in place so that nonpublic personal financial or health information is not disclosed unless the customer or consumer has

authorized the disclosure. The Company was found to be compliant with the provisions of NCGS 58-39-25, 58-39-26, and 58-39-27.

MARKETING

Policy Forms and Filings

Policy forms and filings for the Company were reviewed to determine compliance with appropriate North Carolina statutes and rules. Emphasis of the review was placed on the following lines of business:

1. Homeowners
2. Dwelling Fire
3. Commercial General Liability
4. Commercial Fire

Policy form filings for the dwelling fire line of business were made by the Insurance Services Office (ISO) on the Company's behalf. The homeowners, general liability and commercial fire lines of business utilize American Association of Insurance Services (AAIS) forms, and are filed independently by reference.

The provisions stipulated under 11 NCAC 10.1102(10)(f) exempt the Company from having to submit rate filings to the Department. The Company's rates/rules for homeowners, commercial fire, and commercial general liability are based in part upon the AAIS programs. The Company's rates/rules for its dwelling fire program are based in part upon the North Carolina Rate Bureau (NCRB) and the ISO program.

Sales and Advertising

Sales and advertising practices of the Company were reviewed to determine compliance with the provisions of NCGS 58-63-15. The Company does not conduct any form of advertising.

No unfair or deceptive trade practices were noted in this segment of the examination.

Social Media

The Company reported it does not currently use social media outlets for marketing or advertising purposes.

Producer Licensing

The Company's procedures for appointment and termination of its producers were reviewed to determine compliance with the appropriate North Carolina statutes and rules. Fifty appointed producer files were randomly selected and received for review from a population of 63. The entire population of 5 terminated producer files were selected and received for review.

All appointment and termination forms reviewed were submitted to the Department in accordance with the timetables stipulated under the provisions of NCGS 58-33-40 and 58-33-56.

Agency Management

The Company conducts its business through licensed independent producers. The Company is currently represented by 56 agencies with 74 offices in North Carolina. The marketing effort in North Carolina is the responsibility of the President located in the home office. There are currently no field representatives in the state.

The President is responsible for the activities of the independent agencies. Agency performance reviews are conducted monthly with internal monitoring. Yearly loss ratio and growth are reviewed, with contingency bonuses offered based on these two factors. The Company offers a standard agency contract to its agencies.

UNDERWRITING PRACTICES

Overview

The Company's marketing philosophy in North Carolina focuses on personal and commercial lines. The Company provided the examiners with listings of the following types of active policies for the period under examination:

1. Homeowners

2. Dwelling Fire
3. Commercial General Liability
4. Commercial Fire

A random selection of 200 policies was made from a total population of 4,895. Each policy was reviewed for adherence to underwriting guidelines, file documentation and premium determination. Additionally, the policies were examined to determine compliance with the appropriate North Carolina statutes and rules, policy provisions and the applicable policy manual rules.

Homeowners

The Company provided a listing of 3,505 active homeowners policies issued during the period under examination. Fifty policies were randomly selected and received for review.

The Company's homeowners policies were written on an annual basis. Coverages were written utilizing independent rates. Risk placement was determined by the Company's underwriting guidelines and the underwriter. No discrepancies were noted in the Company's use of its underwriting guidelines.

While the Company is not required to file its rates, the rates must be applied in a fair and consistent manner and in accordance with the Company's rate structure. All files reviewed were deemed rated correctly.

Dwelling Fire

The Company provided a listing of 1,154 active dwelling fire policies issued during the period under examination. Fifty policies were randomly selected and received for review.

The Company's dwelling fire policies were written on an annual basis. Coverages were written utilizing independent rates. Risk placement was determined by the Company's underwriting guidelines and the underwriter. No discrepancies were noted in the Company's use of its underwriting guidelines.

While the Company is not required to file its rates, the rates must be applied in a fair and consistent manner and in accordance with the Company's rate structure. All files reviewed were deemed rated correctly.

Commercial General Liability

The Company provided a listing of 75 active commercial general liability policies issued during the period under examination. Fifty policies were randomly selected and received for review.

The Company's commercial general liability policies were written on an annual basis. Risk placement was determined by the Company's underwriting guidelines and the underwriter.

The Company was deemed to be in apparent violation of the provisions of NCGS 58-33-40 as the producers were not properly appointed by the Company for 11 of the active commercial general liability files reviewed (22.0 percent error ratio).

While the Company is not required to file its rates, the rates must be applied in a fair and consistent manner and in accordance with the Company's rate structure. All files reviewed were deemed rated correctly.

Commercial Fire

The Company provided a listing of 161 active commercial fire policies issued during the period under examination. Fifty policies were randomly selected and received for review.

The Company's commercial fire policies were written on an annual basis. Risk placement was determined by the Company's underwriting guidelines and the underwriter.

The Company was deemed to be in apparent violation of the provisions of NCGS 58-33-40 as the producers were not properly appointed by the Company for 7 of the active commercial fire files reviewed (14.0 percent error ratio).

While the Company is not required to file its rates, the rates must be applied in a fair and consistent manner and in accordance with the Company's rate structure. All files reviewed were deemed rated correctly.

TERMINATIONS

Overview

The Company's termination procedures were reviewed to determine compliance with the appropriate North Carolina statutes and rules, policy provisions and the applicable policy manual rules. The review focused on the following lines of business:

1. Homeowners
2. Dwelling Fire
3. Commercial General Liability
4. Commercial Fire

Special attention was placed on the validity and reason for termination, timeliness in issuance of the termination notice, policy refund (where applicable) and documentation of the policy file. A total of 2,391 policies were terminated during the period under examination. The examiners randomly selected 375 terminations for review.

Homeowners Cancellations

Fifty cancelled homeowners policies were randomly selected and received for review from a population of 991.

The reason for cancellation was deemed valid for all policies reviewed. The review revealed the following reasons for cancellation:

Reason for Cancellation	Number of Policies	Percentage
Nonpayment of premium	23	46.0
Insured's request	13	26.0
Finance company request	7	14.0
Underwriting reasons	6	12.0
Coverage rewritten	1	2.0
Total	50	100.0

The Company was not required to issue cancellation notices for 21 of the cancellations reviewed as these policies were cancelled at the request of the insured or the premium finance company, or coverage was rewritten. Cancellation notices for the remaining 29 policies stated the specific reason for cancellation.

All premium refunds were deemed correct. The Company issued the refunds in a timely manner.

The final area of this review encompassed documentation of the policy file. All policy files reviewed contained sufficient documentation to support the action taken by the Company.

Dwelling Fire Cancellations

Fifty cancelled dwelling fire policies were randomly selected and received for review from a population of 967.

The reason for cancellation was deemed valid for all policies reviewed. The review revealed the following reasons for cancellation:

Reason for Cancellation	Number of Policies	Percentage
Nonpayment of premium	24	48.0
Insured's request	14	28.0
Coverage rewritten	8	16.0
Finance company request	2	4.0
Underwriting reasons	2	4.0
Total	50	100.0

The Company was not required to issue cancellation notices for 24 of the cancellations reviewed as these policies were cancelled at the request of the insured or the premium finance company, or the coverage was rewritten. Cancellation notices for the remaining 26 policies stated the specific reason for cancellation.

All premium refunds were deemed correct. The Company issued the refunds in a timely manner.

The final area of this review encompassed documentation of the policy file. All policy files reviewed contained sufficient documentation to support the action taken by the Company.

Commercial General Liability Cancellations

Fifty cancelled commercial general liability policies were randomly selected and received for review from a population of 63.

The reason for cancellation was deemed valid for all policies reviewed. The review revealed the following reasons for cancellation:

Reason for Cancellation	Number of Policies	Percentage
Finance company request	31	62.0
Nonpayment of premium	14	28.0
Insured's request	4	8.0
Underwriting reasons	1	2.0
Total	50	100.0

The Company was not required to issue cancellation notices for 35 of the cancellations reviewed as these policies were cancelled at the request of the insured or the premium finance company. Cancellation notices for the remaining 15 policies stated the specific reason for cancellation.

All premium refunds were deemed correct. The Company issued the refunds in a timely manner.

The final area of this review encompassed documentation of the policy file. The remaining policy files reviewed contained sufficient documentation to support the action taken by the Company.

Commercial Fire Cancellations

Fifty cancelled commercial fire policies were randomly selected and received for review from a population of 109.

The reason for cancellation was deemed valid for all policies reviewed. The review revealed the following reasons for cancellation:

Reason for Cancellation	Number of Policies	Percentage
Nonpayment of premium	22	44.0
Insured's request	19	38.0
Coverage rewritten	4	8.0
Finance company request	3	6.0
Underwriting reasons	2	4.0
Total	50	100.0

The Company was not required to issue cancellation notices for 26 of the cancellations reviewed as these policies were cancelled at the request of the insured or the premium finance company, or the coverage was rewritten. Cancellation notices for the remaining 24 policies stated the specific reason for cancellation.

All premium refunds were deemed correct. The Company issued the refunds in a timely manner.

The final area of this review encompassed documentation of the policy file. All policy files reviewed contained sufficient documentation to support the action taken by the Company.

Homeowners Nonrenewals

Fifty nonrenewed homeowners policies were randomly selected and received for review from a population of 92.

The reason for nonrenewal was deemed valid for all policies reviewed. The review revealed the following reasons for nonrenewal:

Reason for Nonrenewal	Number of Policies	Percentage
Underwriting reasons	50	100.0
Total	50	100.0

The nonrenewal notices for the policies reviewed stated the specific reason for nonrenewal.

The final area of this review encompassed documentation of the policy file. All files reviewed contained sufficient documentation to support the action taken by the Company.

Dwelling Fire Nonrenewals

Fifty nonrenewed dwelling fire policies were randomly selected and received for review from a population of 94.

The reason for nonrenewal was deemed valid for all policies reviewed. The review revealed the following reason for nonrenewal:

Reason for Nonrenewal	Number of Policies	Percentage
Underwriting reasons	50	100.0
Total	50	100.0

The nonrenewal notices for the policies reviewed stated the specific reason for nonrenewal.

The final area of this review encompassed documentation of the policy file. All files reviewed contained sufficient documentation to support the action taken by the Company.

Commercial General Liability Nonrenewals

The entire population of 30 nonrenewed commercial general liability policies was selected and received for review.

The reason for nonrenewal was deemed valid for all policies reviewed. The review revealed the following reason for nonrenewal:

Reason for Nonrenewal	Number of Policies	Percentage
Underwriting reasons	30	100.0
Total	30	100.0

The nonrenewal notices for the policies reviewed stated the specific reason for nonrenewal.

The final area of this review encompassed documentation of the policy file. All files reviewed contained sufficient documentation to support the action taken by the Company.

Commercial Fire Nonrenewals

The entire population of 45 nonrenewed commercial fire policies was selected and received for review.

The reason for nonrenewal was deemed valid for all policies reviewed. The review revealed the following reason for nonrenewal:

Reason for Nonrenewal	Number of Policies	Percentage
Underwriting reasons	45	100.0
Total	45	100.0

The nonrenewal notices for the policies reviewed stated the specific reason for nonrenewal.

The final area of this review encompassed documentation of the policy file. All files reviewed contained sufficient documentation to support the action taken by the Company.

Declinations/Rejections

The Company reported no declinations/rejections during the exam period.

CLAIMS PRACTICES

Overview

The Company's claims practices were reviewed to determine compliance with the appropriate North Carolina statutes and rules and policy provisions. The review encompassed paid, first and third party bodily injury and closed without payment claims.

The Claims Manager located in the home office oversees the Company's claims operations. Independent adjusters are engaged on an as-needed basis and do not hold any draft authority. The Company's agency force does not adjust any claims.

One hundred three claims were selected for review from a population of 650.

Paid Claims

The examiners randomly selected and received 50 of the 265 first party property damage claims paid during the period under examination. The claim files were reviewed for timeliness of payment, supporting documentation and accuracy of payment.

The following type of claim was reviewed and the average payment time is noted in calendar days:

Type of Claim	Payment Time
First party property damage	19.6

All payments issued by the Company were deemed to be accurate. Deductibles were correctly applied and depreciation taken was reasonable.

All claim files reviewed contained documentation to support the Company's payments. The documentation consisted of appraisals, estimates, repair bills, or inventory listings.

First and Third Party Bodily Injury Claims

The entire population of 3 first and third party bodily injury claims was selected and received for review. The claim files were reviewed to determine whether the Company had engaged in any unfair claims practices. The review of first and third party bodily injury claims disclosed no apparent violations of the provisions of NCGS 58-63-15(11).

Closed Without Payment Claims

Fifty closed without payment claims were randomly selected and received for review from a population of 382. The claim files were reviewed to determine if the Company's reasons for closing the claims without payment were valid.

The claim files reviewed contained documentation that supported the Company's reasons for closing the claims without payment. All reasons for denial or closing the files without payment were deemed valid. Claims were denied on an average of 10.9 calendar days

for the 3-year period. The review of closed without payment claims disclosed no apparent violations of the provisions of NCGS 58-63-15(11).

Subrogated Claims

The Company informed the examiners that it did not have any subrogated claims during the period under examination.

Litigated Claims

The Company informed the examiners that it did not have any litigated claims during the period under examination.

SUMMARY

The Market Conduct examination revealed the following:

Underwriting Practices

- a. The Company was deemed to be in apparent violation of the provisions of NCGS 58-33-40 as the producers were not properly appointed by the Company for 22.0 percent of the active commercial general liability files reviewed.
- b. The Company was deemed to be in apparent violation of the provisions of NCGS 58-33-40 as the producers were not properly appointed by the Company for 14.0 percent of the active commercial fire files reviewed.

TABLE OF STATUTES AND RULES

<u>Statute/Rule</u>	<u>Title</u>
NCGS 58-2-131	Examinations to be made; authority, scope, scheduling, and conduct of examinations.
NCGS 58-7-15	Kinds of insurance authorized.
NCGS 58-33-40	Appointment of agents.
NCGS 58-33-56	Notification to Commissioner of termination.
NCGS 58-39-25	Notice of insurance information practices.
NCGS 58-39-26	Federal privacy disclosure notice requirements.

NCGS 58-39-27	Privacy notice and disclosure requirement exceptions.
NCGS 58-63-15	Unfair methods of competition and unfair or deceptive acts or practices defined.
11 NCAC 10.1102	Rate Filings - Applicability

CONCLUSION

An examination has been conducted on the market conduct affairs of Piedmont Mutual Insurance Company for the period January 1, 2008 through December 31, 2010 with analyses of certain operations of the Company being conducted through August 2, 2012.

This examination was conducted in accordance with the North Carolina Department of Insurance and the National Association of Insurance Commissioners Market Regulation Handbook procedures, including analyses of Company operations in the areas of policyholder treatment, marketing, underwriting practices, terminations and claims practices.

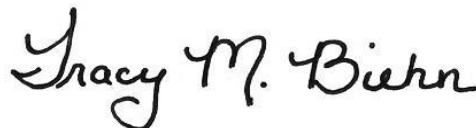
In addition to the undersigned, Gary Jones and Gina Abate, North Carolina Market Conduct Examiners, participated in this examination and in the preparation of this report.

Respectfully submitted,



James P. McQuillan, CPCU, AIT
Examiner-In-Charge
Market Regulation Division

I have reviewed this examination report and it meets the provisions for such reports prescribed by this Division and the North Carolina Department of Insurance.



Tracy M. Biehn, LPCS, MBA
Deputy Commissioner
Market Regulation Division
State of North Carolina