



Report on

Market Conduct Examination

of

Stonewood Insurance Company

Chapel Hill, North Carolina

by Representatives of the
North Carolina Department of Insurance

as of

November 20, 2014

TABLE OF CONTENTS

SALUTATION 1

SCOPE OF EXAMINATION 2

EXECUTIVE SUMMARY..... 2

MARKETING 3

 Policy Forms and Filings 3

UNDERWRITING PRACTICES 4

 Overview 4

 Private Passenger Automobile 4

 Workers' Compensation..... 5

TERMINATIONS..... 6

 Overview 6

 Private Passenger Automobile Cancellations 6

 Workers' Compensation Cancellations..... 7

 Workers' Compensation Nonrenewals 8

COMMENTS, RECOMMENDATIONS AND DIRECTIVES..... 8

CONCLUSION..... 9

Raleigh, North Carolina
November 20, 2014

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 through 58-2-134, a target examination has been made of the market conduct activities of

Stonewood Insurance Company (NAIC #11828)
NAIC Exam Tracking System Exam Number: NC299-M64
Chapel Hill, North Carolina

hereinafter generally referred to as the Company, at the Company's headquarters located at 6131 Falls of Neuse Road, Raleigh, North Carolina. A report thereon is respectfully submitted.

SCOPE OF EXAMINATION

This examination commenced on September 15, 2014, and covered the period of January 1, 2012, through December 31, 2013, with analyses of certain operations of the Company being conducted through November 20, 2014. All comments made in this report reflect conditions observed during the period of the examination.

This examination was performed in accordance with auditing standards established by the Department and procedures established by the National Association of Insurance Commissioners (NAIC). The scope of this examination was not comprehensive, but included a limited review of the Company's practices and procedures in marketing, underwriting practices, and terminations. The findings and conclusions contained within the report are based solely on the work performed on the specific areas of concern and are referenced within the appropriate sections of the examination report.

It is the Department's practice to cite companies in violation of a statute or rule when the results of a sample show errors/noncompliance at or above the following levels: 0 percent for 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; and 10 percent for all other areas reviewed.

EXECUTIVE SUMMARY

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

Marketing - Notice of cancellation for private passenger automobile was not the most recent form filed with and approved by the Department.

Underwriting Practices – Private Passenger Automobile: Unappointed producers; inapplicable credits listed on declarations page; recoupment surcharge calculated without allowing for producer compensation; and rating errors. Workers' Compensation: Unappointed producers.

Terminations – Private Passenger Automobile Cancellations: Improper number of days' notice; and proper notice not given to the loss payee. Workers' Compensation

Nonrenewals: Precise reason for termination not stated on the notice and no proof of mailing of the nonrenewal notice.

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 statutory violations, some of which may extend to other jurisdictions. 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. When applicable, corrective action for other jurisdictions should be addressed.

All statutory violations may not have been discovered or noted in this report. Failure to identify statutory violations in North Carolina or in other jurisdictions does not constitute acceptance of such violations.

MARKETING

Policy Forms and Filings

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

1. Private Passenger Automobile
2. Workers' Compensation

Filings for the private passenger automobile and workers' compensation lines of business were made by the North Carolina Rate Bureau on behalf of the Company.

The Company was deemed to be in violation of NCGS 58-36-85(c) as the notice of cancellation form for private passenger automobile used after December 1, 2013, was not the most recent form filed with and approved by the Department.

UNDERWRITING PRACTICES

Overview

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

1. Private Passenger Automobile
2. Workers' Compensation

A random selection of 100 policies was made from a total population of 720. 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.

Private Passenger Automobile

The Company provided a listing of 360 active private passenger automobile policies issued during the period under examination. Fifty policies were randomly selected for review.

The Company's private passenger automobile coverages were written utilizing manual rates. Policies were written on an annual or semi-annual basis. 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. All policy files contained sufficient documentation to support the Company's classification of the risk.

The Company was deemed to be in violation of the provisions of NCGS 58-33-26 and 58-33-40 as the producer was not properly appointed by the Company for 50 of the files reviewed (100 percent error ratio).

The Company was deemed to be in violation of NCGS 58-63-15(1) as it indicated on the declarations page of seven policies reviewed (14.0 percent error ratio) that an airbag credit applied, although medical payments coverage was not included on the policies.

The Company was deemed to be in violation of NCGS 58-37-40(f) and Section 4, Chapter 13, Item C. Surcharges, 11.c of the North Carolina Reinsurance Facility Standard Practice Manual as it did not include producer compensation in the calculation of the recoupment surcharge for 50 policies reviewed (100 percent error ratio) resulting in an undercharge of the recoupment surcharge.

The Company was deemed to be in violation of NCGS 58-37-35(l) and Rule 5 of the Personal Auto Manual as 25 policies (50.0 percent error ratio) had a total of 28 rating errors:

- An increased limit factor was applied to medical payments premium from a rate table that already incorporated the factor on 14 policies.
- An increased limit factor was applied to property damage premium from a rate table that already incorporated the factor on four policies.
- Incorrect physical damage symbols were used to rate comprehensive and collision coverage on four policies.
- A Safe Driver Insurance Plan (SDIP) surcharge was incorrectly applied to uninsured motorists premium on four policies.
- SDIP points were not properly charged on two policies.

The rating errors resulted in five undercharges and 20 overcharges to the insureds. At the request of the examiners, refunds in the amount of \$219.14 were issued by the Company for the overcharges.

As a result of the rating errors, the examiners requested that the Company conduct a self-audit. The Company identified 567 policies (including multiple policy terms) resulting in overcharges in the amount of \$4,976.56. All overcharges were returned to the policyholders prior to the conclusion of the examination.

Workers' Compensation

The Company provided a listing of 360 active workers' compensation policies issued during the period under examination. Fifty policies were randomly selected for review.

The Company's workers' compensation coverages were written utilizing manual and deviated rates. Policies were written on an annual and pro-rata basis. 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. All files contained sufficient documentation to support the Company's classification of the risk.

The Company was deemed to be in violation of the provisions of NCGS 58-33-26 and 58-33-40 as the producer was not properly appointed by the Company for four of the files reviewed (8.0 percent error ratio).

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 was based on the following lines of business:

1. Private Passenger Automobile
2. Workers' Compensation

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 956 policies were terminated during the period under examination. The examiners randomly selected 141 terminations for review.

Private Passenger Automobile Cancellations

The entire population of 41 cancelled private passenger automobile policies was selected for review. The reason for cancellation was deemed valid for all policies reviewed. The review revealed the following reason for cancellation:

Reason for Cancellation	Number of Policies	Percentage
Nonpayment of premium	41	100.0
Total	41	100.0

Cancellation notices for the 41 cancelled policies reviewed stated the specific reason for cancellation.

The Company was deemed to be in violation of NCGS 58-36-85(c) and the policy termination provisions as five cancellation notices (12.2 percent error ratio) were not issued at least 15 days prior to the cancellation date of the policy.

The Company was deemed to be in violation of the policy termination provisions as the loss payee was not given proper notification of termination for five cancelled policies reviewed (12.2 percent error ratio).

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.

Workers' Compensation Cancellations

Fifty cancelled workers' compensation policies were randomly selected for review from a population of 319.

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
Non-payment of premium	38	76.0
Insured's request	8	16.0
Underwriting reasons	4	8.0
Total	50	100.0

The Company was not required to issue cancellation notices for eight of the cancellations reviewed as these policies were cancelled at the request of the insured. All

cancellation notices stated the specific reason for cancellation. All insureds were given proper and timely notification of cancellation.

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

Workers' Compensation Nonrenewals

Fifty nonrenewed workers' compensation policies were randomly selected for review from a population of 596.

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	46	92.0
Producer no longer represents company	4	8.0
Total	50	100.0

The Company was deemed to be in violation of 58-36-110(e) as the nonrenewal notice for 14 of the nonrenewed workers' compensation policies reviewed (28.0 percent error ratio) did not state the precise reason for nonrenewal.

The final area of this review encompassed documentation of the policy file. The Company was deemed to be in violation of Title 11 of the North Carolina Administrative Code, Chapter 19, Sections 0102(a), 0104, and 0106(a)(4),(g) as ten of the nonrenewed workers' compensation files reviewed (20.0 percent error ratio) did not contain proof of mailing of the nonrenewal notice.

COMMENTS, RECOMMENDATIONS AND DIRECTIVES

The Company must ascertain whether producers who submit applications for insurance to the Company are properly appointed. For private passenger automobile new business, the Company must calculate recoupment surcharges to include the amount necessary to recover

compensation paid to producers. Premium credits must be accurately displayed on declarations pages and premiums should be calculated correctly. For terminations, the Company is directed to give the proper number of days' notice to the insured and state the precise reason for termination. The Company must deliver termination notices to loss payees according to the policy termination provisions. The Company must issue cancellation notices with the most recent form filed with and approved by the Department and retain the proof of mailing of the termination notice for at least five years.

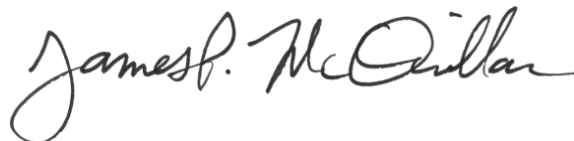
CONCLUSION

An examination has been conducted on the market conduct affairs of Stonewood Insurance Company for the period January 1, 2012, through December 31, 2013, with analyses of certain operations of the Company being conducted through November 20, 2014.

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 marketing, underwriting practices, and terminations.

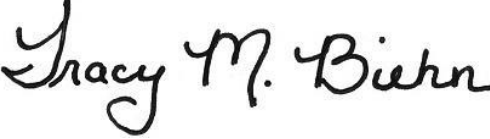
In addition to the undersigned, Larry Cook, CPCU, CIC, AU, ARe, ARM, AIM, AMIM, AIAF, AAI, North Carolina Market Conduct Examiner, participated in this examination.

Respectfully submitted,

A handwritten signature in black ink that reads "James P. McQuillan". The signature is written in a cursive style with a large, looped initial "J".

James P. McQuillan, CPCU, AIT
Examiner-In-Charge
Market Regulation Division
State of North Carolina

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.

A handwritten signature in black ink that reads "Tracy M. Biehn". The signature is written in a cursive, flowing style.

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