

STATE OF ARIZONA
FILED

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DEPT. OF INSURANCE

REPORT OF TARGET MARKET CONDUCT EXAMINATION

OF

AMERICAN SECURITY INSURANCE COMPANY

NAIC # 42978

AS OF

JUNE 30, 2008

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CHRISTINA URIAS
Director of Insurance

Honorable Christina Urias
Director of Insurance
State of Arizona
2910 North 44th Street
Suite 210, Second Floor
Phoenix, Arizona 85108-7256

Dear Director Urias:

Pursuant to your instructions and in conformity with the provisions of the Insurance Laws and Rules of the State of Arizona, an examination has been made of the market conduct affairs of the:

AMERICAN SECURITY INSURANCE COMPANY
NAIC # 42978

The above examination was conducted by William Hobert, Examiner-in Charge, and Market Conduct Examiner James Warrington.

The examination covered the period of July 1, 2007 through June 30, 2008.

As a result of that examination, the following Report of Examination is respectfully submitted.

Sincerely yours,

Helene I. Tomme, CPCU, CIE
Market Conduct Examinations Supervisor
Market Oversight Division

AFFIDAVIT

STATE OF ARIZONA)
)
County of Maricopa) ss.

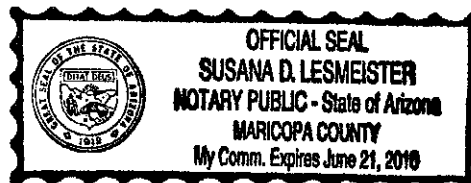
William P. Hobert being first duly sworn, states that I am a duly appointed Market Conduct Examinations Examiner-in-Charge for the Arizona Department of Insurance. That under my direction and with my participation and the participation of Market Conduct Examiner James Warrington on the Examination of American Security Insurance Company, hereinafter referred to as the "Company" was performed at the examiners' residences. A teleconference meeting with appropriate Company officials was held to discuss this Report, but a copy was not provided to management as the Examination was incomplete and had not yet been finalized. The information contained in this Report, consists of the following pages, is true and correct to the best of my knowledge and belief and that any conclusions and recommendations contained in and made a part of this Report are such as may be reasonably warranted from the facts disclosed in the Examination Report.

William P. Hobert
William P. Hobert, CPCU, CLU, CIE
Market Conduct Examinations Supervisor
Market Oversight Division

Subscribed and sworn to before me this 21st day of May, 2009.

Susana D. Lesmeister
Notary Public

My Commission Expires June 21, 2010



FOREWORD

This target market conduct examination report of American Security Insurance Company (herein referred to as the "Company"), was prepared by employees of the Arizona Department of Insurance (Department) as well as independent examiners contracting with the Department. A target market conduct examination is conducted for the purpose of auditing certain business practices of insurers licensed to conduct the business of insurance in the state of Arizona. The examiners conducted the examination of the Company in accordance with Arizona Revised Statutes (A.R.S.) §§ 20-142, 20-156, 20-157, 20-158 and 20-159. The findings in this report, including all work product developed in the production of this report, are the sole property of the Department.

The examination consisted of a review of the following Homeowner, Dwelling Fire, Force Placed Hazard, Involuntary Unemployment and Leave of Absence insurance operations:

1. Complaint Handling
2. Marketing and Sales
3. Producer Compliance
4. Underwriting and Rating
5. Cancellations and Nonrenewals
6. Claims Processing, including Adjuster Licensing

Certain unacceptable or non-complying practices may not have been discovered in the course of this examination. Additionally, findings may not be material to all areas that would serve to assist the Director.

Failure to identify or criticize specific Company practices does not constitute acceptance of those practices by the Department.

SCOPE AND METHODOLOGY

The examination of the Company was conducted in accordance with the standards and procedures established by the National Association of Insurance Commissioners (NAIC) and the Department. The market conduct examination of the Company covered the period of July 1,

2007 through June 30, 2008 for business reviewed. The purpose of the examination was to determine the Company's compliance with Arizona's insurance laws, and whether the Company's operations and practices are consistent with the public interest. This examination was completed by applying tests to each examination standard to determine compliance with the standard. Each standard applied during the examination is stated in this report and the results are reported beginning on page 7.

In accordance with Department procedures, the examiners completed a Preliminary Finding ("Finding") form on those policies, claims and complaints not in apparent compliance with Arizona law. The finding forms were submitted for review and comment to the Company representative designated by Company management to be knowledgeable about the files. For each finding the Company was requested to agree, disagree or otherwise justify the Company's noted action.

The examiners utilized both examinations by test and examination by sample. Examination by test involves review of all records within the population, while examination by sample involves the review of a selected number of records from within the population. Due to the small size of some populations examined, examination by test and by sample were completed without the need to utilize computer software.

File sampling was based on a review of underwriting and claim files that were systematically selected by using Audit Command Language (ACL) software and computer data files provided by the Company. Samples are tested for compliance with standards established by the NAIC and the Department. The tests applied to sample data will result in an exception ratio, which determines whether or not a standard is met. If the exception ratio found in the sample is, generally less than 5%, the standard will be considered as "met." The standard in the areas of procedures and form use will not be met if any exception is identified.

HISTORY OF THE COMPANY

The Company is a Delaware corporation incorporated on November 13, 1958. The Company is a wholly owned subsidiary of Interfinancial, Inc. a Georgia corporation. Previously acquired by Fortis International N.V. in the Netherlands, a diversified banking and insurance services holding company, in early 2004, the Company was spun off with other of Fortis' domestic operations in an initial public offering. This IPO created a new US holding company, Assurant, Inc., collectively known as Assurant, Inc., NYSE ticker symbol AIZ. Assurant, Inc.

has four key business units - (1) Assurant Employee Benefits, (2) Assurant Health, (3) Assurant Solutions and (4) Assurant Specialty Property. The Company is part of Assurant Specialty Property

The Company is both a holding company and a licensed property and casualty insurance company. As a holding company, it is the sole shareowner of Standard Guaranty Insurance Company, a Delaware corporation. As a P&C insurer, the Company is licensed in all fifty states except New Hampshire, the District of Columbia, the US Virgin Islands and Puerto Rico. The Company's products are primarily distributed through financial institutions.

PROCEDURES REVIEWED WITHOUT EXCEPTION

The examiners review of the following Company departments¹ or functions indicates that they appear to be in compliance with Arizona statutes and rules:

Complaint Handling Marketing & Sales Producer Compliance Adjuster Licensing

EXAMINATION REPORT SUMMARY

The examination revealed three (3) compliance issues that resulted in thirty (30) exceptions due to the Company's failure to comply with statutes and rules that govern all insurers operating in Arizona. These issues were found in three (3) of the six (6) sections of Company operations examined. The following is a summary of the examiners' findings:

Underwriting and Rating

In the area of Underwriting and Rating, one (1) compliance issue is addressed in this report. The Company failed on five (5) Dwelling Fire (DW) policies to accurately determine premium consistent with the Company's filed rating plan.

Cancellation and Nonrenewals

In the area of Cancellations and Nonrenewals, one (1) compliance issue is addressed in this report. The Company failed to provide fifteen (15) cardholders / debtors prior notification of coverage termination.

¹ If a department name is listed there were no exceptions noted during the review.

Claims Processing

In the area of Claims Processing, one (1) compliance issue is addressed in this report. The Company failed on three (3) claim forms and seven (7) claim letters to provide a fraud warning.

FACTUAL FINDINGS

RESULTS OF PREVIOUS MARKET EXAMINATIONS

During the past three (3) years, the Company had a market conduct examination conducted by Pennsylvania.

FACTUAL FINDINGS

UNDERWRITING AND RATING

Homeowner, Dwelling Fire, Force Placed Hazard & Involuntary Unemployment

The examiners reviewed fifty (50) Homeowner new business and renewal policies from a population of 258; fifty (50) Dwelling Fire new business and renewal policies from a population of eighty-one (81); and one hundred (100) Force Placed Hazard insurance new business and renewal policies from a population of 26,549.

The Company during the exam period wrote no new Involuntary Unemployment or Leave of Absence insurance policies. The examiners found five (5) rating exceptions. No processing / form exceptions were found.

The following Underwriting and Rating Standards were met:

| # | STANDARD | Regulatory Authority |
|---|---|---|
| 2 | Disclosures to insureds concerning rates and coverage are accurate and timely. | A.R.S. §§ 20-1608, 20-2104, 20-2106, 20-2110, 20-2113 |
| 3 | All mandated disclosures are documented and in accordance with applicable statutes, rules and regulations, including, but not limited to, the Notice of Insurance Information Practices and the Authorization for Release of Information. | A.R.S. §§ 20-1608, 20-2104, 20-2106, 20-2110, 20-2113 |
| 4 | All forms and endorsements forming a part of the contract should be filed with the director (if applicable). | A.R.S. §§ 20-398, 20-1609, 20-1612 |
| 5 | File documentation adequately supports decisions made. | A.R.S. § 20-385 |
| 6 | Policies and endorsements are issued or renewed accurately, timely and completely. | A.R.S. §§ 20-1120, 20-1121, 20-1654 |
| 7 | Rescissions are not made for non-material misrepresentations. | A.R.S. §§ 20-463, 20-1109 |

The following Underwriting and Rating Standard failed:

| # | STANDARD | Regulatory Authority |
|---|--|--|
| 1 | The rates charged for the policy coverage are in accordance with filed rates (if applicable) or the Company Rating Plan. | A.R.S. §§ 20-341 through 20-385, 20-1609, 20-1610) |

Underwriting and Rating Standard # 1 failed

Preliminary Finding #1 – Policy Premium Determination – The Company failed to charge rates for policy coverage in accordance with filed rates, by providing a fire premium credit to policyholders that did not qualify, on five (5) Dwelling Fire policies. These are violations of A.R.S. § 20-385(A).

UNDERWRITING AND RATING

Failed to charge rates for policy coverage in accordance with filed rates
A.R.S. § 20-385(A)

| Population | Sample | # of Exceptions | % to Sample |
|-------------------|---------------|------------------------|--------------------|
| 81 | 50 | 5 | 10.0% |

A 10% error ratio does not meet the Standard; therefore, a recommendation is warranted.

Recommendation #1

Within 90 days of the filed date of this report, provide the Department with documentation that Company programming, procedures and controls are in place to ensure that the rates charged for the policy coverage are in accordance with filed rates.

Subsequent Event

All five (5) Dwelling Fire policies charged the incorrect fire rates by providing a fire premium credit to policyholders that did not qualify. This error resulted in premium undercharges. No restitution was necessary.

Recommendation #2

Within 90 days of the filed date of this report, provide the Department with documentation that Company has completed a self-audit of property only Dwelling Fire policy premiums and reimbursed policyholders where premiums were impacted solely based on the breed of the household's dog.

Subsequent Event

The Company will incorporate specific verbiage in their premium quoting system to remind producers to select aggressive dog breeds only on policies where the insured has opted for liability coverage.

CANCELLATIONS AND NON-RENEWALS

Homeowner, Dwelling Fire, Force Placed Hazard & Involuntary Unemployment

The examiners reviewed:

- (1) fifty (50) Homeowner non-payment cancellations from a population of 220, both non-renewals and fifty (50) other cancellations from a population of 167.;
- (2) all twenty-eight (28) Dwelling Fire non-payment cancellations, the only non-renewal, and all thirteen (13) other cancellations;
- (3) both Force Placed Hazard non-payment cancellations, fifty (50) non-renewals from a population of 121, and one hundred (100) other cancellations from a population of 13,537; and
- (4) fifty (50) Involuntary Unemployment and/or Leave of Absence cancellations from a population of 4,830.

The following Cancellation and Non-Renewal Standards were met:

| # | STANDARD | Regulatory Authority |
|---|---|---|
| 1 | Declinations, Cancellations and Non-Renewal shall comply with state laws and Company including the Summary of Rights to be given to the applicant and shall not be unfairly discriminatory. | A.R.S. §§ 20-448, 20-2108, 20-2109, 20-2110 |
| 3 | Group consumer credit insurance policies and certificates are terminated in accordance with applicable statutes, rules and regulations. | A.R.S. §§ 20-1608, 20-1611 |
| 4 | The effective dates and termination dates of coverage are in accordance with applicable statutes, rules and regulations. | A.R.S. §§ 20-1608, 20-1611 |

The following Cancellation and Non-Renewal Standard failed:

| # | STANDARD | Regulatory Authority |
|---|--|--|
| 2 | Cancellation and Non-Renewal notices comply with state laws, Company guidelines and policy provisions, including the amount of advance notice required and grace period provisions to the policyholder, nonrenewal based on condition of premises, and shall not be unfairly discriminatory. | A.R.S. §§ 20-191, 20-443, 20-448, 20-1631, 20-1632, 20-1632.01 |

Cancellation and Non-Renewal Standard #2 failed

Preliminary Finding #3 – The Company failed to provide fifteen (15) cardholders/debtors prior notification of their coverage termination, in violation of the Company’s policy provisions. This failure to send cancellation notice is a violation of A.R.S. § 20-443.

CONSUMER CREDIT CANCELLATIONS

Failed to provide prior notice of cancellation to cardholder/debtor

Violation of policy provisions

A.R.S. § 20-443

| Population | Sample | # of Exceptions | % to Sample |
|-------------------|---------------|------------------------|--------------------|
| 4,830 | 50 | 15 | 30.0% |

A 30% error ratio does not meet the Standard; therefore, a recommendation is warranted.

Recommendation #3

Within 90 days of the filed date of this report, provide documentation to the Department that Company procedures and controls are in place to ensure that cardholders/debtors are provided notice prior to the termination of coverage.

CLAIMS PROCESSING

Homeowner, Dwelling Fire, Force Placed Hazard & Involuntary Unemployment

The examiners reviewed:

- (1) all eighteen (18) Homeowner claims paid and all twenty-five (25) Homeowner claims closed without payment;
- (2) all four (4) Dwelling Fire claims paid and the only Dwelling Fire claim closed without payment;
- (3) fifty (50) Forced Placed Hazard claims paid from a population of 319 and fifty (50) Forced Placed Hazard claims closed without payment from a population of 305; and
- (4) all nine (9) Involuntary Unemployment claims paid and all fifteen (15) Involuntary Unemployment claims closed without payment. There were no Leave of Absence claims.

All claim files were reviewed to ensure compliance with Arizona Statutes and Rules.

The following Claim Processing Standards were met:

| # | STANDARD | Regulatory Authority |
|----|---|---|
| 1 | The initial contact by the Company with the claimant is within the required time frame. | A.R.S. § 20-461, A.A.C. R20-6-801 |
| 2 | Timely investigations are conducted. | A.R.S. § 20-461, 20-1613, A.A.C. R20-6-801 |
| 4 | Claim files are adequately documented in order to be able to reconstruct the claim. | A.R.S. §§ 20-461, 20-463, 20-466.03, A.A.C. R20-6-801 |
| 5 | Claims are properly handled in accordance with policy provisions and applicable statutes, rules and regulations. | A.R.S. §§ 20-461, 20-462, 20-1613, A.A.C. R20-6-801 |
| 6 | The Company uses reservation of rights and excess of loss letters, when appropriate. | A.R.S. § 20-461, A.A.C. R20-6-801 |
| 7 | Deductible reimbursement to insured upon subrogation recovery is made in a timely and accurate manner. | A.R.S. §§ 20-461, 20-462, A.A.C. R20-6-801 |
| 8 | The Company responds to claim correspondence in a timely manner. | A.R.S. §§ 20-461, 20-462, 20-1613, A.A.C. R20-6-801 |
| 9 | Denied and closed without payment claims are handled in accordance with policy provisions and state law. | A.R.S. §§ 20-461, 20-462, 20-463, 20-466, 20-2110, A.A.C. R20-6-801 |
| 10 | No insurer shall fail to fully disclose to first party insureds all pertinent benefits, coverages, or other provisions of an insurance policy or insurance contract under which a claim is presented. | A.R.S. § 20-1608, A.A.C. R20-6-801 |
| 11 | Adjusters used in the settlement of claims are properly licensed. | A.R.S. §§ 20-321 through 20-321.02, 20-1613 |

The following Claim Processing Standard failed:

| # | STANDARD | Regulatory Authority |
|---|--|--|
| 3 | The Company claim forms are appropriate for the type of product and comply with statutes, rules and regulations. | A.R.S. §§ 20-461, 20-466.03, 20-2106, A.A.C. R20-6-801 |

Claims Processing Standard #3 failed

Preliminary Finding #4 – Fraud Warning Statement – The Company failed to include the fraud warning statement on three (3) claim forms and seven (7) claim letters in violation of A.R.S. § 20-466.03.

The following table summarizes these fraud warning statement findings:

| | Form / Letter Description | Form / Letter # | ADOI ID # |
|--|---|-----------------|-----------|
| 1 | Employer's Statement Unemployment/LOA Claim | None | CCWP-6 |
| 2 | Request for Account Information | RS221 0904 | CCWP-7 |
| 3 | Personal Property Summary Sheet | None | HOCWP-3 |
| Letters requiring affirmative response from recipients - | | | |
| 4 | 1/28/08 Alvarez Letter | None | HOCWP-23 |
| 5 | 4/29/08 Thompson Letter | None | HOPD-12 |
| 6 | 2/18/08 Ferguson Letter | ID8 | CCPD-9 |
| 7 | 4/29/08 Joss Letter | ir00fy | CCWP-1 |
| 8 | 7/17/07 Graymountain Letter | 8OA | CCWP-2 |
| 9 | 10/23/07 Sogol Letter | 0FG | CCWP-6 |
| 10 | 7/16/07 Wilson Letter | 0NV | CCWP-11 |

CLAIM FORMS

Failed to include the fraud warning statement
A.R.S. §§ 20-466.03.

| Population | Sample | # of Exceptions | % to Sample |
|------------|--------|-----------------|-------------|
| N/A | N/A | 10 | N/A |

Any error does not meet the Standard.

Recommendation #4

Within 90 days of the filed date of this report, provide documentation to the Department that the required fraud warning statement, in 12-point type, is included on each of the claim forms and/or letters cited, in accordance with the applicable state statute.

Subsequent Event

The Company independently identified twelve (12) additional documents used to adjudicate Arizona claims that require affirmative action to complete and will voluntarily add the fraud warning statement to them.

SUMMARY OF FAILED STANDARDS

| EXCEPTION | Rec. No. | Page No. |
|--|-----------------|-----------------|
| UNDERWRITING AND RATING | | |
| <u>Standard #1</u> The rates charged for the policy coverage are in accordance with filed rates (if applicable) or the Company Rating Plan. | 1 & 2 | 12 |

| | | |
|--|---|----|
| CANCELLATIONS AND NON RENEWALS | | |
| <u>Standard #2</u> Cancellation and Nonrenewal notices comply with state laws, Company guidelines and policy provisions, including the amount of advance notice required and grace period provisions to the policyholder, nonrenewal based on condition of premises, and shall not be unfairly discriminatory | 3 | 15 |

| | | |
|--|---|----|
| CLAIMS PROCESSING | | |
| <u>Standard #3</u> The Company claim forms are appropriate for the type of product and comply with statutes, rules and regulations. | 4 | 18 |

SUMMARY OF PROPERTY AND CASUALTY STANDARDS

A. Complaint Handling

| # | STANDARD | PASS | FAIL |
|---|--|------|------|
| 1 | The Company takes adequate steps to finalize and dispose of the complaints in accordance with applicable statutes, rules, regulations and contract language. (A.R.S. § 20-461, A.A.C. R20-6-801) | X | |
| 2 | The time frame within which the Company responds to complaints is in accordance with applicable statutes, rules and regulations. (A.R.S. § 20-461, A.A.C. R20-6-801) | X | |

B. Marketing and Sales

| # | STANDARD | PASS | FAIL |
|---|---|------|------|
| 1 | All advertising and sales materials are in compliance with applicable statutes, rules and regulations. (A.R.S. § 20-442 and 20-443) | X | |
| 2 | The Company adequately monitors the activities of its consumer credit accounts as respects their making consumer disclosures, premium collections, claim payments, etc. to assure compliance with applicable statutes, rules, regulations and contract language. (A.R.S. §§ 20-461, 20-1602 thru 20-1616, A.A.C. R20-6-801) | X | |
| 3 | The amount of credit insurance sold is in compliance with the requirements of applicable statutes, rules and regulations. (A.R.S. § 20-1606) | X | |

C. Producer Compliance

| # | STANDARD | PASS | FAIL |
|---|---|------|------|
| 1 | The producers are properly licensed in the jurisdiction where the application was taken. (A.R.S. §§ 20-282, 20-286, 20-287, 20-311 through 311.03, 20-1612) | X | |
| 2 | An insurer shall not pay any commission, fee, or other valuable consideration to unlicensed producers. (A.R.S. § 20-298) | X | |

D. Underwriting and Rating

| # | STANDARD | PASS | FAIL |
|---|---|------|------|
| 1 | The rates charged for the policy coverage are in accordance with filed rates (if applicable) or the Company Rating Plan. (A.R.S. §§ 20-341 through 20-385, 20-1609, 20-1610) | | X |
| 2 | Disclosures to insureds concerning rates and coverage are accurate and timely. (A.R.S. §§ 20-1608, 20-2104, 20-2106, 20-2110, 20-2113) | X | |
| 3 | All mandated disclosures are documented and in accordance with applicable statutes, rules and regulations, including, but not limited to, the Notice of Insurance Information Practices and the Authorization for Release of Information. (A.R.S. §§ 20-1608, 20-2104, 20-2106, 20-2110, 20-2113) | X | |
| 4 | All forms and endorsements forming a part of the contract should be filed with the director (if applicable). (A.R.S. §§ 20-398, 20-1609, 20-1612) | X | |
| 5 | File documentation adequately supports decisions made. (A.R.S. § 20-385) | X | |
| 6 | Policies and endorsements are issued or renewed accurately, timely and completely. (A.R.S. §§ 20-1120, 20-1121, 20-1654) | X | |
| 7 | Rescissions are not made for non-material misrepresentations. (A.R.S. §§ 20-463, 20-1109) | X | |

E. Declinations, Cancellation and Nonrenewals

| # | STANDARD | PASS | FAIL |
|---|--|------|------|
| 1 | Declinations, cancellations and nonrenewals shall comply with state laws and Company guidelines including the Summary of Rights to be given to the applicant and shall not be unfairly discriminatory. (A.R.S. §§ 20-448, 20-2108, 20-2109, 20-2110) | X | |
| 2 | Cancellations and nonrenewal notices comply with state laws, Company guidelines and policy provisions, including the amount of advance notice required and grace period provisions to the policyholder, and shall not be unfairly discriminatory. (A.R.S. §§ 20-191, 20-443, 20-448, 20-1631, 20-1632, 20-1632.01) | | X |
| 3 | Group consumer credit insurance policies and certificates are terminated in accordance with applicable statutes, rules and regulations. (A.R.S. §§ 20-1608, 20-1611) | X | |

| # | STANDARD | PASS | FAIL |
|---|---|------|------|
| 4 | The effective dates and termination dates of coverage are in accordance with applicable statutes, rules and regulations. (A.R.S. §§ 20-1608, 20-1611) | X | |

F. Claims Processing

| # | STANDARD | PASS | FAIL |
|----|--|------|------|
| 1 | The initial contact by the Company with the claimant is within the required time frame. (A.R.S. § 20-461, A.A.C. R20-6-801) | X | |
| 2 | Timely investigations are conducted. (A.R.S. §§ 20-461, 20-1613, A.A.C. R20-6-801) | X | |
| 3 | The Company claim forms are appropriate for the type of product and comply with statutes, rules and regulations. (A.R.S. §§ 20-461, 20-466.03, 20-2106, A.A.C. R20-6-801) | | X |
| 4 | Claim files are adequately documented in order to be able to reconstruct the claim. (A.R.S. §§ 20-461, 20-463, 20-466.03, A.A.C. R20-6-801) | X | |
| 5 | Claims are properly handled in accordance with policy provisions and applicable statutes, rules and regulations. (A.R.S. §§ 20-461, 20-462, 20-1613, A.A.C. R20-6-801) | X | |
| 6 | The Company uses reservation of rights and excess of loss letters, when appropriate. (A.R.S. § 20-461, A.A.C. R20-6-801) | X | |
| 7 | Deductible reimbursement to insured upon subrogation recovery is made in a timely and accurate manner. (A.R.S. §§ 20-461, 20-462, A.A.C. R20-6-801) | X | |
| 8 | The Company responds to claim correspondence in a timely manner. (A.R.S. §§ 20-461, 20-462, 20-1613, A.A.C. R20-6-801) | X | |
| 9 | Denied and closed without payment claims are handled in accordance with policy provisions and state law. (A.R.S. §§ 20-461, 20-462, 20-463, 20-466, 20-2110, A.A.C. R20-6-801) | X | |
| 10 | No insurer shall fail to fully disclose to first party insureds all pertinent benefits, coverages, or other provisions of an insurance policy or insurance contract under which a claim is presented. (A.R.S. § 20-1608, A.A.C. R20-6-801) | X | |
| 11 | Adjusters used in the settlement of claims are properly licensed (A.R.S. §§ 20-321 through 20-321.02, 20-1613) | X | |