

General News

Are You Prepared for the Market Conduct Examiner?

Risk is a common term used quite often in insurance and, essentially, the basis of this business.

According to Webster's Third New International Dictionary "risk" is defined as the possibility of loss; exposure to hazard or danger; the creation of a hazardous or adverse chance. The insurance industry employs underwriters, loss control and claim personnel, among others, to evaluate and mitigate the exposure. When the industry writes a piece of business, there is a certain expectation or degree of probability that the subject matter of coverage provided by the insurance contract will result in a loss. Therefore, policies of insurance are issued and claims are incurred.

While risk is a basic principle of insurance, risk is not a position to be in when it involves compliance with state insurance laws and regulations as it applies to the subject business.

What will you do when a state insurance department comes knocking at your door and announces their intention to conduct a market conduct examination? Panic? Run and hide? Put your hands up in the air, surrender and confess you have not been diligent in the review of files? At that point, it's probably too late.

Compliance with state insurance laws and regulations is a mind-set and one that begins immediately upon underwriting the risk, continues throughout the rating, quoting and policy issuance process and remains in effect for as long as policies are in-force and there is any type of activity on those policies. It's not an after-thought or add-in that can be handled as part of the underwriting process, but a separate and distinct review of the regulatory and processing aspects of producing business.

Routine audits and self-assessments of your operations are the only proactive ways to control the situation and be fully prepared and confident the day the examiner arrives.

There is a general perception that both the underwriting process and the corresponding underwriting audit significantly contribute to a company's results. Ensuring that the proper exposure is written in accordance with underwriting guidelines and adequate price is obtained will produce profitability. Reviewing the procedural and processing aspects of the insurance transaction does not necessarily yield immediate benefits and is sometimes determined to be superfluous.

Compliance departments are not profit centers and are generally viewed as a roadblock, an impediment or even a hindrance to doing business. However, if they provide a full array of services, including regulatory and processing audits, compliance departments can significantly enhance a company's position and reputation in the marketplace and play a key role in the reduction of fines and penalties associated with state insurance department market conduct examinations.

Many believe the underwriter can review compliance issues during the course of the underwriting audit. This is not true. Just as there are specific components to an underwriting audit, there is a separate and distinct approach and factors to consider when conducting compliance audits. The focus is different and there is a need to determine these factors by individuals trained to identify them, in essence, a separate set of eyes that are neither directly associated with nor influenced by the profitability of a particular book of business.

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There are three main ingredients to a compliance audit: the regulatory review, the operational review, and the producer review.

- The regulatory review should concentrate on the statutory obligations of the company with respect to the initial issuance and subsequent servicing of new business and renewal policies including, but not limited to, adherence to filed and approved rates, rating plans and forms, completed applications, binders, certificates of insurance, cancellation/nonrenewal and other mandatory notices, option selection/rejection forms, countersignature and schedule rating worksheets and documentation.
- The operational review should consider the processing timeframes associated with the issuance of declinations, quotations, policies, any type of mid-term change and premium audit (if applicable), both for new business and renewal policies.
- The producer review should examine the representative of the company or insured (in the form of an agent or broker) and include the status of resident and non-resident licenses and insurance coverages, the entire appointment process with state insurance departments, including background investigations and signed producer agreements, their compliance with the terms, conditions and other contractual obligations of the signed agreement and their affiliation with sub-producers. A more thorough review may also include an evaluation of the office workflow, security procedures and disaster recovery plans.

Taken together, these reviews comprise the facets of a state insurance market conduct examination.

Getting control of the process from the beginning enables the company to significantly minimize, if not virtually eliminate, the repercussion of market conduct examinations. It is much easier and more efficient to integrate this process immediately than to backtrack after business has been written.

All audits should conclude with an oral discussion of all findings and a written report that clearly identifies each potential violation and contains remedies for each situation. However, one important factor must be considered. Conducting the audit and writing the report is not enough. Periodic review and follow-up must take place to confirm those issues identified have been appropriately addressed and/or corrected otherwise the process merely becomes a documentation of violations.

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