

REPORT ON
THE MARKET CONDUCT EXAMINATION
OF
PROGRESSIVE NORTHERN INSURANCE COMPANY
(NAIC COMPANY CODE 38628)
AND
PROGRESSIVE NORTHWESTERN INSURANCE COMPANY
(NAIC COMPANY CODE 42919)

6300 Wilson Mills Road
Mayfield Village, Ohio 44143-2182

NAIC GROUP CODE 155

as of

JUNE 30, 1998

State of Rhode Island
Department of Business Regulation
Insurance Division

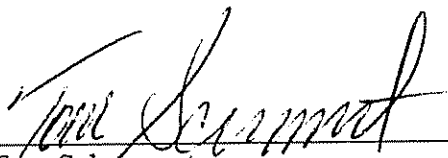
**STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS
DEPARTMENT OF BUSINESS REGULATION
INSURANCE DIVISION**

The attached Report of Examination as of June 30, 1998, of the market condition and affairs of Progressive Northern Insurance Company and Progressive Northwestern Insurance Company was recently completed by duly qualified examiners, pursuant to the provision of the Rhode Island Insurance Code.

Due consideration has been given to the comments of the examiners regarding the operations of Progressive Northern Insurance Company and Progressive Northwestern Insurance Company and their market conduct condition as reflected from the examination report.

It is therefore ORDERED that said Report be, and it is hereby adopted and filed and made an official record of this department as of this date.

DEPARTMENT OF BUSINESS REGULATION



Tom Schumpert
Director/Insurance Commissioner

ORDER NO. 00-0008

DATED: 1-20-00

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Providence, Rhode Island

December 14, 1999

Honorable Tom Schumpert
Insurance Commissioner
State of Rhode Island

Dear Sir:

In accordance with your instructions and pursuant to the statutes of the State of Rhode Island, a Market Conduct Examination was conducted of:

**Progressive Northern Insurance Company
and
Progressive Northwestern Insurance Company**

6300 Wilson Mills Road
Mayfield Village, Ohio 44143-2182

which together are hereinafter referred to as the "Companies." Our report is hereby submitted as follows:

FOREWORD

The Market Conduct Examination Report is, in general, a report by exception. Practices, procedures, and/or files subject to review during our examination may have been omitted from the report if errors and/or improprieties were not evidenced.

SCOPE OF EXAMINATION

Authority for this examination is provided by Title 27, Chapters 13 and 13.1 of the General Laws of Rhode Island. The examination covered the period from January 1, 1996, through June 30, 1998 and was conducted in accordance with standards established by the National Association of Insurance Commissioners, as well as, procedures developed by the Rhode Island Department of Business Regulation, Insurance Division. The examination was conducted at the Companies' claims office located at Summit East, 300 Centerville Road, Suite 220 in Warwick, Rhode Island.

Areas examined include: Certificates of Authority and Personal Automobile Claim Practices.

The purpose of this limited examination was to evaluate the Companies' compliance with Rhode Island Insurance Laws and Insurance Regulations with respect to allowances for paint and related materials in the settlement of personal automobile insurance claims. The examination consisted of verification and evaluation on a test basis of information contained in the insureds' files. We also reviewed other pertinent documents produced by the Companies.

COMPANY OVERVIEW

History

Progressive Northern Insurance Company, "Progressive Northern" was incorporated on August 19, 1980, under the laws of Wisconsin, and began its operations on March 8, 1981. Progressive Northern is owned by The Progressive Corporation, which is a publicly traded holding Company.

Progressive Northwestern Insurance Company, "Progressive Northwestern" was incorporated on September 24, 1982, under the laws of Washington, and began its operations on September 26, 1983. Progressive Northwestern is also wholly owned by The Progressive Corporation.

Company Operations

Progressive Northern Insurance Company is licensed in Rhode Island to write Automobile (B.I. and P.D.), property liability, general liability, inland marine, and commercial auto insurance. This Company is also licensed in the District of Columbia, and all states except: Alaska, Arizona, California, Florida, Hawaii, Illinois, Massachusetts, Michigan, Missouri, New Jersey, North Dakota, Tennessee, Texas, and Wyoming.

Progressive Northwestern Insurance Company is licensed in Rhode Island to write Auto Liability, Auto Physical Damage, and other Liability. This Company is also licensed in the District of Columbia, and all states except: Alaska, Florida, Hawaii, Illinois, Massachusetts, Michigan, New Hampshire, Pennsylvania, Vermont, Wisconsin, and Wyoming.

1997 Rhode Island Premiums Written

| <u>Line of Business</u> | <u>Progressive Northern Insurance Company</u> | <u>Progressive Northwestern Insurance Company</u> |
|---|---|---|
| Inland Marine | | \$ 193,429 |
| Other Liability | | \$ 91,591 |
| Other Private Passenger Auto Liability | \$ 7,702,065 | \$ 24,530,096 |
| Private Passenger Auto Physical Damage | <u>\$ 1,747,238</u> | <u>\$ 7,218,045</u> |
| Total Rhode Island Direct Premium Written | <u>\$ 9,449,303</u> | <u>\$ 32,033,161</u> |

MANAGEMENT

The Companies were managed by the following individuals at December 31, 1997:

Progressive Northern Insurance Company

| | |
|--------------------|-------------------------|
| Charles B. Chokel | President and Treasurer |
| David M. Schneider | Secretary |

Progressive Northwestern Insurance Company

| | |
|--------------------|-----------|
| Michael D. Sieger | President |
| Charles B. Chokel | Treasurer |
| David M. Schneider | Secretary |

CERTIFICATES OF AUTHORITY

The Companies' Rhode Island Certificates of Authority were reviewed in order to determine whether, during the period under examination, the Companies were in compliance with the Licensing Section of the General Laws of the State of Rhode Island, §27-2-11.

Based on this review, it was determined that the Companies were licensed in the State of Rhode Island to write Automobile Liability, Automobile Physical Damage, Other Liability, Inland Marine, and Commercial Vehicle Insurance.

PERSONAL AUTOMOBILE CLAIM PRACTICES
Allowance for Paint and Related Materials

During the period under examination the Companies processed 22,323 personal automobile claims (8,281 first party collision claims and 14,042 third party property damage claims). From this population, a sample of 245 personal automobile claim files was selected to verify whether the Companies were in compliance with the following Rhode Island General Law and Insurance Regulation:

| | |
|-------------------|---|
| 27-29 | Unfair Competition and Practices |
| Regulation LXXIII | Unfair Property/Casualty Claims Settlement Practices Regulation |

Our review determined that the Companies consistently applied a \$12 per hour rate for paint and related materials for the period under examination, except in subrogation cases. In cases involving subrogation, the Companies honored subrogation requests for the amount of damages (an industry practice), including whatever allowances were made by the other carrier for paint and materials. This has been verified by examining two subrogation files.

In addition, it should be noted that the Companies' allowance for paint and related materials was increased from \$12 per hour to \$16 per hour, effective September 3, 1998.

In addition to our testing of 245 personal automobile claim files, we reviewed the following areas described below:

We requested and were provided with a copy of the Companies' time/cost study regarding paint and related materials prepared at the Companies' corporate facility in Cleveland, Ohio. This information is considered by the Companies to be proprietary in nature and prepared for informational purposes only. With regard to the hourly rate utilized in other states, the claim manager did not have information for all markets in which the Companies conduct business, specifically as it relates to paint and material allowances. He did indicate, however, that there are different rates, as rates are based on fair market rates.

We were asked by the Department of Business Regulation to determine whether or not the majority of Rhode Island auto body shops accepted Progressive's \$12 per hour allowance for paint and related materials. This issue was discussed with the claims manager, who stated that he was unaware of any body shop that refused repair work due to the amount of the allowance. The claims manager pointed out that for the period under examination, the Rhode Island Department of Business Regulation received only three inquiries from repair facilities regarding the paint and materials allowance. As such, all remaining licensed repair facilities in Rhode Island must have been willing to accept the \$12 per hour rate. In as much as our review of the complaint files of the Department of Business Regulation confirmed that there were only three complaints received from repair facilities during the period under examination it is a reasonable assumption that all other licensed repair facilities in Rhode Island accepted the \$12 per hour rate. Based upon the claims manager's response, the number of complaints filed with the Department of Business Regulation by the repair facilities on this issue, and the fact we reviewed a sample of 245 claim files which indicate acceptance of the \$12 per hour rate, it appears that there are no exceptions to be noted in this area.

We discussed the Companies' subrogation policy with the claims manager and were advised as follows: When another carrier subrogates, the Companies' claims representative reviews the supporting documentation, including the other carrier's appraisal. If the allowance for paint and materials is within range of allowances for carriers in Rhode Island, and it appears the claim was handled fairly and according to the carrier's standard procedures, the Companies will honor the subrogation request for the amount of damages, including whatever allowances were made by the carrier for paint and materials. We were also advised that the Companies' policy with respect to subrogation is the standard industry practice. The claims manager also stated that except for claims involving subrogation, he is unaware of any instances where the Companies paid a Rhode Island repair facility a rate other than the current "fair market rate" of \$12 per hour. Based upon the claims manager's response and test work we performed, it appears that there is no exception to be noted in this area.

We asked the claims manager to explain the Companies' position in cases where they rejected a repair facility's specific request for the payment of a greater than \$12 per hour rate. We were advised that there have been requests for allowances greater than the \$12 per hour rate, however, in the majority of cases, the repair facility refers to the Mitchell's Guide to Refinishing, an

industry publication that estimates material costs. The claims manager's analysis of the Guide is that it significantly overstates actual costs. The claims manager further advised that on any request for additional material allowances, he asks the repair facility to provide documentation regarding actual expenditures. According to the claims manager, no repair facility has ever provided that information. Based on the claims manager's response and absent any evidence, which contradicts the Companies' position, it appears that there is no exception to be noted in this area.

We asked the claims manager whether or not the Companies allowed Rhode Island body shops the opportunity to provide the actual material costs and expenses incurred for paint and materials in the settlement of a claim to determine if the \$12 per hour rate allowance is adequate. We were advised that one repair facility did submit such documentation. After the claims manager reviewed and discussed this documentation with members of the Companies' physical damage training staff, it was their determination that the information submitted by the repair facility was significantly overstated as to the actual cost and quantity necessary to complete the necessary repair work. In addition, the claims manager stated that he conducted an on-site inspection of a vehicle undergoing repairs at another repair facility with the owner of the facility. He stated that while the owner expressed concern with the allowance, the repair industry does not actually track material usage in any manner that would allow for a meaningful analysis. Based upon the claims manager's reply, it appears that there is no exception to be noted in this area.

The Companies' paint and materials allowance in Rhode Island includes sales tax. The claims manager advised us that he did contact the Rhode Island Division of Taxation and was referred to Sales and Use Tax Regulation US 89-12 which indicated that repair facilities were the end users of paint and materials, and as such, were prohibited from taxing customers on that line item of repairs. The claims manager stated that his analysis of the allowance determined that it adequately addressed the repairer's actual cost of the materials, as well as the tax owed to the state on the purchase of these materials. Based upon this analysis, it appears that there is no exception to be noted in this area.

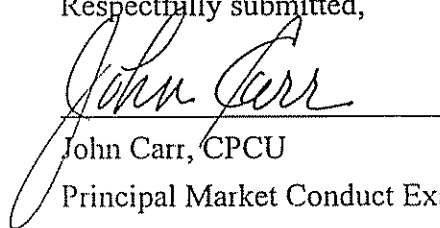
The question of capping allowances for paint and materials was discussed with the claims manager. He replied that the Companies do not cap paint and materials (a hard cap). However, once the allowance exceeds \$300, the repair facility is required to provide some documentation

as to the actual cost and needs. The claims manager advised us that this methodology is a corporate recommended procedure. Based upon the claims manager's response, it appears that there is no exception is to be noted in this area.

In summary, there were no exceptions noted in the test work we performed. In addition, we found that the Companies adequately addressed the questions posed by the Department of Business Regulation as outlined in this report.

Assisting the undersigned in the conduct of this examination from the Rhode Island Insurance Division were Joseph Seow, Market Conduct Examiner, Ronald R. Radtke, Senior Market Conduct Examiner, and Robert G. Arrow, FLMI, Senior Market Conduct Examiner.

Respectfully submitted,

A handwritten signature in cursive script, appearing to read "John Carr", is written over a horizontal line.

John Carr, CPCU
Principal Market Conduct Examiner
State of Rhode Island