



DEPARTMENT OF
INSURANCE AND FINANCIAL INSTITUTIONS

REPORT OF MARKET CONDUCT EXAMINATION

OF

MERCURY CASUALTY COMPANY, NAIC CoCode 11908

AS OF

December 31, 2022

AZ Exam No. 60533

NAIC MATS No. AZ-JESSENK-3

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MARKET CONDUCT SECTION

Arizona Department of Insurance and Financial Institutions

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Katie M. Hobbs, Governor

Barbara D. Richardson, Director

Director Barbara D. Richardson
Arizona Department of Insurance and Financial Institutions
100 N. 15th Ave, Suite 261
Phoenix, Arizona 85007-2624

Dear Director Richardson:

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:

Mercury Casualty Company, NAIC CoCode 11908

Shelly Schuman, ACS, AIE, AMCM, CICSR, CIS, FLMI, HIA, PAHM, Market Regulation Director, conducted the examination with the assistance of Bruce Glaser, CIE, MCM, AIRC, CPCU, CLU, ChFC, FLMI, ARM-Pe, CICSR, CRIS, FAHM, PHIAS Market Conduct Examiner-in-Charge, and Tony Taylor, DM, MCM, Market Conduct Data Management Specialist.

The examination covered January 1, 2019, through December 31, 2022.

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

Sincerely yours,

Maria G. Ailor, AIE, AMCM, Assistant Director
Market Regulation, and Consumer Services Division

AFFIDAVIT

STATE OF MISSOURI)
)
COUNTY OF JACKSON) ss.

Shelly Schuman, ACS, AIE, AMCM, CICS, CIS, FLMI, HIA, PAHM, being first duly sworn, states that I am a duly appointed Market Regulation Director for the Arizona Department of Insurance and Financial Institutions. Under my direction and with my participation and the participation of Bruce Glaser, CIE, MCM, AIRC, CPCU, CLU, ChFC, FLMI, ARM-Pe, CICS, CRIS, FAHM, PHIAS Market Conduct Examiner-in-Charge, and Tony Taylor, DM, MCM, Market Conduct Data Management Specialist, the Examination of Mercury Casualty Company, hereinafter referred to as the "Company," was performed at the request of the Arizona Department of Insurance and Financial Institutions. The information contained in this Report, which consists of the following pages, is true and correct to the best of my knowledge and belief, and 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.

Shelly Schuman

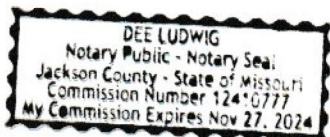
Shelly Schuman, ACS, AIE, AMCM, CICS, CIS, FLMI, HIA, PAHM,
Market Regulation Director
The INS Companies

Subscribed and sworn to before me this 26th day of July 2024,
2024.

Dee Ludwig

Notary Public

My Commission Expires: 11-27-2024



FOREWARD

This market conduct examination report of Mercury Casualty Company (herein referred to as the “Company”) was prepared by employees of the Arizona Department of Insurance and Financial Institutions (“Department” and “DIFI”) as well as independent examiners contracting with the Department. A market conduct examination reviews certain business practices of insurers licensed to conduct insurance business in Arizona. The examiners reviewed the Company in accordance with Arizona Revised Statutes (A.R.S.) §§ 20-142, 20-156, and 20-157. 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 private passenger automobile and homeowner business operations related to underwriting and rating.

Certain unacceptable or non-complying practices may not have been discovered during 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 purpose of the examination was to determine the Company’s compliance with Arizona’s insurance laws.

The focus of the examination was the Company’s compliance with A.R.S. § 20-2110(F)(3) and the use of bankruptcies as a rating factor. The Company was requested to conduct a self-audit of their credit scoring models for all property and casualty products sold in Arizona from January 1, 2019, to December 31, 2022. The purpose of the self-audit was to determine if consumers were rated and paid higher premiums as the result of a bankruptcy aged more than seven years, in violation of A.R.S. § 20-2110(F)(3). If violations were found as part of the self-audit, the Company would be required to submit a Corrective Action Plan to remediate those violations.

EXAMINATION REPORT SUMMARY

The Director may examine and investigate the affairs of every insurance institution or insurance producer doing business in this state to determine whether the insurance institution or insurance producer has been or is engaged in any conduct in violation of this chapter, pursuant to A.R.S. §§ 20-142, 20-156, 20-157, 20-158, 20-159, and 20-2114.

The examination concluded the Mercury Casualty Company's responses during the examination demonstrated noncompliance with A.R.S. § 20-2110(F).

Private Passenger Automobile

- New Business Policies: There are 2 different insureds in which the bankruptcy date was aged to more than 7 years old as of the inception date of the policy, and constitute 2 violations of A.R.S. § 20-2110(F)(3).
- Renewal Policies: There are 6 different insureds affecting 8 renewal terms in which the bankruptcy date was aged to more than 7 years old as of the renewal date of the policy and constitute 8 violations of A.R.S. § 20-2110(F)(3).

Homeowner

- New Business Policies: There were no findings related to the examination.
- Renewal Policies: There were no findings related to the examination.

CORRECTIVE ACTION PLAN

This Corrective Action Plan defines the corrective action requirements applicable to Mercury Casualty Company resulting from the market conduct examination conducted by the Department.

Area of Concern: Bankruptcy Factor Rating of Policies

Corrective Actions

1. Prior to the conclusion of this examination, the Company informed the Department that it intends to implement a 3-year CBIS re-order interval, and limit the age of bankruptcies and/or liens (including those bankruptcies or liens identified or included as part of the “tradeline” model factor) used to calculate CBIS’s to 4 years.
 - a. No later than sixty (60) days after the filing of this Report, the Company will file in SERFF all applicable revisions to the Company’s rate and rule filings based on the Company’s chosen re-order interval noted in paragraph 1 above, related to future compliance with A.R.S. § 20-2110(F). (See A.R.S. § 20-385 which requires the Company to file in SERFF within 30 days of a change to the impacted rate/rule). If this change has already been filed in SERFF, please provide the SERFF filing number(s) to the Department.
2. No later than sixty (60) days after the filing of this Report, the Company will remediate the **7 inactive new and renewal business policyholders**¹ for Private Passenger Automobile that were identified as having been rated for a bankruptcy aged more than 7 years as follows:
 - a. Rated improperly at new business only – \$50
 - b. Rated improperly at 1 renewal – \$50;
 - c. Rated improperly at 2 renewals – \$75; and
 - d. Rated improperly at 3 renewals – \$100.
3. No later than sixty (60) days after the filing of this Report, the Company will remediate the **1 active renewal business policyholder**² Private Passenger Automobile that was identified as having been rated for a bankruptcy aged more than 7 years as follows:
 - a. Rated improperly at 1 renewal – \$50.

¹ These policyholders are identified in Final Finding 01 and Final Finding 02.

² This policyholder is identified in Final Finding 02.

4. No later than ninety (90) days after the filing of this Report, the Company will provide a data set to the Department that at minimum will include:
 - a. The date the refund was issued, the refund amount, and total interest (if applicable) for each policyholder identified in items 2 and 3 above;
 - b. Whether the policyholder is active or inactive; and
 - c. The Department will provide the format of the data set during the compliance monitoring phase.
5. The Company will pay a civil monetary penalty negotiated separately in the forthcoming consent order.
6. The Company will provide the Department with a specific timeline for the implementation of the above process.
7. The Company will provide status updates to the Department every thirty (30) days, on an as needed basis, or at the Department's request during the implementation and compliance monitoring period.
8. During the course of the implementation and compliance period, the Department may request additional documentation and/or supporting materials not specifically listed herein that demonstrate the Companies' progress with the CAP requirements above.

UNDERWRITING AND RATING

Private Passenger Automobile - New Business

The Company provided a list of 16,781 new business private passenger automobile policies active during the examination period. In 599 new business policies, the Company indicated “Yes” that “the consumer was rated for having one or more bankruptcies.” The date of bankruptcy and the policy’s inception date were compared to identify whether the date of bankruptcy was aged more than 7 years old (84 months) as of the inception date.

The following Underwriting and Rating Standard Failed:

Standard	Regulatory Authority
F. An insurer shall not use the following types of credit history to calculate an insurance score to determine property or casualty premiums for insurance transactions that are subject to this article and shall not knowingly use an insurance score developed by a third party if the score is calculated using any of the following types of credit history: 3. A bankruptcy or a lien satisfaction that is more than seven years old.	A.R.S. § 20-2110(F)(3) <i>See also A.R.S. §§ 20-142, 20-156, 20-157, 20-158, 20-159, and 20-2114</i>

Finding #1 – Bankruptcy Rating of Private Passenger Automobile New Business Policies

The examiners identified 188 different insureds from the 599 policies, with an error rate of 31 percent, in which the bankruptcy date was aged more than 7 years old as of the inception date of the policy. Because A.R.S. § 20-2110(F) prohibits the use of bankruptcies that are aged more than 7 years, and this timeline begins on the date that the bankruptcy is adjudicated, the Company’s responses and supporting documentation demonstrated noncompliance with Arizona law.

The Company agreed that bankruptcies older than 7 years were used but disagreed that a violation of A.R.S. § 20-2110 occurred. The preliminary finding directed the Company to “provide evidence to support the argument, including rate comparisons indicating the premium amount with the utilization of bankruptcy as an element of the rate development.” The Company failed to provide the rate comparisons to support the argument that “bankruptcies were not used to calculate the insurance scores utilized ... in rating those policies.”

After the finding was issued, the Department received a demonstration of the model in use during the examination period. For purposes of calculating a credit-based insurance score (CBIS) at policy inception, it was determined that the model did not utilize bankruptcies that were aged to more than 80 months. The Department directed the examiners to review the findings in light of this demonstration. After this review, the examiners concluded that in 181 of the 188 instances, the bankruptcy was aged to more than 84 months as of the inception date. Because the model demonstration properly excluded bankruptcies aged to more than 84 months from the CBIS calculation, these 181 violations have been withdrawn.

Additionally, there were 5 instances where the bankruptcy was aged to less than 84 months as of the policy inception date. These 5 violations have been withdrawn.

Finally, there were 2 instances where the bankruptcy was aged to more than 84 months as of the policy inception date. Accordingly, because the Company did not demonstrate that the bankruptcy was not utilized in the rate development of the identified policies, there are 2 violations of A.R.S. § 20-2110(F)(3).

Recommendation #1 for Private Passenger Automobile New Business Policies

Mercury Casualty Company should implement the Corrective Action Plan as detailed in the Examination Report Summary.

Private Passenger Automobile – Renewal Business

The Company provided a list of 32,555 renewed private passenger automobile policies active during the examination period. In 519 renewal policies, the Company indicated “Yes” that “the consumer was rated for having one or more bankruptcies.” The date of bankruptcy and the policy’s renewal date were compared to identify whether the date of bankruptcy was aged more than 7 years old (84 months) as of the renewal date.

The following Underwriting and Rating Standard Failed:

Standard	Regulatory Authority
F. An insurer shall not use the following types of credit history to calculate an insurance score to determine property or casualty premiums for insurance transactions that are subject to this	A.R.S. § 20-2110(F)(3)

Standard	Regulatory Authority
article and shall not knowingly use an insurance score developed by a third party if the score is calculated using any of the following types of credit history: 3. A bankruptcy or a lien satisfaction that is more than seven years old.	<i>See also</i> A.R.S. §§ 20-142, 20-156, 20-157, 20-158, 20-159, and 20-2114

Finding #2 – Bankruptcy Rating of Private Passenger Automobile Renewal Business Policies

The examiners identified 93 different insureds affecting 165 renewals, with an error rate of 32 percent, in which the bankruptcy date was more than seven years old. Because the bankruptcies were aged over 7 years old (84 months) and continued to be used as a rating factor for the identified renewal periods, the Company violated A.R.S. § 20-2110(F)(3).

These 93 different insureds had a bankruptcy within 7 years of the inception date for the policy. Accordingly, the premium utilized bankruptcy as an element of the rate development at that time. In response to the Target Market Conduct Coordinator’s Handbook, Section B.3.b, the Company stated they do not re-order credit—except at the request of the customer—before calculating the renewal premium. Therefore, for any renewal period in which the bankruptcy was aged over 7 years old as of the renewal date, the calculation of the renewal premium violated A.R.S. § 20-2110(F)(3).

The preliminary finding directed the Company to “provide evidence to support the argument (that A.R.S. § 20-2110(F)(3) had not been violated), including rate comparisons indicating the premium amount with the utilization of bankruptcy as an element of the rate development.” The Company failed to provide the rate comparisons to support the argument that “bankruptcies were not used to calculate the insurance scores utilized ... in rating those policies.” Because A.R.S. § 20-2110(F) prohibits the use of bankruptcies that are aged more than 7 years, and this timeline begins on the date that the bankruptcy is adjudicated, the Company’s responses and supporting documentation demonstrated noncompliance with Arizona law.

As noted above, after the finding was issued, the Department received a demonstration of the model in use during the examination period. For purposes of calculating a credit-based insurance score (CBIS) at policy inception, it was determined that the model did not utilize bankruptcies that were aged to more than 80 months. The Department directed the examiners to

review the findings in light of this demonstration. After this review, the examiners concluded that in 157 of the 165 instances, the bankruptcy was aged to more than 84 months as of the policy inception date. Because the model demonstration properly excluded bankruptcies aged to more than 84 months from the CBIS calculation, these 157 violations have been withdrawn.

The examiners concluded that for the remaining 8 renewal periods the bankruptcy date was aged less than 84 months at the inception date; however, the bankruptcy subsequently aged to more than 84 months as of subsequent renewal date(s). Accordingly, there were 6 insureds, affected by 8 renewal periods, with an error rate of 6 percent, in which the bankruptcy date was aged to more than 7 years (84 months) old. Accordingly, because the Company did not demonstrate that the bankruptcy was not utilized in the rate development of the identified policies, there are 8 violations of A.R.S. § 20-2110(F)(3).

Recommendation #2 for Private Passenger Automobile Renewal Business

Mercury Casualty Company should implement the Corrective Action Plan as detailed in the Examination Report Summary.

Homeowner – New Business

The Company provided a list of 13,653 new business homeowner policies active during the examination period. In 60 new business policies, the Company indicated “Yes” that “the consumer was rated for having one or more bankruptcies.” The date of bankruptcy and the policy’s inception date were compared to identify whether the date of bankruptcy was aged more than 7 years old (84 months) as of the inception date.

The preliminary finding directed the Company to “provide evidence to support the argument (that A.R.S. § 20-2110(F)(3) had not been violated), including rate comparisons indicating the premium amount with the utilization of bankruptcy as an element of the rate development.” The Company failed to provide the rate comparisons to support the argument that “bankruptcies were not used to calculate the insurance scores utilized ... in rating those policies.” Because A.R.S. § 20-2110(F) prohibits the use of bankruptcies that are aged more than 7 years, and this timeline begins on the date that the bankruptcy is adjudicated, the Company’s responses and supporting documentation demonstrated noncompliance with Arizona law. Accordingly, because the Company did not demonstrate that the bankruptcy was not utilized in the rate

development of the identified policies, the examiners identified 23 violations of A.R.S. § 20-2110(F)(3).

After the finding was issued, the Department received a demonstration of the model in use during the examination period. For purposes of calculating a credit-based insurance score (CBIS) at policy inception, it was determined that the model did not utilize bankruptcies that were aged to more than 80 months. The Department directed the examiners to review the findings in light of this demonstration. After this review, the examiners concluded that in each of the 23 identified instances, the bankruptcy was aged to more than 84 months as of the policy inception date. These 23 findings were withdrawn.

Accordingly, there are no findings of A.R.S. § 20-2110(F) violations related to new business homeowner policies for this examination.

The following Underwriting and Rating Standard Passed:

Standard	Regulatory Authority
<p>F. An insurer shall not use the following types of credit history to calculate an insurance score to determine property or casualty premiums for insurance transactions that are subject to this article and shall not knowingly use an insurance score developed by a third party if the score is calculated using any of the following types of credit history:</p> <p>3. A bankruptcy or a lien satisfaction that is more than seven years old.</p>	<p>A.R.S. § 20-2110(F)(3)</p> <p><i>See also</i> A.R.S. §§ 20-142, 20-156, 20-157, 20-158, 20-159, and 20-2114</p>

Homeowner – Renewal Business

The Company provided a list of 21,777 renewed homeowner policies active during the examination period. In 13 renewal policies, the Company indicated “Yes” that “the consumer was rated for having one or more bankruptcies.” The date of bankruptcy and the policy’s renewal date were compared to identify whether the date of bankruptcy was aged more than 7 years old (84 months) as of the renewal date.

The examiners identified 3 different insureds affecting 3 renewal periods from the 13 policies, with an error rate of 23 percent, in which the bankruptcy date was more than seven years

old. Because the bankruptcies were aged over 7 years old (84 months) and continued to be used as a rating factor for the identified renewal periods, the Company violated A.R.S. § 20-2110(F)(3).

These 3 different insureds had a bankruptcy within 7 years of the inception date for the policy. Accordingly, the premium utilized bankruptcy as an element of the rate development at that time. In response to the Target Market Conduct Coordinator's Handbook, Section B.3.b, the Company stated they do not re-order credit—except at the request of the customer—before calculating the renewal premium. Therefore, for any renewal period in which the bankruptcy was aged over 7 years old as of the renewal date, the calculation of the renewal premium violated A.R.S. § 20-2110(F)(3).

The preliminary finding directed the Company to “provide evidence to support the argument (that A.R.S. § 20-2110(F)(3) had not been violated), including rate comparisons indicating the premium amount with the utilization of bankruptcy as an element of the rate development.” The Company failed to provide the rate comparisons to support the argument that “bankruptcies were not used to calculate the insurance scores utilized ... in rating those policies.” Because A.R.S. § 20-2110(F) prohibits the use of bankruptcies that are aged more than 7 years, and this timeline begins on the date that the bankruptcy is adjudicated, the Company's responses and supporting documentation demonstrated noncompliance with Arizona law. Because the Company did not demonstrate that the bankruptcy was not utilized in the rate development of the identified policies, the examiners identified 3 violations of A.R.S. § 20-2110(F)(3).

After the finding was issued, the Department received a demonstration of the model in use during the examination period. For purposes of calculating a credit-based insurance score (CBIS) at policy inception, it was determined that the model did not utilize bankruptcies that were aged to more than 80 months. The Department directed the examiners to review the findings in light of this demonstration. After this review, the examiners concluded that that in the 3 identified instances, the bankruptcy was aged to more than 84 months as of the policy inception date. Because the model demonstration properly excluded bankruptcies aged to more than 84 months from the CBIS calculation at the policy inception, the bankruptcy was not included in the CBIS at subsequent renewal periods. These 3 findings were withdrawn.

Accordingly, there are no findings of A.R.S. § 20-2110(F) violations related to renewal business homeowner policies for this examination.

The following Underwriting and Rating Standard Passed:

Standard	Regulatory Authority
F. An insurer shall not use the following types of credit history to calculate an insurance score to determine property or casualty premiums for insurance transactions that are subject to this article and shall not knowingly use an insurance score developed by a third party if the score is calculated using any of the following types of credit history: 3. A bankruptcy or a lien satisfaction that is more than seven years old.	A.R.S. § 20-2110(F)(3) <i>See also</i> A.R.S. §§ 20-142, 20-156, 20-157, 20-158, 20-159, and 20-2114