



# **THE STATE OF FLORIDA**

## **OFFICE OF INSURANCE REGULATION MARKET INVESTIGATIONS**

**MARKET CONDUCT FINAL EXAMINATION REPORT**

**OF**

**CITIZENS PROPERTY INSURANCE CORPORATION**

**NAIC COMPANY CODE: 10064**

**FEBRUARY 1, 2017**

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## **EXECUTIVE SUMMARY**

The Office of Insurance Regulation (Office) Market Investigations staff and The INS Companies performed a market conduct examination of Citizens Property Insurance Corporation (Citizens) pursuant to Section 627.351(6)(l), Florida Statutes. The scope period of this examination was July 1, 2014 through June 30, 2016. The onsite examination began September 11, 2016 and ended November 10, 2016. Pursuant to Section 627.351(6)(l), Florida Statutes, this report is being prepared for submission to the President of the Senate and the Speaker of the House of Representatives of the Florida Legislature.

The purpose of this market conduct examination was to determine Citizens' compliance with its plan of operation and its internal operational procedures.

Detailed review of Citizens' procedures, operations, activities, and records showed few deficiencies. Information relating to these findings is reported herein.

## **SCOPE OF EXAMINATION**

A review of current operational procedures and controls was performed including evaluation of Citizens' processes, reports of corporate records, general operations, accounting, investments, internal audit, information systems, depopulation, agent licensing, complaint handling, underwriting and rating, cancellations/non-renewals, claims, reinsurance, anti-fraud activities, and integration of legislative changes.

Citizens provided pertinent documentation of its internal controls, as well as its responses to numerous reports received during the scope period. This examination incorporates the reviews of the testing of internal controls performed by Citizens' Office of the Internal Auditor and by the certified public accounting firms of Johnson Lambert & Co. LLP (2014) and Dixon Hughes Goodman LLP (2015).

Citizens' records were examined at 301 West Bay Street, Jacksonville, Florida, and remotely at the offices of INS and the Office. Documentation utilized in this report was provided by Citizens, independent auditors, Citizens' Office of the Internal Auditor, and other external sources.

This Report is based upon information obtained during the examination, additional research conducted by the Office, and additional information provided by Citizens. The files examined were selected systematically from data files provided by Citizens using Audit Command Language software (ACL). Each finding by the Office was reviewed and given due consideration by Citizens. Procedures and conduct of the examination were in accordance with the *Market Regulation Handbook* developed by state insurance regulators and produced by the National Association of Insurance Commissioners (NAIC).

The examination testing procedures included reviews of:

- The Plan of Operation;
- Board and Committee Meeting Minutes;

- Citizens' Organizational Chart;
- Reports of both external and internal audits performed during the scope of the examination;
- IT operations and Cyber Security reviews;
- Depopulation;
- Complaints;
- Agent Licensing;
- Underwriting and Rating;
- The Clearinghouse Program;
- Cancellations and Nonrenewals;
- Claim handling.

### **CORPORATE RECORDS**

Citizens was established on August 1, 2002, pursuant to Section 627.351(6), Florida Statutes, as amended in 2002 by Senate Bill 1418 and House Bill 385 (the Act), to provide certain property and casualty insurance coverage to qualified risks in the state of Florida. The intent of the legislation was that property insurance be provided through Citizens to applicants who are unable to procure insurance through the voluntary market. Citizens was formed from a combination of the Florida Residential Property and Casualty Joint Underwriting Association and the Florida Windstorm Underwriting Association. The Florida Residential Property and Casualty Joint Underwriting Association was renamed Citizens Property Insurance Corporation. The rights, obligations, assets, liabilities and all insurance policies under the Florida Windstorm Underwriting Association were transferred to Citizens. Citizens is not required to have a certificate of authority issued by the Office.

Citizens is to operate under the supervision of a nine-member Board of Governors. Pursuant to its Plan of Operation, Florida's Governor appoints three members, while the Chief Financial Officer, Speaker of the House and President of the Senate each appoint two individuals as members of the Board for three year terms. Each Board member serves at the pleasure of his or her appointing officer. At the time of this examination, due to the recent resignation of a member, there were eight board members with one pending appointment by the Governor.

### **OFFICE OF THE INTERNAL AUDITOR**

In May 2006, Senate Bill 1980 required Citizens to establish the Office of the Internal Auditor to coordinate and be responsible for activities promoting accountability, integrity, and efficiency to the policyholders and taxpayers of the state of Florida. The Office of the Internal Auditor provides direction for, supervises, conducts, and coordinates audits, investigations, and management reviews relating to the programs and operations of Citizens.

During the examination, a review was completed for the following areas of the Office of the Internal Auditor:

- Policies and Procedures;
- Annual Reports;
- Management Reporting of Activities; and,

- Open Items Process.

Florida Statutes require the Chief of Internal Audit to submit an annual report summarizing the activities of the Office of the Internal Auditor during the preceding fiscal year. The report includes:

- Summary of the Office of the Internal Auditor background, duties, organization structure, training, and certifications;
- Overview of the Internal Audit process;
- Summaries of audits, reviews and investigations conducted by the Office of the Internal Auditor;
- An evaluation of the effectiveness of Citizens' internal controls;
- Recommendations for corrective action, if necessary; and,
- Other information as necessary.

The report is presented to the Board of Governors, the Executive Director, the members of the Financial Services Commission, the President of the Senate, and the Speaker of the House of Representatives. Confirmation of the presentation of these annual reports for 2014 and for 2015 was verified by reviewing the Board of Governors' meeting minutes.

No exceptions were noted.

On a quarterly basis, the Office of the Internal Auditor prepares a Dashboard Status Report. The Report consists of an audit plan status, an open audit items status, and a detailed audit plan status report. The Report is issued to Management and the Audit Committee quarterly.

The Office of the Internal Auditor has policies and procedures in place to monitor the open audit items. It is the responsibility of Management to remediate all open items. The Office of the Internal Auditor is responsible for communicating on a quarterly basis to Management and the Audit Committee the status and aging of open items.

Based on our review, Citizens timely reviews, prioritizes and acts on findings resulting from both internal and external audits.

### **INFORMATION SYSTEMS**

A review of Citizens' Information Systems and Cyber Security was conducted in accordance with guidelines and procedures set forth in the NAIC's *Market Regulation Handbook*, including evaluation of controls in information technology planning, implementation and monitoring. Such review included a review of Board and Committee meeting minutes, audits and various IT-related reports, including various enterprise risk management reports. It was concluded that Citizens maintains active and responsive programs for information security.

#### **System Development Life Cycle**

A System Development Life Cycle (SDLC) was implemented by Citizens on August 1, 2014, and the current SDLC Process was put into place in June 2016.

No exceptions were noted.

## **DEPOPULATION**

The guidelines for depopulation were established by the Florida Legislature and are contained in Section 627.3511, Florida Statutes. The intent of this legislation was to reduce the number of property owners who have insurance coverage through Citizens by encouraging new or existing insurance companies to take out policies from Citizens.

During the scope period of this examination, July 1, 2014 to June 30, 2016, 40 companies participated in the depopulation program at Citizens and removed 617,951 policies, resulting in an exposure reduction of \$169,006,989,650.

A review of depopulation activities was conducted and no exceptions were noted.

## **COMPLAINTS REVIEW**

### **COMPLAINT HANDLING PROCESSES AND PROCEDURES**

Section 627.351(6)(k)2., Florida Statutes, requires Citizens to establish a unit to handle consumer complaints. Citizens' written processes and procedures for complaint handling were requested, received and reviewed for compliance with Florida Statutes and the Florida Administrative Code. Files were also reviewed for compliance with Sections 624.307, 627.351, 626.9541 and 627.70131, Florida Statutes, and Rule 69O-166.024, Florida Administrative Code, relating to complaint handling.

The *NAIC Market Regulation Handbook* states that a complaint is "any written communication that expresses dissatisfaction." Citizens follows this protocol and has established a "Customer Correspondence Unit" to handle complaints.

No exceptions were noted.

### **COMPLAINTS REVIEW**

A listing of all complaints received by Citizens during the scope of the examination was requested. Citizens furnished a list of 1,699 complaints consisting of 504 complaints forwarded to Citizens from the Department of Financial Services (DFS) and 1,195 complaints received directly from consumers or other Non-DFS sources.

The examination testing procedures included:

- Reviewing Citizens' complaint handling procedures;
- Reviewing the complaint log of all complaints received during the scope of the examination; and,

- Reviewing a randomly selected sample of 114 complaints from the total population of complaints during the scope period. The sample included 34 complaints filed with DFS and 80 complaints received directly by Citizens.

The examiners' review concluded that in three complaint files, errors involving Citizens' IT systems were noted and found to impact more policyholders than the single complainant. The examiners questioned Citizens about each of these complaints and concluded that Citizens took reasonable steps to provide remedies for the affected policyholders.

The first file was referred from DFS to Citizens. The policyholder complained of receiving two letters for assumption of his policy from other insurers. Only one letter was valid. Citizens discovered that 11,500 policyholders also received two letters in error. On discovery, Citizens took appropriate action to remedy the cause of the erroneous delivery so that it would not recur and also sent a letter to assist impacted policyholders and agents. Citizens also advised policyholders and agents of the option to opt out of the assumption.

The second file was also referred from DFS to Citizens. The policyholder complained that he did not timely receive a refund of premium following cancellation. This was due to an IT error during an earlier conversion process that prevented the complete processing of refunds involving certain mortgage contracts. After investigation, Citizens believes that fewer than 160 policyholders were affected by this transaction processing error. Citizens corrected this error on discovery and also put into place a team that meets frequently to prevent any similar errors in the future.

The third file was a complaint received directly from the insured where a renewal notice was not sent. This error was described in Citizens' documents as a "glitch in the system" during conversion to a new IT system. After investigation, Citizens estimated 50 policyholders were affected by this same system error. Citizens corrected the issue and the affected policyholders were issued renewals with extended due dates for payment.

### **AGENT LICENSING REVIEW**

Citizens sells its products through duly licensed and appointed agents. Agents must hold an active 0220 or 20-44 Florida Resident Agent's License or an active 0920 or 90-44 Non-Resident Agent's License. Section 627.351(6)(c)14., Florida Statutes, provides that an agent must also be appointed by at least one other insurer writing certain types of property coverage.

A listing of all producing agents appointed by Citizens during the scope of the examination was requested. Citizens furnished a list of 10,551 agents. A random sample of 116 agents was reviewed for compliance with licensing requirements of Florida Statutes and the Florida Administrative Code.

No exceptions were noted.

## **UNDERWRITING AND RATING REVIEW**

### **UNDERWRITING AND RATING PROCESSES AND PROCEDURES**

As requested, Citizens provided written processes and procedures for underwriting and rating that included the following:

- a) Underwriting Guidelines;
- b) Procedures for determining adequacy of rates and monitoring process of industry rates;
- c) Rate filings;
- d) Worksheets showing the steps followed for calculating/determining the premium in each rate filing;
- e) List of all forms used during the exam scope that are required to be filed and/or approved;
- f) Hurricane deductibles offered;
- g) Synopsis of policy issuance and renewal guidelines, including the Clearinghouse process and determination of customer eligibility.

This material was received and reviewed by the examiners for compliance with Florida Statutes and the Florida Administrative Code, as well as the file reviews, including Sections 627.062, 626.451, 626.9541, 627.0629, 627.351, 627.3518, 627.4085, 627.4091, 627.410, 627.4133, 627.4143, 627.421, 627.43141, 627.70161, 627.702, 627.706, 627.7011, 627.711, 627.714 and 627.7151, Florida Statutes, and Rules 69O-137.008, 69O-167.001, 69O-167.010, 69O-167.011 and 69O-170.019, Florida Administrative Code.

No exceptions were noted.

### **PERSONAL LINES POLICY REVIEW**

Citizens provided a listing of 1,504,453 personal lines policies in force during the scope of the examination. Citizens also identified the policy types associated with the request.

Examiners noted renewals outnumbered new policies, and the total number of written policies is trending downward during the scope period. The Depopulation Program and Clearinghouse activity during the scope of the examination were significant contributing factors in this development.

Sections 627.351(6)(c)5 and 627.3518, Florida Statutes, require Citizens to divert certain personal and commercial residential risks into the voluntary private market, if eligible. A new residential policy is ineligible to be written by Citizens if at least one comparable private market offer of coverage is received with a premium that is within 15 percent of a comparable Citizens' policy. A policy is ineligible for renewal if there is one or more private-market offers with premiums equal to or less than the Citizens renewal. Citizens takes affirmative steps to determine if there could be private market offers for most policies unless there are considerations that make such steps impractical.



As part of determining eligibility under these requirements, Citizens has instituted an automated process known as the Clearinghouse for certain personal lines that it has determined to be the most amenable for the process of private market coverage. However, these procedures have not been implemented for commercial policies. Citizens has indicated that obstacles exist to prevent commercial application including the complexities of commercial underwriting and the necessity for additional legislation.

For new applications for personal lines to be placed in the Clearinghouse, the agent enters the application information to initiate the process. For renewals, the system initiates automatically. In both scenarios, participating insurers are able to submit quotes for these policies and eligibility is determined. The following policies are currently included in the Clearinghouse:

<b>Clearinghouse Policy Type</b>	<b>New-Business Effective Date</b>	<b>Renewal Effective Date</b>
Homeowners 3 - Special Form (HO-3)	01/27/2014	11/01/2014*
Dwelling Property 1 - Basic Form (DP-1 D)	04/27/2015	07/01/2015
Dwelling Property 3 - Special Form (DP-3 D)	04/27/2015	07/01/2015
Homeowners 6 Unit-Owners Form (HO-6)	12/14/2015	02/17/2016

\*Renewal processing in Policy Center began with policies effective 02/01/2015. However, Clearinghouse processing for renewals effective 02/01/2015 to 02/06/2015 had to be put on hold to facilitate the cutover from ePAS to Policy Center.

A proportional random sample of 116 policies was requested, received and reviewed for compliance with underwriting and rating requirements of Florida Statutes and the Florida Administrative Code. The sample consisted of the following:

<b>Personal Lines</b>	<b>Number of Sample Policies</b>
Homeowners	49
Mobile Homeowners	12
Wind	26
DP Multi-Peril in the PLA and HRA*	29
<b>Total</b>	<b>116</b>

\* Personal Lines Account (PLA) and High Risk Account (HRA)

The rating to calculate premium by Citizens for personal policies (and most commercial policies) is conducted through an automated system with class rates that have been approved by the Office. The use of such a system will typically reduce the likelihood of error from a manual rating process. The examiners selected a proportional random sample of 20 personal policies from the full sample of 116 policies to test the rating of premium. No errors were found. It is also noted that no rating errors were found in a full rating review of A-rated commercial policies as described later in the report. Due to the automated system and the lack of errors in the 20 selected files, no further rating review for these policies took place. However, the full sample was reviewed for underwriting compliance.

No exceptions were noted.

### CANCELLATION AND NONRENEWAL REVIEW

As requested, Citizens provided a listing for the cancellations and nonrenewals of all personal lines policies during the scope of the examination.

Citizens furnished a list of 351,956 cancellations and nonrenewals consisting of the following:

<b>Cancellations and Nonrenewals</b>	<b>Number of Policies</b>
Cancellations	212,206
Nonrenewals	139,750
<b>Total</b>	<b>351,956</b>

A proportional random sample of 116 policies was requested, received and reviewed for compliance with the Florida Statutes and the Florida Administrative Code. The sample consisted of the following:

<b>Cancellations and Nonrenewals</b>	<b>Number of Sample Policies</b>
Cancellations	71
Nonrenewals	45
<b>Total</b>	<b>116</b>

No exceptions were noted.

### COMMERCIAL LINES POLICY FILES

As requested, Citizens provided a listing of 49,079 commercial policies in force during the scope of the examination. Citizens also identified the policy types associated with the request:

<b>Commercial Lines</b>	<b>Citizens' Policy Forms</b>
Commercial Residential (CR)	CR-M, CR-W
Commercial Nonresidential (CNR)	CNR-M, CNR-W

Examiners noted the number of written policies are trending downward during the scope period. A proportional random sample of 116 policies was requested, received and reviewed for compliance with underwriting and rating requirements of Florida Statutes and the Florida Administrative Code. The sample consisted of the following:

<b>Commercial Lines</b>	<b>Number of Sample Policies</b>
Commercial Residential (CR)	55
Commercial Nonresidential (CNR)	61
<b>Total</b>	<b>116</b>

As also described in the personal lines review, the rating to calculate premium by Citizens for most commercial policies is generally conducted through an automated system with class rates that have been approved by the Office. The use of such a system will typically reduce the likelihood of errors from a manual rating process. The examiners selected a proportional random sample of 20 commercial policies from the full sample of 116 policies to test the rating of premium. No errors were found. It is also noted that no rating errors were found in a full rating review of A-rated commercial policies as described later in this report. Due to the automated system and the lack of errors in the 20 selected files, no further rating review for these policies took place. However, the full sample was reviewed for underwriting compliance.

**Findings:**

There were 116 commercial policies reviewed. In seven instances, deviations from written procedures were noted, as follows:

1. In one instance (CNR), the required application was missing from the file. The filed manual states:

*Applications:*

*Completed, signed and dated application with required premium payment including when applicable, a copy of the Cancellation or Non-Renewal Notice from the immediate previous insurer or proof of new purchase or new lease.*

**Citizens' Response:** Citizens agreed with this finding.

**Recommendation:** This was an isolated finding related to a decades-old policy that originated prior to the existence of Citizens.

2. In three instances (CNR), the required photographs were missing from the files. The filed manual states:

*Photos:*

*1. Building: Two photos of the exterior of each building or structure(s) are required. One photo should reflect the front and side of the building with the other photo reflecting the back and remaining side of the building or structure to be insured.*

*2. Business Personal Property Only: A photograph of the building in which the business personal property is contained is required when Citizens writes business personal property only.*

**Citizens' Response:** Citizens agreed with these findings.

**Recommendation:** It is recommended that Citizens comply with its written underwriting requirements and ensure that staff are appropriately trained on those requirements.

3. In three instances (CNR), the required flood waivers were missing from the files. The filed manual states:

*Flood Waivers:*

*A signed “Election Not to Buy Separate Flood Insurance” Form (CIT-FW01) OR a copy of a current flood policy declarations page, if required, as provided in Rule 106.*

*If form CIT-FW01 is not completed and the property does not meet an exception, the insured must maintain a flood policy in effect, subject to the maximum limits available from the NFIP, as follows:*

- 1. With building limits not less than 80% of Citizens’ building limit, or where NFIP issues an Actual Cash Value (ACV) policy, not less than 80% of the building ACV, and*
- 2. With Business Personal Property limits equal to Citizens’ limit, if Citizens provides Business Personal Property coverage.*

***B. ELECTION NOT TO BUY SEPARATE FLOOD INSURANCE***

*Securing flood insurance is not a condition of coverage if the applicant or insured signs the “Election Not to Buy Separate Flood Insurance” (CIT-FW01) form. An applicant or insured located in a Special Flood Hazard Area that does not maintain a flood policy or sign the CITFW01.*

**Citizens’ Response:** Citizens agreed with these findings.

**Recommendation:** It is recommended that Citizens comply with its written underwriting requirements and ensure that staff are appropriately trained on those requirements.

## **A-RATED COMMERCIAL POLICIES**

Personal policies and the majority of commercial policies written by Citizens are class rated. The characteristics of these risks fall into certain classes that have rates filed and approved by the Office.

Citizens also utilizes another system of rating commonly known in the industry as individual risk rating (A-rates) for commercial residential wind policies (CR-W) and commercial residential multi-peril policies (CR-M) for buildings with a replacement cost that exceeds \$10 million. In general, the majority of these risks are large, high-rise condominium buildings located in proximity to the coast.

Section 627.062(3)(a), Florida Statutes, and Rule 69O-170.019(4), Florida Administrative Code, require that Citizens maintain the reason for risks to be A-rated and justification for the individual rate. All buildings insured in the CR-W and CR-M programs in excess of \$10 million are A-rated. These A-rates reflect yearly reviews of the base rates (including territory) for these risks including past and future premiums, losses, expenses and other such factors. Other than the base rates, these policies apply the other class rated factors. The examiners reviewed documents and interviewed a number of Citizens’ personnel regarding actuarial information in A-rating. The examiners conclude that Citizens maintains an active and appropriate program to justify rates applied to A-rated policies.

Citizens is required to file quarterly statistical reports for individually rated policies pursuant to Rule 690-137.008, Florida Administrative Code. These reports have been duly received by the Office.

As requested, Citizens provided a listing of the A-rated policies found within the commercial policies during the scope of the examination. Citizens furnished a list of 438 policies in force during the scope period consisting of the following:

<b>A-Rated Commercial Policies</b>	<b>Number of Policies</b>
Commercial Residential-Wind (CR-W)	223
Commercial Residential-Multi-Peril (CR-M)	215
<b>Total</b>	<b>438</b>

Citizens reports that in the third quarter reporting period of 2016 (outside the exam scope period), only 31 A-rated policies remain in force.

A proportional random sample of 86 A-rated policies was requested, received and reviewed for compliance primarily with the rating requirements of Florida Statutes and the Florida Administrative Code. As with other rating reviews, it is noted that supporting documents for the details used by Citizens in the rating process, such as construction and fire protection classes, were examined. The sample consisted of the following:

<b>A-rated Policies</b>	<b>Number of Sample Policies</b>
Commercial Residential-Wind (CR-W)	44
Commercial Residential-Multi-Peril (CR-M)	42
<b>Total</b>	<b>86</b>

No exceptions were noted.

## **CLAIMS REVIEW**

### **CLAIM PROCESSES AND PROCEDURES**

As requested, Citizens provided written processes and procedures for claim handling during the scope of the examination that included the following:

- a) Claim Settlement guidelines.
- b) Listing of adjusters for July 2014 through June 2016.
- c) Training and certification program for adjusters.
- d) Training program for claim examiners.
- e) Summary of supervisory review process to monitor claim processing practices.

This material was received and reviewed by the examiners for compliance with Florida Statutes and the Florida Administrative Code, as well as the file reviews, including Sections 626.9744, 626.9891, 627.351, 627.409, 627.4137, 627.4265, 627.7011, 627.70121, 627.70131, 627.7015, 627.702, 627.705, 627.707, 627.714, 627.7142 and 626.9541, Florida Statutes, and Rules 69O-166.024 and 69O-167.011, Florida Administrative Code.

No exceptions were noted.

## **ADJUSTER LICENSING**

Citizens handles claims through both company employed adjusters and independent adjusters. Section 626.112, Florida Statutes, requires that company-employed adjusters be licensed as all-lines adjusters and appointed by Citizens.

A listing of all adjusters employed by Citizens during the scope of the examination was requested. Citizens furnished a list of 176 company-employed adjusters. A random sample of 79 adjusters was requested, received and reviewed for compliance with licensing requirements of the Florida Statutes and the Florida Administrative Code.

No exceptions were noted.

## **CLAIM FILES**

As requested, Citizens provided a listing of the claims from personal policies during the scope of the examination. Citizens furnished a list of 56,597 claims from personal lines. The claims received by the top six categories are as follow:

<b>Type of Claim</b>	<b>Number</b>
Water Damage (Non-Weather)	30,771
Water Damage (Weather)	7,953
All Other Physical Damage	3,232
Wind	2,990
Theft from Other than Auto	2,352
Miscellaneous Other Categories	9,299
<b>Total</b>	<b>56,597</b>

A proportionate random sample of 109 claims from personal lines was requested, received and reviewed for compliance with the requirements of Florida Statutes and the Florida Administrative Code. The proportion of the sample was based on top categories of claims reported and consisted of the following:

<b>Type of Claim</b>	<b>Sample Number</b>
Water Damage (Non-Weather)	59
Water Damage (Weather)	15
All Other Physical Damage	6
Wind	6
Theft from Other than Auto	5
Miscellaneous Other Categories	18
<b>Total</b>	<b>109</b>

No exceptions were noted.

### **ANTI-FRAUD PLAN**

The Office reviewed reports and actions of Citizens' Special Investigations Unit (SIU). Citizens has an Anti-Fraud Plan and a specialized team of internal investigators and contract vendors who detect and investigate fraud. The SIU also educates claims and underwriting staff on how to identify signs of fraud and assist agents with procedures for reporting suspected fraud. The unit regularly reports to the board and relevant committees on its activities. Cases of suspected fraud are regularly referred to the Division of Insurance Fraud.

### **EXAMINATION REPORT SUBMISSION**

The Office hereby issues this report as the Final Report, which is based upon information from the examiner's draft report, additional research conducted by the Office, and additional information provided by the Company.