



**Department of Insurance**  
**State of Arizona**  
*Office of the Director*  
**Telephone: (602) 364-3471**  
**Facsimile: (602) 364-3470**

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**JANICE K. BREWER**  
Governor

2910 North 44<sup>th</sup> Street, Suite 210  
Phoenix, Arizona 85018-7269  
[www.azinsurance.gov](http://www.azinsurance.gov)

**GERMAINE L. MARKS**  
Director

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REGULATORY BULLETIN 2014-07<sup>1</sup>

**TO:** All Insurers Authorized to Transact Property & Casualty Insurance in Arizona, Insurance Producers, Insurance Trade Associations, and Other Interested Parties.

**FROM:** Germaine L. Marks  
Director

**DATE:** October 8, 2014

**RE:** **Premium Credit for Subscription to Fire Protection Service**

Property and casualty insurers doing business in Arizona file their rating systems with the Department. Most of these insurers recognize in their rating systems policyholders who subscribe to a private fire protection service and those policyholders pay a lower premium or get a "credit" for subscribing. The purpose of this Bulletin is to reaffirm and update the Department's previously stated position regarding the policyholder premium credit for subscription fire protection. In 1994, then-Director of Insurance Chris Herstam issued Circular Letter No. 94-2 titled "Premium Credit for Subscription to Fire Protection Service." This Bulletin does not state a position contrary to Circular Letter No. 94-2; however, for clarity's sake, this Bulletin supersedes Circular Letter No. 94-2.

It has come to my attention, despite the clear warnings of the previously-issued 1994 Circular Letter, that some insurance producers continue to give policyholders a credit for subscribing to a fire protection service when the agent either knows the policyholder is not a subscriber or the agent does nothing to verify the policyholder's subscription status from policy year to policy year. Insurers also have a responsibility to review their rates and rating plans in use in Arizona and, if necessary, modify those rates and rating plans to ensure appropriate use of the subscription fire protection service credit.

**BACKGROUND**

In order to establish appropriate fire insurance premiums for residential and commercial properties, insurers rely on the Insurance Services Office (ISO) for information about

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subscription fire protection services through ISO's Community Mitigation Classification Manual (CMC). CMC contains Public Protection Classifications (PPCs) which range from 2 (the lowest PPC base rate level) to 10 (the highest PPC base rate level). A policyholder who does not subscribe to a fire protection service will pay a substantially higher premium if rated in a PPC 10 than if the policyholder subscribed to a service and was assigned to a PPC 8 or 9. A fundamental assumption in an insurer's PPC rating rules is that a policyholder will actually have subscribed to a fire protection service before receiving the lower premium or "credit" for being a subscriber.

The determination of whether a property is within a particular fire district or service area is critical to accurate policy risk-rating and the insurer must take appropriate steps to confirm the correct classification status of its covered properties. Fire districts, as well as their taxpayers and subscribers, invest heavily to obtain PPCs that benefit its residents. Applying a lower PPC to a policy on a property not entitled to that classification places that fire district or subscription-based fire service in an unfair competitive position because they are not collecting the fire protection subscription fees to which they are entitled. When a policyholder does not subscribe to the required fire protection service for the PPC applied to their policy, the policyholder will incur a substantial loss as they would have to pay for the expenses of the Fire District to fight their fire.

### **Potential Violations of Title 20**

The Department considers the practice of giving a policyholder a fire protection service credit when the policyholder is **not** a subscriber to a fire protection service to constitute a misrepresentation under Arizona Revised Statutes (ARS) §§20-443(1) and (5), and a rebate under ARS §20-451. Further, a producer may place the insurer it represents in violation of ARS§20-385(A), the rate filing law, if: 1) the insurer has not filed the discount the producer offers; or 2) the insurer has filed the discount but the produce has offered it improperly.

Specifically, ARS §§20-443(1) and (5), 20-451, and 20-385(A) state in material part:

#### ARS §20-443

No person shall make . . . any estimate, illustration, circular, sales material or statement:

1. Misrepresenting the terms of any policy issued or to be issued or the benefits or advantages promised . . .
5. Making any misrepresentation to any policyholder for the purpose of inducing or tending to induce such policyholder to . . . retain or convert any insurance policy.

#### ARS §20-451

No insurer or employee, agent or representative thereof, or broker . . . shall offer, pay allow, or give directly or indirectly, as an inducement to insurance, or after insurance has been effected, any rebate, discount, abatement, credit or reduction of the premium . . . except to the extent provided for in an applicable filing.

#### ARS §20-385(A)

. . . (e)very authorized insurer and every rate service organization . . . shall file with the director all rates and supplementary rate information and all changes and amendments to those rates made by it for use in this state within thirty days after they become effective.

The Department will, through its market conduct and rate examinations, as well as investigations, review whether a fire protection service credit has been allowed when the policyholder does not have a fire protection service contract, will not consider such credits as merely "inadvertent errors," and will take disciplinary action as appropriate against any producer and/or insurer found to be in violation of these Arizona laws.

Please direct any questions relating to this Regulatory Bulletin to Dean Ehler, Property & Casualty Assistant Director at (602) 364-3453, or [dehler@azinsurance.gov](mailto:dehler@azinsurance.gov).