

CERTIFIED MAIL  
RETURN RECEIPT REQUESTED

STATE OF ALASKA  
DEPARTMENT OF COMMERCE, COMMUNITY AND ECONOMIC DEVELOPMENT  
DIVISION OF INSURANCE  
PO BOX 110805  
JUNEAU, AK 99811-0805

Order # TA 17-03 )  
In the Matter of Audit of )  
Pacific International Underwriters Inc. )  
\_\_\_\_\_ )

FINDINGS OF FACT

1. An audit report of Pacific International Underwriters Inc., licensed in the State of Alaska, has been issued by the State of Alaska, Division of Insurance to Pacific International Underwriters Inc.

2. The audit report of Pacific International Underwriters Inc. (TA 17-03) has been transmitted to Randall Blanchard, Compliance Officer, Pacific International Underwriters Inc. (Auditee), and Auditee has been accorded at least 30 days' opportunity to review and comment on this audit report.

3. The director of the Division of Insurance has fully considered and reviewed the report and any relevant portions of the auditor's work papers to the extent she considered necessary.

CONCLUSIONS OF LAW

1. The written audit report referred to in Finding of Fact No. 1 was issued in accordance with Alaska Statute (AS) 21.06.150(b).

2. The actions set forth in finding of Fact No. 2 were conducted in accordance with AS 21.06.150(b).

3. The director of the Division of Insurance has reviewed the audit report and any other relevant work papers as set forth in Finding of Fact No. 3 to the extent she considered necessary in accordance with AS 21.06.150(b).

ORDER

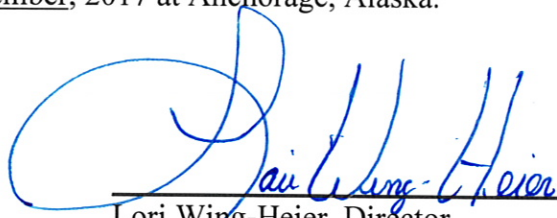
IT IS ORDERED

1. Pursuant to AS 21.06.150(b)(1), the audit report of Pacific International Underwriters Inc. (TA 17-03) is approved as filed.

2. Pursuant to AS 21.06.060, the audit report shall be kept in the office of the director of the Division of Insurance and be open to public inspection.

This order is effective November 27, 2017.

Dated this 27th day of November, 2017 at Anchorage, Alaska.



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Lori Wing-Heier, Director  
State of Alaska  
Division of Insurance

**PREMIUM TAX AUDIT OF**

**Pacific International Underwriters Inc.**

**Edmonds, WA**

**Alaska License # 7891**

**TA 17-03**

**As of December 31, 2016**

**Issued by**

**DIVISION OF INSURANCE**

**DEPARTMENT OF COMMERCE, COMMUNITY AND ECONOMIC**

**DEVELOPMENT**

**STATE OF ALASKA**



**FINAL REPORT:**  
**November 27, 2017**

## TABLE OF CONTENTS

	PAGE
1) TABLE OF CONTENTS.....	2
2) SALUTATION .....	3
3) SCOPE OF AUDIT.....	3
4) METHODOLOGY .....	4
5) PREMIUM TAX AUDIT .....	6
6) SUMMARY AND SUBSEQUENT EVENTS.....	11
7) AFFIDAVIT .....	12



November 27, 2017

P.O. Box 110805  
Juneau, AK 99811-0805  
Main: 907.465.2515  
Fax: 907.465.3422

Lori K Wing-Heier, CRM  
Director, Division of Insurance  
Department of Commerce, Community and Economic Development  
550 West 7<sup>th</sup> Avenue, Suite 1560  
Anchorage, AK 99501-3567

Pursuant to Alaska Statute (AS) 21.06.120, the Alaska Division of Insurance performed a limited and targeted premium tax audit of Pacific International Underwriters Inc. The audit was conducted by Rebecca Nesheim, tax auditor for the Alaska Division of Insurance.

**Pacific International Underwriters Inc.**

**SCOPE OF AUDIT**

This premium tax audit was called to review compliance with the surplus lines statutes AS 21.34, and regulations 3 AAC 25 and the premium tax regulations 3 AAC 21.550 – 570. This is the first premium tax audit of Pacific International Underwriters Inc. conducted by the Alaska Division of Insurance (the division).

**Subject Matters Audited**

Pacific International Underwriters Inc. (the broker) is an Alaska licensed surplus lines broker based in Edmonds, WA. The division elected to audit their quarterly filings, premium taxes and filing fees paid for accuracy and timeliness as well as required diligent search efforts, disclosures, notifications, and prompt delivery of material facts in evidence of insurance to the insured.

**Time Frame**

The audit covered the broker's surplus lines business for policy effective dates occurring between January 1, 2015 and December 31, 2016.

## **METHODOLOGY**

The division sent the call letter and initial data requests to the broker's office in Location. A list of all Alaska business transactions with nonadmitted insurers was requested for the period to be audited. The broker complied on a timely basis with all data requests. The number of policies written during the audit period was 262, from which a sample of 50 files were selected for audit.

### *The following are the procedure steps for the audit:*

- 1) Verify that quarterly reports and accompanying forms were filed on time.
  - i) Audit steps taken:
    - (1) Reviewed the quarterly reports sent to the Alaska Division of Insurance and verified they were filed by the due date.
- 2) Verify the accuracy of the premium calculation.
  - i) Audit steps taken:
    - (1) Reviewed policy, binders, and invoices to determine how taxable premium was calculated.
    - (2) Verified the correct premium was reported on the reports as filed.
- 3) Verify the accuracy of quarterly reports filed.
  - i) Audit steps taken:
    - (1) Reviewed the policy, binder, and endorsement pages in each file.
    - (2) If the effective date did not match the quarterly filing, reviewed the correspondence to ensure the documentation in the file matched when the policy was booked. Most of these occurred with endorsements that often require additional information and sometimes company approval before it can be added to the policy. The invoice date determines in which quarter the endorsement is required to be filed.
    - (3) Verified the quarterly reports as filed with the division were accurately filled out to reflect the correct effective date, premiums, taxes and fees based upon the information in the files.
    - (4) Verified a statement of exempt premiums was filed when appropriate.
    - (5) Verified the policy was included in the quarterly filing based upon the effective date of the policy.
    - (6) Verified the insured name, insurance company, policy type codes, producer names and license numbers were accurate on the forms filed.
    - (7) Verified the descriptions of the subject and locations of risk were identified on the reports.
- 4) Confirm Alaska is the home state of the insured.
  - i) Audit steps taken:
    - (1) Verified where the principal place of business or residence of the insured is located.
    - (2) Verified at least partial risk is located in Alaska or the highest % of premium in Alaska if headquarters not in Alaska with no risk in the headquarters state.
- 5) Verify if tax and filing fee payments were made on time and by ACH.
  - i) Audit steps taken:
    - (1) Confirmed when the payments were received by the Alaska Division of Insurance and the payment method.
- 6) Verify tax and filing fee payments were made accurately.

- i) Audit steps taken:
    - (1) Confirmed if the tax and fee payments matched the quarterly reports as filed.
- 7) Review effort made to place insured with an admitted insurer.
  - i) Audit steps taken:
    - (1) Verified the diligent search was documented prior to binding and received within 15 days from binding. If there were no declinations due to risk on the placement list, the list effective at the time of placement was reviewed to ensure the risk was on the list
- 8) Review prompt delivery of evidence of insurance AS 21.34.100(a) and 3 AAC 25.060.
  - i) Audit steps taken:
    - (1) Reviewed dates of binding and forwarding evidence of insurance to insured.
- 9) Review required material facts are located on evidence of insurance AS 21.34.100(a).
  - i) Audit steps taken:
    - (1) Reviewed documents to confirm required material facts were located on the evidence of insurance when policy not available within 30 days of binding.
- 10) Review disclosures for use of non-admitted insurer.
  - i) Audit steps taken:
    - (1) Reviewed the evidence of insurance to ensure the broker's name and language required by statute AS 21.34.100(e) is present and legible.
- 11) Review notifications for use of non-admitted insurer.
  - i) Audit steps taken:
    - (1) Reviewed the correspondence and other documentation in the files to find a copy of the notification sent to the insured that meets the requirement in AS 21.34.110
- 12) Confirm coverage is placed with an eligible non-admitted insurer.
  - i) Audit steps taken:
    - (1) Reviewed the Alaska published white lists and NAIC Quarterly Listings of Alien Insurers to ensure the company was eligible at the time of placement.
- 13) Review notice regarding nonrenewal and premium increase
  - i) Audit steps taken:
    - (1) Verified there was an Alaska Policyholder Notice regarding nonrenewal and premium increase included with the policy in the format approved by the Director of the Alaska Division of Insurance.
- 14) Other issues not previously identified as a procedure step were included when not in compliance with Alaska laws.
  - i) Audit steps taken:
    - (1) Reviewed documents to ensure other surplus lines statutes and regulations requirements were met.

**Acceptable Error Rate:**

The Broker's acceptable error rate for the above referenced standards and tests must be less than 10%.

## **PREMIUM TAX AUDIT**

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|---|
| <b>1. Verify quarterly reports and accompanying forms were filed on time</b><br><b>AS 21.34.080 and .170, 3 AAC 25.090 and .100</b> |
|---|

*Comments:* The eight original quarterly reports with accompanying forms were filed on time.

*Results:* Passed (error rate 0%)

- |   |
|---|
| <b>2. Verify the accuracy of the premium calculation</b><br><b>AS 21.34.180</b> |
|---|

*Comments:* The premium was calculated incorrectly on one policy in the audit files. Premium did not include inspection fees and were not part of the calculation of the tax and fees due to the Division. It is irrelevant who charges for the inspection as it is made in consideration for an insurance contract.

The broker charges a broker fee but they call it a policy fee. Policy fee is a term generally associated with an insurance company fee made in consideration of an insurance contract and would be part of premium and taxable. The broker also labels their wholesaler's wholesale access fee as a "carrier policy fee," which also is a term associated with a company fee.

This error affects two additional audit tests:

1. Accuracy of the Quarterly Reports
2. Accuracy of Tax and Fee Payments

*Results:* Passed (49 files passed & 1 failed, error rate 2%)

*Recommendations:* It is recommended the broker create written procedures to ensure all insurance company fees are included in the calculation of premium tax and filing fees regardless of who actually charges the fee. The broker should read bulletin 04-14 to reinforce their understanding of what fees are to be included in premium and what are not. It is also recommended the broker rename their "policy fee" to "broker fee" or something similar and "carrier policy fee" to "wholesale access fee" or something similar so the other entities in the transaction chain plus the insured knows what the fee is for and they are not given a name synonymous with insurance company fee terminology.

*The broker response:* PIU has updated their agency management/accounting system to ensure all inspection fees are included as premium in the calculation of tax and fees. PIU has also updated their procedure so that their own broker fee is now called a "wholesale policy fee".

- |   |
|---|
| <b>3. Verify the accuracy of all quarterly reports filed</b><br><b>AS 21.34.080 and .170, 3 AAC 25.090 and .100</b> |
|---|

*Comments:* Multiple errors were noted on the Report of Surplus Lines Transaction forms and Quarterly Reports filed with the division:

- Transaction not filed on the original report but on an amended report – 1



- Endorsement was missing invoice date – 1
- Missing full address of insured – 1
- Company NAIC# incorrect – 1
- Insurance company incorrect on original report – 1
- Producer license # incorrect on both initial & endorsement transactions – 2

Total accuracy errors: 7 within 5 distinct files

After July 21, 2011, there was some confusion with multi-state risk transactions if the location of risk was still required to be reported when the insured's home state was Alaska with 100% of the premium reported to Alaska. Locations of risk are still required to be reported per statute AS 21.34.080(a)(3). For five multi-state policies in the audit, the other states were not identified on the reports as filed to the division. This will not be a finding in this audit but all future quarterly reports need to have locations of risk accurately identified. This can include either listing each state involved or a complete spreadsheet of all separate address locations or something in between.

One policy and one endorsement were filed with the transaction date one day off from the actual date but all within the same quarter. There was no effect on the quarterly report or the taxes and fees so will not be considered an error for this audit but this will need to be fixed for future reports so as not to cause a filing made in the wrong quarter report.

*Results:* Failed (45 files passed & 5 failed, error rate 10%)

*Recommendations:* It is recommended the broker create written procedures for ensuring all information on the Quarterly Report and related Report of Surplus Lines Transaction forms are complete and accurate based upon the information in the policy files. The procedures should include the different components of the form and how they are to be filled out.

*The broker response:* Written procedures have been put into place to ensure all information on the quarterly report and report of surplus lines transaction forms are accurate. Procedures include verifying the date of the transaction, making sure addresses are correct/complete and matching the dec page, company names and NAIC numbers are completed and producer license numbers are correct and complete. PIU will also perform an internal audit of transaction forms on a quarterly basis to ensure all information is accurate and complete.

<p><b>4. Verify the home state for insured is Alaska</b></p>
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**AS 21.34.180**

*Comments:* The broker writes some multi-state policies. The home state was correctly identified as Alaska for all policies.

*Results:* Passed (error rate 0%)

**5. Verify if tax and filing fee payments were made on time and by ACH**  
**AS 21.34.180, 3 AAC 21.550 - .570**

*Comments:* All payments were made on or before the required due date for the quarterly payments and made by ACH.

*Results:* Passed (error rate 0%)

**6. Verify tax and filing fees payments were made accurately**  
**AS 21.34.180, 3 AAC 21.550 - .570**

*Comments:* All tax and fee payments made by the broker were accurate based upon the quarterly reports as filed. The error found during the audit in the premium calculation affects the accuracy of the tax and fee payments. This flow-through finding is addressed in its respective audit test.

*Results:* Passed (error rate 0%)

**7. Review diligent search effort made to place insured with an admitted insurer**  
**AS 21.34.020, 3 AAC 25.010 and .035**

*Comments:* The broker has elected to use the Affidavit of Due Diligence for documenting the diligent search. In two files, the affidavits were received from the producer after the allowed 15 days from binding.

*Results:* Passed (48 files passed & 2 failed, error rate 4%)

*Recommendations:* It is recommended the broker create written procedures to ensure all Affidavits of Due Diligence are received no later than 15 days after binding. One avenue to consider would be to require receipt of the Affidavit prior to binding or releasing the binder or policy to the producer.

*The broker response:* PIU has instructed staff to obtain a copy of the due diligence affidavit from the retail producer prior to binding coverage.

**8. Review prompt delivery of evidence of insurance**  
**AS 21.34.100(a) and 3 AAC 25.060**

*Comments:* All initial evidence of insurance was provided within 30 days from binding.

*Results:* Passed (error rate 0%)

**9. Review required material facts located on evidence of insurance**  
**AS 21.34.100(a)**

*Comments:* The broker generates binders but they are sometimes not sent to the producer/insured. These binders do not have all the required material facts as required by statute.

The policies were all sent within 30 days so those were evaluated for the material facts. Four policies were missing the broker license number.

*Results:* Passed (46 files passed & 4 failed, error rate 8%)

*Recommendations:* It is recommended the broker create written procedures to include what material facts regarding the coverage, insured, insurer, and broker must be on evidence of insurance. Review statute for details. It is also recommended the binders be modified to include all required material facts to ensure those sent to the producer/insured contain all required information. Binders that reference quotes as “see attached for...” should include the following language: “Quote Number \_\_\_\_\_ dated \_\_\_\_\_ is incorporated by reference and is part of this binder as though fully set forth herein.” This is especially important when quotes are revised.

*The broker response:* PIU has updated our agency management system so that binders include all material facts as per statute. Staff have been instructed and trained as to what material facts are required on the binders. This includes our broker license number.

<b>10. Review disclosures on evidence of insurance for use of non-admitted insurer</b> <b>AS 21.34.100(e) &amp; .100(f)</b>
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*Comments:* Forty-nine files demonstrated a problem with the required disclosure language on all evidence of insurance. The disclosure language the broker routinely used referenced an incorrect statute or was missing a word. Since the language is in quotations in the statute, it must be word-for-word. Here are the different problems found in the files:

- No disclosure on binder sent to producer/insured – 12
- No disclosure on dec – 1
- No disclosure on endorsement – 35
- No disclosure on certificate – 2
- Incorrect disclosure language on binder sent to producer/insured – 20
- Incorrect disclosure language on dec – 47
- Incorrect disclosure language on endorsement – 13
- Broker name not on endorsement – 4
- Disclosure less than 10 point type on dec – 6
- Disclosure less than 10 point type on endorsement - 1

Total disclosure errors: 141 within 49 distinct files

*Results:* Failed (1 file passed & 49 failed, error rate 98%)

*Recommendations:* It is recommended the broker create written procedures to ensure all evidence of insurance have the required correct disclosure language and is at least 10 point type. It is further recommended to revise the written procedures to include the disclosure language on all premium bearing and non-premium bearing endorsements as they are also evidence of insurance. One last recommendation is to ensure the broker firm name is included on all evidence of insurance.

*The broker response:* PIU has updated our disclosure stamp – copy of the updated stamp provided showing correct disclosure language and broker firm name. Written procedures have been put into place outlining when the disclosure is to be placed – quotes, binders, dec pages, all premium and non premium bearing endorsements and certificates of insurance.

**11. Review notification for use of non-admitted insurer**

**AS 21.34.110**

*Comments:* The broker currently requires the retail producer send the notification to the insured and provide the broker with a copy. Forty-four files were missing the notification in the files as the broker did not receive the notification from the producer.

*Results:* Failed (6 files passed & 44 failed, error rate 88%)

*Recommendations:* It is recommended the broker not rely upon the retail producer to provide the notification to the insured but to create written procedures to include the Alaska notification language on or with the quote to the insured describing the surplus lines insurance company as required by statute. The information should include the three points of the notification: the company does not have a certificate of authority, they are not regulated by the Alaska Division of Insurance and in the event of insolvency losses will not be covered by the Alaska Insurance Guaranty Association Act.

*The broker response:* PIU has implemented a procedure so that the following wording is placed on all AK surplus line quotes sent out: “We require proof of notification of surplus line placement to the insured, per AS 21.34.110”. A copy of the notification (AS 21.34.110) is emailed with each quote.

**12. Confirm coverage is placed with an eligible non-admitted insurer**

**AS 21.34.050**

*Comments:* All policies in the audit were placed with eligible surplus lines companies.

*Results:* Passed (error rate 0%)

**13. Review notice regarding nonrenewal and premium increase**

**3 AAC 25.050**

*Comments:* All policies included the Alaska Policyholder Notice.

*Results:* Passed (error rate 0%)

## **SUMMARY AND SUBSEQUENT EVENTS**

### **Summary**

This was a premium tax audit of Pacific International Underwriters Inc. The auditor tested 13 standards focusing on the broker's filing of quarterly reports and the subsequent payment of premium taxes and filing fees as well as diligent search efforts, disclosure and notification requirements for using a non-admitted insurer, and prompt delivery of material facts to insured.

The audit was conducted in the auditor's office as she received electronic versions of the broker's files under audit. The broker responded quickly to all requests for additional information. The auditor appreciated this behavior.

Several significant issues did arise during the audit that affect the service to the insured and compliance with Alaska statutes and regulations.

- 1) Several quarterly reports were not accurate when filed.
- 2) The disclosure language was either missing or incorrect on most of the evidence of insurance.
- 3) The required notification to the insured regarding the use of a nonadmitted insurer was not found in most files

The auditor would like to review any new or revised procedures to help the broker ensure all problems identified in the audit were captured accurately.

### **Re-Audit**

In closing, the auditor's recommended actions and review of the procedures should help the broker correct the problems encountered. It is recommended that Pacific International Underwriters Inc. be re-audited within the next three years to ascertain compliance.


Submitted by:  
Rebecca Nesheim  
Tax Auditor

Affidavit

PACIFIC INTERNATIONAL UNDERWRITERS INC.  
As of December 31, 2016  
TA 17-03


Juneau, Alaska )  
November 27, 2017 )  
State of Alaska ) ss.  
First Judicial District )

I, being duly sworn, do verify that the report of premium tax audit as of December 31, 2016 of Pacific International Underwriters Inc. is true to the best of my knowledge and belief.

  
Rebecca Nesheim  
Tax Auditor

SUBSCRIBED and SWORN to before me this 27<sup>th</sup> day of November, 2017



  
Notary Public in and for Alaska  
My Commission Expires office