



1 examination was conducted both at the site of the examinee's offices in Anchorage and at the  
2 offices of the division in Anchorage, Alaska. Mr. Christian F. Ulmann was the Examiner-in-  
3 Charge.

4  
5 Finding No. 4.

6  
7 A Report, MCE-P-05-04, of the Market Conduct Examination of Marsh in compliance  
8 with Alaska statute and matters enumerated in the Notice of Examination was presented to the  
9 examinee on May 15, 2006 and filed with the division in accordance with AS 21.06.150(b).

10  
11 Finding No. 5.

12  
13 In accordance with AS 21.06.150(b), Marsh was afforded the opportunity to respond to  
14 the division concerning matters contained in the Report of Market Conduct Examination. A  
15 response was received on June 14, 2006. Marsh took issue with certain items in the report. The  
16 division and Marsh agreed to have further discussion and Marsh agreed to provide additional  
17 information in an effort to resolve their differences. Marsh also agreed to satisfy the  
18 recommendations in the report. Between May 2006 and April 2007, Marsh provided additional  
19 information that the division reviewed and Marsh also performed all of the requirements  
20 contained in the recommendations to the satisfaction of the Director. Based on the foregoing,  
21 MCE-P-05-04 was withdrawn and was re-issued as MCE-P-05-04B, the subject of this adoption  
22 order.

23  
24 Finding No. 6.

25  
26 The Director has fully considered and reviewed to the extent that she considered  
27 necessary the Report of Market Conduct Examination, together with the written response of  
28 Marsh, the subsequent performance by Marsh of the requirements under the report and  
29 agreement with the division, and any relevant portion of the examiners' work papers.

30  
31 Finding No. 7.

32  
33 The examination of Marsh was conducted in accordance with applicable Alaska statutes.  
34 The report is a factual account of the findings of the examiners based on tests that determine  
35 compliance with Alaska statutes and regulations and supported with appropriate documentation.

36  
37  
38  
39 **CONCLUSIONS OF LAW**

40  
41 Conclusion No. 1.

42  
43 The examination report was filed with the division and transmitted to Marsh in  
44 accordance with AS 21.06.150(b).  
45

1 Conclusion No. 2.  
2

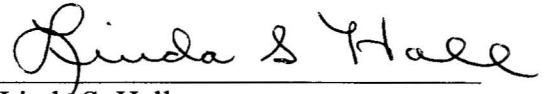
3 An order should be issued in accordance with AS 21.06.150(b) approving the  
4 examination report.  
5

6  
7  
8 **ORDER**  
9

10 It is hereby ordered that under AS 21.06.150(b) the attached Report of the Market  
11 Conduct Examination of MARSH USA, INC., formerly MARSH USA, INC. (Alaska), (MCE-P-  
12 05-04B) dated April 25, 2007 is approved.  
13

14 This order is effective April 27, 2007.  
15

16 Dated this 27<sup>th</sup> day of April 2007, at Anchorage, Alaska.  
17  
18

19   
20

21 Linda S. Hall  
22 Director

**STATE OF ALASKA  
DEPARTMENT OF COMMERCE,  
COMMUNITY, AND ECONOMIC  
DEVELOPMENT**

**DIVISION OF INSURANCE**

**REPORT OF MARKET  
CONDUCT EXAMINATION**

**OF**

**MARSH USA, INC., formerly  
MARSH USA, INC. (ALASKA)  
ANCHORAGE, ALASKA**

**MCE -P-05-04B**



**Submitted by  
H. Theodore Lehrbach  
Chief Examiner, Market Conduct Section**

**April 25, 2007**

**TABLE OF CONTENTS**

	<b>PAGE</b>
1) FINDINGS.....	ii
2) ACTION SUMMARY.....	iii
3) SCOPE OF EXAMINATION.....	1
4) COMPANY AND PRODUCTION PROFILE.....	2
5) METHODOLOGY .....	3
6) SAMPLE.....	3
7) MARKETING AND PLACEMENTS OF INSURANCE.....	4
8) CONTINGENCY FEES .....	4
9) MARSH’S ACCOUNTING OF CONTINGENCY FEES.....	5
10) MARSH’S USE OF BROKER’S FEE AGREEMENTS .....	5
11) CONTRACTUAL OBLIGATIONS.....	6
12) CONDITION OF FILES.....	11
13) COOPERATION .....	11
14) CERTIFICATION .....	12

## **FINDINGS**

The examiners made two findings. The support for those findings is shown under the applicable sections.

### **FINDING ONE**

**The examiners determined that MARSH diligently searches the market and places the coverage with the consumer's best interest in mind. The MARSH marketing files reviewed were well documented concerning its marketing efforts. The examiners found no evidence of bid rigging or steering of accounts.**

**(See MARKETING AND PLACEMENTS OF INSURANCE FOR CLIENTS, Page 04)**

Although the above finding addresses two of the initiating reasons for the examination, the following finding directly addresses one of the main components of the Division's concerns.

### **FINDING TWO**

**The examiners determined that MARSH breached the contractual obligations owed to three clients, under the contracts they entered into as regulated by AS 21.27.560, by not disclosing the receipt of commissions and refunding and/or offsetting these commissions to the clients as stipulated in the contracts.**

**(See Pages 6-10)**

## Action Summary

### Recommendation # 1

The examiners recommend that MARSH perform an internal file audit for the period of January 1, 2001 to November 09, 2004, involving clients with broker's fee agreements, assuring that disclosure and refunds of commissions, if applicable, have been adhered to according to their contracts. (Page 10)

### Recommendation # 2

The examiners recommend that MARSH implement procedures and controls to assure that MARSH discloses and refunds commissions received, if required by their broker's fee agreement(s), to assure compliance with AS 21.27.560. (Page 10)

### Recommendation # 3

The examiners recommended that in order to be in compliance with AS 21.27.350, MARSH needs to adequately disclose to the consumer a detailed itemization of all charges billed to the consumer. (Page 11)

April 25, 2007

Linda S. Hall, CPCU, CIC  
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, AS §21.06.080, AS §21.06.130, AS §21.06.140 and AS §21.06.150, The Alaska Division of Insurance (Division) performed a Limited Market Conduct Examination at the Anchorage, Alaska office, of MARSH USA, INC. (Alaska) (MARSH) on June 02, 2005, to August 16, 2005. The data collection and verification process ended on September 30, 2005. The examination team consisted of: Mr. Christian F. Ulmann, Examiner-in Charge and Ms. Carol Harbeson, Market Conduct Examiner. The examiners are employees of the Alaska Division of Insurance.

**MARSH USA, INC., formerly  
MARSH USA, INC. (Alaska)  
(MARSH)**

**MCE-P-05-04B**

**SCOPE OF EXAMINATION**

This Market Conduct Examination was initiated in part by the recent attention given by the NAIC and other states to the issues of illegal bid rigging and the steering of business through the improper use of contingency fees. The NAIC established a 13 state Executive Task Force on Broker Activities. This task force initiated a coordinated effort by all states to assess and address the issues raised by a New York investigation of the industry. Alaska initiated this review in conjunction with the NAIC Executive Task Force efforts to investigate whether, and the extent to which, this practice is found among the various states. Additionally, the states of California and New York initiated independent probes into the same issues.

On November 09, 2004, the Alaska Division of Insurance initiated a review with the purpose to ascertain the extent, if any, of potential violations of Alaska Insurance Statutes, as it relates to solicitation or placement of



insurance based upon improper incentives that conflict with the best interest of the insured or prospective insured. This examination consisted of reviewing a multitude of requested documents, provided to the Division by Insurance Producers. The examiners reviewed in the Anchorage office of the Alaska Division of Insurance the submitted information from 210 Insurance Producers. This segment of the examination was referred to as Phase 1. This examination is a continuation of the previous examination. The information contained in this report reflects the activities of a second, more detailed examination and is referred to as Phase 2.

#### Purpose and Description:

The purpose of this targeted Market Conduct review was to see if any illegal bid rigging, improper steering of business, or if any other breach of fiduciary responsibility has occurred in Alaska by MARSH.

#### Supplemental Note:

This report reflects additional information received from the examinee between May 2006 and the date of this report. Upon agreement with the Director and the examinee, MARSH has fulfilled the requirements contained in recommendations 1, 2, and 3. The Director is satisfied with the results of the audits conducted by MARSH and their response to those results of the audits.

#### Time Frame

The initial examination review covered the MARSH operations on Alaska business from January 01, 2001, through November 09, 2004.

## **COMPANY & PRODUCTION PROFILE**

### **MARSH USA, INC. (Alaska)**

MARSH USA, Inc. bought the Alaska resident insurance brokerage firm of Brady and Company on December 31, 2003. Effective January 01, 2004, Brady & Company became MARSH USA, Inc, (Alaska). It is therefore an indirect, wholly-owned subsidiary of MARSH USA Inc. and a licensed insurance broker, with principal offices in Anchorage, Alaska. MARSH USA, Inc. (Alaska) is licensed in Alaska and holds firm license #8567 for the Anchorage office. On November 1, 2005 that firm license was cancelled and business in Alaska continued under firm license #7782. MARSH handles mostly medium and large commercial accounts. In addition to the commercial operation, MARSH also operates a Benefits Section and a Benefits Consulting Section.

The customers are handled with a team approach. Each account is assigned an account executive, who serves as the team leader. Every account executive has an account manager and other support staff to service the account. The team approach provides the customer with several staff contacts and their individual expertise.

Since January 01, 2004, all premium payments as well as premium refunds and all revenue are processed through MARSH's Denver Finance office in Colorado. Alaskan premium payments are sent to their Lockbox in Chicago. Any funds received in the local office are forwarded to the Chicago lockbox.

### **The National Settlement of \$850 million**

The examiners would like to emphasize that the practices that lead to the \$850 million national settlement with

the New York Attorney General stand apart from the findings in this report. According to the settlement language, MARSH USA INC. will pay this amount in four annual payments to identified Alaskan policyholders who retained MARSH to place, renew, consult on, or service insurance where such placement resulted in contingent commissions or overrides.

The Alaska Division of Insurance received a list showing the future recipients of funds from MARSH's settlement with the New York Attorney General's office. In a June 02, 2005, meeting with the local MARSH representatives and their attorney, the examiners discussed the criteria used to identify Alaskan policyholders who are entitled to a portion of the proceeds of the settlement. Then on June 08, 2005, the examiners asked what role, if any, the local office played in deciding the criteria used to identify Alaska policyholders who were entitled to participate in the settlement.

On June 8, 2005, MARSH replied:

*"No role. Those determinations were made solely at the national level."*

The examiners further inquired whether the Alaskan policyholders shown on the list and eligible for the settlement, obtained insurance from the local Marsh affiliate or its' predecessors.

On June 08, 2005, MARSH replied:

*"The answer is that only Marsh placed policies were involved; no policies placed by Marsh's Alaska predecessors were at issue."*

The examiners compared the clients identified on the benefit recipient list with the Alaska clients provided by MARSH USA of Alaska. The examiners determined that MARSH USA of Alaska clients are not shown on the national settlement recipient list and therefore stand apart from the national settlement. As a result, the Alaska Policyholders which came to MARSH USA of Alaska through the Brady and Company acquisition will not partake in the \$ 850 million settlement. None of the reviewed client files during this examination are shown on the settlement recipient list of the national settlement.

Although Alaska has participated in the NAIC multi-state agreement, there was no restriction in the agreement regarding independent findings arising out of this examination.

## METHODOLOGY

The examiners conducted interviews with Company staff; reviewed materials (including procedure manuals); and reviewed files. In addition, the examiners were provided printouts of accounting records and taught how to operate and access the electronic data systems.

MARSH responded to the examiners with verification sheets identifying policies and/or issues requiring additional information and/or clarification.

MARSH responded to all inquiries. The collected data, verification sheets and responses to such, support all statements made in this report.

On September 30, 2005, MARSH provided the final response requested in the fieldwork process. Analysis of the data collected at the examination site and correspondence warranted closure of the fieldwork phase of the examination on October 31, 2005.

## SAMPLE

MARSH's files are a combination of hard copies and electronic documents retained in the Anchorage office. Because of the history of ownership changes, the examiners found two electronic management systems applicable to the examination period. The first system, is the Agency Management System (AMS), a transactional filing system, which was in use during the time the examinee was under the Brady & Company ownership. The second management system, BASYS, has been in use since January 2004 the time Marsh purchased Brady & Company.

It must be noted that the examiners encountered significant difficulty in recreating the complete history of relevant events within the accounts reviewed. There were reasons for this difficulty. First, it was necessary to search in each of the management systems, as well as the hard copy file and the transactional filings in order to recreate the relevant events for each account. Second, each account executive utilized the various management systems according to his/her preference. Therefore, each account was documented in a manner specific to the account executive assigned. For the time period reviewed, there was no apparent consistency in the method of file management within the agency.

The examiners had difficulty re-creating the relevant events in the files. This created a time constraint which lead to the limitation on the number of accounts reviewed to a total of eight client accounts. These eight account records were quite voluminous.

All eight accounts reviewed were Alaska risks. They involved admitted as well as non-admitted placements. The sampling was based on accounts showing fee agreements and/or large premiums. Some of these selected accounts did not contain a broker's fee agreement and were on a commission-only basis. However, they contained large premiums. The types of placements included property, casualty, surety and employee benefits lines.

## MARKETING AND PLACEMENTS OF INSURANCE FOR CLIENTS

MARSH of Alaska demonstrated that they market all accounts extensively without regard or preference for the relationships with insurers or wholesalers with whom they have contingency fee agreements.

### **FINDING ONE**

**The examiners determined that MARSH diligently searches the market and places the coverage with the consumer's best interest in mind. The MARSH marketing files reviewed were well documented concerning its marketing efforts. The examiners found no evidence of bid rigging or steering of accounts.**

## CONTINGENCY FEES

Contingency fees are additional commissions paid by some insurers to brokers and are calculated by the insurer based on a variety of elements, such as total profitability of the broker's book of business, retention, volume of the book, and any increase in the amount of new business written over the previous year. Contingency fees are never guaranteed and are often calculated based on the loss and profit of the present year and the loss and profit history from previous years. Contingency fee calculations rest solely with the insurer. The insurer will in most cases not identify a specific account which contributed to its profitability. The conditions for a broker to receive a contingency fee, are described in a contract between the insurer and the broker. Contingency fee commissions are not universally offered by all insurance companies.

Consequently, insurance producers often view contingency fees as as profit sharing and not as additional commission income.

## **MARSH'S ACCOUNTING OF CONTINGENCY FEES**

For the examination period, the Anchorage office of MARSH received approximately \$2.0 million in contingency fees for business produced in Alaska.

The contingency fee agreements reviewed by the examiners contained positive loss ratio requirements. None were based solely on volume. All contingency fees were deposited into a separate revenue account.

The examiners found an unusual divergence from "standard" contingency fee receipts. The examiners found contingency checks "naming" specific clients. For some of the "named" clients, the examiners noted there were broker's fee agreements in place that required disclosure and refunds to the client for any commissions and/or remunerations received by the insurance producer. The examiners then checked the account files to see if there were indeed refunds made to the client account. In the two applicable cases discovered, there were no refunds applied. The examiners brought this matter to MARSH's attention and inquired as to why no disclosure or refunds were made to the client(s).

On July 28, 2005, MARSH explained their position on this matter to the examiners by stating that for two separate clients:

*"The (Insurer) checks were incentive bonuses/profit sharing checks and based upon the entire book of business along with other factors common to profit sharing checks. The back-up to these payments listed the client, but also included all qualified business placed through (insurer) with the various factors of the (insurer) incentive formulas. We consider these profit sharing/contingencies and not override commissions. The fee agreement with the client does not require that we disclose or return these amounts."*

and

*"As for the sum received from Worldwide Facilities, Inc., the client was not informed due to the fact that the check was a contingency check. . . ."*

The examiners determined that MARSH chose not to disclose to clients the receipt of contingency fees earned and refund/offset such. The examiners found that some contingency fee checks identified an amount attributable to a specific client. MARSH maintains that no refund or disclosure is applicable even if a broker's fee agreement with the client was in place, requiring disclosure and refund of commissions.

However, as of September 30, 2004, MARSH no longer accepts contingency fees and has implemented a policy of returning contingency fee checks to the issuing insurers.

## **MARSH'S USE OF BROKER'S FEE AGREEMENTS**

MARSH handles some large commercial accounts. Consequently, MARSH is often compensated by those customers through a broker's fee rather than a commission. Due to the nature of the clientele, the broker fee agreements differ. Some require specific disclosures; others define the lines of insurance to be covered by the agreement and allow MARSH to retain commissions for the lines of insurance not addressed by the agreement. The agreements provide a defined amount to be paid by the client for defined services and duties to be provided

by MARSH.

In some contracts, MARSH contractually agreed not to obtain commissions and/or to offset or reimburse a portion of the broker's fee by the amount of any commissions received. Alaska Statute 21.27.560 provides a legal framework for broker's fee agreements.

## CONTRACTUAL OBLIGATIONS

The examiners focused on MARSH's contracts to discern if MARSH satisfied all responsibilities due their clients with respect to the broker's fee agreements, contingency fees and disclosure requirements. The examiners found three cases with several problems.

To protect the identity of the insured, the insured will only be referred to as "the client." We will discuss each case by number. The DOI numbers listed in parentheses refer to specific documents contained in the examination work papers and copies of which have been retained by MARSH. These are for MARSH's reference only, are not considered part of the market conduct report and are considered confidential work papers under AS 21.06.150(g).

### Case one

MARSH, under its previous owner, Brady and Company (B&C) entered into a broker's fee agreement with the client as provided for by Alaska Statute 21.27.560. This contract became effective on December 09, 2002, and terminates on December 31, 2006. This contract (DOI 3869), was signed by the consumer on September 05, 2003.

#### Background:

There are two key elements of the brokers' fee agreement (DOI 3869) that are critical to the examiner's concerns:

- A. The compensation is based on a fee and any commissions or other remuneration earned shall be promptly divulged and offset against the annual fee (DOI 3878).
- B. The contract contains a provision that allows any wholesalers (DOI 3878) to earn commissions on business placed for this client. Because the wholesalers are not party to the broker's fee agreement, they can therefore receive commissions for their placements of insurance.

When MARSH/B&C became the new 'broker of record' for the client, the existing policies placed by the previous broker were continued. Then in 2003, the policies needed to be renewed and/or remarketed. Due to the size and complexity of the client accounts, MARSH/B&C entered into a joint marketing relationship with McGriff, Seibels and Williams of Texas (MSW), a wholesaler with expertise and access to markets for specialized accounts. This alliance was entered into in order to assist in the marketing and placing of insurance coverage for the client in areas of the USA, where B&C was not licensed to operate. This in itself is not uncommon. To assure, that MSW could obtain commissions from the insurers, MARSH/B&C included the provision described in segment "B" above.

On October 01, 2003, MSW issued a check to MARSH in the amount of \$70,000.13 (DOI 04070) with a notational description of "*finders' fee*" for the subject account (DOI 04071). In light of the provision described in segment "A" above, the examiners expected that these funds would have been disclosed and/or refunded/offset accordingly. The examiners could not find any evidence that this *finders' fee* was either

disclosed or refunded/offset to the client.

The examiners were advised that the account executive and the account manager were not told of this payment as this *finders' fee* came directly to the accounting department and was deposited into a separate account, apart from the standard consumer account; therefore, not showing up as revenue for this client.

On July 07, 2005, the examiners asked (Verification Memorandum LOU-01) why there was no disclosure or refund of the \$70,000.13 *finders' fee* as required by the Broker's fee agreement.

On August 03, 2005 MARSH answered with the following statement:

*"The compensation from the (client) Property & Casualty placements was originally \$510,000. Shortly after the RFP was awarded, Brady & Company became aware of additional services that were not originally requested. **No mechanism for additional compensation was built into the contract under negotiation**; hence, Brady & Company entered into discussions with the client to increase the fee to compensate Brady & Company for these additional services. The client responded that their budget was set and did not see a way to increase it for additional work.*

*Consequently, the contract was reviewed and revised to make it clear that wholesalers could receive commission and Brady & Company could receive profit sharing/contingency checks from the wholesaler. This could all be done without additional cost to the client as it was part of the premium originally paid by the client . . ." (emphasis added)*

First Concern: Marsh's explanation (see emphasis above) for their failure to disclose, refund or offset the \$70,000.13 finders' fee is contradictory to both the facts and to the terms contained in the broker fee agreement (DOI 3878). Contrary to the answer to LOU-01, there is a mechanism to amend the contract.

We observed that the contract does provide for a mechanism to amend the contract sum for the purpose of obtaining additional compensation. This is shown on Page 6, Section 10, titled Entire Agreement. This section reads in part; **"...It may be amended, supplemented, modified or canceled only by a duly executed written instrument . . . (emphasis added)"**.

This contractual mechanism was applied, in three change orders, as evidenced by documents (DOI 03885, 03886 and 03887), which provided for an amendment to the broker's fee agreement to increase the fee. These three documents, referred to as change orders #001, #002, and #003, were drawn up by MARSH five days after the contract was signed by the client. However, while these change orders were not signed by the client, they are clear evidence that MARSH/B&C indeed intended to use the contractual mechanism to increase the fee.

Consequently, the examiners inquired with MARSH on September 01, 2005, as to why MARSH claimed that "no mechanism" was in place.

On September 8, 2005, MARSH did not answer the question directly, but responded by stating:

*"The client refused to increase the contract sum of \$510,000 which was the actual total fee collected from them. . ."*

Also on September 01, 2005, the examiners posed the question:

**"Please explain the reasons why you modified the broker's fee agreement, collected the \$70,000 and did not disclose, refund or offset the discussed sum after you increased the contract sum with the amendments as provided in section 10 of the broker's fee agreement? If you should have offset this amount from the increased contract sum, please demonstrate to the examiners how and when this was accomplished."**

On September 08, 2005, MARSH responded by stating:

*"The three change orders or amendments were never executed. Only \$510,000 was billed and collected directly from the client for the 2003 year. See also prior response. . . (See above). No offset or refund was required."*

Indirectly, all the above amount to an admission by MARSH/B&C that there was no documented disclosure regarding the \$70,000.

In addition, MARSH showed and provided the examiners with the revised contract segment (DOI 3878) segment "B", that allows the wholesaler to retain commissions. The contract segment, consisting of one phrase, does not provide for an exemption to the contract language commissions segment "A". Therefore the examiners do not find that the "revised" contract authorizes MARSH/B&C to obtain commissions from the wholesaler without disclosing and/or refunding/offsetting such amount to the client. MARSH staff repeatedly told the examiners, that the client was verbally informed of their receipt of the finder's fee.

After the examiners brought the concern about the *finders' fee* to MARSH's attention, MARSH contacted the client on July 14, 2005 by e-mail. MARSH provided the examiners with a copy of this e-mail (DOI 4767 and 4768). This is the only document that MARSH produced as verification of contact with the client regarding their retention of the \$70,000. In this e-mail, MARSH states to the client:

*". . . You and I had discussed the need to increase our fee during that time due to some of (client's name) projects that were out of the scope of the original contract, permitting us to pay the wholesaler and having them share some of that with us, was a way to not cost any additional money to (client's name) but to still compensate us for the additional work brought on by those projects."*

The billings did not break out any funds to be paid as a commission to the wholesaler. Further, segment "B" of the broker's fee agreement does not include the wholesaler in this agreement and therefore the wholesaler can collect commissions. Within the same correspondence, MARSH further states:

*". . . The examiner seems to be concerned that this was additional compensation paid by (the client), when in fact, it was standard commission for a wholesaler like MSW and was not an additional cost to (client). (Client) would have paid this amount to MSW regardless of MSW's decision to share with Brady and Company."*

The examiners are not concerned that MSW earned standard commission which were part of the premium. The genesis of the examiners concern is that MARSH/B&C obtained from MSW some of these commissions and did not disclose or refund the obtained \$70,000 to the client as required by their brokers' fee agreement, segment "A".

#### Retention of commissions by MARSH for Transport Policies

On July 15, 2005, the client's Risk Manager gave MARSH a response (DOI 4767), implying that they understood what transpired. The examiners were left with the impression, that at some time an additional compensation from the client through the retention of commissions by MARSH/B&C occurred. The E-mail from the client seems to focus on some rather cloudy memory of events. And indeed, the examiners found a situation where commissions were retained by MARSH/B&C:

MARSH collected commissions on the transport policies for this client (DOI 4170) and obtained written

permission to retain such. The broker's fee agreement does not provide for any exemptions for transportation policies(DOI 3878). Therefore, the examiners inquired, and on July 28, 2005, MARSH responded by stating:

*“(Client) Transport was set up as a total separate client because it was never included in the RFP or any other scope of service. Per DOI 4170, the insured confirmed that these commissions were outside the contract and that Brady & Company was entitled to them.”*

The quoted document, DOI 4170, constitutes an e-mail dated December 23, 2004, from the client to MARSH, stating:

*“. . .the commission can be kept as (client) Transport was not a part of the original (client) RFP when issued in 2002.”*

The examiners found that the transport policy, commissions were disclosed and agreed to **“by a duly executed written instrument”**.

### Conclusion

The examiners concluded the following:

1. Mechanisms were in place to increase the fees; however, it required the approval of the client and could only be executed by a written instrument.
2. MARSH had an avenue to collect more revenue as described by the Transport policy. The situation with the Transport policy also shows that the client was willing to allow MARSH to obtain more fees, but only for lines of insurance that were outside of the original scope of the contract.
3. MARSH cannot provide evidence and documentation that according to their broker's fee agreement, the client was provided with the required information and a written instrument was executed allowing MARSH/B\$C to retain the \$70,000 “finders' fee” in the year 2003.
4. MARSH describes this finders' fee as a “profit sharing/contingency fee.” The \$70,000 is not a profit sharing/contingency fee, but by MARSH's own admission a commission, as shown in their e-mail to the client dated July 14, 2005. Profit sharing and contingency fees are customarily paid after a completed policy year contingent on the business or the performance of the total book of business. This finders' fee was paid at the beginning of the new policies placed through MSW and therefore can only be understood to be a commission, and further would correctly be considered as “other remuneration.” Consequently, the “finders' fee” of \$70,000 should have been disclosed and/or refunded/offset to the client according to the contract, or should have only been retained as a result of written approval from the client. The examiners have found no evidence of written consent by the client.

Due to the lack of documentation, the examiners have no evidence that the client was adequately informed of the \$70,000 in 2003. The latest discussion with the client is at best inadequate. The examiners find the use of an alleged verbal side agreement to modify the monetary terms of a contract, that contains a clause which requires modification **“only by a duly executed written instrument”**, highly unconventional. The examiners also find disturbing, Marsh's unconventional method of increasing the service fee.

Consequently, the examiners determined that MARSH did not disclose or refund/offset commissions amounting to **\$70,000.13** as contractually required by their broker's fee agreements

### Case two:

Marsh USA, under its previous owner, Brady and Company (B&C), entered into broker's fee agreements according to Alaska Statute 21.27.560. These contracts were signed by the consumer December 15, 2000 (DOI 3504) and on December 19, 2003 (DOI 3513). The agreements contained the following two features:



1. The compensation was based on a fee alone. The contract (DOI 3516) states: "This fee is in lieu of any commissions from the insurer with the understanding that all insurance shall be placed by the broker net of commissions."
2. It provides for disclosure of any commissions or fees received by Marsh/B&C (DOI 3506, Section 14) and (DOI 3515, Section n).

This case is again very similar to case one described in the preceding section. Although the examinee has subsequently refunded \$51,425.41 of previously undisclosed commissions in a compromise agreement dated August 01, 2005 (DOI 04794), it was not until the examiners brought the matter to MARSH's attention (via Verification Memo LOU-02) that action was taken by Marsh.

Therefore, without going into the same level of detail as provided in case one, the examiners came to the same conclusion that Marsh did not provide the proper disclosure and timely refund for case two. Marsh does get credit for their efforts at mitigating the error.

### **Case three:**

Again, as in cases one and two, Marsh USA, under its previous owner, Brady and Company (B&C), entered into several broker's fee agreements according to Alaska Statute 21.27.560. These agreements (DOI 03544) (DOI 03561) (DOI 03587) describe the services to be rendered based upon line of coverage. The agreements (DOI 03576) (DOI 03586) do not provide for retention of commissions, however they do require disclosure/offset of commissions.

The examiners established that Marsh collected commissions on the Travel Accident, the Crime Bond and the Long Term Disability segments of these placements (DOI 04958). The examiners found that these commissions were retained against the conditions of the fee arrangement as addressed in Exhibit C of the contracts. Exhibit C remained unchanged and was renewed year after year.

The examiners brought this matter to MARSH's attention by Verification Memo Lou-03 on August 15, 2005. Marsh reviewed the matter and again took mitigating action (DOI 04901) to correct their error on the travel accident and long term disability portions of the account. Subsequent refunds of previously undisclosed commissions retained in error were made in the amount of \$14,090.09. A review of previously issued policies of the same account resulted in additional refunds of \$26,760\_ (DOI 04884).

### **FINDING TWO**

**The examiners determined that MARSH breached the contractual obligations owed to three clients, under the contracts they entered into as regulated by AS 21.27.560, by not disclosing the receipt of commissions and refunding and/or offsetting these commissions to the clients as stipulated in the contracts.**

#### **Recommendation # 1**

**The examiners recommend that MARSH perform an internal file audit for the period of January 1, 2001 to November 09, 2004, involving all clients with broker's fee agreements, assuring that disclosure and refunds of commissions, if applicable, have been adhered to according to their contracts.**

#### **Recommendation # 2**

**The examiners recommend that MARSH implement procedures and controls to assure that MARSH discloses and refunds commissions received, if required by their broker's fee agreement(s), to assure compliance with AS 21.27.560.**

The examiners reviewed two other large accounts that required disclosure and refund or offset of commissions received. The examiners noticed that Mr. Dave Taylor, Chief Financial Officer, personally monitored those arrangements. For those clients, refunds and offsets were made according to the contract and the examiners found that the commissions received vs. refund/offsets to client, matched to the penny.

## CONDITION OF FILES

Alaska Statute 21.27.350 requires MARSH to document each action taken relating to insurance transactions. The documentation must contain all notes, papers, documents and similar material, and be in sufficient detail that relevant events, the dates of those events, and all persons participating in those events can be identified.

As previously addressed in the "SAMPLE" section on page four of this report, the file organization was inconsistent in structure depending on the account executive assigned.

Alaska Statutes and Regulations require disclosure of broker's fees and/or other charges. MARSH's invoices lacked a detailed description of additional charges, such as engineering fees, inspection fees or other similar fees which may not be described simply as broker fees.

### **Recommendation # 3**

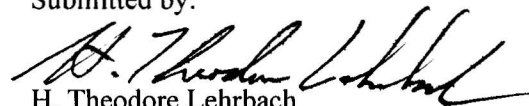
**The examiners recommended that in order to be in compliance with AS 21.27.350, MARSH needs to adequately disclose to the consumer a detailed itemization of all charges billed to the consumer.**

## COOPERATION

MARSH promptly responded to inquiries from the examiners during the on site examination and provided all the necessary documentation promptly with no delay. As observed in the Supplemental Note on page 2, Marsh has responded to and fulfilled each of the examination recommendations, and the Director is satisfied with those responses.

The EIC, Christian F. Ulmann, and his examination team wishes to express their appreciation for the courtesy and the cooperation extended by the MARSH personnel, especially to Ms. Kristin Zakrzewski, who provided consistent, patient help and cooperation; thus, enabling the examiners to do a thorough review of the files and data.

Submitted by:

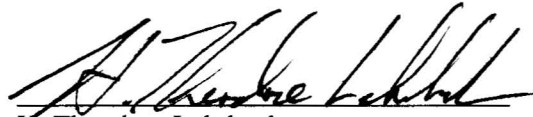


H. Theodore Lehrbach  
Chief Examiner,  
Market Conduct Section

**REPORT ON MARKET CONDUCT EXAMINATION CERTIFICATION**

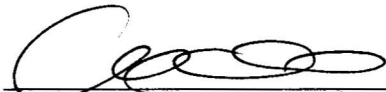
State of Alaska            )  
  ) ss.  
Third Judicial District    )

H. Theodore Lehrbach, being duly sworn, deposes and says that the foregoing report submitted by him is true to the best of his knowledge and belief.



H. Theodore Lehrbach  
Chief Examiner,  
Market Conduct Section

SUBSCRIBED and SWORN to before me this 25<sup>th</sup> day of April, 2007

  
\_\_\_\_\_  
Notary Public in and for Alaska  
My Commission Expires 1/24/2009