

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 08-02)
In the Matter of Audit of)
NAIS Inc)
_____)

FINDINGS OF FACT

1. An audit report of NAIS Inc, licensed in the state of Alaska, has been issued by the State of Alaska, Division of Insurance to NAIS Inc.
2. The audit report of NAIS Inc (TA 08-02) has been transmitted to Bill Carr, Compliance Officer, NAIS 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 NAIS Inc (TA 08-02) 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 October 15, 2008.

Dated this 15th day of October, 2008 at Anchorage, Alaska.



Linda S. Hall, Director
State of Alaska
Division of Insurance

PREMIUM TAX AUDIT OF

**NAIS Inc
Frederick, Maryland**

TA 08-02

As of December 31, 2007

**Issued by
DIVISION OF INSURANCE
DEPARTMENT OF COMMERCE, COMMUNITY AND ECONOMIC
DEVELOPMENT
STATE OF ALASKA**



**FINAL REPORT:
October 15, 2008**

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DEPARTMENT OF
COMMERCE
COMMUNITY AND
ECONOMIC DEVELOPMENT
Division of Insurance

Sarah Palin, Governor
Emil Notti, Commissioner
Linda S. Hall, Director

October 15, 2008

Linda S. Hall, CPCU
Director, Division of Insurance
Department of Commerce, Community and Economic Development
550 West 7th Avenue, Suite 1560
Anchorage, AK 99501-3567

Pursuant to Alaska Statute (AS) 21.06.130, the Alaska Division of Insurance performed a limited and targeted premium tax audit of NAIS Inc (the broker) on June 9, 2008 through June 13, 2008, in the broker's Frederick, MD office. The audit was conducted by Rebecca Nesheim, tax auditor for the Alaska Division of Insurance.

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 NAIS Inc conducted by the Alaska Division of Insurance.

Subject Matters Audited

NAIS Inc is an Alaska licensed surplus lines broker based in Frederick, MD. The division elected to audit their monthly filings, premium taxes paid, and filing fees paid, for accuracy and timeliness as well as required due diligence and disclosures to the insured.

Time Frame

The audit covered this broker's surplus lines business for the two years of January 1, 2006 through December 31, 2007.

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METHODOLOGY

The tax auditor sent the call letter and initial data requests to NAIS Inc's office in Frederick, MD. A list of all Alaska business transactions with non-admitted insurers was requested for the period to be audited. NAIS Inc complied timely with all data requests. The number of policies and endorsements written during the audit period was 566, from which a sample of 50 files was selected for audit.

The following are the procedures steps for the audit:

- 1) Verify that monthly premium reports and accompanying forms were filed in a timely manner.
 - i) Audit steps taken:
 - (1) Reviewed the monthly files sent to the Alaska Division of Insurance and verified the policy was included in the monthly filing based upon the effective date of the policy.
 - (2) Verified a statement of exempt premiums was filed when appropriate.
- 2) Verify the accuracy of the premium calculation
 - i) Audit steps taken:
 - (1) Reviewed policy, declaration page, and invoices to determine how they calculated the premium.
 - (2) Verified the correct premium was reported on the monthly reports as filed.
- 3) Verify the accuracy of all monthly reports filed.
 - i) Audit steps taken:
 - (1) Reviewed the policy & declaration pages in each file.
 - (2) If the effective date did not match the monthly 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 effective date may be a month or more prior to the actual book date or invoice date. In this case, the invoice date usually determined in which month the endorsement is required to be filed.
 - (3) Verified the monthly 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) If the placement is a multi-state placement, check the calculation and reasonableness of the methodology to allocate.
 - i) Audit steps taken:
 - (1) Verified the allocation of premium for each state is reasonable and the calculation is accurate.
- 5) Verify quarterly and annual premium tax reports were filed in a timely manner.
 - i) Audit steps taken:
 - (1) Confirmed when the quarterly and annual premium tax reports were mailed to the Alaska Division of Insurance.
- 6) Verify the accuracy of the quarterly and annual premium tax reports
 - i) Audit steps taken:
 - (1) Verified the quarterly and annual premium tax reports as filed with the division were accurately filled out to reflect the correct premiums, taxes and fees.

- 7) Verify if tax and filing fee payments were made timely and by ACH
 - i) Audit steps taken:
 - (1) Confirmed when the payments were made to the Alaska Division of Insurance and the payment method
- 8) Verify tax and filing fees payments were made accurately
 - i) Audit steps taken:
 - (1) Confirmed if the tax and fee payments matched the monthly reports as filed.
- 9) Review effort made to place insured with an admitted insurer
 - i) Audit steps taken:
 - (1) Verified an affidavit of due diligence was in the file and the declinations filled out. If it was marked as using the placement list, the list effective at the time of placement was reviewed to ensure the risk was on the list
- 10) Review disclosures 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
- 11) Confirm coverage is placed with an eligible non-admitted insurer
 - i) Audit steps taken:
 - (1) Reviewed the white lists to ensure the company was eligible at the time of placement
- 12) Review notice regarding nonrenewal and premium increase
 - i) Audit steps taken:
 - (1) Verified in each file there was a policyholder notice regarding nonrenewal and premium increase included with the policy or other evidence of insurance.

Acceptable Error Rate:

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

PREMIUM TAX AUDIT

- | |
|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <ol style="list-style-type: none">1. Verify that monthly premium reports and accompanying forms were filed in a timely manner.
AS 21.34.080 and .170, 3 AAC 25.090 and .100 |
|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|

Comments: Nineteen of the 24 monthly premium reports were filed late. Four were prior to when a new regulatory penalty was implemented. All remaining late months were penalized for being filed late. The penalties were assessed and paid prior to the audit.

Result: Failed (5 reports passed & 19 failed, error rate 79%)

Recommendation: It is recommended that the broker follow their written procedures to ensure the monthly reports are filed timely.

2. Verify the accuracy of the premium calculation

AS 21.34.180

Comments: The premium was calculated correctly for every transaction in the audit files.

Result: Passed (error rate 0%)

3. Verify the accuracy of all monthly reports filed

AS 21.34.080 and .170, 3 AAC 25.090 and .100

Comments: A computer report is run for a particular month and state. The information from this report is downloaded into Excel and all the Alaska transaction reports are created from the information. It appears as though the report is generated based upon invoice date after two pieces of information are input by staff: the policy number and the billing. If those two items are not done, the report will not include that policy. Four monthly reports were not accurate due to four policies: 1. one policy was filed twice, once in 2005 and again in 2006; 2. two endorsements were never filed; 3. one policy was filed as an amended report after the due date for the monthly report, all tax and fees were paid on the policy.

The April, May, and June 2006 report of surplus lines transactions premium amounts included the taxes and fees. This is a minor issue as the tax and fees were not based upon the premium but correctly calculated and the summary forms had the correct premium.

Result: Passed (56 files passed & 4 failed, error rate 8%)

Recommendations: It is recommended that the broker modify their written procedures to add a necessary step when preparing the monthly reports. The computer run report used to prepare the monthly reports should be run towards the end of the following month in order to find other policies that were invoiced in the subsequent month but effective in the report month. In addition, the computer report parameters should be modified to incorporate the effective date of policies and invoice date of endorsements, as that predominately is the first known date. This should eliminate the possibility of a policy invoice date being outside the parameters of the computer report and not caught in time to include in the correct monthly report. It would also be beneficial to set up a procedure to request policy numbers from Tudor Insurance Company when running low instead of waiting until the numbers are gone.

4. Verify the multi-state placements are filed correctly

AS 21.34.180

Comments: The broker does not write any multi-state policies that affect Alaska.

Result: N/A

5. Verify quarterly and annual premium tax reports were filed in a timely manner

AS 21.34.180, 3 AAC 21

Comments: Four out of the eight tax reports required to be filed were filed late:

- 1st quarter 2006: due May 31, 2006, received July 14, 2006
- 2nd quarter 2006: due August 31, 2006, received September 15, 2006
- Annual 2006: due March 1, 2007, received initially March 8, 2007 unsigned. Signed report received April 9, 2007
- 1st quarter 2007: due May 31, 2007, received June 12, 2008

Result: Failed (4 reports passed & 4 failed, error rate 50%)

Recommendation: It is recommended that the broker follow their written procedures to ensure the tax reports are all filed timely.

6. Verify the accuracy of the quarterly and annual premium tax reports

AS 21.34.180, 3 AAC 21

Comments: Four errors found during the audit in the accuracy of the monthly reports affect the tax reports.

Result: Passed (error rate 0%)

7. Verify if tax and filing fee payments were made timely and by ACH

AS 21.34.180, 3 AAC 21

Comments: Three quarter tax payments and one annual tax and fee payment were made late. Penalties for late payment were assessed and paid prior to the audit.

- 1st quarter 2006: due May 31, 2006, received July 12, 2006
- 2nd quarter 2006: due August 31, 2006, received September 13, 2006
- Annual 2006: due March 1, 2007, received March 6, 2007
- 1st quarter 2007: due May 31, 2007, received June 5, 2007

Result: Failed (4 payments passed & 4 failed, error rate 50%)

Recommendation: It is recommended that the broker follow their written procedures to ensure the tax and fee payments are made by the statutory due dates.

8. Verify tax and filing fees payments were made accurately

AS 21.34.180, 3 AAC 21

Comments: All tax and fee payments made by the broker were accurately based upon the tax reports as filed.

Results: Passed (error rate 0%)

9. Review effort made to place insured with an admitted insurer

AS 21.34.020, 3 AAC 25.030 and .035

Comments: All files included documentation for the diligent search in the admitted market prior to binding in the surplus lines market.

Results: Passed (error rate 0%)

10. Review disclosures on evidence of insurance for use of non-admitted insurer

AS 21.34.100(e)

Comments: The disclosure stamp as required by Alaska Statute 21.34.100(e) to the insured that the company is a surplus lines company was not located on the first page of any of the evidence of insurance. In some cases, the broker inserts a separate piece of paper when mailing the policy but this does not meet statute requirements.

Results: (error rate 100%)

Recommendations: It is recommended that the broker modify their business practices and begin stamping the required language using the newly purchased stamp on the evidence of insurance and scanning the page into the insured's electronic record. An alternative solution is to add the required stamp language to all evidence of insurance prior to printing for the insured. This will reduce the requirement of scanning a stamped page into the electronic file and allow for emailing the document with the correct language on it. The method chosen should be included in the procedure manual.

11. Review notification for use of non-admitted insurer

AS 21.34.110

Comments: The broker does inform the insured in writing on the proposal that the company the policy is to be written with does not have a certificate of authority, is not regulated by the State of Alaska and in the event of insolvency, the losses will not covered by the Alaska Guaranty Association. However, the proposal is not saved in the database for renewal business so they do not meet statute requirements of maintaining the written copy given to insured so all renewal policies part of the audit fail. For all new business, the proposal stays as part of the electronic record. The audit contained three new business records and they all contained a copy of the proposal.

Results: Failed (3 files passed & 47 failed, error rate 94%)

Recommendations: It is recommended that the broker modify their written procedures to ensure a copy of the proposal is maintained in every insured's electronic file for all policies.

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 companies.

Results: Passed (error rate 0%)

13. Review notice regarding nonrenewal and premium increase

3 AAC 25.050

Comments: No policy included the required notice of nonrenewal and premium increase. Although this is an insurance company requirement, the broker is responsible for ensuring it is included with the policy and to contact the company for its inclusion.

Results: Failed (error rate 100%)

Recommendations: It is recommended that the broker modify the procedures manual to include in the policy checklist this nonrenewal and premium increase notification. If the insurance company will not include in the policy, NAIS should report this to the Alaska Division of Insurance who will follow up with the company.

Prompt Issuance of Policy or Evidence of Insurance 3 AAC 25.060

Comments: One policy was not issued promptly as required by state. The effective date of the policy was 5/19/06, the issue date was 7/14/06 and the date sent to insured was 8/19/06. No binder or other evidence of insurance appears to have been sent prior to policy. Promptness means 30 days from effective date.

Recommendations: It is recommended that the broker ensure evidence of insurance is provided to the insured within 30 days of the effective date.

Endorsements

The 50 audit files did not include very many premium-bearing endorsements and with two endorsements not filed with Alaska DOI within the audit files, a decision was made to review as many electronic files as possible in the limited time available after all tests were completed, for endorsements and whether they were filed. It turns out an additional 20 endorsements were not filed with Alaska DOI. The overall result to tax and fees is (\$492.66).

Recommendations: It is recommended that the broker revise the current computer run reports to ensure all premium-bearing endorsements are captured so they can be filed with the Alaska Division of Insurance timely. The broker should amend previously filed reports to incorporate all the 22 endorsements not filed with the Alaska Division of Insurance. The Division will then refund the tax and fees to the broker to pass on to the insured.

SUMMARY AND SUBSEQUENT EVENTS

Summary

This was a premium tax audit of NAIS Inc. The auditor tested 13 standards focusing on the broker's filing of monthly and annual tax reports and the subsequent payment of premium taxes and filing fees as well as due diligence and notification requirements for using a non-admitted insurer. The compliance officer and staff were very cooperative during the audit. The tax auditor appreciated this attitude and enjoyed working with the broker's management and staff.

Several significant issues did arise during the audit.

- 1) Late filed monthly reports and late paid taxes and fees generated many penalties.
- 2) The required notification to the insured regarding the use of a non-admitted insurer was not found in most files
- 3) The required disclosure stamp was not on the documents sent to the insured or maintained in the electronic files.
- 4) Endorsements are not showing up on many of the computer run reports; therefore, are not being reported to the Alaska DOI.

Re-Audit

In closing, while the auditor found problems with the reports and payments, she also found that the broker wants to do things right. The auditor's recommended actions, including those already implemented by the broker, should correct the problems encountered and it is recommended that NAIS Inc be re-audited within the next three years to ascertain compliance with them.

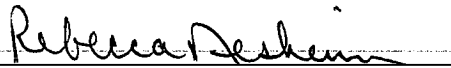
Submitted by:
Rebecca Nesheim
Tax Auditor

Affidavit

NAIS Inc
As of December 31, 2007
TA 08-02

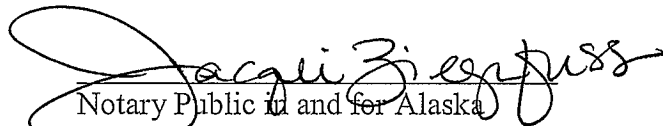
Juneau, Alaska)
October 15, 2008)
State of Alaska) ss.
First Judicial District)

I, being duly sworn, do verify that the report of premium tax audit as of December 31, 2007 of NAIS Inc is true to the best of my knowledge and belief.



Rebecca Nesheim
Tax Auditor

SUBSCRIBED and SWORN to before me this 16 day of October, 2008



Notary Public in and for Alaska

My Commission Expires with office