

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 10-03)
In the Matter of Audit of)
Marsh USA Inc)
_____)

FINDINGS OF FACT

1. An audit report of Marsh USA Inc, licensed in the state of Alaska, has been issued by the State of Alaska, Division of Insurance to Marsh USA Inc.
2. The audit report of Marsh USA Inc (TA 10-03) has been transmitted to Daniel J Ashburn, Compliance Officer, Marsh USA 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

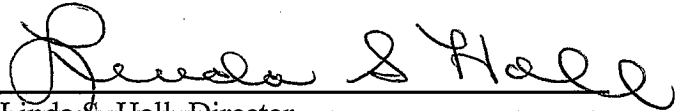
IT IS ORDERED

1. Pursuant to AS 21.06.150(b)(1), the audit report of Marsh USA Inc (TA 10-03) 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 Sept. 27, 2011.

Dated this 27th day of Sept, 2011 at Anchorage, Alaska.



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

PREMIUM TAX AUDIT OF

**Marsh USA Inc
Seattle, WA**

TA 10-03

As of December 31, 2009

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



**FINAL REPORT:
September 22, 2011**

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DEPARTMENT OF
COMMERCE
COMMUNITY AND
ECONOMIC DEVELOPMENT

Division of Insurance

Sean Parnell, Governor
Susan K. Bell, Commissioner
Linda S. Hall, Director

September 22, 2011

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 Marsh USA Inc (the broker) on December 6, 2010 through December 9, 2010, in the broker's Seattle, WA office. The audit was conducted by Rebecca Nesheim, tax auditor for the Alaska Division of Insurance.

Marsh USA 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 Marsh USA Inc conducted by the Alaska Division of Insurance.

Subject Matters Audited

Marsh USA Inc is an Alaska licensed surplus lines broker based in Seattle, WA with branches all over the country. As this agency ranked number one in premium volume among all Alaska licensed surplus lines brokers in 2009, 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, 2008 through December 31, 2009.

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METHODOLOGY

The tax auditor sent the call letter and initial data requests to Marsh USA Inc's office in Seattle, WA. A list of all Alaska business transactions with nonadmitted insurers was requested for the period to be audited. Marsh USA Inc complied on a timely basis with all data requests. The number of policies written during the audit period was 757, from which a sample of 50 files was selected for audit. Once on-site, three were determined to not be non-admitted or no Alaska exposure, or amount of premium too low so these were replaced with three others from the original list of policies.

The following are the procedures steps for the audit:

- 1) Verify that monthly premium reports and accompanying forms were filed on time.
 - 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) 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, and endorsement 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 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) Verified a statement of exempt premiums was filed when appropriate.
- 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.
 - (2) Verified the multi-state allocation form was filed when appropriate
- 5) Verify quarterly and annual premium tax reports were filed on time.
 - 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 on time 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 tax reports as filed.
- 9) 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 the declinations completed. If 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
- 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 stamp 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 white lists 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 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

1. Verify that monthly premium reports and accompanying forms were filed on time
 AS 21.34.080 and .170, 3 AAC 25.090 and .100

Comments: All 24 original monthly premium reports and accompanying forms were filed on time.

Result: Passed (error rate 0%)

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: Ninety-eight late monthly reports were filed after the original report was filed on time. These 98 reports included at least one new transaction that had not previously been filed. Every late transaction was penalized when filed.

Of the 50 audit policy files, 27 were not filed in the original monthly report. Many of these were multi-state policies for which the premium allocation was prepared in plenty of time to be filed on time. Six of the 27 files were not filed at all and 14 policies related to the audit files were found to also not be filed. The total tax and filing fees due for those not filed are \$496.21 and \$183.78 respectively.

These errors affect two additional audit tests:

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

Result: Failed (23 files passed & 27 failed, error rate 54%)

Recommendations: It is recommended that the broker revise written procedures for when initial or renewal policies as well as endorsements are to be reported to the Alaska Division of Insurance. Statute and regulation dates should be included in these procedures. For those multi-state policies where Alaska is the Home State of the insured that need premium allocated, these should be reported to Alaska as soon as the initial allocation is completed since these take longer to determine. If the initial allocation is modified after additional information is obtained, then the policy transaction information should be amended with the Division. No penalty will be assessed on a transaction that was previously filed on time but an adjustment needs to be subsequently made. A review by a second individual might be considered in order to catch the mistakes before the paperwork is filed with the Division. The broker should consider utilizing email capabilities for transferring paperwork between offices as that will reduce the filing time. In addition, the broker needs to amend prior monthly reports and tax reports to include the policies not previously reported.

Marsh USA Inc Response: Marsh will amend our written procedures for when initial policies, renewal policies and endorsements are to be reported to the Alaska Division of Insurance to ensure timely and accurate monthly reports. Further, Marsh procedures will be amended to ask for timely filing of an initial premium allocation with the understanding that no penalty will be assessed for a timely filing that may subsequently need adjustment to the allocation.

Alaska Division of Insurance Response: Amended monthly reports for missing transactions were filed September 20, 2011. Five transactions were filed and paid to another jurisdiction and the Division will not require the duplication of filings or tax.

4. Verify the multi-state placements are filed correctly

AS 21.34.180

Comments: The broker writes many multi-state policies. One policy for an insured based in Alaska appears to have multi-state & country exposures yet the entire policy was filed 100% in Alaska. This error would normally require the reports to be amended. However, to go back and amend the taxes on a policy that has already expired and try to file the taxes in another state may be difficult at this late date. All other policies have an allocation form prepared by the broker that appear to be a reasonable allocation.

This error affects four additional audit tests:

1. Accuracy of Premium
2. Accuracy of Monthly Reports
3. Accuracy of Tax Reports
4. Accuracy of Tax and Fee Payments

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

Recommendation: It is recommended the broker follow the written procedures for determining allocation between multiple states and countries involved in policies. For all policies effective July 21, 2011 and subsequent, only multi-state policies where Alaska is the home state of the insured should be reported to Alaska.

Marsh USA Inc Response: Marsh will follow Alaska guidelines for multi-state placement reporting.

5. Verify quarterly and annual premium tax reports were filed on time

AS 21.34.180, 3 AAC 21

Comments: The broker filed all quarterly tax reports and annual premium tax reports on time. Due to some unauthorized insurance companies used for some policies, the broker was also required to file the Unauthorized Tax Report which was also filed on time.

Result: Passed (error rate 0%)

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

AS 21.34.180, 3 AAC 21

Comments: The tax reports as received are accurate based upon the monthly reports and late transactions as filed up until the due date of the tax reports. There are 19 audit files that were either not filed or filed after the due date for their respective quarter or annual tax filing which

affected the actual accuracy of the tax reports. These flow-through findings are addressed in their respective audit tests.

Result: Passed (error rate 0%)

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

AS 21.34.180, 3 AAC 21

Comments: The third quarter 2008 tax payment was made late. A penalty was assessed and paid prior to the audit. The remaining payments were made on or before the required due date for the annual payments and all payments were made by ACH.

Results: Failed (9 payments passed & 1 failed, error rate 10%)

Recommendation: It is recommended that the broker continue to follow written procedures for when payments are to be made to the Alaska Division of Insurance.

Marsh USA Inc Response: Marsh will continue to follow written procedures for on time payments to the Alaska Division of Insurance.

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 accurate based upon the tax reports as filed, which included late transactions. There are 19 audit files that were either not filed or filed after the due date for their respective quarter or annual tax filing which affected the actual accuracy of the tax reports. These flow-through findings are addressed in their respective audit tests.

Due to the policies not filed, the broker owes additional tax and fees of \$496.21 and \$183.78 respectively.

Results: Passed (error rate 0%)

Alaska Division of Insurance Follow-up: the additional taxes and fees were paid on 9/22/2011.

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

AS 21.34.020 and .060, 3 AAC 25.030 and .035

Comments: The broker has elected to use the Affidavit of Due Diligence for documenting the diligent search. Seven files have problems with that documentation:

- Declinations done after bound date – 3
- No documentation in file – 1
- Unauthorized placement did not canvas eligible surplus lines companies or the documentation of such diligent search not in files – 3

Eight additional files show the coverage was on the placement list but the Affidavit of Due Diligence was created and signed after the bound date. Since the broker is also the producer and would know the coverage was on the placement list, the Division will allow this practice in this audit even though the Affidavit was signed after the bound date. In addition, the description of risk as listed on the placement list must be accurate as a description of the insured is not adequate.

Results: Failed (43 files passed & 7 failed, error rate 14%)

Recommendations: It is recommended that the broker create written procedures to ensure all Affidavits of Due Diligence are received or created prior to binding including those with risks located on the placement list. If another form of documentation is maintained, there must be clear indications that the declinations were done before binding. When a policy will include the use of an unauthorized insurance company, additional diligent search is required of the eligible surplus lines companies and notifications to the Alaska Division of Insurance are required within 30 days of placing coverage. It is recommended the broker create written procedures to account for the additional requirements.

Marsh USA Inc Response: Marsh will remind brokers of the requirement to ensure that Affidavits of Due Diligence, or other forms of diligent search declinations, be created prior to binding. Notifications of diligent search of eligible surplus lines companies will be provided to the Alaska Division of Insurance within 30 days of placing coverage.

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

AS 21.34.100(e)

Comments: Forty-five files included a problem with the required disclosure stamp on evidence of insurance. The multi-state policies included the various states disclosure wording as a separate document attached to the policy. However, the Alaska disclosure wording is not the language required by statute. It was the notification information required for statute AS 21.34.110 instead. Here are all the different problems found in the files:

- No stamp on policy dec – 36, includes those with the incorrect wording for Alaska
- No stamp on binder – 40
- No stamp on endorsement - 3
- Stamp was illegible on dec – 1, although two others had a couple of words that were not identifiable but was easy enough to figure out but it's very important the stamp can be read by the insured.
- Broker name not on dec - 1

Total disclosure errors: 81 within 45 distinct files

Results: Failed (5 files passed & 45 failed, error rate 90%)

Recommendations: It is recommended that the broker ensure written procedures are followed that all evidence of insurance have the required disclosure stamp wording. The disclosure document for multi-state policies must be modified to include the correct language. When Alaska is the only risk exposure or one of two states, the stamp should be located on the first

page of the declaration page so the insured will not miss it. It is further recommended to revise the written procedures to include the stamp requirement on all premium bearing and non-premium bearing endorsements as they are also evidence of insurance. One last recommendation is to ensure the broker's name is included on all evidence of insurance.

Marsh USA Inc Response: Marsh will ensure that all evidences of insurance including endorsements for which Alaska is the home state will include the required disclosure stamp wording. Marsh electronically generates this wording on a separate page rather than use a stamp and we will ensure this wording is prominently attached to all evidences of insurance. Marsh (name) will be included on all evidences of insurance.

11. Review notification for use of non-admitted insurer

AS 21.34.110

Comments: The broker includes the notification that the insurance is being placed with a company that is not regulated by the Alaska Division of Insurance in their proposal and pre-binding notice. However, there were 13 files with problems regarding the notification to the insured:

- No Alaska notification on pre-binding notice or nothing in file – 8
- Notification after binding – 5

Two files included a description in the proposal of admitted vs nonadmitted. The information about the non-admitted company implies but does not clearly state that the Division of Insurance does not authorize this company and is not regulated by the Division.

Results: Failed (37 files passed & 13 failed, error rate 26%)

Recommendations: It is recommended that the broker revise their written procedures to include Alaska notification language on the required pre-binding notification to the insured about the surplus lines insurance company as required by statute. The information in the proposal 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.

Marsh USA Inc Response: Marsh will provide each insured prior to binding the required pre-binding notification to the insured about the surplus lines insurance company including that the insurer does not have a certificate of authority, is 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.

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

AS 21.34.050 & .060

Comments: Four policies in the audit were placed with ineligible companies. The broker did not follow statute requirements when the coverage is placed with an ineligible insurance company. No notification was provided by the broker within 30 days after placing the coverage as required.

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

Recommendation: It is recommended that the broker revise their written procedures to include the documentation requirements when coverage must be placed with an ineligible insurance company.

Marsh USA Inc Response: Marsh procedures will be revised to include the documentation requirements within 30 days after coverage is placed with an ineligible insurance company.

13. Review notice regarding nonrenewal and premium increase

3 AAC 25.050

Comments: Thirty-nine files did not have evidence of the required Alaska Policyholder Notice of nonrenewal and premium increase being sent to the insured. Two files included the notice but it was an older version than required.

Results: Failed (11 files passed & 39 failed, error rate 78%)

Recommendations: It is recommended that the broker revise their written procedures to include a step in the processing of evidence of insurance to ensure the notice is included from the insurance company. If the notice is outdated, the broker should contact the insurance company to replace the notice. A step on a checklist is one way to ensure this document is reviewed.

Marsh USA Inc Response: Marsh will endeavor to ensure that each insurer include the most current Alaska Policyholder Notice of nonrenewal and premium increase on evidences of insurance they issue.

File Documentation

Several files had policy numbers coded in the computer that did not match the actual policy number or the name of the insured was the parent corporation instead of the subsidiary who was actually the insured.

SUMMARY AND SUBSEQUENT EVENTS

Summary

This was a premium tax audit of Marsh USA 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 cooperative during the audit. The tax auditor appreciated this attitude and enjoyed working with Marsh USA Inc's management and staff.

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

- 1) The monthly reports are consistently not accurate when filed. Numerous transactions are filed late, subjecting the broker to large volumes of penalties.
- 2) Many transactions were not filed with the Alaska Division of Insurance resulting in additional tax and fees due.
- 3) The diligent search in the admitted market was not documented in many of the files or if it was, some were created after binding. The diligent search of the eligible surplus lines carriers before using a nonadmitted carrier was not documented in many files.
- 4) The disclosure stamps used on the majority of evidence of insurance do not meet statutory requirements.
- 5) Several policies used nonadmitted carriers and the required notification to the Division was not provided.
- 6) The required notification to the insured regarding the use of a nonadmitted insurer was not found in some files

Re-Audit

In closing, the auditor's recommended actions should help the broker correct the problems encountered. It is recommended that Marsh USA Inc be re-audited within the next three years to ascertain compliance.

Submitted by:
Rebecca Nesheim
Tax Auditor

Affidavit

Marsh USA Inc
As of December 31, 2009
TA 10-03

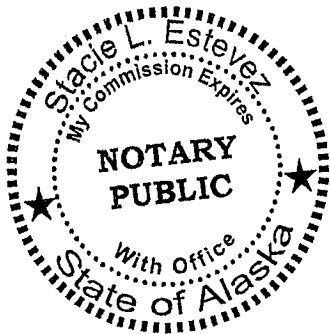
Juneau, Alaska)
September 22, 2011)
State of Alaska) ss.
First Judicial District)

I, being duly sworn, do verify that the report of premium tax audit as of December 31, 2009 of Marsh USA Inc is true to the best of my knowledge and belief.

Rebecca Nesheim

Rebecca Nesheim
Tax Auditor

SUBSCRIBED and SWORN to before me this 10th day of October, 2011 :



Stacie Estevez
Notary Public in and for Alaska

My Commission Expires with office