

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 16-04 )  
In the Matter of Audit of )  
Brown and Riding Ins Services Inc. )  
\_\_\_\_\_ )

FINDINGS OF FACT

1. An audit report of Brown and Riding Ins Services Inc., licensed in the State of Alaska, has been issued by the State of Alaska, Division of Insurance to Brown and Riding Ins Services Inc.
2. The audit report of Brown and Riding Ins Services Inc. (TA 16-04) has been transmitted to Jeffrey Jarboe, Compliance Officer, Brown and Riding Ins Services 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

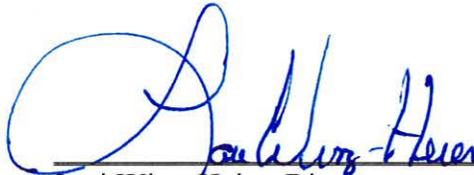
IT IS ORDERED

1. Pursuant to AS 21.06.150(b)(1), the audit report of Brown and Riding Ins Services Inc. (TA 16-04) 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 December 2<sup>nd</sup>, 2016.

Dated this 2<sup>nd</sup> day of December, 2016 at Anchorage, Alaska.



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

**PREMIUM TAX AUDIT OF**

**Brown and Riding Ins Services Inc.**

**Los Angeles, CA**

**Alaska License #93079**

**TA 16-04**

**As of December 31, 2015**

**Issued by**

**DIVISION OF INSURANCE**

**DEPARTMENT OF COMMERCE, COMMUNITY AND ECONOMIC**

**DEVELOPMENT**

**STATE OF ALASKA**



**FINAL REPORT:**  
**December 2, 2016**

**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 .....	12
7) AFFIDAVIT .....	13



December 2, 2016

Lori K Wing-Heier, CIC, 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) 21.06.130, the Alaska Division of Insurance performed a limited and targeted premium tax audit of Brown and Riding Ins Services Inc. The audit was conducted by Rebecca Nesheim, tax auditor for the Alaska Division of Insurance.

**Brown and Riding Ins Services 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 Brown and Riding Ins Services Inc. conducted by the Alaska Division of Insurance (the division).

**Subject Matters Audited**

Brown and Riding Ins Services Inc. (the broker) is an Alaska licensed surplus lines broker based in Los Angeles, CA. 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 this broker's surplus lines business for the years January 1, 2014 through December 31, 2015.

## **METHODOLOGY**

The division sent the call letter and initial data requests to the broker's office in Los Angeles, CA. 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 1124, from which a sample of 50 files was 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.
  - (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.
- 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 the declinations completed. 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
    - (2) For effective dates beginning 9/4/14, verified the documentation was received within 15 days of binding with the actual search completed prior to binding.
- 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.
- 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**

- |   |
|---|
| <b>1. Verify that quarterly reports and accompanying forms were filed on time</b><br><b style="text-align: right;">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. Five amended reports with additional transactions were filed for three quarters.

*Results:* Passed (error rate 0%)

- |  |
|--|
| <b>2. Verify the accuracy of the premium calculation</b><br><b style="text-align: right;">AS 21.34.180</b> |
|--|

*Comments:* The premium was calculated correctly for all policies in the audit files.

*Results:* Passed (error rate 0%)

- |  |
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| <b>3. Verify the accuracy of all quarterly reports filed</b><br><b style="text-align: right;">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:

- Missing or incorrect producer license # - 2
- Incorrect producer name - 3
- Missing description of subject - 4
- Missing statement of exempt premiums – 1, see explanation below
- Wrong policy # - 1
- Missing Lloyd's syndicate information – 2

Total accuracy errors: 13 within 12 distinct files

One insured is not subject to taxes and fees per AS 21.80.130 yet taxes and fees were assessed and paid on this entity. The broker will need to amend the 4<sup>th</sup> Quarter 2014 to include the statement of exempt premiums and reverse the taxes and fees for a refund to return to the insured. This error affects one additional audit test: Accuracy of tax and fee payments

Seven out of the eight original quarterly reports filed had multiple errors for which the division staff spent numerous hours working with the broker's staff to correct. Seventy-eight transaction reports were fixed or replaced during the reviews. One transaction form included the wrong premium but was corrected prior to audit. These changes show a significant problem in accuracy.

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 one multi-state policy in the audit, the other state was not identified on the reports as filed to the division. This will not be a finding in this audit but all future 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.

*Results:* Failed (38 files passed & 12 failed, error rate 24%)

*Recommendations:* It is recommended the broker revise written procedures to include a list of what is required on the Report of Surplus Lines Transaction (RSLT). The list should be provided to both production staff, which creates these reports, and to the compliance section staff. It is recommended there be a second review by the compliance section to review all required information on the transaction form and fix errors themselves or send back to production staff for fixes. If the producer information is coded in the broker's database, it is recommended there be a database review of all producers to ensure names and license numbers are fixed with accurate information.

*The broker response:* We have amended procedures to include a checklist for reviewing the RSLTs and explain all required information. We have also amended our procedures to state that the compliance staff performs a secondary review of the RSLT to ensure all information is accurate. In these procedures is a step for the compliance staff to review producer name and licensing information in review and to amend the database when necessary to ensure accuracy.

**4. Verify the home state for insured is Alaska**

**AS 21.34.180**

*Comments:* The broker writes some multi-state policies. All policies were correctly identified with Alaska as the home state and Alaska laws were applied to the 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:* The original eight and four amended reports tax and fee payments were made on or before the required due date and made by ACH. One amended report's taxes and fees were made late for which a penalty was assessed prior to the audit.

*Results:* Passed (12 payments passed & 1 failed, error rate 8%)

*Recommendations:* It is recommended the broker revise written procedures to include the due dates for when taxes and filing fees are due. It should include additional taxes and fees are due from amended quarterly reports as of the next due date.

*The broker response:* We have amended the procedures to make sure we are processing all initial filings and endorsements when due to ensure compliance

**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 original quarterly reports as filed. However, due to all the adjustments made to the quarterly reports with the corrected transaction reports, payments were not readily identifiable with which quarter they applied to. Many hours were spent reconciling the payments with the taxes and fees due.

The error to the exempt policy found during the audit affects the accuracy of the tax and fee payments. This flow-through finding is addressed in the respective audit test. After an amended report is filed, the broker will be due a refund to pass on to the insured.

*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. Two files have problems with that documentation:

- Prior to 9/4/14 regulation change, the diligent search documentation was required to be received prior to binding. One policy had the documentation received after binding.
- After the 9/4/14 regulation change, the documentation was required to be received no later than 15 days after binding. One policy's documentation was received 21 days after binding.

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

*Recommendations:* It is recommended the broker revise written procedures to ensure all Affidavits of Due Diligence (DD) are received within 15 days of binding. If they choose to require a shorter time frame from their retailers, that is acceptable as long as there is no risk to the insured.

*The broker response:* Our written procedures do state that we receive the DD affidavit at time of binding. The compliance staff reviews all files to ensure compliance and alerts the staff if not received.

**8. Review prompt delivery of evidence of insurance**

**AS 21.34.100(a) and 3 AAC 25.060**

*Comments:* All files included documentation showing evidence of insurance was provided to the insured via producers within the required 30 days prompt delivery time frame.

*Results:* Passed (error rate 0%)

**9. Review required material facts located on evidence of insurance**

**AS 21.34.100(a)**

*Comments:* Two files missed some required material facts on policies:

- No premium amount on policy - 1
- No tax on policy – 2

Total errors: 3 within 2 distinct files

Six files included binders that reference the quote for the material facts but did not identify which quote was being referenced.

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

*Recommendations:* It is recommended the broker revise their written procedures to include what material facts must be on evidence of insurance. Review statute for details. It is recommended the broker revise their written binder procedures to identify exactly which quote is being referenced by including the quote number and the date and to ensure the quote is sent with the binder: “Quote Number\_\_\_\_\_, dated \_\_\_\_\_is incorporated by reference and is part of this certificate of coverage as though fully set forth herein.”

*The broker response:* We are working with production staff and in our management system to ensure accuracy on this issue. We are setting up training for those who place business in AK to make sure they understand the requirements.

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

**AS 21.34.100(e)**

*Comments:* The disclosure statement the broker used was missing a word and since it’s in quotes in statute, the entire statement is wrong. In addition, nine files had other problems related to the statement. Auditor reviewed the evidence of insurance as emailed to the producers for the insureds. Here are the different problems found in the files:

- Confirmation of Coverage – 50 included wrong statement
- Dec – 40 included the wrong statement
- Dec – 3 missing disclosure statement
- Endorsements – 17 included the wrong statement
- Endorsements – 5 missing disclosure statement
- Stamp on endorsement was smaller than required 10 point type – 1

Total disclosure errors: 116 within 50 distinct files

In two files, quotations were used around the disclosure statement but the quotes were converted to odd characters, which was presented to the insured.

*Results:* Failed (error rate 100%)

*Recommendations:* It is recommended the broker add the missing word to their disclosure statement and ensure written procedures are followed requiring all evidence of insurance have the correct statement and is legible in at least 10 point type. If quotations will be used, it is

recommended a second review is performed to ensure odd characters are not created in place of the quotations.

*The broker response:* This is wording that automatically generates in our system, and has been updated to correct the error.

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

**AS 21.34.110**

*Comments:* Seven files included the required notification that the insurance is being placed with a company that is not regulated by the Alaska Division of Insurance in their quote prior to invoicing. However, 43 files did not. Of those 43, 31 files included the disclosure stamp from AS 21.34.100(e), but this is not sufficient to meet the statute requirements. Twenty-three of the 43 files stated the company was nonadmitted, but this is also not sufficient to meet the statute requirements.

*Results:* Failed (7 files passed & 43 failed, error rate 86%)

*Recommendations:* It is recommended the broker revise their written procedures to include the Alaska notification language in the quote or on a separate document to the insured describing the surplus lines insurance company as required by statute. The information should include: 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:* We have set our agency management system to automatically attach the required disclosure on all quotes as a separate document

**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 documentation for sufficient detail of each transaction as well as the additional surplus lines broker records that must be maintained.**

**AS 21.27.350 and .810**

*Comments:* One file included an outdated version of the Alaska Policyholder Notice and a request should have been made to the company to provide a current version based upon bulletin B 08-06.

*Results:* Passed (error rate 0%)

**Advisory:**

- Invoices are not dated. This is problematic as the invoice date determines in which quarter an endorsement is to be filed.
- The confirmation of coverage is also not dated showing when bound.

*The broker response:* We are working with leadership to amend these documents to add a date to ensure it is clear when the invoice was generated and the bound date is clearly identified.

## **SUMMARY AND SUBSEQUENT EVENTS**

### **Summary**

This was a premium tax audit of Brown and Riding Ins Services 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 affects the service to the insured and compliance with Alaska statutes and regulations.

- 1) The quarterly reports are consistently not accurate when filed. Numerous transactions were modified or replaced yet many were still incorrect as found in the audit.
- 2) The disclosure statement was missing a word; thus, all files failed. In addition, the disclosure statement was missing from many of the evidence of insurance.
- 3) The required notification to the insured regarding the use of a nonadmitted insurer was not found in the majority of 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 Brown and Riding Ins Services Inc. be re-audited within the next three years to ascertain compliance.

Submitted by:  
Rebecca Nesheim  
Tax Auditor

Affidavit

Brown and Riding Ins Services Inc.  
As of December 31, 2015  
TA 16-04

Juneau, Alaska )  
December 2, 2016 )  
State of Alaska ) ss.  
First Judicial District )

I, being duly sworn, do verify that the report of premium tax audit as of December 31, 2015 of Brown and Riding Ins Services Inc. is true to the best of my knowledge and belief.

*Rebecca Nesheim*

Rebecca Nesheim  
Tax Auditor

SUBSCRIBED and SWORN to before me this 2<sup>nd</sup> day of December, 2016



*Brian Sonesen*  
Notary Public in and for Alaska

My Commission Expires office