

CERTIFIED MAIL
RETURN RECEIPT REQUESTED

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

Order # TA 17-02(b))
In the Matter of Audit of)
Affinity Insurance Services Inc.)
_____)

FINDINGS OF FACT

1. An audit report of Affinity Insurance Services Inc., licensed in the State of Alaska, has been issued by the State of Alaska, Division of Insurance to Affinity Insurance Services Inc.
2. The audit report of Affinity Insurance Services Inc. (TA 17-02(b)) has been transmitted to Kenneth MacKunis, Compliance Officer, Affinity Insurance 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 Affinity Insurance Services Inc. (TA 17-02(b)) 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 April 13, 2018.

Dated this 13th day of April, 2018 at Juneau, Alaska.



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

PREMIUM TAX AUDIT OF

Affinity Insurance Services Inc.

Fort Washington, PA

Alaska License # 9435

TA 17-02(b)

As of December 31, 2016

Issued by

DIVISION OF INSURANCE

DEPARTMENT OF COMMERCE, COMMUNITY AND ECONOMIC

DEVELOPMENT

STATE OF ALASKA



FINAL REPORT:

April 13, 2018

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



April 13, 2018

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

Affinity Insurance 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, the premium tax regulations 3 AAC 21.550 – 570 and licensing statutes AS 21.27.350 and 21.27.810. This is the first premium tax audit of Affinity Insurance Services Inc. conducted by the Alaska Division of Insurance (the division).

Subject Matters Audited

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

Time Frame

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

METHODOLOGY

The division sent the call letter and initial data requests to the broker's office in Fort Washington, PA. 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 756, from which a sample of 50 files was selected for audit. After a final report and order were completed, the broker filed an additional 43 transactions which were effective during the audit period but were not on the original list of transactions in which to select the audit sample from although the broker was aware of these before the audit began. Consequently, the original final report and order were vacated with order 17-02(a) for the audit to continue with the additional 43 transactions added to the audit for a total number of files now 93.

The following are the procedure steps for the audit:

- 1) Verify that quarterly reports and accompanying forms were filed on time.
 - i) Audit steps taken:
 - (1) Reviewed the quarterly reports sent to the Alaska Division of Insurance and verified they were filed by the due date.
- 2) Verify the accuracy of the premium calculation.
 - i) Audit steps taken:
 - (1) Reviewed policy, binders, and invoices to determine how taxable premium was calculated.
 - (2) Verified the correct premium was reported on the reports as filed.
- 3) Verify the accuracy of quarterly reports filed.
 - i) Audit steps taken:
 - (1) Reviewed the policy, binder, and endorsement pages in each file.
 - (2) If the effective date did not match the quarterly filing, reviewed the correspondence to ensure the documentation in the file matched when the policy was booked. Most of these occurred with endorsements that often require additional information and sometimes company approval before it can be added to the policy. The invoice date determines in which quarter the endorsement is required to be filed.
 - (3) Verified the quarterly reports as filed with the division were accurately filled out to reflect the correct effective date, premiums, taxes and fees based upon the information in the files.
 - (4) Verified a statement of exempt premiums was filed when appropriate.
 - (5) Verified the policy was included in the quarterly filing based upon the effective date of the policy.
 - (6) Verified the insured name, insurance company, policy type codes, producer names and license numbers were accurate on the forms filed.
 - (7) Verified the descriptions of the subject and locations of risk were identified on the reports.
- 4) Confirm Alaska is the home state of the insured.
 - i) Audit steps taken:
 - (1) Verified where the principal place of business or residence of the insured is located.

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

Acceptable Error Rate:

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

PREMIUM TAX AUDIT

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

Comments: The eight original quarterly reports with accompanying forms were filed on time. A total of nine amended reports were filed after the original due date.

Results: Passed (error rate 0%)

- | |
|---|
| 2. Verify the accuracy of the premium calculation
AS 21.34.180 |
|---|

Comments: The premium was calculated correctly for all policies as the broker is correctly reporting the full amount of the premium on the quarterly reports and paying the taxes and filing fees when due.

However, the broker is not collecting the money first then paying the division on the Healthy Paws policies since the premium, tax and filing fees are collected from the insured on a monthly basis. There is not a problem with the premium being paid on a monthly basis between the insured and the broker, it is the tax and fees being collected on the monthly basis that does not meet statute requirements. Alaska statute 21.34.180(a) states “the broker shall collect and pay to the director a tax of 2.7% on the net premium, which is the total gross premiums written, less any return premiums.” “Collect” means the broker has to get the money first-then pay the tax. Alaska regulation 3 AAC 25.080 requires the tax be collected “for the full amount of the premium charged,” not on a periodic or piecemeal manner.

Results: Failed (3 files passed & 90 failed, error rate 97%)

Recommendations: It is recommended the broker immediately start collecting 100% of the taxes and filing fees as part of the first payment charged to the insured to ensure the broker has all the taxes and fees to pay the division as required by law.

The broker’s response: A project is underway to adjust our current processes to align and to adhere to the division’s requirement.

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

Comments: Ninety Quarterly Reports were filed with incorrect information. The following are the different issues identified:

- 90 - Producing broker identified incorrectly as Affinity. Healthy Paws Pet Ins LLC is the producing broker. Healthy Paws is a separate entity owed by Affinity.
- 43 - Report of Surplus Lines Transaction forms filed on amended Quarterly Reports after the due date.
- 2 - policy number incorrect or missing

- 1 - insurance company's NAIC number and policy type code were missing
- Total errors: 136 within 90 distinct files

Two policies were cancelled prior to the expiration date. An endorsement was not received by the broker or invoiced for either policy but can be filed with the division once invoiced for a return of tax and filing fees to send back to the insured.

Results: Failed (3 files passed & 90 failed, error rate 97%)

Recommendations: It is recommended the broker revise written procedures to include how to complete the Report of Surplus Lines Transaction form. Procedures should include what data is entered into each field. A second individual reviewing documents before submission could reduce the errors received by the division.

The broker's response: Our current procedures now reflect a step by step procedure on how to complete a Report of Surplus Lines Transaction Form. Procedures provided to the division. This has been reviewed with the Surplus Lines Team.

As part of our updates a quality control process has been added. Once a filing has been processed by a surplus lines team member (SLTM) it is now reviewed by management prior to submission. If anything is incorrect it is sent back for revision. If the information is accurate the SLTM will be advised to submit. This process was not in place previously and will allow us to be more efficient.

4. Verify the home state for insured is Alaska	AS 21.34.180
---	---------------------

Comments: The broker does not write multi-state policies. If a Healthy Paws policyholder moves into Alaska, the policy must be re-written. The home state is Alaska for all policies.

Results: Passed (error rate 0%)

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

Comments: All payments were made on or before the required due date for the quarterly payments and made by ACH, including the amended reports payments.

Results: Passed (error rate 0%)

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

Comments: All tax and fee payments made by the broker were accurate based upon the quarterly reports as filed. The error found during the audit on the accuracy of the Quarterly Report affects the accuracy of the tax and fee payments. The flow-through finding is addressed in a separate audit test.

Results: Passed (error rate 0%)

7. Review diligent search effort made to place insured with an admitted insurer

AS 21.34.020, 3 AAC 25.010 and .035

Comments: The broker has elected to use the Affidavit of Due Diligence (Affidavit) for documenting the diligent search. During the audit period, the lines were blurred between the producer and the broker as the declinations were completed by Healthy Paws Pet Ins LLC staff but Affinity staff created the Affidavit for an Affinity surplus lines broker and officer of Healthy Paws to sign. There were numerous issues with the diligent search efforts:

- 80 – Affidavits created after allowed 15 days from binding
- 6 – Affidavits show the diligent search was completed after binding and Affidavits of Due Diligence created after allowed 15 days from binding
- 4 – Affidavits created within allowed 15 days from binding but after the 180 days allowed for the same declinations to apply to the same class of insurance.
- 2 – Declinations not valid as the admitted companies canvassed did not write the full amount, kind, or class of insurance the insured's needed.

Results: Failed (1 file passed & 92 failed, error rate 99%)

Recommendations: It is recommended the broker revise their written procedures to ensure all Affidavits of Due Diligence are created or received within 15 days of binding. If broker wants to use 3 AAC 25.035(a)(2) as their diligent search documentation, all admitted companies they can reach must be contacted and documentation maintained they do not write the full amount, kind, or class of insurance. It is recommended the broker read Bulletin 15-10, published 10/28/2015 for details.

The broker's response: Our written procedures have been updated to ensure Due Diligence affidavits are created within 15 days of binding. Implementation of the revised procedures was completed on September 15, 2017. Procedures were provided to the division.

Due diligence will be performed and documented with a maximum of every 180 days per insured account if coverage of risk is the same. If coverage of risk is not the same 3 admitted companies will be contacted prior to binding. Affinity has re-reviewed Bulletin 15-10 and understands and, per the above, will carry out the requirements pertaining to a diligent effort in AK.

8. Review prompt delivery of evidence of insurance

AS 21.34.100(a) and 3 AAC 25.060

Comments: Two files have no documentation showing when the evidence of insurance was provided to the insured. The broker has 30 days from binding to provide the evidence of insurance to the insured.

Results: Passed (91 files passed & 2 failed, error rate 2%)

Recommendations: It is recommended the broker revise their written procedures to include the prompt delivery of the policy or, if the policy is not available, a cover note, binder, or other evidence of insurance. Documentation showing prompt delivery must be maintained in the insured's file.

The broker's response: Our current procedures now reflect the proper timing requirements of policy issuance. Documentation showing prompt delivery will now remain within the insured's file.

The operations/sales team members have been instructed on all policy issuance procedures regarding the required timing. All training was completed in October 2017. Procedures have been provided to the division.

9. Review required material facts located on evidence of insurance

AS 21.34.100(a)

Comments: All 93 files are missing some required material facts on binders and/or policies. Here are the different issues the broker is not compliant with regarding this statute:

- 90 – For all Healthy Paws files no binders are provided to the insured just the policy, which means all material facts must be on policy. The license number of the broker is missing on all policies.
- 3 – Binders missing the license number of the broker
- 3 – Policies missing the license number of the broker

Total errors: 96 within 93 distinct files

Results: Failed (93 files failed, error rate 100%)

Recommendations: It is recommended the broker revise their written procedures to include what material facts must be on evidence of insurance. The license number is the only material fact missing from the evidence of insurance identified in the audit.

The broker's response: Our written procedures have been updated to include the specific details needed on all evidence of insurance documents. Training has been completed for all areas to ensure consistency within the organization. This was completed October 2017. Procedures have been provided to the division.

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

AS 21.34.100(e)

Comments: Problems were identified in all 93 files regarding the required disclosure statement on evidence of insurance. The statement is in quotes in statute so it is required to be word-for-word. Here are the different problems found in the files:

- 93 – Dec included disclosure statement but was missing a word
- 1 – No disclosure statement on binder
- 2 – Binder included statement but was missing a word
- 1 – Dec missing broker name

Total disclosure errors: 97 within 93 distinct files

Results: Failed (93 files failed, error rate 100%)

Recommendations: It is recommended the broker revise their written procedures to include the requirement that all evidence of insurance have the correct word-for-word disclosure statement. Read statute AS 21.34.100(e) for the language. This includes all premium and non-premium endorsements. It is further recommended to revise the written procedures to ensure the broker's name is included on all evidence of insurance.

The broker's response: Our written procedures have been updated to reflect the proper language specific to Statute AS 21.34.100(e). The original language was missing a word, ("the"), before Alaska Surplus Lines. This has since been corrected.

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

AS 21.34.110

Comments: All 93 files failed regarding the notification requirements informing the insured about the surplus lines insurance company as required by statute. The broker's database data entry group created the notification but none were sent to any of the insureds. In addition, they were all created after binding.

Results: Failed (93 files failed, error rate 100%)

Recommendations: It is recommended the broker revise their written procedures to include the Alaska notification language in the quote provided to the insured describing the surplus lines insurance company as required by statute. The information should include the three points of the notification: the company does not have a certificate of authority, they are not regulated by the Alaska Division of Insurance and in the event of insolvency losses will not be covered by the Alaska Insurance Guaranty Association Act. The producing broker can provide the notification to the insured electronically but must also provide to the broker for their files.

The broker's response: Our procedures have been updated to reflect proper procedures regarding the Alaska notification language. These procedures were updated October 2017. All insured's will be properly notified at each placement. Updated procedures have been provided to the division.

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

AS 21.34.050

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

Results: Passed (error rate 0%)

13. Review notice regarding nonrenewal and premium increase

3 AAC 25.050

Comments: Ninety-one policies were missing the Alaska Policyholder Notice.

Results: Failed (2 files passed & 91 failed, error rate 98%)

Recommendations: It is recommended the broker include a step in the processing of the policy to ensure the Alaska Policyholder Notice is part of the policy. If the notice is missing, they will need to contact the insurance company to include it.

The broker's response: Our procedures now include the step to ensure the Alaska Policyholder Notice is part of the policy. Business areas have been instructed on the proper process and advise to communicate with the insurance company to ensure delivery if necessary. Training was completed in October 2017. Procedures have been provided to the division.

14. Other Compliance Issues

Comments: AS 21.27.350 and 21.27.810: The broker does not maintain complete documentation to be in sufficient detail that relevant events, the dates of those events, and all persons participating in those events can be identified. The binders and policies for some of their accounts are delivered directly from the insurance company to the insured without any information provided to the broker as to when these communications took place.

Additionally, the data as entered into the broker's database is not accurate. The dates of receipt for specific documents are when the data entry unit receives the data to enter and not the actual dates of receipt or when the documents are created. Therefore these dates cannot be relied upon to identify when relevant events occurred as required by statute.

Recommendations: It is recommended the broker ensure they are included in communications between the insurance company and the insured. Review statute for listing of all required records and information that must be maintained. The procedures for data entry should be evaluated and modified to maintain accurate data to bring the broker into compliance with Alaska laws.

The broker's response: For accounts issued direct by the insurance company, Affinity will continue to work with the insurance company to ensure the accuracy of the information. Our current procedures have been evaluated and updated to reflect the data entry requirements on Alaska filings. Our compliance department will continue to work on ensuring compliance with Alaska Laws.

SUMMARY AND SUBSEQUENT EVENTS

Summary

This was a premium tax audit of Affinity Insurance 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. An additional compliance issue was discovered during the audit.

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 broker has not collected all the tax and filing fees from the insured by the time they pay the tax and filing fees to the division.
- 2) The Quarterly Reports as filed were consistently inaccurate.
- 3) The diligent search was not documented adequately in most files and most documentation was created beyond the 15 days of binding.
- 4) Not all material facts were included on binders or policies.
- 5) The disclosure statement was missing a word when included on evidence of insurance.
- 6) The required notification to the insured regarding the use of a nonadmitted insurer was not provided prior to binding or receipt of premium.
- 7) The Alaska Policyholder Notice was missing from most policies.
- 8) The broker does not maintain all communications with the insured either internally or those between the company and the insured.

The auditor has reviewed the broker's revised procedures and they appear to accurately capture the problems identified in the audit.

Re-Audit

In closing, the auditor's recommended actions and the new procedures should help the broker correct the problems encountered. It is recommended that Affinity Insurance Services Inc. be re-audited within the next two years to ascertain compliance.

Submitted by:
Rebecca Nesheim
Tax Auditor

Affidavit

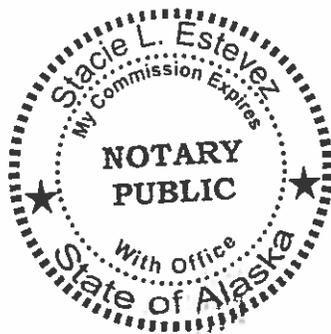
Affinity Insurance Services Inc.
As of December 31, 2016
TA 17-02(b)

Juneau, Alaska)
April 13, 2018)
State of Alaska) ss.
First Judicial District)

I, being duly sworn, do verify that the report of premium tax audit as of December 31, 2016 of Affinity Insurance 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 13 day of April, 2018



Stacie L. Estevez
Notary Public in and for Alaska
My Commission Expires with office