

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 22-02 )  
In the Matter of Audit of )  
Lockton Affinity, LLC )  
\_\_\_\_\_ )

FINDINGS OF FACT

1. An audit report of Lockton Affinity, LLC, licensed in the State of Alaska, has been issued by the State of Alaska, Division of Insurance to Lockton Affinity, LLC.
2. The audit report of Lockton Affinity, LLC (TA 22-02) has been transmitted to Jeffrey Hewitt, Compliance Officer, Lockton Affinity, LLC (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 Lockton Affinity, LLC (TA 22-02) 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 November 2, 2022.

Dated this 2 day of November, 2022 at Anchorage, Alaska.



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

**PREMIUM TAX AUDIT OF**

**Lockton Affinity, LLC  
Overland Park, KS  
Alaska License #10851**

**TA 22-02**

**As of December 31, 2021**

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



**FINAL REPORT:  
October 31, 2022**

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October 31, 2022

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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 Lockton Affinity, LLC. The audit was conducted by Rebecca Nesheim, tax auditor for the Alaska Division of Insurance.

## **Lockton Affinity, LLC**

### **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 second premium tax audit of Lockton Affinity, LLC conducted by the Alaska Division of Insurance (the division).

### **Subject Matters Audited**

Lockton Affinity, LLC (the broker) is an Alaska licensed surplus lines broker based in Overland Park, KS. 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, 2020 and December 31, 2021.

## **METHODOLOGY**

The division sent the call letter and initial data requests to the broker's office in Overland Park, KS. 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 569, 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.
  - 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 the policy was included in the quarterly filing based upon the effective date of the policy.
    - (5) Verified the insured name, insured address, insurance company, producer names and license numbers were accurate on the forms filed.
    - (6) Verified the descriptions of the subject and locations of risk were identified on the reports.
- 4) 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.
- 5) 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.
- 6) 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 or in the case of individuals, the residence state.
- 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 of 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 and at least 10-point type.
- 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**

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| <b>1. Verify 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> |
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*Comments:* The eight original quarterly reports with accompanying forms were filed on time.

*Results:* Passed (error rate 0%)

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| <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 incorrectly on one policy as \$11 terrorism premium was missed. Negligible tax and fees are calculated on the \$11 so no amendment required.

This error affects two additional audit tests:

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

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

*Recommendations:* It is recommended the broker modify Alaska specific written procedures to ensure all premium for the various coverages are included in taxable premium as well as any company fees.

*The broker's response:* Lockton Affinity utilizes the Surplus Lines tax calculator on all transactions with the current Alaska tax rates built in. Rates are based upon information made available through the Lockton Intranet maintained by our Lockton Surplus Lines Tax Department. Per written procedures and prior to submission to our Lockton Surplus Lines Department, each policy is reviewed to verify that all premiums have been taxed. In addition, our Lockton Surplus Lines department will review the policy and invoices a second time. This will ensure the full written premium and any company fees listed on the declaration page of the policy or on an endorsement are being taxed before they are submitted through OPTins.

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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:

- Policy # incorrect – 2
- Company Name and NAIC# incorrect – 3
- Insured address incorrect, the location of risk used instead of insured's actual address – 4
- Filed late on amended report – 4
- Endorsement date incorrect – 1



- Description of subject inadequate – 1
- Endorsement not identified as an endorsement – 1
- Expiration date incorrect – 1

Total accuracy errors: 17 within 13 distinct files

For the two-year audit period, there were 30 amended reports and 104 errors amongst all the reports filed. It takes hours for the division staff to identify the problems, write up the issues, and confirm the corrections with each subsequent report filed.

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

*Recommendations:* It is recommended the broker ensure their Alaska specific written procedures are followed on what documents to review to ensure the quarterly report is completed accurately. It is recommended the broker consider adding to their procedures what data is entered into each field, not just list each field. A second individual reviewing documents before submission should reduce the number of errors received by the division.

*The broker's response:* Each Alaska surplus lines policy is reviewed against the written procedure requirements prior to submission to our Lockton Surplus Lines Department. Written procedures include the Alaska location of data that is to be reviewed and verified. Lockton Affinity relies upon our Lockton Surplus Lines Department to submit the required quarterly surplus lines tax filings. In addition, our Lockton Surplus Lines Department will review it a second time to ensure the policy number, insureds name, insurance company- NAIC#, address and location of risk address, effective and expiration dates, description of subject, producer name, and license number are accurate and included in the forms filed and on the quarterly filing. They will verify the full written premium and company fees listed on the declarations page of the policy or any on endorsement to ensure they are being taxed before they are submitted through OPTins.

**4. Verify if tax and filing fee payments were made on time and by ACH**  
**AS 21.34.180, AS 21.34.190, 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.

*Results:* Passed (error rate 0%)

**5. 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 errors found during the audit in the premium calculation and home state of the insured affects the accuracy of the tax and fee payments. These flow-through findings are addressed in their respective audit tests.

*Results:* Passed (error rate 0%)

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

**AS 21.34.180**

*Comments:* All policies were correctly identified with Alaska as the home state.

*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 contacts the admitted companies at least once every 180 days for multiple insureds with the same risk as allowed per regulation. All files had the necessary diligent search efforts documented.

*Results:* Passed (error rate 0%)

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

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

*Comments:* All files have documentation showing the evidence of insurance was provided to the insured within the 30 days of binding.

*Results:* Passed (error rate 0%)

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

**AS 21.34.100(a)**

*Comments:* Twenty-eight files show the broker license number was missing on the evidence of insurance sent to the insured within 30 days of binding. If the proof of coverage was missing the license number, the policy sent within the 30 days from binding was evaluated.

*Results:* Failed (22 files passed & 28 failed, error rate 56%)

*Recommendations:* It is recommended the broker add to their Alaska specific written procedures to include what material facts regarding the coverage, insured, insurer, and broker must be on evidence of insurance. Review statute for details.

*The broker's response:* Documents that accompany Alaska surplus lines policies have been updated to include required material facts regarding coverage, insured, insurer, broker, and broker license number. Written procedures for surplus lines review of each Alaska policy include a check for these material facts.

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

AS 21.34.100(e)

*Comments:* Thirty-eight files had problems with the required disclosure statement on the evidence of insurance. Where the insured's copy was unavailable, auditor relied upon the broker copy. Here are the different problems found in the files:

- Dec was missing one word in disclosure, generally in disclosure added by insurer – 12
- No disclosure on proof of coverage – 29
- No disclosure on certificates – 46
- No disclosure on endorsement – 5

Total disclosure errors: 92 within 38 distinct files

*Results:* Failed (12 files passed & 38 failed, error rate 76%)

*Recommendations:* It is recommended the broker modify their written procedures to identify which evidence of insurance must have the required disclosure statement. The disclosure statement should be located on the first page of the evidence of insurance so the insured will not miss it or if necessary, before the evidence of insurance. It is further recommended to revise the written procedures to include the disclosure statement on all premium bearing and non-premium bearing endorsements and certificates as they are also evidence of insurance.

*The broker's response:* Documents that accompany every Alaska surplus lines evidence of insurance have been updated to include the Alaska Surplus Lines warning language. This document is added as the first page to every evidence of insurance for Alaska surplus lines policies. Written procedures for surplus lines review of each Alaska evidence of insurance includes a check for the specific surplus lines warning (AS 21.34.100(e)) language.

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

AS 21.34.110

*Comments:* Twenty-eight files did not have documentation to the insured providing the required 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.

*Results:* Failed (22 files passed & 28 failed, error rate 56%)

*Recommendations:* It is recommended the broker modify Alaska specific written procedures to include when the Alaska notification language will be provided to the insured. Preferably, it should be with the quote to the insured describing the surplus lines insurance company as required by statute.

*The broker's response:* New Business-The Notification for Use of Non-admitted Insurer is provided to a customer for Alaska surplus lines policies as part of the proposal process. The requisite language is part of Lockton Affinity's general Terms and Conditions. The documents that accompany Alaska surplus lines policy renewals have been updated to include the

Notification for Use of Non-Admitted insurer. Written procedures for surplus lines review of each Alaska policy- new business and renewal include a check for the Notification for Use of Non-Admitted Insurer.

**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:* One policy did not include the Alaska Policyholder Notice of premium increase and nonrenewal until it was noticed when pulling the documentation for the audit then the notice was provided to the insured.

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

*Recommendations:* It is recommended the broker modify Alaska specific written procedures to include a step to ensure policies contain the Alaska Policyholder Notice. Bulletin 08-06 should be reviewed for the exact wording. The broker should contact the insurance company to include the notice when it is missing.

*The broker's response:* The language for Lockton Affinity's Alaska Policyholder Notice language has been updated to match the exact wording of Bulletin 08-06. Written procedures for surplus lines review for each Alaska policy include a check for the Alaska Policyholder Notice language.

## **SUMMARY AND SUBSEQUENT EVENTS**

### **Summary**

This was a premium tax audit of Lockton Affinity, LLC. 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 often not accurate when filed. Numerous transactions are filed late, subjecting the broker to penalties.
- 2) Not all required material facts were provided on the evidence of insurance.
- 3) The disclosure language was missing from many evidence of insurance or incorrect.
- 4) The required notification to the insured regarding the use of a nonadmitted insurer was not found in many 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 Lockton Affinity, LLC be re-audited within the next three years to ascertain compliance.

Submitted by:  
Rebecca Nesheim  
Tax Auditor

Affidavit

LOCKTON AFFINITY, LLC  
As of December 31, 2021  
TA 22-02

Juneau, Alaska        )  
October 31, 2022    )  
                              )  
State of Alaska       ) ss.  
First Judicial District )

I, being duly sworn, do verify that the report of premium tax audit as of December 31, 2021 of Lockton Affinity, LLC is true to the best of my knowledge and belief.

Rebecca Nesheim  
Rebecca Nesheim  
Tax Auditor

SUBSCRIBED and SWORN to before me this 3 day of November, 2022



Kelli Patterson  
Notary Public in and for Alaska

My Commission Expires with office