

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 11-04 )  
In the Matter of Audit of )  
M J Hall & Co of Alaska Inc )  
\_\_\_\_\_ )

FINDINGS OF FACT

1. An audit report of M J Hall & Co of Alaska Inc, licensed in the state of Alaska, has been issued by the State of Alaska, Division of Insurance to M J Hall & Co of Alaska Inc.
2. The audit report of M J Hall & Co of Alaska Inc (TA 11-04) has been transmitted to Suzy Baird, Compliance Officer, M J Hall & Co of Alaska 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 M J Hall & Co of Alaska Inc (TA 11-04) 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 April 5, 2012.

Dated this 5<sup>th</sup> day of April, 2012 at Juneau, Alaska.



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

**PREMIUM TAX AUDIT OF**

**M J Hall & Co of Alaska Inc  
Anchorage, AK**

**TA 11-04**

**As of December 31, 2010**

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



**FINAL REPORT:  
April 5, 2012**

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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*

April 5, 2012

Linda S. Hall, CPCU  
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 M J Hall & Co of Alaska Inc (the broker) on October 24, 2011 through October 27, 2011, in the broker's Anchorage, AK office. The audit was conducted by Rebecca Nesheim, tax auditor for the Alaska Division of Insurance.

**M J Hall & Co of Alaska 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 second premium tax audit of the broker conducted by the Alaska Division of Insurance. The first premium tax audit was completed May 18, 2006.

**Subject Matters Audited**

The broker is an Alaska licensed surplus lines broker based in Anchorage, AK. The division included in the current audit a review of the statutory compliance with monthly filings, premium tax and filing fees payments, of accuracy and timeliness as well as required due diligence and disclosures and notifications to the insured.

**Time Frame**

The audit covered this broker's surplus lines business for the two years of January 1, 2009 through December 31, 2010.

P.O. Box 110805, Juneau, Alaska 99811-0805  
Telephone: (907) 465-2515 Fax: (907) 465-3422 Text Telephone: (907) 465-5437  
Email: [insurance@alaska.gov](mailto:insurance@alaska.gov) Website: <http://www.commerce.state.ak.us/insurance/>

## METHODOLOGY

The tax auditor sent the call letter and initial data requests to the broker's office in Anchorage, AK. 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 612, from which a sample of 50 files was selected for audit.

### The following are the procedures steps for the audit:

- 1) Verify that monthly premium reports and accompanying forms were filed on time.
  - i) Audit steps taken:
    - (1) Reviewed the monthly files sent to the Alaska Division of Insurance and verified the reports were filed by the due date.
- 2) Verify the accuracy of the premium calculation
  - i) Audit steps taken:
    - (1) Reviewed policy, declaration page, 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 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.
    - (5) Verified the policy was included in the monthly filing based upon the effective date of the policy.
- 4) If the placement is a multi-state placement, check the calculation and reasonableness of the methodology used 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 sent 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 received by 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 an Alaska 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 monthly reports 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:* All new or renewal policies in the audit were filed accurately on the monthly reports. However, five endorsements within three distinct policy files were either not filed or were filed after the original monthly report filed. Several endorsements were installment payments over several months that are not allowed by Alaska statute. The fix for two of these endorsements was to have the return premium endorsement deleted that was originally filed with the Division, which was completed while the auditor was in the broker's office. Additional taxes and fees on the five endorsements will be due to the Alaska Division of Insurance in the amounts of \$163.04 and \$60.39 respectively after amended reports are filed.

This error affects two additional audit tests:

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

*Result:* Passed (47 files passed & 3 failed, error rate 6%)

*Recommendations:* It is recommended that the broker revise written procedures to include when endorsements are to be reported to the Division. Statute and regulation dates should be included in these procedures. Following the written procedures will ensure all transactions are filed correctly. If an insured wants to pay by installment, ensure that the tax and fees are collected in the first payment so the entire premium can be reported as required on time to the Division. A review by a second individual should be considered in order to catch mistakes before the paperwork is filed with the Division. For all policies effective 7/21/11, procedures will need to be revised to incorporate new law changes from monthly reports to quarterly reports.

*M J Hall & Company of Alaska Response:*

- New Procedural Changes has due dates of policies and endorsements that will be followed:
  1. Policies
    - a. Those bound prior to 7/21/11 must be filed in the month they are effective.
    - b. Those bound 7/21/11 or later will be filed on a quarterly basis defined as follows:
      - I. 3rd Quarter 2011 - July 21, 2011 through September 30, 2011
      - II. 4th Quarter 2011 - October 1, 2011 through December 31, 2011
      - III. 1st Quarter 2012 - January 1, 2012 through March 31, 2012
      - IV. 2nd Quarter 2012 - April 1, 2012 through June 30, 2012
      - V. 3rd Quarter 2012 - July 1, 2012 through September 30, 2012
      - VI. 4th Quarter 2012 - October 1, 2012 through December 31, 2012
      - VII. Subsequent years will be filed on a calendar quarterly basis.



2. All premium endorsements are to be processed as follows.
  - a. Those with policy effective dates prior to July 21, 2011 will be filed monthly using invoice date as the monthly reporting period.
  - b. Premium endorsements with policy effective dates on or after July 21, 2011 will be filed on a quarterly basis defined as follows:
    - I. 3rd Quarter 2011 - July 21, 2011 through September 30, 2011
    - II. 4th Quarter 2011 - October 1, 2011 through December 31, 2011
    - III. 1st Quarter 2012 - January 1, 2012 through March 31, 2012
    - IV. 2nd Quarter 2012 - April 1, 2012 through June 30, 2012
    - V. 3rd Quarter 2012 - July 1, 2012 through September 30, 2012
    - VI. 4th Quarter 2012 - October 1, 2012 through December 31, 2012
    - VII. Subsequent years will be filed on a calendar quarterly basis.
3. Policies with multi-year terms.
  - a. The state tax and stamp fee must be invoiced at inception, using the estimated premium for the multi-year term and filed based as outlined in section 1 shown above.
  - b. Any endorsements (excluding installment endorsements) after inception must be filed based as outlined in section 2 shown above.

- Monthly reports are currently processed by the Branch Manager/Compliance Officer
- Monthly reports are sent to the CFO for the company where they are reviewed for accuracy
- The amounts of \$163.04 and \$60.39 will be remitted by the CFO for correction to the incorrect filings outlined by the Tax Auditor.

A Non-Admitted Compliance Checklist will be used beginning April 1, 2012 that includes a step for ensuring the accuracy of the Report of Surplus Lines Transaction.

4. Verify the multi-state placements are filed correctly
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**AS 21.34.180**

*Comments:* None of the files included in the audit were multi-state.

Result: N/A

5. Verify quarterly and annual premium tax reports were filed on time
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**AS 21.34.180, 3 AAC 21**

*Comments:* Four tax reports were filed late:

- 3<sup>rd</sup> quarter 2009
- 1<sup>st</sup> quarter 2010
- 2<sup>nd</sup> quarter 2010
- 2010 annual tax report.

The remaining four tax reports were filed on time.

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

*Recommendation:* It is recommended that the broker create written procedures to ensure all tax reports are filed on time. Statute and regulation dates should be included in these procedures. For all policies effective 7/21/11, procedures will need to include new law changes from monthly and tax reports to only quarterly reports.

*M J Hall & Company of Alaska Response:*

- New staff's lack of familiarity with the report process initially resulted in the late reports. Although the ultimate responsibility falls on the compliance officer, the new procedures yet to be written needs to be reviewed and enforced to maintain compliance.
- Documents were mailed between the home office and branch office resulting in reports being filed late. Email is used exclusively now.
- New procedures will be established for handling of the 7/21/11 policy placements once their computer program is updated to reflect the correct premiums to be reported. Until then they will be processed manually using Excel

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

**AS 21.34.180, 3 AAC 21**

*Comments:* The 2010 annual tax report was not accurate when filed. After reconciling the tax report with the monthly reports, two errors were identified: a duplicate transaction in one month and a missing transaction in another. The remaining tax reports were accurate when filed based upon the monthly reports for the same time frame. Other audit tests results in these tax reports not being accurate but the errors will be accounted for in their respective tests.

This error affects one additional audit test:

1. Accuracy of Tax and Fee Payments

*Result:* Failed (7 reports passed & 1 failed, error rate 13%)

*Recommendation:* It is recommended that the broker create written procedures to ensure all appropriate transactions are reported on the tax reports. The written procedures should include changes due to new laws effective 7/21/11.

*M J Hall & Company of Alaska Response:*

- The quarterly and annual reports are compiled by the CFO. Prior to August 15, 2011 they were prepared by the Accounting Manager.
- The office does have written procedures for the transactions for the 2009-2010 audit years that are a step by step procedure for the monthly filing process. This will be updated to ensure proper filings of new policy and subsequent endorsement on or after the 7/21/11 filing changes.

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

AS 21.34.180, 3 AAC 21

*Comments:* All payments were made on or before the required due date for the payments and made by ACH.

*Results:* Passed (error rate 0%)

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. Other audit tests results in these payments not being accurate but the errors will be accounted for in their respective tests.

*Results:* Passed (error rate 0%)

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

AS 21.34.020, 3 AAC 25.030 and .035

*Comments:* The broker has elected to use the Affidavit of Due Diligence for documenting the diligent search. Seven files did not contain documentation that the diligent search was conducted. Two files had the required documentation but it was not received by the broker prior to binding. In addition, the description of the insured is not sufficient to verify the risk is on the placement list.

Therefore, nine files failed to show the efforts to place with an admitted insurer were documented prior to binding.

*Results:* Failed (41 files passed & 9 failed, error rate 18%)

*Recommendations:* It is recommended that the broker create written procedures for ensuring all Affidavits of Due Diligence are received prior to binding. If another form of documentation is maintained, there must be clear indications that the declinations were done before binding or an accurate description of how the risk is qualified on the placement list.

*MJ Hall & Company of Alaska Response:* After a change in staff in 2010, it was discovered the procedure of maintaining diligent search efforts evidence in file prior to processing binder wasn't being utilized by support staff. Additional guidelines and procedures were implemented in April 2011 to ensure the required support documents are in file before the binder is issued:

- When a request to bind is received for a non-admitted carrier, there is an Adobe folder set up by year and month. Inside this folder each binding document is named and saved. At minimum the documents required to process an evidence of insurance include the due diligence affidavit and the surplus line fee disclosure. However, additionally our office requires the insured & producer signed application and/or supplement (if required), and the TRIA.
- The affidavit is reviewed for the following:

1. Sections 3 for: policy type code, date bound, policy term.
  2. Proper completion of section 4A or 4B.
  3. In section 4B carrier names, decline date and declination reason.
  4. Section 5 is checked for the producer's name and license number.
- If there is any incomplete information, the affidavit is rejected and returned for correction. A new step has been added effective this date. Upon receipt of the properly completed form, a watermark will be imbedded in the form reflecting an "Accepted" status. This will be imported into the file with the balance of the binding documents.
  - Once all documents are accepted the evidence of insurance will be issued.

A Non-Admitted Compliance Checklist will be used beginning April 1, 2012 that includes a step for ensuring the Affidavit of Due Diligence was received and accurate prior to binding.

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

**AS 21.34.100(e)**

*Comments:* Twenty-five files demonstrated a problem with the required disclosure stamp on the evidence of insurance. Since the insured's copy is unavailable, auditor relied upon the broker copy. Here are the different problems found in the files:

- No stamp on binder – 24
- No stamp on dec – 1

Total disclosure errors: 25 within 24 distinct files

*Results:* Failed (26 files passed & 24 failed, error rate 48%)

*Recommendations:* It is recommended that the broker create written procedures to ensure all evidence of insurance has the required disclosure stamp wording. The written procedures should include the stamp requirement on all premium bearing and non-premium bearing endorsements as they are also evidence of insurance. It is further recommended that if a hard copy is printed for the insured and then stamped that a copy of the stamped document be scanned into the insured's file.

*MJ Hall & Company of Alaska Response:*

- During the time of the audit, it is apparent written procedures were not followed when issuing quotes, evidences of insurance or policies. Though the statements could be attached on a separate document for quotes, evidences of insurance or policies, they were not consistently attached.
- Immediately following the completion of the Premium Tax Audit, the proper disclosures for quotes and all evidences of insurance for non-admitted placements were set up for embedding the disclosure statements as required by AS 21.34.100(e).
- When issuing quotes with our binding authority companies - Burlington, Essex, and Scottsdale, the templates used in quoting were amended to include the disclosure in the first field of the quote. When issuing quotes with our brokerage markets, a stamp is created on the front page of the quote with the disclosure.
- Once a quote is in the bind process, a suspense was set in the insured's file to prompt for compliance of the AS 21.34.100 requirement. This suspense requires the processor to

show the date of the change. That date, time and who performed the task is recorded as follows in our Event log of JET file.

*Susp. Compl: Is AS2134 stamp on binder.*

*Susp. Compl: FN - Fee Notice*

This event/task cannot be deleted from JET file.

A Non-Admitted Compliance Checklist will be used beginning April 1, 2012 that includes a step for ensuring the disclosure stamp is on the declaration page.

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

**AS 21.34.110**

*Comments:* The broker provides notification to the insured as a separate document sent at the time of quoting coverage and was found in every file.

*Results:* Passed (error rate 0%)

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

**AS 21.34.050**

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

*Results:* Passed (error rate 0%)

**13. Review notice regarding nonrenewal and premium increase**

**3 AAC 25.050**

*Comments:* Seven files did not have the Alaska Policyholder Notice. Four files included the notice but it was not the correct language required by the Director.

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

*Recommendations:* It is recommended that the broker create written procedures to ensure all policies include the Alaska Policyholder Notice. A checklist is a useful tool to provide a guide for the broker to confirm the Notice is part of the policy. The insurance company must be contacted if the Notice is missing or not accurate.

*MJ Hall & Company of Alaska Response:*

- The use of the Alaska Policyholder Notice has been a difficult document to mandate use by non-admitted carriers. During the past years carriers have elected to use their "own" version of the form. Though M.J. Hall is clear on the intent and enforcement of the verbiage, it was unclear to management whether it was within the scope of our licensing to use a version of the form we knew was correct, attaching it to the policy and sending to the insured.
- However, since the completion of the audit visit, if the form is missing we notify the carrier and have them process the missing form. At the time of receipt of the missing form, we then mail the policy to the producer.

A Non-Admitted Compliance Checklist will be used beginning April 1, 2012 that includes a step for ensuring the Alaska Policyholder Notice is attached to the policy and if not request from the carrier before sending policy to insured.

### **File Documentation**

Two policy files have other insured's documents mixed in with the insured's file.

## **SUMMARY AND SUBSEQUENT EVENTS**

### **Summary**

This was the second premium tax audit of M J Hall & Co of Alaska Inc. The auditor tested 13 standards focusing on the broker's filing of monthly and 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 was cooperative during the audit. The tax auditor appreciated this attitude and enjoyed working with M J Hall & Co of Alaska Inc's management.

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

- 1) Several monthly reports were not accurate when filed, which has a cascading effect on the accuracies of tax reports and payments. Several transactions were not filed and will subject the broker to penalties when filed.
- 2) Several tax reports were not filed on time and some were not accurate when filed.
- 3) The diligent search in the admitted market first was not documented in many of the files or if it was, some were received after binding.
- 4) The required disclosure stamp was missing on many evidence of insurance.
- 5) The Alaska Policyholder Notice was missing from many files or was outdated.

### **Re-Audit**

In closing, the auditor's recommended actions should help the broker correct the problems encountered. It is recommended that M J Hall & Co of Alaska Inc be re-audited within the next three years to ascertain compliance.

Submitted by:  
Rebecca Nesheim  
Tax Auditor

Affidavit

M J Hall & Co of Alaska Inc  
As of December 31, 2010  
TA 11-04

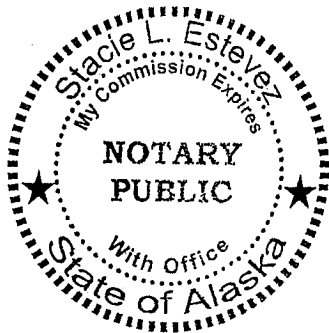
Juneau, Alaska )  
April 5, 2012 )  
State of Alaska ) ss.  
First Judicial District )

I, being duly sworn, do verify that the report of premium tax audit as of December 31, 2010 of M J Hall & Co of Alaska Inc is true to the best of my knowledge and belief.

*Rebecca Nesheim*

Rebecca Nesheim  
Tax Auditor

SUBSCRIBED and SWORN to before me this 5<sup>th</sup> day of April, 2012



*Stacie L. Estevez*  
Notary Public in and for Alaska

My Commission Expires with office