

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 07-04)
In the Matter of Audit of)
Socius Insurance Services, Inc)
_____)

FINDINGS OF FACT

1. An audit report of Socius Insurance Services, Inc, licensed in the state of Alaska, has been issued by the State of Alaska, Division of Insurance to Socius Insurance Services, Inc.
2. The audit report of Socius Insurance Services, Inc (TA 07-04) has been transmitted to Carol Rizzo, Compliance Officer, Socius 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 Socius Insurance Services, Inc (TA 07-04) 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 July 17, 2008.

Dated this 17th day of July, 2008 at Anchorage, Alaska.



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

**PREMIUM TAX AUDIT OF
SOCIUS INSURANCE SERVICES INC
SAN FRANCISCO, CA**

TA 07-04

As of December 31, 2006

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



**FINAL REPORT:
July 17, 2008**

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STATE OF ALASKA
DEPARTMENT OF
COMMERCE
COMMUNITY AND
ECONOMIC DEVELOPMENT

Sarah Palin, Governor
Emil Notti, Commissioner
Linda S. Hall, Director

Division of Insurance

July 17, 2008

Linda S. Hall, CPCU, CIC
Director, Division of Insurance
Department of Commerce, Community and Economic Development
550 West 7th Avenue, Suite 1560
Anchorage, AK 99501-3567

Pursuant to Alaska Statute (AS) 21.06.130, the Alaska Division of Insurance performed a limited and targeted premium tax audit of Socius Insurance Services Inc (the broker) on November 5, 2007, through November 9, 2007, in the broker's San Francisco, CA office. The audit was conducted by Rebecca Nesheim, tax auditor for the Alaska Division of Insurance.

SCOPE OF AUDIT

This premium tax audit was called to review compliance with the surplus lines statutes AS 21.34, regulations 3 AAC 25, and the premium tax regulations 3 AAC 21.550 – 570. This is the first premium tax audit of Socius Insurance Services Inc conducted by the Alaska Division of Insurance.

Subject Matters Audited

Socius Insurance Services Inc is an Alaska-licensed surplus lines broker based in San Francisco, CA, with several locations. The majority of Alaska business is procured in the Sacramento office. The division elected to audit their monthly filings, premium taxes paid, and filing fees paid, for accuracy and timeliness as well as the required diligent search and disclosures to the insured.

Time Frame

The audit covered this broker's surplus lines business for the two years of January 1, 2005 through December 31, 2006.

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METHODOLOGY

The tax auditor sent the call letter and initial data requests to Socius Insurance Services Inc's office in San Francisco. A list of all Alaska business transactions with nonadmitted insurers was requested for the period to be audited. Socius Insurance Services Inc complied timely with all data requests. The number of policies and endorsements written during the audit period was 54 on the initial list provided so all 54 were selected for audit. While on-site, one policy turned out to be outside of the audit period and was deleted from the audit. Thus, there were a total of 53 policy files included in the audit.

The following are the procedures steps for the audit:

- 1) Verify that monthly premium reports and accompanying forms were filed in a timely manner.
 - i) Audit steps taken:
 - (1) Reviewed the monthly files sent to the Alaska Division of Insurance and verified the policy was included in the monthly filing based upon the effective date of the policy.
 - (2) Verified a statement of exempt premiums was filed when appropriate.
- 2) Verify the accuracy of the premium calculation
 - i) Audit steps taken:
 - (1) Reviewed policy, declaration page, and invoices to determine how they calculated the premium.
 - (2) Verified the correct premium was reported on the monthly reports as filed.
- 3) Verify the accuracy of all monthly reports filed.
 - i) Audit steps taken:
 - (1) Reviewed the policy & declaration 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 usually 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) If the placement is a multi-state placement, check the calculation and reasonableness of the methodology to allocate.
 - i) Audit steps taken:
 - (1) Verified the allocation of premium for each state is reasonable and the calculation is accurate.
- 5) Verify quarterly and annual premium tax reports were filed in a timely manner.
 - i) Audit steps taken:
 - (1) Confirmed when the quarterly and annual premium tax reports were mailed to the Alaska Division of Insurance.
- 6) Verify the accuracy of the quarterly and annual premium tax reports

- i) Audit steps taken:
 - (1) Verified the quarterly and annual premium tax reports as filed with the division were accurately filled out to reflect the correct premiums, taxes and fees based upon the monthly reports filed.
- 7) Verify if tax and filing fee payments were made timely and by ACH
 - i) Audit steps taken:
 - (1) Confirmed when the payments were made to the Alaska Division of Insurance and the payment method
- 8) Verify tax and filing fees payments were made accurately
 - i) Audit steps taken:
 - (1) Confirmed if the tax and fee payments matched the tax reports as filed.
- 9) Review effort made to place insured with an admitted insurer
 - i) Audit steps taken:
 - (1) Verified an affidavit of due diligence was in the file and the declinations filled out. If it was marked as using 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 per AS 21.34.100(e)
 - i) Audit steps taken:
 - (1) Reviewed the evidence of insurance to ensure the required broker information and stamp were visible.
- 11) Review disclosures for use of non-admitted insurer per AS 21.34.110
 - i) Audit steps taken:
 - (1) Reviewed the correspondence and other documentation in the files to find a copy of the notification sent to the insured that meets the requirement in AS 21.34.110
- 12) Confirm coverage is placed with an eligible non-admitted insurer
 - i) Audit steps taken:
 - (1) Reviewed the white lists to ensure the company was eligible at the time of placement
- 13) Review notice regarding nonrenewal and premium increase
 - i) Audit steps taken:
 - (1) Verified in each file there was a policyholder notice regarding nonrenewal and premium increase included with the policy.

Acceptable Error Rate:

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

PREMIUM TAX AUDIT

- | |
|--|
| <p>1. Verify that monthly premium reports and accompanying forms were filed in a timely manner.
AS 21.34.080 and .170, 3 AAC 25.100 and 25.090</p> |
|--|

Comments: Seventeen out of the 24 monthly filings for the two year audit period were filed after the due date. The owner signed many of the 2005 reports but he does not have a surplus lines broker license so by the time a licensed broker signed them, the due date was past. For several reports, the postmark showed the report was filed a day late. The 2007 reports have all been filed timely.

Result: Failed (7 reports passed and 17 failed, error rate 71%)

Recommendations: It is recommended that the broker continue to file the monthly reports timely as they currently are by following their written procedures.

Socius Insurance Services Response Received June 13, 2008: The permanent position of "Surplus Lines Coordinator" was created in October 2006 and this individual is committed to the timeliness of each report. This is evidenced by our record for 2007 and 2008.

2. Verify the accuracy of the premium calculation

AS 21.34.180

Comments: There were seven files where the premium was incorrectly calculated. Five of them were missing company fees that results in additional tax and fees due. Two of them included the broker fee which results in a return of tax and fees.

The incorrect premium error affects three others accuracy tests: the monthly reports, the tax reports, and the tax and filing fee payments.

Result: Failed (46 files passed & 7 failed, error rate 13%)

Recommendations: It is recommended that the broker be more diligent in following their written procedures to include all company fees as part of premium for calculating the tax and fees and to not include broker fees.

Socius Insurance Services Response Received June 13, 2008: The coordinator has created a spreadsheet for all states, including Alaska. This spreadsheet is now used by every support person at Socius. It lists all requirements for each state, along with all appropriate taxes, fees, timeframes and nuances. Each transaction is monitored and verified before tax reports are sent to each state.

3. Verify the accuracy of all monthly reports filed

AS 21.34.080 and .170, 3 AAC 25.100 and 25.090

Comments: Ten policies were not reported accurately in the monthly reports as filed.

1. Two transactions were not filed in a monthly report and found during the audit. These two result in additional tax and fees due.
2. Five transactions were not filed in the correct month. Three of these affect when the taxes should have been paid or reversed (cancellation) since the broker reports tax quarterly.
3. Two transactions were filed in the correct month but were done as late amended as they were not filed with the original monthly report.
4. One transaction was filed that was 100% WA risk and should not have been filed at all. See multi-state test for issue. This error will not be included in the error rate for this test as it is included in another test.

The inaccurate monthly reports affects three other tests: the accuracy of the tax reports and the tax and filing fee payments, and the timeliness of the tax and fee payment.

Result: Failed (44 files passed & 9 failed, error rate 17%)

Recommendations: It is recommended that the broker create some additional procedures to ensure all transactions are reported and in the correct month. There should be some additional double checking between what the computer system reports as Alaska surplus lines transactions and what is received by the preparer of the monthly reports. It is also recommended to include a check of the report titled "items due to be paid" each month for transactions with outstanding tax and fees to be paid to Alaska. In addition, all staff working on surplus lines transactions need to be diligent in coding the taxes and fees correctly so the transactions will show up on the necessary reports.

Socius Insurance Services Response Received June 13, 2008: To remedy this issue, we have enlisted the help of our accounting department. Each month a detailed report is generated for each state. Together, our accounting department and coordinator reconcile the transaction reports that are run each month. Any discrepancies are handled immediately.

4. Verify the multi-state placements are filed correctly

AS 21.34.180

Comments: One policy has a component of risk located in Washington State via an endorsement to cover a house in Seattle; therefore, the premium for the endorsement should have been allocated to WA. Instead this endorsement was filed with Alaska. There will be a refund on the taxes and fees paid of \$13.50 and \$5.00 respectively.

Result: Passed (52 files passed & 1 failed, error rate 2%)

Recommendations: It is recommended that the broker create procedures that all staff is aware of for risks that are located partially in another state. A multi-state allocation form must accompany the monthly filing to show the other state(s) and the tax paid to the other state(s) for the transaction.

Socius Insurance Services Response Received June 13, 2008: Multi-state policies are a bit tricky and our staff has been made aware of the need to be diligent in reporting to the proper state.

5. Verify quarterly and annual premium tax reports were filed in a timely manner

AS 21.34.180, 3 AAC 21

Comments: Four out of five tax reports for the two year audit period were filed late or not at all. The broker was not required to make quarterly tax filings in 2005.

2006:

1st quarter: received 6/5/06 was due 5/31/06

2nd quarter: Not filed was due 8/31/06

3rd quarter: received 12/26/06 was due 11/30/06

Annual: received 3/29/07 was due 3/1/07

Result: Failed (1 report passed & 4 failed, error rate 80%)

Recommendations: It is recommended that the broker follow their written procedures to file the tax reports timely.

Socius Insurance Services Response Received June 13, 2008: As mentioned previously, we now have a dedicated employee handling all our tax reports, hopefully eliminating this issue completely.

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

AS 21.34.180, 3 AAC 21

Comments: One tax report was found to be inaccurate prior to the audit findings. While preparing for the audit, one transaction was found as filed in the monthly reports but not included on the annual tax report. The broker corrected the annual tax report and paid the additional tax and fees prior to the audit.

The errors to the premium calculation and the monthly reports' accuracy found during the audit also affect how accurate the tax reports are.

This error affects the accuracy of the taxes and fees payment.

Result: Failed (4 reports passed & 1 failed, error rate 20%)

Recommendations: It is recommended that the broker continue to follow their written procedures to ensure all tax reports are accurate. Once the underlying issues found during the audit are reported correctly, the tax reports should be accurate. It is also recommended to include a double check with reports created from the computer to compare with what transactions should be on each report.

Socius Insurance Services Response Received June 13, 2008: To remedy this issue, we have enlisted the help of our accounting department. Each month a detailed report is generated for each state. Together, our accounting department and coordinator reconcile the transaction reports that are run each month. Any discrepancies are handled immediately.

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

AS 21.34.180, 3 AAC 21

Comments: Three payments were paid late resulting in penalties to Socius Insurance Services Inc. All penalties were assessed and paid prior to the audit. The broker was not required to make quarterly tax filings in 2005.

Results: Failed (2 payments passed & 3 failed, error rate 60%)

Recommendations: It is recommended that the broker continue to follow their written procedures to make certain the tax and fee payments are made timely. They should consider making payments several days in advance of the due date to ensure the payment is received in the State of Alaska's bank account on or before the due date.

Socius Insurance Services Response Received June 13, 2008: Recommendation so noted and stressed with our coordinator.

8. Verify tax and filing fees payments were made accurately

AS 21.34.180, 3 AAC 21

Comments: The accuracy of the tax and fee payments is based entirely on the accuracy of the monthly reports and the tax reports. During the audit, numerous inaccuracies were found in how the reports were created which in turn affected the accuracy of the tax and fee payments.

The correct tax and fees due after including the audit adjustments and reduced by payments received for each year are:

2005:

Surplus Lines Tax: \$23,793.67

Annual Filing Fees: \$8,812.47

Payments made: \$32,550.65

Difference \$55.49

2006:

Surplus Lines Tax: \$27,038.45

Annual Filing Fees: \$10,014.24

Payments made: \$35,767.46

Difference \$1,285.23

Total tax and fees due \$1,340.72

Recommendation: It is recommended that the broker revise their written procedures to ensure all monthly reports and tax reports are accurate as filed so that the tax and fee payments will be accurate. It is the request of the Division for Socius Insurance Services Inc to make the tax and fee payment due now.

Socius Insurance Services Response Received June 13, 2008: Recommendation so noted and addressed in issue #2. Payment was received with the response.

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

AS 21.34.020, 3 AAC 25.030

Comments: Two policy files did not have documentation a diligent search of the admitted market was completed prior to accessing the surplus lines market.

Results: Passed (51 files passed & 2 failed, error rate 4%)

Recommendations: It is recommended that the broker continue to follow their written procedures to maintain documentation in each file showing the diligent search of the admitted market was completed by the producer prior to the broker accessing the surplus lines market.

Socius Insurance Services Response Received June 13, 2008: Our policy regarding this issue is pretty straight forward and consistent for all states. We can only suggest that both of these reports were misfiled. Hopefully the chance of this happening in the future will be eliminated as our office is poised to go paperless in the very near future.

10. Review disclosures for use of non-admitted insurer

AS 21.34.100(e)

Comments: Many files did not have the stamp on all evidence of insurance. In fact not a single binder had the stamp and the broker said they were unaware of this requirement. Many of the declarations (dec) pages had the required stamp although two of them were illegible. Several insurers include some surplus lines language on their dec page but it isn't Alaska-specific and often the stamp wasn't used because the broker thought the language printed by the company was enough. Some multiple dec pages included the correct language but located on subsequent pages and not on the front page of the dec.

Results:

Dec: Failed (33 files passed & 20 failed, error rate 38%)

Binder: Failed (error rate 100%)

Recommendations: It is recommended that the broker ensure that all evidence of insurance includes the necessary stamp per statute AS 21.34.100(e). This stamp must be located on the front page of the evidence of insurance. If the required language will be made part of a template, be sure it stands out for the insured to see.

Socius Insurance Services Response Received June 13, 2008: To address this item, our office has added the exact wording required as part of our binder template. It will automatically be attached and not optional. Regarding the stamp on the dec page, the only point we wish to make is that several of the carriers dec pages do not provide enough space for this stamp, thereby rendering them illegible. We will, however, do everything possible to comply.

Alaska Division of Insurance Response: As mentioned, Socius is moving to a paperless filing system. In order to comply with the requirements of this statute, a copy of the stamped dec will need to be scanned into the electronic file. An electronic notation is not adequate evidence of statutory compliance.

11. Review disclosures for use of non-admitted insurer

AS 21.34.110

Comments: There was no documentation in the files showing the broker met the requirements in Alaska Statute 21.34.110 that requires notification by either the producer or the surplus lines broker to the insured in writing, a copy of which shall be maintained by the surplus lines broker with the records of the contract, available for examination, that the insurer with whom the surplus lines broker places the insurance does not hold a certificate of authority issued by this state and is not subject to its supervision.

Results: Failed (error rate 100%)

Recommendations: It is recommended that the broker include this written notification requirement to the insured in the quote they provide to the producer. If the producer is going to provide the notification to the insured, the broker must have a copy of the notification in the insured's file.

Socius Insurance Services Response Received June 13, 2008: Recommendation so noted and as outlined in issue #10, has been added to our quote template and will be generated automatically.

Alaska Division of Insurance Response: The required wording in statute 21.34.100(e) is not the same information as required in statute 21.34.110. Socius needs to ensure the necessary information printed on their quote template meets the requirements of 21.34.110.

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

AS 21.34.050

Comments: All insurance companies the broker used were eligible surplus lines carriers in the State of Alaska.

Results: Passed (error rate 0%)

13. Review notice regarding nonrenewal and premium increase

3 AAC 25.050

Comments: Twenty-four policies did not include the required Alaska Policyholder Notice per regulation. Three policies included some nonrenewal and premium increase language; however, it did not meet the director's required language per regulation via bulletin. Although it is the insurance company's requirement to include the notice, it is the brokers' responsibility to determine if the policy includes the notice and if not to contact the company to include it.

Results: Failed (26 files passed & 27 failed, error rate 51%)

Recommendation: It is recommended that the broker include on their policy checklist the Alaska Policyholder Notice to ensure all Alaska surplus lines policies are examined for the correct notification. If the checklist is not the appropriate location, then it is recommended that the broker write up procedures to ensure the required notification is part of Alaska surplus lines policies.

Socius Insurance Services Response Received June 13, 2008: This has been added to our internal "policy checklist" which is used to verify that the policy has been checked for accuracy prior to sending to the retail broker for transmittal to the insured.

File and computer documentation

Comments: Several files included documents that belong to another insured, which could lead to inadvertent disclosure of confidential information if a piece of misinformation was provided to the wrong person. Several files showed the computer system did not have accurate information based upon the documents in the file and several others have incorrect information on the file

label. The audit reflects that more attention needs to be devoted to careful file preparation, documentation and computer input.

Recommendation: It is recommended that the broker create better quality control over what is input into the computer and what is included in the policy files. Out of 53 files, having nine with incorrect data is a significant problem.

SUMMARY AND SUBSEQUENT EVENTS

Summary

This was a premium tax audit of Socius Insurance Services Inc. The auditor tested 13 standards focusing on the broker's filing of monthly and annual tax reports and the subsequent payment of premium taxes and filing fees as well as admitted market diligent search and notification requirements for using a non admitted insurer.

The compliance officer and staff were very cooperative during the audit. The tax auditor appreciated this attitude and enjoyed working with Socius Insurance Services Inc's management and staff.

Several significant issues did arise during the audit.

- 1) Many of the monthly reports were not accurately filled out which leads to inaccurate tax reports and inaccurate premium tax and filing fee payments. Once the root cause of the inaccuracies is fixed with the recommendations laid out by the auditor, the resulting inaccuracies should be corrected.
- 2) Many monthly reports and tax payments were filed or paid late during the two years under audit resulting in numerous penalties.
- 3) The manual system of ensuring the accuracy of the premium calculation and the monthly reports in use by the broker is prone to errors.
- 4) The required notification to the insured regarding the use of a non admitted insurer prior to binding was not found in any file. And the stamp per statute required on all evidence of insurance was often missing or not Alaska specific language.

Re-Audit

In closing, while the auditor found problems with the reports and payments, she also found that the broker wants to do things right. The auditor's recommended actions and the actions taken by the broker should correct the problems encountered and it is recommended that Socius Insurance Services Inc be re-audited within the next three years to ascertain compliance with them.

Submitted by:
Rebecca Nesheim
Tax Auditor

Affidavit

Socius Insurance Services Inc
As of December 31, 2006
TA 07-04

Juneau, Alaska)
July 17, 2008)
State of Alaska) ss.
First Judicial District)

I, being duly sworn, do verify that the report of premium tax audit as of December 31, 2006 of Socius 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 18th day of July, 2008



C.A.W.
Notary Public in and for Alaska

My Commission Expires 1/24/2009