

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 10-02)
In the Matter of Audit of)
Parker, Smith & Feek Inc)
_____)

FINDINGS OF FACT

1. An audit report of Parker, Smith & Feek Inc, licensed in the state of Alaska, has been issued by the State of Alaska, Division of Insurance to Parker, Smith & Feek Inc.
2. The audit report of Parker, Smith & Feek Inc (TA 10-02) has been transmitted to Jana Smith, Compliance Officer, Parker, Smith & Feek 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

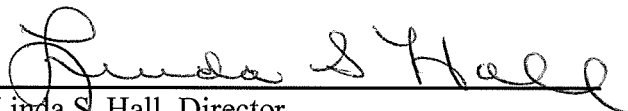
IT IS ORDERED

1. Pursuant to AS 21.06.150(b)(1), the audit report of Parker, Smith & Feek Inc (TA 10-02) 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 March 21, 2011.

Dated this 21st day of March, 2011 at Anchorage, Alaska.



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

PREMIUM TAX AUDIT OF

**Parker, Smith & Feek Inc
Anchorage, AK**

TA 10-02

As of December 31, 2009

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



**FINAL REPORT:
March 17, 2011**

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DEPARTMENT OF
COMMERCE
COMMUNITY AND
ECONOMIC DEVELOPMENT

Division of Insurance

Sean Parnell, Governor
Susan Bell, Commissioner
Linda S. Hall, Director

March 17, 2011

Linda S. Hall, CPCU
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 Parker, Smith & Feek Inc (the broker) on November 16, 2010 through November 19, 2010, in the broker's Anchorage, AK office. The audit was conducted by Rebecca Nesheim, tax auditor for the Alaska Division of Insurance.

Parker, Smith & Feek 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 Parker, Smith & Feek Inc conducted by the Alaska Division of Insurance. The first premium tax audit was completed July 9, 2007.

Subject Matters Audited

The broker is an Alaska licensed surplus lines broker based in Anchorage, AK and Bellevue, WA. 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, 2008 through December 31, 2009.

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METHODOLOGY

The tax auditor sent the call letter and initial data requests to Parker, Smith & Feek Inc's office in Anchorage, AK. A list of all Alaska business transactions with nonadmitted insurers was requested for the period to be audited. Parker, Smith & Feek Inc complied with all data requests. The number of policies and endorsements written during the audit period was 65, from which a sample of 50 files was selected for audit. Two of the original policies on the list were actually endorsements and time ran out to pull another file to review; therefore, 49 files were reviewed as part of the 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 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) Verified the multi-state allocation form was filed when appropriate.
- 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 on time.
 - 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.
- 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 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 received prior to binding 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
 - i) Audit steps taken:
 - (1) Reviewed the evidence of insurance to ensure the broker's name, license number, 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 a 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: The August 2008 monthly report was filed late as the one transaction was filed in the September 2008 monthly report. When the transaction was corrected back to August, the report was considered late. The penalty was assessed and paid prior to the audit. August 2009 was not filed as there were not transactions for that month. Therefore, the monthly reports the broker was responsible for the audit period was 23.

Result: Passed (22 reports passed & 1 failed, error rate 4.3%)

Recommendation: It is recommended that the broker create written procedures to be followed when preparing and filing a monthly report to ensure the timeliness of future filings. Due dates should be included in the procedures.

Parker, Smith & Feek Inc response: A written procedure how to file monthly premium tax reports with examples is in process of being completed and will be saved in a central file accessible to each Surplus Lines Broker.

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. Two transactions when filed in the original monthly reports were not accurate but were corrected prior to the audit. There were no additional premium problems found during the audit.

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: There still seems to be confusion on the part of the individual writing the policy how to code the surplus lines portion as there are many corrections made in the computer system at the time of preparing the monthly reports. This is an issue that was brought up in the last audit that appears to not be solved other than being caught sooner than before. It is affecting when transactions are included in the monthly reports. There were five monthly reports that were not filed accurately. Two had included an incorrect premium and were corrected in an amended report prior to the audit. Three policies were not filed on the original monthly reports. The reports were amended and penalties assessed and paid prior to the audit.

The incorrect monthly reports affect two other tests in the audit:

1. Accuracy of the tax reports
2. Accuracy of the premium tax and filing fee payments

Result: Failed (44 files passed & 5 failed, error rate 10.2%)

Recommendations: It is recommended that the broker ensure their written procedures are followed for when initial or renewal policies as well as endorsements are to be reported to the Alaska Division of Insurance. Following the written procedures should ensure all transactions are filed in the correct month.

Parker, Smith & Feek Inc response: A written procedure is in place, outlined in our surplus lines workflow, for computation of Surplus Lines Taxes and Filing Fees for renewal policies and endorsements.

4. Verify the multi-state placements are filed correctly

AS 21.34.180

Comments: The broker wrote five multi-state policies that were not correctly allocated between Alaska risk and the other states. Several of the policies were excess and umbrella that covered small percentages of risks outside of Alaska. Documentation was not conclusive to identify when locations outside of Alaska were or were not covered as part of the policy and the broker was not forthcoming with the requested information.

The incorrect multi-state placements affect four other tests in the audit:

1. Accuracy of the premium amount
2. Accuracy of the monthly reports
3. Accuracy of the tax reports
4. Accuracy of the premium tax and filing fee payments

Result: Failed (44 files passed & 5 failed, error rate 10.2%)

Recommendations: It is recommended that the broker follow their written procedures for allocating multi-state placements. Following the written procedures should ensure all transactions are filed accurately. The broker should review the audit files and make any necessary paperwork adjustments to the Division to allocate the risks and then file the transactions with the other states.

Parker, Smith & Feek Inc response: Our Surplus Lines Worksheet includes instructions to correctly allocate Alaska premium tax and filing fees for multi-state exposure. Multi State Tax and Filing Fee billings on the five accounts have been corrected in the month of February 2011 and will be reported on the appropriate monthly transaction and summary reports.

5. Verify quarterly and annual premium tax reports were filed on time

AS 21.34.180, 3 AAC 21

Comments: The broker filed the first quarter 2009 tax report 16 days late. All other tax reports were filed on time.

Result: Failed (7 reports passed & 1 failed, error rate 12.5%)

Recommendations: It is recommended the broker ensure their written procedures are followed to file the tax reports on or before their due date.

Parker, Smith & Feek Inc response: Reminders with filing due dates will be set via electronic calendar for the office supervisor and quality control supervisor.

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

AS 21.34.180, 3 AAC 21

Comments: The 2008 annual premium tax report was not correct when filed. After some research by both Division staff and the broker staff, several transactions were not filed with the Division. Amended monthly reports were filed prior to the audit.

Result: Failed (7 reports passed & 1 failed, error rate 12.5%)

Recommendations: It is recommended the broker ensure their written procedures are followed to account for all transactions written for the year when filing both the quarterly and annual tax reports.

Parker, Smith & Feek Inc response: Quarterly and annual reports will be double checked either by the office supervisor or quality control supervisor.

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

AS 21.34.180, 3 AAC 21

Comments: The 2008 annual tax and filing fee payment was received two days after the due date. The late penalty was assessed and paid prior to the audit. All other payments were made on time and by ACH.

Results: Failed (7 payments passed & 1 failed, error rate 12.5%)

Recommendations: It is recommended the broker ensure their written procedures are followed to pay the tax and fees on or before their due date. If the amount of time provided for communication between the two offices is insufficient to ensure on time payments then it is recommended that the time be increased.

Parker, Smith & Feek Inc response: Quality control supervisor or office supervisor will double check with Bellevue Accounting department to verify payment has been made.

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 accurately based upon the tax reports as filed.

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: Four files did not contain an affidavit of due diligence, which is the mode of documentation the broker has chosen to use to meet regulations. It was communicated to the auditor that two of these affidavits were not completed.

Results: Passed (45 files passed & 4 failed, error rate 8.2%)

Recommendations: It is recommended that the broker modify their written procedures to include that all diligent search efforts are clearly documented prior to binding. When the risk is on the placement list, the affidavit of due diligence must still be created prior to binding and provided to the surplus lines broker.

Parker, Smith & Feek Inc response: A written procedure is in place outlining the requirement of a completed Alaska Due Diligence report. Instructions are provided to save the report in the electronic client folder, and a copy of the report will be submitted to the employee completing all monthly tax and filing reports.

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

AS 21.34.100(e)

Comments: Thirteen files had no required disclosure stamp on at least one evidence of insurance or was illegible due to covering words so insured could not read either the document or the stamp:

- No stamp on policy dec - 3
- No stamp on binder - 6
- Stamp was illegible on dec - 2
- Stamp was illegible on binder - 2

Total disclosure errors: 13 within 12 distinct files

Results: Failed (37 files passed & 12 failed, error rate 24.5%)

Recommendations: It is recommended that the broker ensure written procedures are followed that all evidence of insurance have the required stamp. As the insured copy has the stamps, it would be recommended to maintain a scanned version of the insured copy of the evidence of insurance as sometimes the broker's copy does not receive that same attention. Alternatively would be to ensure all evidence of insurance regardless of whose copy it is has the required stamps. It is further recommended to revise the written procedures to include the stamp requirement on all endorsements.

Parker, Smith & Feek Inc response: Our written procedure clearly instructs that a disclosure stamp needs to be applied to the insured's policy declaration page and the agency copy in the computer system. It also indicates the disclosure stamp needs to be fully visible.

Alaska Division of Insurance response: The written procedures must include that all evidence of insurance including endorsements has the required stamp and not just the policy declaration page. These procedures should be revised to include this requirement.

11. Review notification for use of non-admitted insurer

AS 21.34.110

Comments: The broker's procedure is to include the information regarding use of a non-admitted insurance company in their proposal to the insured. However, although three proposals for the audit files had the required information, they did not indicate which company was the non-admitted insurance company and on that company's individual page of the proposal, there was nothing to further identify it as non-admitted. One proposal did not include all the correct information as it used the required stamp from statute 21.34.100(e), which is not sufficient documentation. For one file, nothing was provided so could not determine if the insured was provided the information.

Results: Failed (44 files passed & 5 failed, error rate 10.2%)

Recommendations: It is recommended that the broker follow their written procedures to ensure the required notification is in every proposal to the insured about the surplus lines insurance company as required by statute and that the company is clearly identified as non-admitted.

Parker, Smith & Feek Inc response: Our written proposal workflow will include the necessity to include proper wording alerting the client that the coverage quote has been provided by a non-admitted carrier. Wording will appear on each page of the proposal showing the name of the non-admitted carrier.

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: Seventeen files did not have the Alaska Policyholder Notice as part of the policy. Two of these files included documentation the company was notified to provide the notice for the policies which were received while the auditor was performing the audit, so these will not be considered part of the finding. Seven policies included the notice but it was an older version than required by regulations.

Results: Failed (34 files passed & 15 failed, error rate 30.6%)

Recommendations: It is recommended that the broker revise their written procedures to include a step in the processing of evidence of insurance to ensure the notice is included from the

insurance company. Consider adding this step to the checklists. If the notice is outdated, the broker should contact the insurance company to replace the notice.

Parker, Smith & Feek Inc response: Our written procedure outlines the requirement of the correct form for “Notice regarding nonrenewal and premium increase” is attached to the policy. Procedure also outlines the need to request the correct form from the non-admitted carrier and setting a 30 day suspense for follow up.

Alaska Division of Insurance response: The correct title for the notice of nonrenewal and premium increase is the Alaska Policyholder Notice. The Division has provided the required language in Bulletin B 08-06. It is recommended the broker include a copy of this bulletin in the written procedures for the brokers to refer to when reviewing the policies for completeness.

File Documentation:

Several files included the procedure checklists but they were only partially filled out. Several of the broker’s staff mentioned they may or may not use it at all. In order for the checklists to be effective to meet all statute and regulation requirements, they need to be used consistently.

Parker, Smith & Feek Inc response: Parker, Smith and Feek Inc has appointed a quality control supervisor, who will perform quarterly file audits throughout the office in order to comply with internal workflows and tax and filing accuracy.

SUMMARY AND SUBSEQUENT EVENTS

Summary

This was a follow-up to the premium tax audit of Parker, Smith & Feek Inc completed on July 9, 2007. 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 due diligence and notification requirements for using a non-admitted insurer.

The broker’s staff was cooperative during the audit. The tax auditor appreciated this attitude and enjoyed working with the broker’s staff.

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

- 1) Transactions are still not being identified accurately as to which month they need to be filed. It could be a training issue for the licensed surplus lines brokers who place the business as to the correct coding to use. This causes penalties for late transactions to be assessed.
- 2) Tax & filing fee payments continue to be made late for which penalties are assessed.
- 3) Multi-state policies are not being properly allocated between Alaska and the other states in which there is exposure.
- 4) Evidence of insurance is not receiving the disclosure stamp as required.

- 5) The diligent search in the admitted market first was not documented in several of the files.
- 6) Several files did not contain documentation that the insured was notified when proposing coverage with a non-admitted insurance company.
- 7) The Alaska Policyholder Notice was missing in a many of the files.

Re-Audit

In closing, the auditor's recommended actions should help the broker correct the problems encountered. It is recommended that Parker, Smith & Feek Inc be re-audited within the next three years to ascertain compliance.

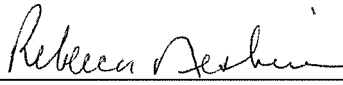
Submitted by:
Rebecca Nesheim
Tax Auditor

Affidavit

Parker Smith & Feek Inc
As of December 31, 2009
TA 10-02

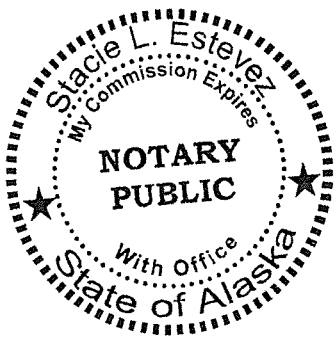
Juneau, Alaska)
March 17, 2011)
)
State of Alaska) ss.
First Judicial District)

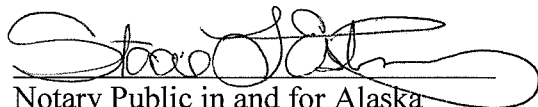
I, being duly sworn, do verify that the report of premium tax audit as of December 31, 2009 of Parker, Smith & Feek Inc is true to the best of my knowledge and belief.



Rebecca Nesheim
Tax Auditor

SUBSCRIBED and SWORN to before me this 21 day of March, 2011




Notary Public in and for Alaska
My Commission Expires with office