

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 13-05)
In the Matter of Audit of)
Gerald J Sullivan & Assoc of Oregon LLC)
_____)

FINDINGS OF FACT

1. An audit report of Gerald J Sullivan & Assoc of Oregon LLC, licensed in the State of Alaska, has been issued by the State of Alaska, Division of Insurance to Gerald J Sullivan & Assoc of Oregon LLC.
2. The audit report of Gerald J Sullivan & Assoc of Oregon LLC (TA 13-05) has been transmitted to John Coleman, Compliance Officer, Gerald J Sullivan & Assoc of Oregon 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 he 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 he 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 Gerald J Sullivan & Assoc of Oregon LLC (TA 13-05) 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 7, 2013.

Dated this 7th day of November, 2013 at Anchorage, Alaska.



Bret S. Kolb, Director
State of Alaska
Division of Insurance

PREMIUM TAX AUDIT OF

Gerald J Sullivan & Assoc of Oregon LLC

Portland, OR

Alaska License # 15882

TA 13-05

As of December 31, 2012

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



**FINAL REPORT:
November 7, 2013**

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THE STATE
of **ALASKA**
GOVERNOR SEAN PARNELL

Department of Commerce, Community,
and Economic Development

DIVISION OF INSURANCE
Juneau Office

P.O. Box 110805
Juneau, Alaska 99811-0805
Main: 907.465.2515
Fax: 907.465.3422
TDD: 907.465.5437

November 7, 2013

Bret S. Kolb
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 Gerald J Sullivan & Assoc of Oregon LLC (the broker) on October 7, 2013 through October 10, 2013, in the broker's Portland, OR office. The audit was conducted by Rebecca Nesheim, tax auditor for the Alaska Division of Insurance.

Gerald J Sullivan & Assoc of Oregon 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 and the premium tax regulations 3 AAC 21.550 – 570. This is the first premium tax audit of Gerald J Sullivan & Assoc of Oregon LLC conducted by the Alaska Division of Insurance.

Subject Matters Audited

Gerald J Sullivan & Assoc of Oregon LLC is an Alaska licensed surplus lines broker based in Portland, OR. The Division elected to audit their monthly filings, premium taxes paid, and filing fees paid, for accuracy and timeliness as well as required due diligence, disclosures and notifications to the insured. For 2012, the broker had the third highest taxes and fees paid to the Division.

Time Frame

The audit covered this broker's surplus lines business for the years January 1, 2011 through December 31, 2012.

METHODOLOGY

The tax auditor sent the call letter and initial data requests to the broker's office in Portland, OR. 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 215, from which a sample of 50 files was selected for audit.

The following are the procedures steps for the audit:

- 1) Verify that monthly reports, quarterly reports, and accompanying forms were filed on time.
 - i) Audit steps taken:
 - (1) Reviewed the monthly and 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, 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 and quarterly 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 or 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 month or quarter the endorsement is required to be filed.
 - (3) Verified the monthly and quarterly reports as filed with the division were accurately filled out to reflect the correct effective date, premiums, taxes and fees based upon the information in the files.
 - (4) Verified a statement of exempt premiums was filed when appropriate.
 - (5) Verified the policy was included in the monthly or quarterly filing based upon the effective date of the policy.
 - (6) Confirmed which state is the home state of the insured to determine if the filing in Alaska was appropriate.
- 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 tax and annual premium tax reports were filed on time.
 - i) Audit steps taken:
 - (1) Confirmed when the quarterly tax and annual premium tax reports were sent to the Alaska Division of Insurance.
- 6) Verify the accuracy of the quarterly tax and annual premium tax reports
 - i) Audit steps taken:

- (1) Verified the quarterly tax 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 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.

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

Comments: During the two audit years, 21 monthly reports were required to be filed and six quarterly reports. Four monthly reports were not required to be filed. All reports required to be filed were filed on time.

Results: Passed (error rate 0%)

2. Verify the accuracy of the premium calculation

AS 21.34.180

Comments: The premium was reported incorrectly for one policy file. There was no explanation for why the amount reported differed from the policy premium. An amended quarterly report was filed 10/10/2013 to adjust to the accurate premium resulting in a credit to the broker that will be claimed on the next quarterly report. The insured was charged the correct taxes and fees.

This error affects two additional audit tests:

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

The broker identifies their broker fee as a policy fee on documents to the insured. It is not included in the calculation of premium.

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

Recommendations: It is recommended the broker create written procedures to ensure all fees are identified as taxable or nontaxable. It is also recommended the broker rename their "policy fee" to "broker fee" or something similar to the other entities in the transaction chain plus the insured knows what the fee is for.

The Broker Response: Procedures have been implemented to identify our fee as broker fee and company fee as policy fee.

3. Verify the accuracy of all monthly reports and quarterly reports filed

AS 21.34.080 and .170, 3 AAC 25.090 and .100

Comments: Two transaction reports contained minor entry errors for which amended forms were filed with the Division on 10/8/2013. There is no effect on any other procedure test. Otherwise, all transactions were accurate when filed.

Results: Passed (error rate 0%)

4. Verify the multi-state placements are filed correctly

AS 21.34.180

Comments: The broker writes many multi-state policies. Out of the 50 audit files, 16 policies were multi-state. For those policies effective prior to 7/21/2011, the allocation to the states involved was accurate based upon the information in the files. For those effective after 7/20/2011, the broker has a home state determination document that walks them through each step to ensure the accuracy of the insured's home state. All policies in the audit were accurately determined to be Alaska as the home state and 100% of the risk was reported to the Division.

Results: Passed (error rate 0%)

5. Verify quarterly and annual premium tax reports were filed on time
AS 21.34.180, 3 AAC 21.550 and .560

Comments: The broker filed all quarterly tax and annual premium tax reports on time.

Results: Passed (error rate 0%)

6. Verify the accuracy of the quarterly and annual premium tax reports
AS 21.34.180, 3 AAC 21.550 and .560

Comments: The premium error found during the audit did not affect the quarterly tax or annual premium tax reports. The quarterly tax and annual premium tax reports were filed accurately.

Results: Passed (error rate 0%)

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

Comments: All payments were made on or before the required due dates 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 21.550 - .570

Comments: All tax and fee payments made by the broker were accurate based upon the tax reports and quarterly reports as filed. The error found during the audit in the premium calculation affects the accuracy of the tax and fee payments for that quarterly report. This flow-through finding is addressed in its own audit test.

Due to the premium not reported accurately, the broker has a credit of tax and filing fees of \$27.03 and \$10.01 respectively that will be claimed on the next quarterly report.

Results: Passed (error rate 0%)

9. Review effort made to place insured with an admitted insurer
AS 21.34.020, 3 AAC 25.010 and .035

Comments: The broker has elected to use the Affidavit of Due Diligence for documenting the diligent search. Thirty files have problems with that documentation:

- No documentation in file – 3
- Affidavits received after binding – 25
- Exempt commercial purchaser documentation received after binding or unable to determine when received - 2

Results: Failed (20 files passed & 30 failed, error rate 60%)

Recommendations: It is recommended that the broker create written procedures to ensure all Affidavits of Due Diligence and exempt commercial purchaser documentation are received prior to binding.

The Broker Response: Written procedures have been implemented to ensure receipt of the Affidavit of Due Diligence or Exempt Commercial Purchaser documentation prior to binding.

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

AS 21.34.100(e)

Comments: Eight 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:

- Stamp illegible on dec – 1
- Stamp on binder not complete -- 5
- Stamp on endorsement missing -- 3

Total disclosure errors: 9 within 8 distinct files

Results: Failed (42 files passed & 8 failed, error rate 16%)

Recommendations: It is recommended that the broker create written procedures to ensure that all evidence of insurance have the required disclosure stamp wording and is legible. The stamp should be located on the first page of the evidence of insurance so the insured will not miss it.

The Broker Response: Stamping procedures have been reviewed with staff.

11. Review notification for use of non-admitted insurer

AS 21.34.110

Comments: The broker does not provide the required notification that the insurance is being placed with a company that is not regulated by the Alaska Division of Insurance to the insured. One policy file included the notification as it was provided by the company which was transferred to the documentation to the insured. A stamp was created while the auditor was in the broker's office that will be used on all surplus lines quotes. The information included on the new stamp is: 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 (1 file passed & 49 failed, error rate 98%)

Recommendations: It is recommended that the broker create written procedures to include Alaska notification language as part of their quote to the insured describing the surplus lines insurance company as required by statute.

The Broker Response: Written procedures have been implemented for use of new stamp with compliant wording. The stamp is for the notification requirement that will be added to all quotes.

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: Seven files did not have the required Alaska Policyholder Notice of nonrenewal and premium increase in the file. One policy's statement of forms listed the notice but the broker failed to identify this as a missing document and request the form from the company. Generally, if the insurance company does not include the notice with the policy, the broker will send the notice instead of contacting the company.

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

Recommendations: It is recommended that the broker create written procedures to include a step in the processing of the policy to ensure the notice is included from the insurance company. If the notice is missing, the broker should contact the insurance company to add the notice. A step on a checklist is one way to ensure this document is reviewed.

The Broker Response: The staff have been reminded to contact the carrier when the Alaska Policyholder Notice is missing at policy issuance.

14. File Documentation

AS 21.27.350

Comments: Several issues came up regarding file documentation

1. In one file, other insured information was in the file.
2. All email documentation is not currently maintained in each file as required.

Recommendations: It is recommended the broker maintain all emails relating to a given policy in the paper files. A double check through a file looking for misfiled documentation is also recommended.

The Broker Response: Staff have been reminded to print and maintain all correspondence for a given policy within the file.

SUMMARY AND SUBSEQUENT EVENTS

Summary

This was a premium tax audit of Gerald J Sullivan & Assoc of Oregon LLC. The auditor tested 13 standards focusing on the broker's filing of monthly, quarterly and annual tax reports and the subsequent payment of premium taxes and filing fees as well as due diligence, disclosure, and notification requirements for using a non-admitted insurer.

The compliance officer and staff were cooperative during the audit. The tax auditor appreciated this attitude and enjoyed working with Gerald J Sullivan & Assoc of Oregon LLC's management and staff.

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

- 1) The diligent search of the admitted market was not documented in several of the files or many were received after binding.
- 2) Several disclosure stamps were missing from evidence of insurance.
- 3) The required notification to the insured regarding the use of a nonadmitted insurer was not found in most files
- 4) The Alaska Policyholder Notice was missing from several files.

Re-Audit

In closing, the auditor's recommended actions should help the broker correct the problems encountered. It is recommended that Gerald J Sullivan & Assoc of Oregon LLC be re-audited within the next three years to ascertain compliance.


Submitted by:
Rebecca Nesheim
Tax Auditor

Affidavit

Gerald J Sullivan & Assoc of Oregon LLC
As of December 31, 2012
TA 13-05

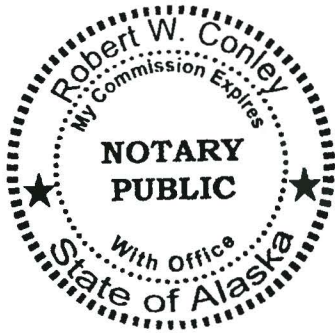
Juneau, Alaska)
November 7, 2013)
)
State of Alaska) ss.
First Judicial District)


I, being duly sworn, do verify that the report of premium tax audit as of December 31, 2012 of Gerald J Sullivan & Assoc of Oregon LLC is true to the best of my knowledge and belief.



Rebecca Nesheim
Tax Auditor

SUBSCRIBED and SWORN to before me this 12 day of November, 2013





Notary Public in and for Alaska
My Commission Expires with office