



## Market Conduct Agency Audit News

Office of Insurance Licensing and Market Conduct

### Introduction

Welcome to the 2016 Market Conduct **Agency Audit News!** In February 2015, the Department of Insurance and Financial Services (DIFS) Market Conduct Agency Audit Unit (Audit Unit) published the first Audit News. It was well received and appreciated by the industry. The purpose for the Audit News is to provide licensees with information and guidance on establishing sound business practices that comply with statutory requirements.

We hope you find the Audit News beneficial to your business operations and encourage you to visit the Licensing Communications page online where the Audit News as well as other pertinent communications can be viewed by the year they were published. Here is the link to the webpage: [http://www.michigan.gov/difs/0,5269,7-303-12900\\_28882---Y\\_2016,00.html](http://www.michigan.gov/difs/0,5269,7-303-12900_28882---Y_2016,00.html)

### Risk Assessment Program

The risk assessment program was implemented in 2015. In the context of an insurance agency business, risks can be defined as processes, procedures, and situations that could make an agency susceptible to noncompliance with laws, rules, and regulations, thus having the potential to cause harm to the consumers and other parties they serve. In practical terms, the primary focus of the risk assessment program is to identify and analyze relevant risks to an agency and to determine appropriate ways to manage those risks based on our preliminary assessments.

In the first Audit News we introduced to you the basic audit programs which typically involve an in-depth review of an agency's books and records for a period of two to four years. Unlike routine agency audits, risk assessments focus on limited areas within a rather short timeframe as determined by the audit team. The outcome of a risk assessment is summarized as follows:

- A closing letter with no identified areas of concern;
- A closing letter with identified areas of concern and our recommendation to remediate the deficiencies;
- A notification letter of an upcoming audit. This happens when the auditors feel a strong need to perform more detailed reviews over a longer timespan when the risk assessment has detected several risky areas.

Upon completion of a risk assessment, we send out a post-review questionnaire to seek your feedback regarding the review process. Your input is highly valuable for us to make further improvements and updates to the new program.

DIFS has identified a number of statutory violations and/or structural weaknesses in some of the risk assessments including, but not limited to, lack of segregation of duties, unappointed and unlicensed activities, and lack of separation of fiduciary funds and the agency operating accounts.

Though some of the aforementioned scenarios do not necessarily constitute direct violations of the Code, the auditors will bring them to your attention and make recommendations to assist your agency in improving business practices. Further, DIFS has published an “Insurance Agency Best Practices” document that provides guidance for agency operations. Please take a few minutes to review the document at [http://www.michigan.gov/difs/0,5269,7-303-12902\\_56869---,00.html](http://www.michigan.gov/difs/0,5269,7-303-12902_56869---,00.html).

### **Unappointed Activity**

While conducting risk assessments and audits the Audit Unit has detected instances where agencies and/or affiliated producers do not have direct appointments with insurers. This constitutes a violation of [\*MCL Section 500.1208a\(1\) & \(2\)\*](#) of the Michigan Insurance Code (Code). The Code is specific in stating that:

“An insurance producer shall not act as an agent of an insurer unless the insurance producer becomes an appointed agent of that insurer.”

The responsibility of ensuring proper appointments with *ALL* insurers rests not only on the insurers, but also on the agency. An agency may not receive its appointment until an affiliated individual producer is licensed for the identical qualification and is appointed by the same insurer. A notice of appointment for the qualifications held by the producer must be electronically filed with the licensing department by the insurer, within 15 days from the date the first application is submitted or an agency contract is executed, whichever is sooner. Appointments are filed electronically by the insurer through the National Insurance Producer Registry (NIPR) at: <http://nipr.com/>.

A licensed agency in Michigan should have an established procedure to ensure that their licensing information is up-to-date. This procedure should include verifying your agency information including licensure, appointments, affiliations, address, and other contact information, on the DIFS website at <http://difs.state.mi.us/locators?searchtype=InsAgency>. Making sure your licensing information is up-to-date with DIFS is a requirement in the Code.

### **DIFS Insurance Appointments Bulletin**

DIFS issued Bulletin 2015-11-INS titled “Insurance Producer Appointments” on April 14, 2015 to provide guidance to licensed producers as to when an appointment is required. Any producer who sells, solicits, or negotiates a contract of insurance on behalf of the insurer is required to have an appointment. The Bulletin provides a list of circumstances in which a producer must be appointed to act as an agent on behalf of the insurer. Please take the time to review the Bulletin at [http://www.michigan.gov/documents/difs/Bulletin\\_2015-11-INS\\_487070\\_7.pdf](http://www.michigan.gov/documents/difs/Bulletin_2015-11-INS_487070_7.pdf) and ensure your agency is in compliance with the Code. Any questions regarding whether an appointment is needed may be directed to the Agency Audit Unit at 877-999-6442.

## Information Regarding Maintaining a Current Agency License

Producers are required under [MCL 500.1238\(1\)](#) to update their mailing and electronic mailing address with DIFS within 30 days of any change. Individual producers may change their addresses electronically at [www.nipr.com](http://www.nipr.com). Agencies can now change their addresses via the new portal [Insurance Licensing Online Services \(ILOS\)](#).

An agency must maintain a designated responsible licensed producer (DRLP) in order for the agency license to remain active. Additionally, agencies must affiliate owners, officers, directors, partners, LLC member or manager, and producers working for the agency. Utilize the new portal [ILOS](#) to update the agency DRLP and affiliate information (addition and cancellation).

Agencies operating in any office location other than the primary location must register each branch office location using the [FIS 2268 Branch Office Registration or Cancellation](#) form.

More information about requirements for maintaining a current agency license may be viewed at the [Producer Agency Licensing webpage](#).

## Surplus Lines Tax Filings – For Surplus Lines Licensees Only

The Audit Unit is designated by the Director to collect and monitor statutory surplus lines taxes and regulatory fees on insurance business placed with nonadmitted insurers. DIFS has mandated surplus lines taxes and fees submitted by all surplus lines licensees, foreign risk retention groups, and purchasing groups be reported and paid electronically via the NAIC OPTins system. Please see Bulletin 2015-09-INS, Mandatory Use of NAIC OPTins issued March 23, 2015 for more details: [http://www.michigan.gov/documents/difs/Bulletin\\_2015-09-INS\\_484989\\_7.pdf](http://www.michigan.gov/documents/difs/Bulletin_2015-09-INS_484989_7.pdf).

Last October, we updated the OPTins semiannual tax form with specific instructions in order to better assist tax filers in completing the OPTins filings. In this newsletter, we will include a selection of frequently received inquiries from the tax filers regarding the semiannual tax forms.

- **Zero Reports** – It is requested that all surplus lines licensees file zero reports with DIFS through OPTins when no business is written during the semiannual period, or when all collected taxes are forwarded to a third party to remit to DIFS. Individual producers do not need to file separate zero reports with DIFS if reports are filed under the agency with which they are affiliated.
- **Tax Credits** – DIFS does not have the statutory authority to issue a refund of surplus lines taxes that have been collected, but does allow credits to be claimed on cancelled business with supporting documentation. There are two line items on the “Semi-Annual Licensee Form” tab in the tax form designated for credits claimed during a semiannual period. Line 30 captures cancelled premiums as a result of mid-term cancellations, premium adjustments, or any other scenarios causing reduction in premium amounts which incurred during the current reporting period. The total amount entered on line 30 should match the total amount of credit premiums reported by policy on the Page 2 tab. Further, line 31 allows tax payers to use any unused credits carried forward from prior tax periods.
- **Effective Date and Invoice Date** – In addition to the “Policy Transaction Effective Date”, a separate column “Invoice Date” is now inserted on Page 2 in the current semiannual tax form.

This additional information provides clarity in various circumstances, for example the effective date of an original policy falls under an earlier semiannual period than an endorsement policy.

- **Tax Calculation** – MCL Section 500.1915 of the Insurance Code authorizes a surplus lines licensee to charge fees to cover the costs incurred in the placement of the indemnity. Those fees shall be excluded from the policy premium in the computation of premium taxes.
- **Multiple Carriers** – If a surplus lines policy is underwritten by multiple carriers, you only need to report the carrier that provides the highest percentage of coverage as reflected in the policy declaration page.

Any questions regarding the content of this newsletter, or any other situations that may arise, may be directed to the DIFS Market Conduct Section, Audit Unit at our toll free number 877-999-6442 or by sending an email to [DIFS-MarketConduct@michigan.gov](mailto:DIFS-MarketConduct@michigan.gov).