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We have completed an audit of the Division of Insurance. This audit is part of the ongoing program of the Legislative Auditor as authorized by the Legislative Commission. The purpose of legislative audits is to improve state government by providing the Legislature, state officials, and Nevada citizens with independent and reliable information about the operations of state agencies, programs, activities, and functions. The results of our audit, including findings, conclusions, recommendations, and the Division's response, are presented in this report.

We wish to express our appreciation to the management and staff of the Division of Insurance for their assistance during the audit.

Respectfully presented,

Paul V. Townsend, CPA
Legislative Auditor

August 22, 2006
Carson City, Nevada

STATE OF NEVADA
DEPARTMENT OF BUSINESS AND INDUSTRY
DIVISION OF INSURANCE

AUDIT REPORT

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STATE OF NEVADA
DEPARTMENT OF BUSINESS AND INDUSTRY
DIVISION OF INSURANCE

AUDIT REPORT

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EXECUTIVE SUMMARY

DEPARTMENT OF BUSINESS AND INDUSTRY DIVISION OF INSURANCE

Background

The Division of Insurance (DOI) is charged with protecting the rights of the consumer and the public's interest in dealing with the insurance industry and ensuring the financial solvency of insurers. According to DOI, its mission will be fulfilled by advancing a sound regulatory environment that is responsive to the insurance needs in Nevada.

DOI consists of the Commissioner's Office and eight operating sections. In fiscal year 2005, DOI had a total of 72 authorized full-time equivalent positions and collected approximately $19 million in assessments, fees, fines, and taxes. Actual expenditures for fiscal year 2005 were about $10.4 million, which included approximately $1.7 million in intra-agency transfers.

Purpose

The purpose of this audit was to evaluate the Division of Insurance's financial and administrative activities, including whether activities were carried out in accordance with applicable state laws, regulations, and policies. This audit focused on the Division's financial and administrative activities during fiscal year 2005, and activities through February 2006 for certain audit issues.

Results in Brief

The Division of Insurance could improve its oversight of financial solvency for domestic companies. DOI did not always ensure required financial reports were submitted and reviewed timely. If problems related to financial solvency are not detected timely, there is an increased risk the insurer will become insolvent. Claims against an insolvent insurer may be paid by a guaranty fund, which is funded by assessments to licensed insurers. These assessments may be passed on to consumers in the form of higher insurance costs. In addition, accounts receivable processes need strengthening to minimize the risk accounts will not be collected. Further, controls over certain administrative functions were not adequate.

Principal Findings

- DOI did not always take timely action for domestic companies that did not submit financial reports or review reports in a timely manner. For example, we found 14 of 20 (70%) annual statements were either not reviewed or had not been reviewed timely. Further, 9 of 17 submitted audited financial statements were either not reviewed or had not been reviewed timely. Domestic companies are those formed under the laws of Nevada. It is the responsibility of state governments to monitor the financial solvency of insurance companies licensed in their states. Effective solvency regulation provides crucial safeguards for insurance customers related to payment of claims and competitive pricing. (page 8)

- DOI's monitoring process for captive insurers does not provide reasonable assurance all reports significant to financial solvency are submitted and reviewed timely. Captive insurance is a type of self-insurance where a company insures its own risks and exposure to loss. Our review of 15 captive insurers found 5 of 15 annual statements were not submitted, and 9 of 10 submitted annual statements were either not reviewed or had not been reviewed timely. Further, 8 of 15 actuarial opinions were not submitted, and 5 of 7 submitted actuarial opinions were either not reviewed or had not been reviewed timely. DOI procedures for captives do not address timely review for all financial reports, or follow-up for non-submitting companies. (page 10)

- DOI did not always schedule examinations and issue orders accepting or rejecting examination reports as required. Further, monitoring was not performed to ensure examiners complied with laws for timely submittal of examination reports. For all 16 examinations selected, no documents were provided to determine when the examinations were completed. NRS 679B.270 requires the examiner to make a report no later than 60 days after the completion of an examination. DOI does not have a written policy that clearly defines completion of an examination. As a result, DOI does not know if examiners are complying with requirements relative to timely submittal. Financial examinations are conducted to determine a company's financial condition. Timely detection and correction of financial concerns is crucial to safeguarding consumers. (page 12)

- DOI did not always monitor the timely submittal and review of other types of required reports. For example, the Producer Licensing Section does not have an adequate process for follow-up on non-submitting entities and timely review of certain required reports. We found instances when Third Party Administrator (TPA) reports were not reviewed as required by law. Further, for TPA financial reports due July 1, 2004, follow-up for non-submitting TPA's was not performed until 11 months past the due date. Timely submittal and review of financial and other reports is critical in protecting consumers. (page 13)

- DOI's monitoring system does not ensure all examination fees are billed to examinees and paid timely. DOI reported over $700,000 in accounts receivable from examination fees to the Controller in March 2005, and over 68% of the receivables were over 60 days past due. A majority of this amount represented cash paid by the State that had not been reimbursed. Our review of 20 examinations found untimely billings, payments, and collection efforts. NRS 679B.290 requires the expense of all examinations be borne by the person examined. DOI took corrective action late in fiscal year 2005. The June 2005 report to the Controller shows accounts receivable for examination fees totaling just over $500,000, and about 55% of the receivables were over 60 days past due. (page 16)

- Collection efforts were not always timely for various user fees. For example, DOI identified 66 companies as delinquent in paying annual continuation fees totaling $112,488, due March 1, 2005. However, as of November 1, 2005, no collection efforts had been made for these fees. When certain entities do not pay their annual renewal fee timely, they are operating without a license. Further, it is inequitable regulation to allow some companies to operate without paying all fees due the State. (page 17)

- DOI does not have sound record keeping or inventory practices in place to provide adequate safeguarding of fixed assets. DOI did not perform a complete annual physical count of all assets or update the state's records as required. Therefore, we could not locate 3 of 20 assets selected from DOI's inventory list. This consisted of a laptop computer, laser printer, and computer network component. Further, 8 of 20 assets did not have asset tags affixed. In addition, we tested four equipment purchases and found two items had not been added to the state's inventory list. As a result, there is an increased risk that loss or abuse could go undetected. (page 19)

- DOI did not retain records used in computing performance measures. Therefore, we could not verify performance measures reported in the Executive Budget were reliable. The State

Administrative Manual (SAM) 2512 requires the performance measurement data in the Executive Budget to be reliable. SAM also requires agencies to retain the records used in computing performance measures for 3 fiscal years. (page 21)

Recommendations

This audit report contains 15 recommendations to improve the Division of Insurance's financial and administrative activities. These recommendations include policies, procedures and other controls to help ensure timely action for required financial reports and adequate monitoring of accounts receivable. We also made recommendations to improve controls over some administrative functions. (page 38)

Agency Response

The Division, in response to our report, accepted the 15 recommendations. (page 31)

Introduction

Background

The Division of Insurance (DOI) is charged with protecting the rights of the consumer and the public's interest in dealing with the insurance industry and ensuring the financial solvency of insurers. According to DOI, its mission will be fulfilled by advancing a sound regulatory environment that is responsive to the insurance needs in Nevada. DOI regulates and licenses insurance producers and other professionals; sets ethical and financial standards for insurance companies; and reviews rates. DOI also reviews programs operated by self-insured employers for workers' compensation and investigates claims of insurance fraud.

DOI consists of the Commissioner's Office and eight operating sections which include Legal and Enforcement, Corporate & Financial Affairs, Property & Casualty, Life & Health, Captive Insurers, Producer Licensing, Self-Insured Workers' Compensation, and Consumer Services.

DOI's main office is located in Carson City, with a field office in Las Vegas. During fiscal year 2005, DOI had a total of 72 authorized full-time equivalent positions. DOI has eight operating budget accounts and also administers four non-operating budget accounts. The main operating account is primarily funded by a General Fund appropriation. This account is also supported by fees, an allocation from the Division of Industrial Relations, and a share of the fraud assessment, which is paid by most insurers authorized to transact insurance in Nevada. One other operating account is funded by an authorization from the Workers' Compensation and Safety Fund. All other operating accounts are funded by assessments and various user fees. In fiscal year 2005, DOI collected approximately $19 million in assessments, fees, fines, and taxes. Expenditures for fiscal year 2005 were about $10.4 million, which included approximately $1.7 million in intra-agency transfers.

Exhibit 1 shows fiscal year 2005 funding sources and expenditures for DOI's eight operating budget accounts.

Exhibit 1

Funding Sources and Expenditures
Operating Budget Accounts
Fiscal Year 2005

	Insurance Regulation	Insurance Examiners	Captive Insurers	Insurance Recovery	Insurance Education & Research	NAIC Fees	Insurance Cost Stabilization	Self-Insured Workers Compensation
Funding Sources:								
Appropriations	$2,904,709	$ --	$ --	$ --	$ --	$ --	$ --	$483,306
Beginning Cash	52,140	125,984	97,417	40,000	759,749	29,528	96,201	--
Assessments & Fees	1,337,119	3,082,130	151,402	608,603	--	33,250	180,324	32,399
Transfers In	1,245,071	--	--	--	658,603	--	--	--
Carry Forward	(71,269)	(111,934)	(133,992)	(40,000)	(939,584)	(29,902)	(117,829)	--
Reversions	(926)	--	--	--	--	--	--	(25,884)
Total Funding	**$5,466,844**	**$3,096,180**	**$114,827**	**$608,603**	**$478,768**	**$32,876**	**$158,696**	**$489,821**
Expenditures:								
Personnel	$3,888,163	$ --	$ 1,257	$ --	$138,039	$ --	$ 56,111	$338,922
Other	1,578,681	2,237,524	113,570	--	246,467	25,506	30,295	52,852
Intra-Agency Transfers	--	858,656	--	608,603	94,262	7,370	72,290	98,047
Total Expenditures	**$5,466,844**	**$3,096,180**	**$114,827**	**$608,603**	**$478,768**	**$32,876**	**$158,696**	**$489,821**

Source: State accounting records.

Scope and Objective

This audit is part of the ongoing program of the Legislative Auditor as authorized by the Legislative Commission, and was made pursuant to the provisions of NRS 218.737 to 218.893. The Legislative Auditor conducts audits as part of the Legislature's oversight responsibility for public programs. The purpose of legislative audits is to improve state government by providing the Legislature, state officials, and Nevada citizens with independent and reliable information about the operations of state agencies, programs, activities, and functions.

This audit included a review of the Division's financial and administrative activities for the fiscal year ended June 30, 2005, and activities through February 2006 for certain audit issues. The objective of our audit was to evaluate the Division's financial and administrative activities, including whether activities were carried out in accordance with applicable state laws, regulations, and policies.

Findings and Recommendations

The Division of Insurance (DOI) could improve its oversight of financial solvency for domestic companies. DOI did not always ensure required financial reports were submitted and reviewed timely. If problems related to financial solvency are not detected timely, there is an increased risk the insurer will become insolvent. Claims against an insolvent insurer may be paid by a guaranty fund, which is funded by assessments to licensed insurers. These assessments may be passed on to consumers in the form of higher insurance costs. In addition, accounts receivable processes need strengthening to minimize the risk accounts will not be collected. Further, controls over certain administrative functions were not adequate.

Monitoring of Required Industry Reports Could Be Improved

Better monitoring of required industry reports is needed to ensure consumer protection. DOI did not always take appropriate action to ensure certain reports were submitted and reviewed timely. Further, timeliness requirements for financial examinations were not always met. As a result, there is an increased risk financial concerns would not be detected timely.

Financial Reports for Domestic Companies Not Adequately Monitored

DOI's Corporate and Financial Affairs Section did not always take timely action for domestic companies that did not submit financial reports. Further, DOI did not review reports in a timely manner and proper approval was not always obtained for companies requesting an exemption from filing. DOI procedures applicable to required reports do not address follow-up for non-submitting companies, timely review of all significant reports, or proper approval for requested exemptions and extensions.

We tested the submittal and review of four reports that are significant to monitoring financial solvency. Our review found 14 of 20 (70%) annual statements were either not reviewed or had not been reviewed timely. Further, 9 of 17 submitted audited financial statements were either not reviewed or had not been reviewed timely. In addition, we found three instances when exemptions from filing actuarial opinions or audited financial statements were not properly approved by the Commissioner. Exhibit 2 shows a breakdown of our test results for 20 domestic companies.

Exhibit 2

Submittal and Review of Financial Reports
Domestic Companies

Type of Report	Report Was Not Submitted	Report Was Not Reviewed[3]	Report Was Not Reviewed Timely[4]	Total Exceptions
Annual Statement	0 of 20	6 of 20	8 of 20	14
Actuarial Opinion	3 of 19[1]	4 of 16	7 of 16	14
Audited Financial Statements	3 of 20	6 of 17	3 of 17	12
Management Discussion & Analysis	0 of 20	6 of 20	6 of 20	12
Total Exceptions	**6[2]**	**22**	**24**	**52**

Source: Auditor review of DOI records.

(1) For one company, an exemption was requested and properly approved.

(2) Three of these exceptions were for non-submittal, and three were for improperly approved exemptions.

(3) Not reviewed as of October 2005. Annual statements and actuarial opinions are due March 1. Audited financial statements are due June 1, or 120 days after the end of the fiscal year for certain types of entities. The Management Discussion & Analysis is due April 1.

(4) Our criterion for determining timely review was 90 days from the due date or date of receipt, whichever was later.

The objective of the National Association of Insurance Commissioner's (NAIC) accreditation program is to provide a process whereby solvency regulation of multi-state insurance companies can be enhanced and adequately monitored. Further, the NAIC requires emphasis on effective and efficient financial analysis. DOI management has stated that part of the NAIC accreditation process included a review of how effectively DOI analyzed the financial information of the state's domestic insurers.

NRS 679A.090 defines a domestic company as one formed under the laws of Nevada. According to the National Organization of Life & Health Insurance Guaranty Associations, insurance companies are regulated by the state governments of the individual states where they are licensed. It is ultimately the responsibility of those governments to monitor the solvency of domestic insurers. The Insurance Information Institute recommends state regulators monitor the financial health of insurance companies through regular in-depth financial analyses and on-site examinations.

According to the NAIC, a system of effective solvency regulation provides crucial safeguards for insurance customers. Insurance consumers benefit when the insurance industry is strong enough financially to be able to pay and settle claims in a timely manner, to provide diverse and competitively priced products, and to provide meaningful customer service. Listed below is a brief description of each report we tested. [1]

- **Annual Statements** – The annual statement is a summary of an insurer's financial operations for a particular year. The report normally includes financial statements, as well as a directors' report. The details provided in the report are of use in gaining an understanding of the company's financial position. Various statutes require submittal of annual statements for domestic companies, depending on the NRS Chapter under which the entity was formed. Per DOI procedures, reviews should be performed within 90 days of the due date. NRS 680A.270, applicable to certain domestics, states the Commissioner may refuse to continue, or may suspend or revoke, the certificate of authority of any insurer failing to file its annual statement when due.

- **Actuarial Opinion** – An actuary is an insurance professional who evaluates reserves and determines rates, rating methods, and other business and financial risks. This report is to include the opinion of a qualified actuary regarding reserves, proper computations, and compliance with applicable laws of the State. NAIC guidelines recommend analysis of this filing to be completed timely.

- **Audited Financial Statements** – Various statutes require submittal of annual audited financial statements, depending on the NRS Chapter under which the entity was formed. NRS 680A.265, applicable to certain types of domestic companies, states an insurer who does not file a report is subject to a penalty. NAIC guidelines recommend analysis of this filing to be completed within 60 to 90 days from receipt. High priority multi-state domestics should be analyzed well before the 60 to 90 day timeframe.

- **Management Discussion & Analysis (MD&A)** – The MD&A is a section of a company's annual report in which management discusses numerous aspects of the company, both past and present. The MD&A provides an overview of the previous year of operations and will usually address the upcoming year, outlining future goals. This report may also include a description of currently known facts, decisions, or conditions that are expected to have a significant effect on an entity's financial position. Further, NAIC guidelines recommend analysis of this filing to be completed within 60 to 90 days from receipt.

Process for Captive Insurers Does Not Ensure Compliance

DOI does not have a monitoring process for captive insurers that provides reasonable assurance all reports significant to financial solvency are submitted and reviewed timely. Since the legislation allowing captives was passed in 1999, Nevada

[1] See Appendix C for a schedule of sources that require the selected reports.

has licensed 62 captives. Management has stated that the Nevada captive insurance industry, while still young, has grown beyond expectations. Therefore, the need to provide adequate monitoring of this emerging market has increased.

The Insurance Journal defines a captive insurer as a form of self-insurance by which a company can insure all or part of its own or its affiliates' risks. Further, there are various types of captives.[2]

We tested the submittal and review of financial reports for 15 captive insurers. Our review found 5 of 15 annual statements were not submitted and 3 did not comply with requirements in state regulations. Nine of the 10 submitted annual statements were either not reviewed or had not been reviewed timely. Further, 8 of 15 actuarial opinions were not submitted and 2 did not comply with requirements in state regulations. Five of the seven submitted actuarial opinions were either not reviewed or had not been reviewed timely. Exhibit 3 shows a breakdown of our test results.

Exhibit 3

Submittal and Review of Financial Reports
Captive Insurers

Type of Report	Report Was Not Properly Submitted	Report Was Not Reviewed(2)	Report Was Not Reviewed Timely(3)	Total Exceptions
Annual Statement	8 of 15	6 of 10	3 of 10	17
Actuarial Opinion	10 of 15	3 of 7	2 of 7	15
Audited Financial Statements	6 of 15	4 of 9	1 of 9	11
Total Exceptions	**24(1)**	**13**	**6**	**43**

Source: Auditor review of DOI records.

(1) Four of these exceptions were for submitted statements that did not comply with requirements set forth in NAC 694C.200 or NAC 694C.210. Also, one exception was for a company that did not submit until 120 days after the deadline.

(2) Not reviewed as of October 2005. Annual statements are due March 1. Audited financial statements and actuarial opinions are due June 30.

(3) Our criterion for determining timely review was 90 days from the due date.

DOI did not always obtain required industry reports and follow-up with non-submitting captives in a timely manner. DOI procedures applicable to required reports for captives do not address timely review for all financial reports, or follow-up on non-submittals. NRS 694C.400 requires a captive insurer to submit an annual statement.

[2] See Appendix D for a list and definitions of various types of captives.

NAC 694C.210 requires a captive insurer to have an annual audit by an independent certified public accountant, and the annual audit is to include an actuarial opinion.

Further, DOI had not developed a form for the annual report of financial condition for "pure" captives due March 2005. Effective January 2000, NAC 694C.200(4) states:

> **A report of financial condition filed by a pure captive insurer pursuant to NRS 694C.400 must be verified by the oath of two executive officers of the pure captive insurer. The report must be on the form prescribed by the commissioner known as "Captive Annual Statement: Pure."**

This form would help ensure that information provided is consistent and complete, which would facilitate DOI's ability to efficiently and effectively monitor the financial condition of "pure" captives. A captive premium tax return must include a copy of its income statement. Therefore, the income statement portion of this form could help facilitate proper filing of the premium tax. Management stated in February 2006 this form had been developed and was available at the DOI website.

<u>Requirements for Examinations Were Not Always Met</u>

DOI did not always schedule examinations and issue orders accepting or rejecting examination reports as required. Further, monitoring was not performed to ensure examiners complied with state law requiring timely submittal of examination reports. Also, documentation was not maintained to explain why reports were not issued within the timeframe required by the NAIC. As a result, if reports contain deficiencies, there is an increased risk that corrective action would not begin timely. Timely detection and correction of financial concerns is crucial to safeguarding consumers.

Financial examinations are conducted in accordance with procedures and guidelines prescribed by the NAIC for the purpose of determining a company's financial condition. Our review of 16 examinations found:

- One company had an examination period of 6 years. NRS 679B.230 requires the Commissioner to examine each authorized insurer not less frequently than every 5 years. Also, NAIC guidelines require an examination of each domestic company at least once every 5 years.
- Two reports were issued 22 months and 30 months after the period under review. NAIC guidelines require examination reports to be issued within 18 months of the period under review. Exceptions to this rule are permissible if contemporaneous documentation highlights mitigating circumstances. No documents were provided to justify the reasons for the delays.

- No documents were provided to determine when any of the 16 examinations were completed. Therefore, we could not verify reports were submitted timely to the Commissioner by the examiners. NRS 679B.270 requires the examiner to make a report no later than 60 days after the completion of an examination. We inquired into the agency's interpretation of "completion of an examination" and found that DOI does not have a written policy that clearly defines the completion of an examination. As a result, DOI does not know if examiners are complying with requirements relative to timely submittal.
- For seven examinations, the order was not issued timely. These seven orders ranged from 3 weeks to 10 1/2 months late. NRS 679B.280 requires the Commissioner to fully review the report and enter an order within 30 days after the end of the period allowed for the receipt of written submissions or rebuttals.

NAIC Financial Regulation Standards require procedures for examinations to ensure the examination was conducted in an efficient and timely manner. In addition, NAIC guidelines say reports should be prepared in a timely manner as set forth in statute. Exceptions to these timing requirements should be properly documented.

Monitoring of Other Required Reports Could Be More Timely

DOI did not always monitor the timely submittal and review of other types of required reports. We found instances when reports were not reviewed as required by law, and follow-up with non-submitting entities was inconsistent among the different sections. Certain sections within DOI are responsible for monitoring various types of required reports. Implementation of consistent timeframes for taking enforcement action would improve efficiency and effectiveness.

Process for Producer Licensing Section Not Always Timely

The Producer Licensing Section does not have an adequate process for follow-up on non-submitting entities and timely review of certain required reports. We selected 25 Third Party Administrators' (TPA) annual financial reports for 2 years. From the 50 reports selected, we found 6 were not submitted and 3 were exempt from filing. For 15 of 41 submitted reports, we could not verify timely review because the review date was not documented. Of the remaining 26 reports, 25 were either not reviewed or were not reviewed as required by law. NRS 683A.08528 requires DOI to review these annual reports by September 1 of each year.

For TPA financial reports due July 1, 2005, we found no evidence of follow-up for non-submittals. For TPA financial reports due July 1, 2004, follow-up for non-submittals was not performed until 11 months past the due date. Enforcement action was taken, but not until June 2005.

Further, DOI has not issued certificates to indicate TPA's are currently licensed and in good standing. NRS 683A.08528 requires the Commissioner to issue a certificate as soon as practicable after reviewing the annual report. DOI procedures do not provide guidelines for timely issuance of certificates. Timely submittal and review of financial and other reports is critical in protecting consumers.

Process for Life & Health Section Follow-Up Could Be Improved

The Life & Health (L&H) Section has an adequate process for tracking and reviewing reports. However, the process for identifying non-submitting companies and performing follow-up action was not always timely. Procedures do not establish guidelines for timely follow-up with non-submitting companies.

For complaint reports due in 2005, identification of non-submitting companies did not occur until 4 1/2 months after the due date. Multiple statutes require the different types of L&H insurers to submit annual complaint reports. Complaint reports can help DOI staff identify insurers that have an unusually high number of complaints. This information can also be useful to examiners performing market conduct examinations.

For companies that did not submit an actuarial certification, DOI did not follow up until 7 1/2 months after the due date. NRS 689A.690 requires carriers of individual health insurance to submit an annual actuarial certification. The certification is to include a statement that the rating methods of the carrier are actuarially sound.

Workers' Compensation Section Goals Not Always Met

The Workers' Compensation Section did not always meet its goals for reviewing certain reports. Our review of 20 annual claims reports found 10 were not reviewed within the 60 day time period established in a performance measure. Untimely reviews ranged from 4 to 63 days late. Further, self-insured workers' compensation programs are required to submit audited financial statements. Staff indicated requests for extensions are fairly common. DOI procedures do not address the process for granting extensions.

Recommendations

1. Improve the process for required reports monitored by the Corporate & Financial Affairs Section. The process should include steps to help ensure all domestic companies, including captive insurers, submit financial reports by the due date and reports are reviewed timely.
2. Implement a monitoring process to help ensure all examination requirements are met, including guidance for determining completion of an examination.
3. Improve the process for required reports monitored by sections other than the Corporate & Financial Affairs Section. The process should establish timeframes for identification and follow-up for entities that do not submit required reports, and timely review of submitted reports.
4. Develop procedures for issuing certificates to all licensed Third Party Administrators in good standing.
5. Develop procedures to help ensure requested exemptions and extensions for required reports are properly approved.

Accounts Receivable Processes Need Strengthening

Accounts receivable processes need strengthening to minimize the risk accounts will not be collected. We found collection efforts for examination fees and other types of fees were not always timely. Further, certain delinquent accounts have not been considered for write-off and the list of accounts submitted to the Controller's Office for outside collection was incomplete. Improvements to these accounts receivable processes would help encourage prompt payment of fees, improve the accuracy of reports, and help ensure an all inclusive list of accounts for the outside collection agency to pursue.

DOI is responsible for monitoring payments from many sources, which are recorded into various operating and non-operating budget accounts. Therefore, the importance of adequate monitoring is significant. Exhibit 4 shows the various fees, fines, assessments, and other revenues collected by DOI during fiscal year 2005.

Exhibit 4

Collections
All Budget Accounts
Fiscal Year 2005

Budget Account Name	Fees	Fines	Assessments	Other	Totals
Insolvency	$ --	$ --	$ 447,944	$ --	$ 447,944
Self-Insured Insolvency	--	--	35,726	--	35,726
Insurance Regulation	137,915	--	1,157,678	41,526	1,337,119
Insurance Examiners	$3,082,130	--	--	--	3,082,130
Captive Insurers	112,410	--	--	38,992	151,402
Insurance Recovery	608,603	--	--	--	608,603
NAIC Fees	33,250	--	--	--	33,250
Cost Stabilization	180,324	--	--	--	180,324
Self-Insured Workers' Comp	26,399	6,000	--	--	32,399
Insurance Division Bonds	--	--	--	376,948	376,948
Insurance Division	--	576,036	--	12,129,727[(1)]	12,705,763
Totals	**$4,181,031**	**$582,036**	**$1,641,348**	**$12,587,193**	**$18,991,608**

Source: State accounting records.
[(1)] Includes approximately $11.4 million in insurance licenses.

Examination Fees Not Always Billed or Paid Timely

DOI does not have a monitoring system in place to ensure all examination fees are billed to examinees and paid timely. Our review of examination invoices found instances when DOI had paid the examiner but did not bill the examinee in a timely manner. We also found instances when DOI billed the examinee timely, but did not make adequate collection efforts to encourage timely payment.

NRS 679B.290 requires the expense of all examinations to be borne by the person examined. Further, this statute requires the person examined to pay promptly upon presentation by the Commissioner of a reasonably detailed written statement. Examinations of insurance companies are performed by contract examiners. The examiners bill DOI at different times during the examination. DOI pays the examiner when invoices are received. DOI then bills the examinee for reimbursement plus an administrative fee.

Our review of 46 invoices, from 20 examinations, found untimely billings, payments, and collection efforts.

- **Untimely Billings** – For 4 of 46 invoices tested, DOI did not bill the examinee timely. For these four instances, DOI took from 84 days to over 3 years from being billed by the examiner until billing the examinee. For two of these four instances, the examiner invoices were from 2002 and DOI did not bill the examinee until 2005. For example, DOI was billed by an examiner on May 15, 2002, and did not bill the examinee until June 7, 2005.

- **Untimely Payments and Collection Efforts** - For 14 of 46 invoices tested, DOI was not paid timely or has not been paid. We found instances when examinees did eventually make full payment, but there were no collection efforts by DOI. For example, one company paid 1 1/2 years after the date of DOI's invoice, but there was no evidence of collection efforts during this period. Further, there were five invoices that have not been paid to DOI. One company was billed by DOI on November 24, 2003. As of November 22, 2005, no payment had been made and collection letters had not been sent.

The March 2005 report to the Controller had over $700,000 in accounts receivable from examination fees, and over 68% of the receivables were over 60 days past due. A majority of this amount represented cash paid by the State that had not been reimbursed. Some of these accounts were from as far back as 2001. This may not have occurred if an adequate monitoring process were in place. The problem was identified and corrective action taken in late fiscal year 2005. DOI's June 2005 report to the Controller shows accounts receivable for examination fees totaling just over $500,000, and about 55% of the receivables were over 60 days past due.

Collection Efforts Not Always Timely or Consistent for Some Fees

Collection efforts were not always timely for various user fees. Further, collection efforts were not consistently applied by various sections responsible for different types of user fees. When certain entities do not pay their annual renewal fee timely, they are operating without a license. In addition, it is inequitable regulation to allow some companies to operate without paying all fees due the State.

The DOI section responsible for monitoring payment is determined by the type of entity that owes the fee.

- **Corporate & Financial Section** – responsible for monitoring payment of annual continuation fees due March 1, 2005. A total of 66 companies were identified by DOI as delinquent, with an amount due of $112,488. As of November 1, 2005, no collection efforts were made for these fees. This is a period of 8 months. Pursuant to NRS 680A.180, each insurance company authorized to transact insurance in Nevada is required to pay an annual continuation fee. Subsection 2 states if the continuation fee is not paid timely, an insurer's certificate of authority expires at midnight on May 31.

- **Property & Casualty Section** – responsible for monitoring payment of annual extended service contract fees. For two companies, we found no efforts were made to collect unpaid fees that were 6 to 8 months past due. NRS 690C.160 requires a provider of service contracts to submit an annual renewal application that includes payment of a $1,000 fee, prior to expiration of its current certificate. A certificate of registration is valid for 1 year.
- **Producer Licensing Section** – responsible for monitoring payment of the annual Third Party Administrator (TPA) renewal fee due July 1, 2004. DOI did not perform any collection efforts for 67 non-compliant TPA's until 11 months after the due date, in June 2005.

Our review also found collection efforts within certain sections were not consistent. For example, the Producer Licensing Section performed follow-up within 2 months after the due date for unpaid insurer appointment fees. However, follow-up for unpaid Third Party Administrator fees took 11 months from the due date.

DOI procedures for accounts receivable do not include timeframes for when internal collection efforts should be taken. Procedures issued by the Controller for accounts receivable state collection efforts should include sending a request for payment letter after 30 and 60 days. When collection efforts are not timely, there is an increased risk accounts receivable will not be collected.

Review of Delinquent Accounts Could Be Improved

DOI did not write off bad debt or submit a complete list of accounts for outside collection. Our review of DOI's schedule for accounts turned over to outside collection in February 2004 identified numerous accounts that were more than 5 years old. One account was from 1995, and nine others were from 1996 to 1999. None of these accounts have been written off as bad debt. DOI does not have policies and procedures for bad debt.

NRS 353C.220 states if an agency determines that it is impossible or impractical to collect a debt, the agency may request the State Board of Examiners to designate the debt as a bad debt. Accounting policies and procedures, issued by the Controller's Office, state accounts receivable should be valued at net realizable value, that is, the amount that will be collected on the outstanding receivables. Delinquent accounts greater than 90 days should be reviewed and considered for write-down or write-off unless otherwise specified in the statutes.

Further, we found the list of accounts turned over to the Controller for outside collection does not agree with the Legal Section's supporting schedule. The amount reported to the Controller at June 30, 2005 was understated by $1,414,000. The Legal Section's schedule is the source document for tracking overdue fines because it is responsible for attempting to collect these fines. Once the Legal Section has exhausted its efforts, it forwards these accounts to the Accounting Section for submittal to the Controller. DOI did not reconcile the schedule from the Legal Section with the list submitted to the Controller to ensure it was complete.

Recommendations

6. Implement a process to provide reasonable assurance that all examination fees are billed and collected timely.
7. Implement a monitoring process to help ensure timely collection efforts for all accounts receivable. This should include timeframes for performing internal collection efforts.
8. Develop procedures for bad debt. Procedures should establish timeframes for reviewing accounts to determine if they are collectible or subject to write-off.
9. Periodically review the list of accounts turned over for outside collection to ensure it is complete.

Weak Controls Over Some Administrative Functions

Controls over some administrative functions need to be strengthened. Weaknesses were noted in areas related to fixed assets, performance measures, complaints, deposits, and personnel. Controls in these areas are important to help ensure adequate safeguarding of assets, accurate management information, and compliance with state laws.

Poor Record Keeping and Inventory Practices for Fixed Assets

DOI does not have sound record keeping or inventory practices in place to provide adequate safeguarding of fixed assets. DOI did not perform a complete annual physical count of all assets or update the state's records as required. Further, asset tags were not attached to many items and a tracking system was not in place that documents what computer is assigned to each employee. As a result, there is an increased risk that loss or abuse could go undetected.

We could not locate 3 of 20 assets selected from DOI's inventory list, and DOI could not provide evidence of their existence. This consisted of a laptop computer, laser printer, and computer network component. For 8 of the 20 assets, DOI did not have asset tags affixed. All eight of these assets were computers. In addition, 40 new computers were received in August 2005. As of December 23, 2005, these computers still did not have tags affixed.

We observed an additional 27 assets and 9 could not be traced to inventory lists because no asset tag was affixed. Further, one item located in Carson City was on the Las Vegas inventory report. We found 3 of 12 assets in Las Vegas were inaccurately listed on the Carson City inventory report.

In addition, DOI did not always add equipment acquisitions to the inventory list. We tested four equipment purchases and found two items had not been added to the state's inventory list. One of the two transactions was the purchase of three computers. Two of the computers were on the inventory list, but one was not. Further, a $2,500 chair was purchased that meets the criteria of equipment, but was not on the list. The State Administrative Manual (SAM 1544) requires equipment purchases of $1,000 or more and computers with licensed software to be added to the state's inventory list.

NRS 333.220 requires the Chief of the Purchasing Division to establish a process for identifying and tracking the state's personal property. This process requires all agencies to conduct an annual physical inventory of their personal property and report the disposition of property to the Purchasing Division. Further, the state asset tag numbers are key information within the state's inventory system. Attaching asset tags is important to effectively identify and locate assets. Assets that do not have identification tags attached are at a greater risk of being lost or misappropriated. Accurate property records are important for maintaining accountability and preventing loss or theft.

Performance Measures Could Not Be Verified

DOI did not retain records used in computing performance measures. Therefore, we could not verify performance measures reported in the Executive Budget were reliable. SAM 2512 requires the performance measurement data in the Executive Budget to be reliable. SAM also requires agencies to retain the records used in computing performance measures for 3 fiscal years. We tested 10 performance measures and found the reliability of 9 measures could not be verified. Listed below are some examples of our review:

- DOI has a performance measure for premium taxes paid by captive insurers. We found DOI did not properly record all deposits for this tax. NRS 694C.450 requires 90% of the captive premium tax to be deposited in the General Fund, and the remaining 10% in the Captive Insurer Budget Account. We found one deposit was recorded entirely in the Captive Insurer account. As a result, deposits into the General Fund were understated by $5,353. Further, the performance measure reported in the Executive Budget was overstated by $53,466, which is an error rate of 17%.
- DOI has one measure for the percentage of life and health filings completed within 45 days of receipt and one for the percentage of rate change requests reviewed and completed within 45 days. The only documents provided to support these measures were monthly sheets with percentages. No documents could be provided to support how these percentages were calculated. Therefore, we could not verify the accuracy of the numbers used to calculate these measures. Further, the methodology used to calculate the measure is incorrect.
- Another measure we selected was percentage of property and casualty filings completed within 60 days of receipt. DOI attempted to recalculate the number reported using an Access Database report. When the Division attempted to duplicate the same report 2 days later, a different set of numbers was produced by the database. The person assigned to this measure had no explanation for the differences. Prior to our testing, we obtained the same report which contained a third set of numbers. No documents could be provided to show how the number reported in the Executive Budget was calculated. Therefore, the accuracy of the measure could not be verified.
- DOI has a measure for the percentage of fraud assessments collected. The methodology used to calculate the measure was incorrect. Documents provided showed that DOI calculated the ratio of paying companies to those assessed. Because companies are assessed different amounts, the methodology should be the ratio of dollars collected to dollars assessed. In addition, no documents could be provided to support the number reported in the Executive Budget.

Complaint Data Not Always Accurate

DOI did not always maintain complete records or enter accurate data into the complaint database. When records are inaccurate or incomplete, management may use inaccurate information when reviewing the status of complaints.

We found that 7 of 40 complaint files lacked adequate documentation to determine when or if certain work was performed. All seven were for the Carson City office. For 8 of 40 complaints, we found the opening or closing date entered into the database did not match documents in the file. Six of the eight were for the Carson City office. Although exceptions were noted for Las Vegas, the exception rate was not significant.

Controls Over Deposits Could Be Improved

Separation of duties in Carson City is not adequate for receipts. The same person enters deposit data into the state's accounting system, makes deposits, and reconciles deposits to the state's records. Standards for internal control require key duties and responsibilities to be divided or segregated among different people to reduce the risk of error or fraud. This should include separating the responsibilities for authorizing transactions, processing and recording them, reviewing the transactions, and handling any related assets. No one individual should control all key aspects of a transaction or event.

Further, deposits were not always timely. For 5 of 18 deposits tested when receipted amounts exceeded $10,000 in one day, the deposit was not made by the next working day. These deposits ranged from 1 to 2 days late. NRS 353.250(3) requires that, if on any given day the money accumulated for deposit is $10,000 or more, a deposit must be made no later than the next working day.

Personnel Requirements Were Not Always Met

DOI did not comply with personnel requirements for timely employee evaluations. For 17 of 20 employee files reviewed, evaluations were either not performed or were not performed timely.

- For four of the employees, there was no evidence all required probationary evaluations were performed.

- For 13 permanent status employees, the annual evaluations were not performed within 12 months of each other. Evaluations deemed untimely were between 1½ and 7 months late.

NRS 284.340 sets forth requirements for evaluations of probationary and permanent status employees. When evaluations are not performed when due, deficiencies in performance may not be corrected timely.

Recommendations

10. Implement controls over fixed assets that help ensure compliance with requirements for annual inventory, reconciliation to the state's inventory records, accurate record keeping, and addition of purchased equipment to the state's inventory records.
11. Develop procedures to help ensure accurate reporting of performance measures, including supervisory review and maintenance of supporting documents.
12. Review deposits for captive insurer premium taxes to ensure they are properly recorded and transfer $5,353 to the appropriate General Fund account for captive insurer premium taxes improperly recorded.
13. Improve the complaint process for Carson City. The process should include steps to help ensure database accuracy and complete records.
14. Revise procedures to include separation of duties for recording, making, and reconciling deposits. Ensure deposits comply with NRS 353.250.
15. Implement controls over personnel administration to help ensure compliance with NRS 284.340.

Appendices

Appendix A
Audit Methodology

To gain an understanding of the Division of Insurance (DOI), we interviewed agency staff and reviewed statutes, regulations, and policies and procedures significant to DOI's operations. In addition, we reviewed the agency's financial information, budgets, minutes of various legislative committees, and other information describing the activities of DOI. We documented and assessed DOI's internal controls for accounts receivable, fixed assets, revenues, expenditures, personnel, required industry reports, and performance measures.

To evaluate the process for monitoring submittal and review of required industry reports by the Corporate & Financial Affairs Section, we selected 20 domestic insurers and 15 captive insurers. We also judgmentally selected four types of reports. Judgment for selecting reports was based on statutory requirements, NAIC guidelines, and reports deemed most significant for assessing financial solvency. For each insurer selected, we documented the dates reports were submitted and reviewed. We also documented follow-up actions taken for late or non-submittal of reports.

To determine if examination requirements were met, we selected 20 domestic insurers. Judgment was based on insurers that should have been examined between January 2004 and December 2005, and at least one insurer with annual, biennial, and triennial examination requirements. For each insurer selected, we obtained the most recent examination report and determined if the insurer's examination status complied with statutory timeframes, the report was issued no more than 18 months after the "as of date," and the Commissioner issued an order within 30 days after the period allowed for written submissions or rebuttals by the examinee. We also inquired into DOI's interpretation of completion of an examination.

To evaluate the process for submittal and review of required industry reports monitored by other sections, we selected three sections, five types of reports, and a total of 65 entities. Judgment was based on reports most significant to consumer protection or financial solvency. Judgment was also based on requirements set forth in statute and regulation, and standards established by DOI in their performance measures. For each entity selected, we documented the dates reports were submitted and reviewed. We also documented follow-up actions taken for late or non-submittals.

To evaluate the monitoring of accounts receivable and internal collection efforts for examination fees, we selected 20 examinations. For each examination selected, we documented a timeline showing the dates the examiner billed DOI, the dates DOI billed the examinee, the dates DOI paid the examiner, and the dates the examinee paid DOI. If full payment was not made timely by the examinee, we documented DOI's collection efforts and monitoring of the account receivable.

To evaluate the monitoring of accounts receivable and internal collection efforts for annual fees and assessments, we selected 25 companies from DOI accounts receivable reports. Judgment was based on companies with fees due in fiscal year 2005, from three sections, and at least five companies for each section. For each selection, we documented a timeline showing key dates of collection efforts. We also requested DOI management confirm in writing that there has been no write-off for bad debt.

To evaluate compliance with laws for fixed assets, we judgmentally selected 20 assets from the state's inventory list, including at least 10 computers. For each selection, we observed if the asset existed and determined if an asset tag was affixed. We also observed an additional 15 assets, with at least 2 items from 6 sections, and a minimum of 10 computers. For each asset observed, we determined if an asset tag was affixed and if the asset was properly recorded in the state's inventory lists. We also requested DOI management confirm in writing that there has been no annual inventory and reconciliation to the state's inventory system.

To evaluate compliance with laws and regulations for expenditures, we selected 20 transactions. Selection was based on transactions recorded in the operating, equipment, and information systems categories, primarily from the operating budget account. For each equipment or computer acquisition, we determined if the purchase was properly approved, and added to the inventory report. We also selected 20 travel claims. For each selection, we determined if the travel was properly authorized, reimbursement amounts were proper, the claim was filed timely, and the employee was on state business.

To evaluate DOI's performance measures, we selected 10 measures. Judgment was based on measures deemed most significant and applicable to at least four different sections. For each measure selected, we requested and reviewed supporting documents to assess the methodology, and determined if the measures were mathematically accurate and underlying records were competent.

To determine if the complaint process is adequate, we selected 40 complaints received in fiscal year 2005, 25 complaints for the Las Vegas office and 15 for Carson City. For each complaint, we documented key dates to assess compliance with applicable statutes, policies, and procedures. We also determined whether the complaint was properly recorded in the database and files contained necessary supporting documents.

To evaluate the processing of revenues and deposits, we selected 30 payments. Selection was based on at least two payments from each month during fiscal year 2005, and at least one transaction from six different budget accounts. For each selection, we determined if the payment amount was correct and the payment was properly entered in the electronic cash receipts log. We assessed whether the corresponding deposit was timely, accurate, and properly recorded in the state's accounting system. For each deposit, we also documented who made the deposit and who performed reconciliation to the state's records. To evaluate the completeness of recorded receipts, we selected payments from 25 companies. Selection was based on payments received in Carson City and Las Vegas, with at least three types of payments applicable to two different sections. For each selection, we determined if the amount paid was properly recorded in the cash receipts log.

We selected 20 employees from the evaluation past due report in the state's Human Resources Data Warehouse to evaluate compliance with laws for personnel. Selection was based on employees from at least three sections. For each selection, we reviewed personnel files to determine if all required employee evaluations were performed timely and work performance standards were developed. We also selected 10 employees from the overtime report in the state's Human Resources Data

Warehouse for fiscal year 2005. For each selection, we determined if the employee had a written agreement to accrue compensatory time, and overtime was approved in advance.

Our audit work was conducted from June 2005 to February 2006 in accordance with generally accepted government auditing standards.

In accordance with NRS 218.821, we furnished a copy of our preliminary report to the Director of the Department of Business and Industry and the Commissioner of the Division of Insurance. On July 26, 2006, we met with agency officials to discuss the results of our audit and requested a written response to the preliminary report. That response is contained in Appendix E which begins on page 31.

Contributors to this report included:

Dennis Klenczar, CPA Deputy Legislative Auditor	David Steele, CPA Deputy Legislative Auditor
Jane Bailey Audit Supervisor	Stephen M. Wood, CPA Chief Deputy Legislative Auditor

Appendix B
Prior Audit Recommendations

Our prior audit of the Division of Insurance contained six recommendations. Two of the six were within the scope of the current audit. As part of our audit, we assessed the implementation of the two recommendations. We determined one was fully implemented and one was partially implemented. We have modified and repeated the partially implemented recommendation in this audit report, which relates to the accuracy of the consumer complaint database.

Appendix C

Sources Requiring Selected Reports

Entity Type(s)	Entity Formed Under NRS Chapter	Annual Report Required By	Actuarial Opinion Required By	Audited Financials Required By	Management Discussion & Analysis Required By
Insurance Companies (For example, Property & Casualty or Life & Health)	680A	NRS 680A.270	DOI, NAIC,[(1)] and NRS 681B.210[(2)]	NRS 680A.265	DOI & NAIC[(1)]
Insurance for Home Protection	690B	NRS 690B.150	DOI & NAIC[(1)]	DOI & NAIC[(1)]	DOI & NAIC[(1)]
Nonprofit Medical Service Organization	695B	NRS 695B.160	DOI & NAIC[(1)]	DOI & NAIC[(1)]	DOI & NAIC[(1)]
Health Maintenance Organizations	695C	NRS 695C.210	DOI & NAIC[(1)]	NRS 695C.210	DOI & NAIC[(1)]
Plans for Dental Care	695D	NRS 695D.260	DOI & NAIC[(1)]	NRS 695D.260	DOI & NAIC[(1)]
Prepaid Limited Health Service Organizations	695F	NRS 695F.320	DOI & NAIC[(1)]	NRS 695F.320	DOI & NAIC[(1)]

Sources: Nevada Revised Statutes (NRS), Division of Insurance (DOI), and the National Association of Insurance Commissioners (NAIC).

[(1)] According to DOI's website, all Nevada domestic companies must file this report. The NAIC requirement is applicable to multi-state domestics.

[(2)] NRS 681B.210 is only applicable to insurers offering life insurance.

Appendix D

List and Definitions of Various Types of Captive Insurers

Captive insurers generally can be described as insurers formed by non-insurance entities in which the entities forming the captive are the primary beneficiaries. Captives can be owned by a parent company or have multiple owners. There are a few types of captives that are difficult to characterize as either single-owner or multi-owner, such as agency and rental captives. According to American Risk Managers, a captive is an insurance company formed by any entity for the purpose of insuring its own risks and exposures to loss.

1. Captive insurer - per NRS 694C.060, any pure captive insurer, association captive insurer, agency captive insurer, and rental captive insurer licensed pursuant to this chapter.

2. Pure captive insurer – per NRS 694C.120, a captive insurer that only insures risks of its parent and affiliated companies.

3. Association captive insurer – per NRS 694C.050, a captive insurer that only insures risks of the member organizations of an association and the affiliated companies of those members, including groups formed pursuant to the Product Liability Risk Retention Act of 1981.

4. Agency captive insurer - per NRS 694C.030, a captive insurer that is owned by an insurance agency or brokerage and that only insures risks of policies which are placed by or through the agency or brokerage. According to businessforum.com, agency captives are formed by a group of insurance agents for the purpose of profiting from their clients' business. In this type of captive, the agents and promoters generally benefit financially. The clients may or may not profit from the success of the captive.

5. Rental captive insurer – per NRS 694C.140, a captive insurer formed to enter into contractual agreements with policyholders or associations to offer some or all of the benefits of a program of captive insurance and that only insures risks of such policyholders or associations. According to businessforum.com, "rent-a-captives" are insurers organized by a sponsor to benefit the sponsor and the shareholder financially. The sponsor, not the shareholder, controls the rental. The sponsor issues the policies, collects the premiums, and invests the funds until losses are paid.

Appendix E

Response From the Division of Insurance

KENNY C. GUINN
Governor

SYDNEY H. WICKLIFFE, C.P.A.
Director

STATE OF NEVADA

ALICE A. MOLASKY-ARMAN
Commissioner of Insurance

DEPARTMENT OF BUSINESS AND INDUSTRY
DIVISION OF INSURANCE
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August 16, 2006

Paul V. Townsend, CPA
Legislative Auditor
Legislative Commission
Legislative Building
Carson City, Nevada

Dear Mr. Townsend:

Enclosed and as requested, please find the agency's response to the findings and recommendations contained in the legislative audit of the Division of Insurance. The Division has accepted all 15 recommendations in full.

Thank you for the courtesy of extending the deadline for the agency's response. This is an especially busy time for us and your consideration is appreciated.

Sincerely,

Alice A. Molasky-Arman

ALICE A. MOLASKY-ARMAN
COMMISSIONER OF INSURANCE

Encl.

c. Sydney H. Wickliffe, CPA

L 5

2006 LEGISLATIVE AUDIT
AGENCY RESPONSE

Finding No. I: Monitoring of Required Industry Reports Could Be Improved

A. Financial Reports for Domestic Companies Not Adequately Monitored
B. Process for Captive Insurers Does Not Ensure Compliance
C. Requirements for Examinations Were Not Always Met
D. Monitoring of Other Required Reports Could Be More Timely

Recommendation 1. Improve the process for required reports monitored by the Corporate & Financial Affairs Section. The process should include steps to help ensure all domestic companies, including captive insurers, submit financial reports by the due date and reports are reviewed timely.

RESPONSE. Accepted.

COMMENT. The auditors identified four reports required of insurers that are significant to an evaluation of solvency (annual financial statements, actuarial opinions, audited financial statements and management discussions & analyses (MD&As)). Perhaps due to misinformation provided by division staff, the auditors concluded that all four reports are required annually of all domestic insurers. This conclusion is incorrect, and the division apologizes for any information it may have provided in error. The division will develop written procedures clearly identifying which reports are due from which insurers, when these reports are due, when review of these reports must be accomplished, and the consequences of failing to timely report or mis-reporting.

The auditors' recommendation, although perhaps too broad in its particulars, is nonetheless accurate in selective application. The Corporate & Financial Section has already embarked upon a project to identify and sanction those insurers failing to timely report. As a first step, 170 insurers have been identified for failing to renew their certificates of authority and pay appropriate renewal fees on time in 2005. These companies are in the process of being sanctioned. Compliance in this regard for 2006 will be the target of a second round of inquiry upon completion of the 2005 round.

Recommendation 2. Implement a monitoring process to help ensure all examination requirements are met, including guidance for determining completion of an examination.

RESPONSE. Accepted.

COMMENT. The Corporate & Financial Section has implemented a monitoring process to ensure all future (calendar 2006 and beyond) examination requirements are met, especially the NAIC requirement that examination reports be accepted and issued with 18 months of the period under review. All examinations for the period ending December 31, 2005 have been calendared for completion by April 30, 2007. Written procedures will be developed to document and guide this process. The procedures will identify key mileposts during examinations – including start and end dates for site work, reporting, analysis and acceptance.

Those examinations for periods ending December 31, 2004 and earlier either have been completed (i.e., reports have been submitted to and accepted by the Commissioner and an order has issued) or are in the last stages of completion. These reports are and will be untimely. The division approached the Governor in March, 2006 to ask for his support of a supplemental appropriation to add examination and analysis staff. This request resulted in two additional staff being hired in May, 2006 to assist with financial analysis with a promise to support two additional analysts to assist with examinations in October/November 2006 or, alternatively, in the division's budget request for FY 2007-09. The additional staff has enabled the division to meet NAIC standards for timely financial analysis; the additional staff to come will enable the division to meet NAIC standards for timely examinations.

Recommendation 3. Improve the process for required reports monitored by sections other than the Corporate & Financial Affairs Section. The process should establish timeframes for identification and follow-up for entities that do not submit required reports, and timely review of submitted reports.

RESPONSE. Accepted.

COMMENT. The division agrees with the recommendation. However, the bulk of required industry reports far exceeds the division's capacity for timely review and follow-up.

As a result of an audit conducted in 2003, the executive branch auditors recommended that the division "implement a system for identifying insurers failing to provide required reports." The division accepted the recommendation and implemented corrective action by developing a Required Industry Reports & Other Actions Matrix which identified every required report or event, cited the statutory or regulatory authority, described the notification mechanism, established the amount of any corresponding fee, set the date due and dates for timely follow-up, established the fine(s) for non-compliance and set the date for referral to the Legal Section for enforcement action. The matrix identified 59 annual and quarterly reports for which sections other than Corporate & Financial are responsible. The Division of Internal Audits was satisfied with the corrective action taken.

In its response to the 2003 executive branch audit, the division stated:

> *Throughout the on-site phase of this audit, the division stressed to the auditors that the life illustration project of the Life & Health Section – an enforcement activity highly regarded by the auditors – was a special project enabled only through the Budget Director's approval of paid overtime. The development of the Required Industry Reports & Other Actions Matrix has identified a significant number of events similar to the required filing of the life illustrations which could engender similar enforcement activity. The division does not have the staff resources to initiate a long series of special enforcement actions, whether overtime is authorized or not. It must be repeated that the purpose of the division is to regulate the business of insurance in Nevada, not to impose and collect fines as a source of revenue to the State. In an environment of restricted resources, the Commissioner must allocate her staff to primary regulatory activities, usually at the expense of pursuing minor technical violations. If the Governor and the Legislature want the division to pursue enforcement actions on a broader scale, significant additional resources must be committed.*

The division stands by its position from three years ago. The improved process recommended by the auditors is in place but can only be implemented on a piecemeal basis as time allows. Priority will be afforded to those industry reports that have a substantial bearing on regulation, like the Third Party Administrators' annual reports and the actuarial certifications required of individual health insurers (both noted in the audit). The division will develop written procedures requiring timely review of these reports and, to document timeliness, will require that the dates of receipt and review be documented. Due to a perpetual shortage of resources, however, the division cannot – and cannot be expected to – competently review and follow-up (i.e., take enforcement action against non-reporters) all the industry reporting required by statute.

Recommendation 4. Develop procedures for issuing certificates to all licensed Third Party Administrators in good standing.

RESPONSE. Accepted.

COMMENT. The Producer Licensing Section collects and reviews the TPA annual reports required by NRS 683A.08528. If questions arise from the review of the financial statements submitted with the annual reports, the statements are referred to the financial analysts in the Corporate & Financial Section. Annual reports are due not later than July 1. The length of time required to review the report varies with the complexity of the financial information contained. The reviews are statutorily required to be completed by September 1 and a certificate letter indicating good standing is to be issued as soon as practicable after a review has been completed. The division will develop written procedures requiring that certificate letters be issued not more than 30 days following a review.

Recommendation 5. Develop procedures to help ensure requested exemptions and extensions for required reports are properly approved.

RESPONSE. Accepted.

COMMENT. Exemptions and extensions have been occasionally granted by staff without authority. Written procedures detailing (and limiting) allowable circumstances and lines of authority will be developed.

Finding No. II: Accounts Receivable Processes Need Strengthening

A. Examination Fees Not Always Billed or Paid Timely
B. Collection Efforts Not Always Timely or Consistent for Some Fees
C. Review of Delinquent Accounts Could Be Improved

Recommendation 6. Implement a process to provide reasonable assurance that all examination fees are billed and collected timely.

RESPONSE. Accepted.

COMMENT. An examination billing is initiated by the receipt of an invoice from the contract examiner conducting the examination. The invoice is reviewed, verified and approved for payment by staff of the Corporate & Financial Section. The examiner invoice is then routed to the Accounting Section for payment. Upon receipt of an approved examiner invoice, the Accounting Section prepares a payment voucher and simultaneously prepares an invoice for reimbursement of costs which is sent to the examinee. In the past, the reimbursement invoice has occasionally been held pending completion of the examination. This was and is contrary to established procedures and the practice has been prohibited. Simultaneous reimbursement billing is now the standard. As of August 10, 2006, all costs of examinations have been billed.

Payment of reimbursement invoices has not always been prompt. Examinees disagreeing with invoiced amounts have been withholding payment until a hearing could be convened to consider their disagreements. This has been allowed in the past but will not be tolerated in the future. NRS 679B.290 requires the examinee to promptly pay the expenses of an examination upon presentation of an invoice. This provision has begun to be strictly enforced. As a result, only $94,507 (25.7%) of the receivables for examination billings are over 60 days past due as of August 4, 2006. Of this amount, almost half is attributable to one examination and this company has been referred to the Legal Section for enforcement action.

Recommendation 7. Implement a monitoring process to help ensure timely collection efforts for all accounts receivable. This should include timeframes for performing internal collection efforts.

RESPONSE. Accepted.

COMMENT. Procedures will be developed requiring monthly review of the aged receivables report with written notice to those accounts determined to be over 60 days past due. Accounts over 90 days past due will receive a second notice demanding payment. If payment is not received within 30 days of the second notice, the account will be referred to the Legal Section for enforcement action.

Recommendation 8. Develop procedures for bad debt. Procedures should establish timeframes for reviewing accounts to determine if they are collectible or subject to write-off.

RESPONSE. Accepted.

COMMENT. Because of her authority to suspend and revoke licenses, the Commissioner can exert, through enforcement actions, the very highest degree of influence over collections. Only after enforcement actions have been exhausted should any consideration be given to writing-down or writing-off a receivable as a bad debt. The enforcement process cannot be described in terms of timeframes, because due process requires the availability of administrative hearings which seldom adhere to a fixed timetable. The division will develop and implement procedures for bad debt as recommended, but the only timeframe will be "upon conclusion of the enforcement process."

Recommendation 9. Periodically review the list of accounts turned over for outside collection to ensure it is complete.

RESPONSE. Accepted

COMMENT. As described in the comment to Recommendation 8, above, accounts receivable are not written-down, written-off or referred to the Controller for collection until the division has exhausted its collection efforts through enforcement actions. At that point, the Legal Section refers the account to the Accounting Section for inclusion in Accounting's list of accounts referred for collection. A disconnect has occurred because, on occasion, an enforcement action is instituted against multiple parties who are jointly and severally liable for the debt, yet when the account(s) are referred to Accounting, this distinction has not been made clear. For example, a fine may be levied against Smith and Jones in the amount of $1,000 total. When the referral is made to Accounting, the debt is listed as $1,000 owed by Smith and $1,000 owed by Jones. To clarify all accounts, the Legal and Accounting Sections will reconcile all entries through June 30, 2006. Thereafter, the Sections will reconcile accounts on a quarterly and annual basis. Procedures will be written to describe this process and assign responsibilities.

Finding No. III: Weak Controls Over Some Administrative Functions

- **A. Poor Record Keeping and Inventory Practices for Fixed Assets**
- **B. Performance Measures Could Not Be Verified**
- **C. Complaint Process for Carson City Could Be Strengthened**
- **D. Controls Over Deposits Could Be Improved**
- **E. Personnel Requirements Were Not Always Met**

Recommendation 10. Implement controls over fixed assets that help ensure compliance with requirements for annual inventory, reconciliation to the state's inventory records, accurate record keeping, and addition of purchased equipment to the state's inventory records.

RESPONSE. Accepted.

COMMENT. The division has adequate written procedures for fixed asset control in place. Staff shortages and competing priorities have resulted in the division's failure to implement and enforce existing procedures. The division acknowledges the importance of accounting for all state resources and has initiated a thorough physical inventory of all fixed assets and reconciliation of the division's records with those maintained by the state. Asset tags will be affixed to all appropriate equipment. Thereafter, annual physical inventories will be conducted every January as prescribed.

Recommendation 11. Develop procedures to help ensure adequate reporting of performance measures, including supervisory review and maintenance of supporting documents.

RESPONSE. Accepted.

COMMENT. The Management Analyst position responsible for collecting performance measurement data, vacant since April 14, 2006, was filled on July 24, 2006. During orientation, this new employee was briefed on his responsibility to ensure that all sections reporting performance measurement data have written procedures governing the collection and reporting of this data. Procedures to be developed will require supervisory review and approval of all reports and maintenance of supporting documents.

Recommendation 12. Review deposits for captive insurer premium taxes to ensure they are properly recorded and transfer $5,353 to the appropriate General Fund account for captive premium taxes improperly recorded.

RESPONSE. Accepted.

COMMENT. Captive premium taxes are collected by the division and, upon deposit, are split between the division's captive insurer account (B/A 3818) and the General Fund in accordance with a percentage established in NRS 694C.450. The auditors identified one instance, on April 26, 2004, in which the entire premium tax paid by Contractors Liability Insurance Company RRG - $5,948.20 – was deposited to the captive insurer account rather than splitting the deposit between the captive account ($595) and the General Fund ($5,353). A request to process a transfer of $5,353 via JVD 741 10000036784 from B/A 3818 to the General Fund as a stale claim was prepared on August 3, 2006.

A review of all captive premium taxes paid since the authorization of captives in 1999 has been initiated. Procedures requiring discrete reporting of premium tax collections and deposits will be developed and implemented prior to March 1, 2007 when the next tax year's reports and payments are due.

Recommendation 13. Improve the complaint process for Carson City. The process should include steps to help ensure database accuracy and complete records.

RESPONSE. Accepted.

COMMENT. The procedures for complaint handling in Carson City and Las Vegas are identical. The differences noted by the auditors which have led to disparate performance is attributable to process and resources. While the process in Carson City is contained within the three-person section (with monthly caseload review by the Chief Insurance Assistant), the process in Las Vegas includes a dedicated data entry point and intervention by the Deputy

Commissioner at closure. The additional resources in Las Vegas account for that office's superior performance. While the additional resources are not available in Carson City, there are opportunities to improve the process. Procedures will be written to require additional case documentation, probably through the enhanced utilization of case notes, at both opening and closure. The procedures will require a review of the electronic record at closure, which will present the opportunity to identify and correct errors.

Recommendation 14. Revise procedures to include separation of duties for recording, making, and reconciling deposits. Ensure deposits comply with NRS 353.250.

RESPONSE. Accepted.

COMMENT. Existing practice requires the Administrative Aid (pcn 3813-0341) to collect all checks and cash from the daily mail, stamp the checks for deposit and prepare the deposit log. The Accountant Technician I (pcn 3813-0037) verifies the information on the deposit log, prepares the deposit and makes the daily deposit at the Bank of America. The Accountant Technician III (pcn 3813-0064) reconciles each deposit to the Budget Status Reports. A secondary reconciliation of deposits is done by the Administrative Assistants in the substantive sections, who match deposits with the payers and confirm amounts paid equal amounts due. Procedures governing this process will be reviewed and amended as appropriate.

The division is aware of the timing requirements of NRS 353.250 and makes every effort to comply. Rare is the day that deposits do not exceed $10,000, so daily deposits are the norm. As is common in smaller agencies, employee absences stress the capacity to comply and redundant systems are unreliable. During the period of review, the Accountant Technician I was absent on maternity leave for three months and occasional instances of noncompliance did occur. With the addition of accounting/administrative positions authorized by the 2005 Legislature and requested of the 2007 session, redundant systems have and will become more reliable and compliance will be without exception.

Recommendation 15. Implement controls over personnel administration to help ensure compliance with NRS 284.340.

RESPONSE. Accepted.

COMMENT. NRS 284.340 requires the appointing authority to file timely reports on the performance of his classified employees. The auditors correctly identified several instances in which such reports were delinquent. The division has implemented controls over personnel administration to ensure compliance. As of August 10, 2006, work performance appraisals have been completed for all but one classified division employee. The exception involves a disagreement between supervisor and subordinate. An informal resolution of the disagreement is being sought; failing that, the formal appeals process will be initiated, further delaying the timely appraisal.

Division of Insurance
Response to Audit Recommendations

Recommendation Number		Accepted	Rejected
1	Improve the process for required reports monitored by the Corporate & Financial Affairs Section. The process should include steps to help ensure all domestic companies, including captive insurers, submit financial reports by the due date and reports are reviewed timely	X	
2	Implement a monitoring process to help ensure all examination requirements are met, including guidance for determining completion of an examination	X	
3	Improve the process for required reports monitored by sections other than the Corporate & Financial Affairs Section. The process should establish timeframes for identification and follow-up for entities that do not submit required reports, and timely review of submitted reports..	X	
4	Develop procedures for issuing certificates to all licensed Third Party Administrators in good standing	X	
5	Develop procedures to help ensure requested exemptions and extensions for required reports are properly approved	X	
6	Implement a process to provide reasonable assurance that all examination fees are billed and collected timely	X	
7	Implement a monitoring process to help ensure timely collection efforts for all accounts receivable. This should include timeframes for performing internal collection efforts	X	
8	Develop procedures for bad debt. Procedures should establish timeframes for reviewing accounts to determine if they are collectible or subject to write-off .	X	
9	Periodically review the list of accounts turned over for outside collection to ensure it is complete	X	
10	Implement controls over fixed assets that help ensure compliance with requirements for annual inventory, reconciliation to the state's inventory records, accurate record keeping, and addition of purchased equipment to the state's inventory records	X	

Division of Insurance
Response to Audit Recommendations
(continued)

Recommendation Number		Accepted	Rejected
11	Develop procedures to help ensure accurate reporting of performance measures, including supervisory review and maintenance of supporting documents	X	
12	Review deposits for captive insurer premium taxes to ensure they are properly recorded and transfer $5,353 to the appropriate General Fund account for captive insurer premium taxes improperly recorded	X	
13	Improve the complaint process for Carson City. The process should include steps to help ensure database accuracy and complete records	X	
14	Revise procedures to include separation of duties for recording, making, and reconciling deposits. Ensure deposits comply with NRS 353.250	X	
15	Implement controls over personnel administration to help ensure compliance with NRS 284.340	X	
	TOTALS	15	0