

**NEW MEXICO OFFICE OF THE  
SUPERINTENDENT OF INSURANCE**

**SPECIAL AUDIT OF NEW MEXICO PREMIUM TAX FILINGS**

**FOR THE PERIOD JANUARY 1, 2003 THROUGH DECEMBER 31, 2016**

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A STERLING APPROACH.

TO FINDING SOLUTIONS.  
TOGETHER.



Mr. John G. Franchini, New Mexico Superintendent of Insurance  
and Mr. Timothy Keller, New Mexico State Auditor  
Santa Fe, New Mexico

We performed research and a review of the premium tax processes of the Financial Audit Bureau of the New Mexico Office of Superintendent of Insurance. In addition, we performed a recalculation of the premium tax liabilities, payments received and resulting net over- or under-payments for each year between 2003 and 2016 for select insurance companies. The attached Summary of Procedures Performed and Summary of Findings provide the results of these procedures.

The consulting procedures under this engagement do not constitute an examination, investigation, or an audit made in accordance with U.S. generally accepted auditing standards, the objective of which would be the expression of an opinion on the items outlined in the attached supplement or on the financial statements of the Company taken as a whole. Our responsibility under this engagement was not to detect fraud. Accordingly, we do not express such an opinion or give any other form of assurance. We performed our engagement under the AICPA Statement on Standards for Consulting Services, the Audit Act (NMSA 1978, Sections 12-6-1 et seq.) and the Audit Rule (NMAC 2.2.2.1 et seq.).

This report is intended solely for the information, use and reliance by any agency of the State of New Mexico and is not intended to be and should not be used by anyone other than these specified parties.

We wish to take this opportunity to express our sincere appreciation for all the courtesies and cooperation extended to us by the management and staff and thank you for the opportunity to be of service.

*Examination Resources, LLC*

**Examination Resources, LLC**  
Atlanta Georgia  
September 30, 2017

## **EXECUTIVE SUMMARY**

The New Mexico Office of Superintendent of Insurance (OSI) became its own governmental entity on July 1, 2013. Prior to this date, it was the Insurance Division within the New Mexico Public Regulation Commission (PRC). Since 2003, premium tax collection has been under the authority of the PRC, OSI and three different Superintendents of Insurance. In 2014, the Legislature made a special appropriation to OSI to conduct an audit of the agency's premium tax collection processes. In 2015, the Legislature required the premium tax audit to be overseen by the New Mexico Office of the State Auditor (OSA). The audit, which covered the period from 2010 through 2015, was limited in scope and relied on data and documentation provided and maintained by OSI. The independent auditors performing the engagement did not have access to insurance company records, however, the report did identify serious weaknesses in OSI's processes that may have resulted in significant tax underpayments. The report was released on September 20, 2016.

Based on the concerns highlighted in the initial report and the need to hire specialized insurance industry auditors to conduct a more in-depth analysis, on November 30, 2016 the State Auditor designated the OSI for a special audit of premium taxes. Pursuant to NMSA 1978, Section 12-6-3(C) (Audit Act) the State Auditor "may cause the financial affairs and transactions of an agency to be audited in whole or in part." Additionally, in accordance with 2.2.2.15 NMAC (Audit Rule), the State Auditor may initiate a special audit regarding the financial affairs and transactions of an agency or local public body based on information it receives. Due to the significant issues raised in the first audit, OSA worked with OSI, the New Mexico Legislative Finance Committee (LFC), and the New Mexico Department of Finance and Administration (DFA) in developing the scope and timeline for completion of the special audit.

On May 2, 2017, the OSI entered into an agreement with Examination Resources, LLC (ER) to provide audit consulting services in accordance with the American Institute of Certified Public Accountants Statement on Standards for Consulting Services. Additionally, on April 12, 2017, OSI entered into a Memorandum of Understanding (MOU) with the OSA to provide professional services to supervise the special audit of premium tax collections.

The objective of the special audit was to independently develop defensible procedures for calculating historic premium tax liability that could be used in assessments for any past shortfalls in payment, and to apply those procedures to a recalculation of premium tax liability for a defined population of taxpayers. An additional objective of the special audit was to develop a detailed

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audit program for the insurance lines evaluated with step-by-step instructions on how to conduct future audits for use by OSI staff.

The scope of the special audit was from 2003 to 2016. A total of 30 insurers were selected for review consisting of twelve health insurers, nine life insurers and nine property and casualty insurers. During the audit period, the 30 insurers selected had a collective market share of approximately 84% of the New Mexico Life and Health and Property and Casualty insurance markets combined. The criteria for the sample population was agreed to by all involved parties. ER obtained and reviewed all premium tax related statutes, along with any amendments enacted during the audit period, and held discussions with legal counsel, the OSI, and the OSA to assist with determining the appropriate application of each statute.

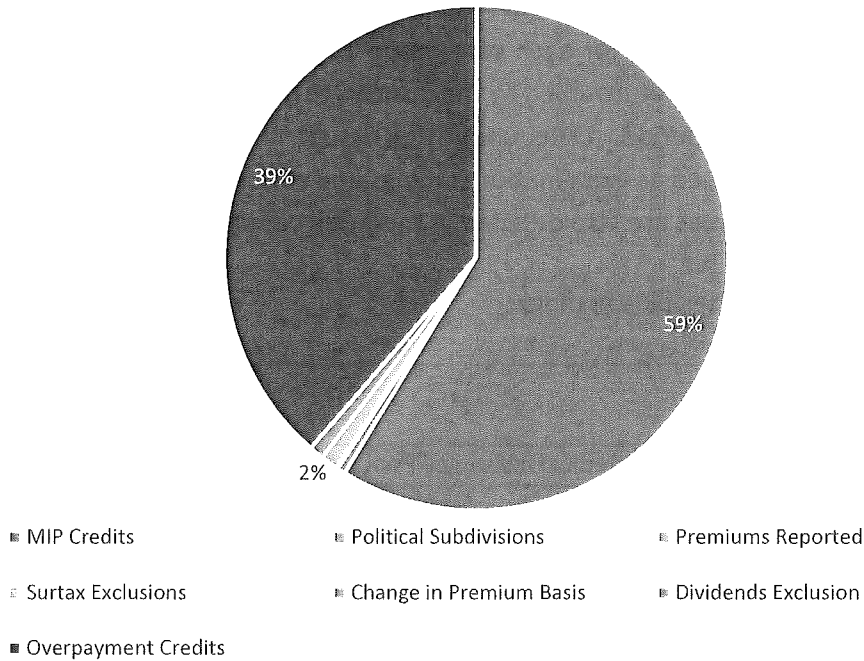
Parallel to this audit, the OSI called Limited Scope Examinations of the 30 insurers selected for review in order to verify whether the insurers were properly calculating and remitting premium tax and health insurance premium surtax. During each examination, ER reviewed all components of the insurers' premium tax filings for each year, taking into consideration any changes that may have occurred in statutes and any official bulletins, other directives or form instructions issued by the OSI, or by the Insurance Division of the PRC. ER recalculated the premium tax and health insurance premium surtax amounts for each year based upon its interpretation of the statutes and compared the results to the returns filed by the insurers to determine any net over- or under-payments during the audit period. The underlying issues that resulted in the identified discrepancies were documented as examination findings and communicated to the insurers and the OSI. These underlying issues are also detailed in this audit report.

The following table summarizes ER's findings:

<b>Finding #</b>	<b>Description</b>	<b>Net Tax Effect Over/(Under) Payment</b>
2017-001	Improper Application of Medical Insurance Pool (MIP) Credits	\$(37,993,243)
2017-002	Erroneous Political Subdivisions	(317,576)
2017-003	Discrepancies in Premiums Reported	(79,674)
2017-004	Improper Surtax Exclusions	(710,001)
2017-005	Errors Switching from Premiums Received to Direct Written Premium Basis	(596,478)
2017-006	Improper Exclusion of the Dividends to Policyholders Deduction by the OSI	47,699
2017-007	Erroneously Applied Overpayment Credits	(24,957,746)
	<b>Total Net Tax Effects</b>	<b>\$(64,607,018)</b>

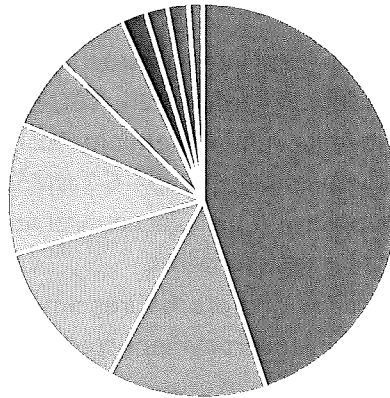
Net differences directly related to the findings noted above totaled \$171,890,861 which resulted in a net underpayment tax effect of \$64,607,018. Of the 30 companies reviewed, 17 companies were found to have underpayments. Penalties and interest, related to either annual or quarterly underpayments, have not been considered as part of this special audit. While the special audit provides what it believes to be the premium tax underpayments, it is incumbent upon the OSI to issue the necessary underpayment assessments to the insurers as well as allow the insurers the opportunity to assert their rights/defenses as part of the examination process. Any applicable penalty and interest charges related to these findings should be considered for assessment by the OSI pursuant to the New Mexico Insurance Code. The charts below illustrate each findings' percentage of the total underpayment as well as each companies' percentage of the total underpayment:

Premium Tax Underpayment by Finding



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### Premium Tax Underpayment by Company



■ Company M                      ■ Company F                      ■ Company L                      ■ Company C  
■ Company R                      ■ Company J                      ■ Company E                      ■ Company N  
■ Company K                      ■ All Other Companies

In response to the findings, ER recommends the OSI take the following actions:

- The OSI should ensure insurance companies are utilizing Medical Insurance Pool (MIP) credits in compliance with 59A-54-10 NMSA 1978 and in accordance with Bulletin No. 2015-14 and Bulletin No. 2015-027. The total potential MIP credit should be compared with the actual amount taken by all taxpayers to ensure total amount taken does not exceed the total amount of the available credit. The OSI should also consider examining additional premium tax filings to ensure MIP credits were properly applied and not utilized in more than one tax year.
- The OSI should actively ensure insurance companies are taking deductions for political subdivisions in accordance with 59A-6-2 NMSA 1978. This verification should take place as part of the Financial Audit Bureau's (FAB) premium processing and audit procedures.
- The OSI should ensure insurance companies are reporting annual premiums from policies within the State of New Mexico that agree to the New Mexico State Business Page and/or Schedule T of the annual statement filed with the OSI. This verification should take place as part of the FAB's premium processing and audit procedures.
- The OSI should ensure insurance companies are reporting premiums subject to surtax in accordance with 59A-6-2 NMSA 1978. The premium tax forms should be re-designed to include a formal attachment to provide a detailed listing of the surtax exemptions claimed. Surtax exemption verification should take place as part of the FAB's premium processing and audit procedures.

- The OSI should consider reviewing additional premium tax filings to ensure applicable insurance companies properly accounted for the change from a premium received to a direct written premium basis.
- Premium tax forms and their associated instructions should be designed to facilitate accurate tax filings. The OSI should immediately reestablish the column for dividends paid or credited to policyholders in its annual Premium Tax Return so that insurers may again deduct these amounts in compliance with 59A-6-2 NMSA 1978. Premium tax filing forms and instructions should be reviewed by legal counsel and revised as needed to correctly accommodate all tax reporting requirements.
- The OSI should establish policies and procedures among all affected Bureaus to ensure insurance companies are utilizing overpayment credits in accordance with 59A-6-5 NMSA 1978. Before issuing refunds for overpayments, overpayment balances should be reviewed, verified and approved prior to disbursing the funds. This verification should take place as part of the FAB's premium processing and audit procedures.

The OSI provided responses to each audit finding. The responses are included in the Summary of Findings.

#### **SCOPE AND PROCEDURES PERFORMED**

The OSI, in coordination with the OSA, engaged ER to perform certain procedures to independently develop defensible procedures for calculating historic premium tax liability that could be used in assessments for any past shortfalls in payment, and to apply those procedures to a recalculation of premium tax liability for a defined population of taxpayers. The required procedures performed as part of this Special Audit included the following:

- A. Develop methodology for recalculating premium tax liability, payments received, and resulting net over- or under-payments (if any) for each year between 2003 and 2016;
- B. Obtain written approval of OSI and OSA on the recommended methodology for recalculating premium taxes;
- C. Recalculate premium tax liability, payments received, and resulting net over- or under-payments (if any) for selected insurance companies for each year from 2003 to 2016 for the purpose of making demand for any under-payments or refunding any over-payments;
- D. Prepare a detailed report on procedures applied and conclusions.

The population criteria for insurer selection was based upon insurers with a calculated premium tax liability of \$1 million or more for any year during the period 2003 through 2016 before



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considering exempt lines of business or credits received from the MIP and New Mexico Health Insurance Alliance (NMHIA).

ER obtained New Mexico direct written premium data for Health, Life, Property and Casualty, Fraternal and Title companies for the years 2003 through 2016 from S&P Global Market Intelligence, a division of S&P Global. A total of 72 insurance companies met the population criteria. This population was comprised of 12 health insurance companies, 35 life insurance companies and 25 property and casualty insurance companies.

From this population, 30 total insurance companies were selected for review consisting of all 12 health companies in the population, the top nine life companies and top nine property and casualty companies based on total direct written premium in the State of New Mexico during the audit period. Below is a table that breaks out total market share coverage by insurance type and total combined coverage:

Type of Insurance	Market Share of Companies Reviewed
Health	98.7%
Life	61.9%
Property and Casualty	64.6%
Total Combined Coverage	84.3%

ER obtained all New Mexico premium tax related statutes along with any amendments enacted during the audit period. As part of the premium tax audit, ER reviewed all applicable statutes and held discussions with internal legal counsel and the OSI to assist with determining the appropriate application of each statute. ER identified the following statutes that were applicable to New Mexico's Premium Tax and Surtax filings and payments:

- 52-6-13 NMSA 1978 – Premium Tax Workers' Compensation Group Self-Insured's;
- 59A-5-29 NMSA 1978 – Authorization of Insurers and General Requirements Annual Statement;
- 59A-5-29.1 NMSA 1978 – Authorization of Insurers and General Requirements Quarterly Statements;
- 59A-6-1 NMSA 1978 – Fees and Taxes Fee Schedule;
- 59A-6-2 NMSA 1978 – Premium Tax; health insurance premium surtax
- 59A-6-3 NMSA 1978 – Insurer Must Pay Tax on Withdrawal from State;
- 59A-6-4 NMSA 1978 – Penalty for Failure to Report or Pay Tax or Fees;

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- 59A-6-5 NMSA 1978 – Distribution of Division Collections;
- 59A-15-4 NMSA 1978 – Unauthorized Insurers; Insurance Independently Procured Duty to Report and Pay Tax;
- 59A-16C-14 NMSA 1978 – Insurance Fraud Act, Insurance Fraud Fund Created;
- 59A-40-5 NMSA 1978 – Mexican Casualty Insurers Fees Taxes and Reports;
- 59A-44-24 NMSA 1978- Taxation of Fraternal Benefit Societies;
- 59A-54-10 NMSA 1978 – Medical Insurance Pool (MIP) Assessments;
- 59A-55-6 NMSA 1978 - Taxation of Risk Retention Groups;
- 59A-55-15 NMSA 1978 – Penalties;
- 59A-55-21 NMSA 1978 – Purchasing Group Taxation;
- 59A-55-23 NMSA 1978 – Penalties;
- 59A-56-11 NMSA 1978 – Assessments; and
- 42 US Code Section 1395 mm(g) – Risk Sharing Contract

Parallel to this audit, the OSI called Limited Scope Examinations of the 30 insurers selected as part of this audit to verify whether the insurers were properly calculating and remitting annual premium tax and health insurance premium surtax. The examinations did not assess whether the companies were underpaying quarterly estimates, and thus did not determine any penalties related to quarterly underpayments.

During each examination, ER reviewed all components of the premium tax filing form for each year, taking into consideration any changes that may have occurred in statutes and any bulletins, directives or form instructions issued. ER recalculated the premium tax and surtax amounts for each year based upon its interpretation of the statutes and compared the results to the returns filed by the companies to determine any net over- or under-payments for each year between 2003 and 2016.

At the conclusion of each examination, it is anticipated that OSI will issue Reports of Examination to the companies, in accordance with the New Mexico Insurance Code.

### **LEGAL INTERPRETATIONS**

ER performed the necessary research and worked with the OSI and internal counsel to gain an understanding of the New Mexico Statutes and Bulletins issued relating to insurance premium tax and health insurance premium surtax. The timing and effective date of any statute, statute amendment, or bulletin was carefully considered when applying an interpretation to the

recalculations performed. Key interpretations based on ER's research of the Statutes and Bulletins are identified below.

### **Statutes**

**Section 59A-6-2 NMSA 1978 Premium Tax; Health Insurance Premium Surtax:** Statute 59A-6-2 states that each insurer authorized to transact insurance in New Mexico and each insurer formerly authorized to transact insurance in New Mexico and receiving premiums on policies remaining in force in New Mexico are subject to a premium tax of 3.003%. Also subject to the tax are plans operating under provisions Chapter 59A, Articles 46-49 NMSA 1978, each property bondsman, and each unauthorized insurer that has assumed a contract or policy of insurance directly or indirectly from an authorized or formerly authorized insurer and is receiving premiums on such policies remaining in force in New Mexico. The tax is based on 3.003% of gross premiums as reported on Schedule T of the insurer's annual financial statements less all return premiums including dividends paid or credited to policyholders or contract holders and premiums received for reinsurance on New Mexico risks.

In addition to the premium tax, each insurer shall pay a health insurance premium surtax of one percent of the gross health insurance premiums and membership and policy fees received by it on hospital and medical expense incurred insurance or contracts; nonprofit health care service plan contracts, excluding non-profit dental or vision only contracts; and health maintenance organization subscriber contracts covering health risks within this state during the preceding calendar year, less all return health insurance premiums, including dividends paid or credited to policyholders or contract holders and health insurance premiums received for reinsurance on New Mexico risks.

For each calendar quarter, an estimated payment of the premium tax and the health insurance premium surtax shall be made on April 15, July 15, October 15 and the following January 15. The estimated payments shall be equal to at least one-fourth of the payment made during the previous calendar year or one-fifth of the actual payment due for the current calendar year, whichever is greater. The final adjustment for payments due for the prior year shall be made with the return, which shall be filed on April 15 of each year, at which time all taxes for that year are due.

Dividends paid or credited to policyholders or contract holders and refunds, savings, savings coupons and similar returns or credits applied or credited to payment of premiums for existing, new or additional insurance shall, in the amount so used, constitute premiums subject to tax under this section for the year in which so applied or credited. Premiums attributable to insurance or contracts purchased by the state or a political subdivision for the state's or political

subdivision's active or retired employees; and payments received by a health maintenance organization from the federal secretary of health and human services pursuant to a contract issued under the provisions of 42 U.S.C. 1395 mm(g) are exempt from the premium and surtax.

**Section 59A-6-5 NMSA 1978 Distribution of Division Collections:** The OSI is required to make daily deposits to the state treasurer for fees, licenses, penalties and taxes received, unless an exception applies and properly distribute monies received. Payments received are to be credited to the "insurance department suspense fund" (This fund is referred to in the financial statements as Insurance Suspense Fund (11820)); except as provided by The Law Enforcement Protection Fund Act (LEPFA) (Chapter 29, Article 13, NMSA 1978) and 59A-6-1.1. LEPFA reserves 10% of all money received for fees, licenses, penalties, and taxes from life, general casualty, and title insurance business for the law enforcement protection fund. The 10% reserve is to be paid on a monthly basis and credited to the law enforcement protection fund. However, the 10% calculation does not include money received from the health insurance premium surtax imposed by (C).

The superintendent may authorize refund of money erroneously paid as fees, licenses, penalties or taxes from the insurance department suspense fund under request for refund made within three years after the erroneous payment. In the case of premium taxes erroneously paid or overpaid in accordance with law, refund may also be requested as a credit against premium taxes due in annual or quarterly tax returns filed within three years of the erroneous or excess payment. To receive a refund for erroneous payment, a claim must be made within three years after the erroneous payment. Refund may be made as a credit against premium taxes. A credit is determined when a company submits its annual return, not an estimated quarterly premium tax report. As a result, a credit for any given year is generated when the annual return is filed, typically in April of the following year, and the deadline to apply the credit is three years from when it is generated.

Subsection C states the superintendent shall authorize the allocation of premiums collected pursuant to 59A-14-12 NMSA 1978 to other states that have joined the compact pursuant to an allocation formula agreed upon by the compacting states. See NMSA 1978 § 29-13-3.

The "insurance operations fund" is created in the state treasury. The fund consists of balances derived from fees imposed by subsections A and E of 59A-6-1. The legislature annually appropriates from the fund to the division those amounts necessary for the division to carry out its responsibilities pursuant to the Insurance Code and other laws. Any balance in the fund at the end of a fiscal year greater than one-half of that fiscal year's appropriation shall revert to the General Fund.

At the end of every month, OSI is required to distribute net collections (after refunds and amounts distributed to the LEPF) as follows: Balances derived from property and vehicle insurance business shall be distributed to the fire protection fund, balances derived from fees imposed by subsections A and E of 59A-6-1 to the insurance operations fund, and the remaining balances derived from other sources to the General Fund.

**Section 59A-6-4 NMSA 1978 Penalty for Failure to Report or Pay Tax or Fees:** This statute explains that every insurer, nonprofit health care plan, health maintenance organization, prepaid dental plan or prearranged funeral plan doing business in New Mexico that fails to file when any report for taxation, regardless of whether tax is due, is liable to the state the amount thereof and a \$1,000 penalty for each month after due and after OSI has made a demand for the penalty. Penalty will also be assessed if the report was filed, but no payment was rendered.

**Section 59A-54-10 NMSA 1978 Medical Insurance Pool Assessments:** After the close of the fiscal year, the medical insurance pool administrator shall determine the net premium, which is premiums less administrative expense allowances, the pool expenses and claim expense losses for the year, taking into account investment income and other appropriate gains and losses. The assessment for each insurer shall be determined by multiplying the total cost of pool operation by a fraction, the numerator of which equals that insurer's premium and subscriber contract charges or their equivalent for health insurance written in the state during the preceding calendar year and the denominator of which equals the total of all premiums and subscriber contract charges written in the state; provided that premium income shall include receipts of Medicaid managed care premiums but shall not include any payments by the secretary of health and human services pursuant to a contract issued under Section 1876 of the Social Security Act, as amended.

The assessment for each insurer is calculated using the following formula: Total cost of pool operation is multiplied by (insurer's premium and subscriber contract charges during the preceding calendar year / total of all premiums and subscriber contract charges written in the state). In the event assessments exceed actual losses and administrative expenses of the pool, the excess is to be held at interest and used by the board to offset future losses or reduce pool premiums. The OSI is to apply a credit to the premium tax returns of each MIP member after the MIP member is assessed by the MIP board. All pool members are to receive a 50% or 75% credit on their premium tax return. A 75% credit is applied to pool members receiving premiums—in whole or in part—through the Ryan White CARE Act, or the Ted R. Montoya Hemophilia Program,

the Children's Medical Services Bureau of the Department of Health, or other program receiving state funding.

**Section 59A-56-11 NMSA 1978 Health Insurance Alliance Assessments:** This statute, which was repealed in 2014, stated that after the end of each year, the Health Insurance Alliance (HIA) assessed its members, which included all insurers authorized to transact insurance in New Mexico, for the net reinsurance loss in the previous calendar year and for the net administrative loss that occurred in the previous calendar year, taking into account investment income for the period and other appropriate gains and losses. The assessment for each member was determined by multiplying the total losses of the HIA's operation by a fraction, the numerator of which was an amount equal to that member's total premiums, or the equivalent, exclusive of premiums received by the member for an approved health plan for health insurance written in the state during the preceding calendar year and the denominator of which equaled the total premiums of all health insurance written in the state during the preceding calendar year exclusive of premiums for approved health plans; provided that total premiums shall not include payments by the secretary of human services pursuant to a contract issued under Section 1876 of the federal Social Security Act, total premiums exempted by the federal Employee Retirement Income Security Act of 1974 or federal government programs.

By April 15 of each year, each member offering an approved health plan submitted a listing of all incurred claims for the previous year; and by April 15 of each year, each member submitted a report that included the total earned premiums received during the prior year less the total earned premiums exempted by federal government programs. The HIA notified each member of the amount of its assessment due by May 15 of each year. The assessment was due to be paid by the member by June 15 of each year. The proportion of participation of each member was determined annually by the HIA board, based on annual statements filed by each member and other reports deemed necessary by the HIA board. Any deficit incurred by the HIA was recouped by assessments apportioned among the members; provided that fifty percent of the assessment paid for any member was allowed as a credit on the member's following annual premium tax return.

The HIA board could defer, in whole or in part, the payment of an assessment of a member if, in the opinion of the board, after approval of the Superintendent, payment of the assessment would endanger the ability of the member to fulfill its contractual obligations. In the event payment of an assessment against a member was deferred, the amount deferred could be assessed against the other members. The member receiving the deferment could pay the assessment in full plus interest at the prevailing rate as determined by regulation of the

Superintendent within four years from the date payment was deferred. After four years but within five years of the date of the deferment, the HIA board could have sued to recover the amount of the deferred payment plus interest and costs. Board actions to recover deferred payments brought after five years of the date of deferment were barred. Any amount received would have been deducted from future assessments or reimbursed pro rata to the members paying the deferred assessment.

All statutes relating to the Health Insurance Alliance were repealed in 2014.

**42 U.S.C. 1395 mm(g) Risk Sharing Contract:** This US Code statute defines a risk sharing contract, what payments are made under such contracts, and the special benefits allowed under these contracts. This is the statute that is mentioned in NM Statute 59A-6-2(E) as payments allowed to be exempt from premium tax.

### **Bulletins**

Bulletins are formal guidance or other directives issued by the Superintendent. Under the scope of this audit the bulletins listed below were either issued under the authority of the PRC or the OSI.

**Bulletin 2014-010 The issue of Rounding Premium Tax Calculations:** This bulletin states that beginning July 1, 2014, payments of premium tax will be rounded to the nearest hundredth.

**Bulletin 2015-02 Procedures for Filing and Penalty Notice and Demand for Failure to Report or Pay Premium Taxes and Fees as Required by NMSA 1978, Section 59A-6-4:** Effective January 12, 2015, quarterly premium tax returns and payments must be postmarked or received by April 15<sup>th</sup>, July 15<sup>th</sup>, October 15<sup>th</sup>, and January 15<sup>th</sup> and the final annual return by April 15<sup>th</sup> of the preceding year. Late payments and filings will render the filer liable for penalties as stated in NMSA 1978, Section 59A-6-4. Incomplete or inaccurate returns resulting in underpayment when originally filed are also subject to the above-mentioned penalties. Entities that fail to file or pay when due, are liable for a penalty of \$1,000 for each month or part thereof after demand has been made. OSI shall issue demand notice by email, telephone, or US mail and penalties will be imposed prospectively from the date of demand.

**Bulletin 2015-14 Application of Medical Insurance Pool (MIP) Credits to Premium Tax Liability, NMSA 1978, Section 59A-54-10 (B):** Effective March 30, 2015, OSI began to accept application of MIP credits to final premium tax return using the following guidelines:

- MIP amounts recorded on the company's final MIP assessment for the preceding year will be applied to the return due the subsequent April;
- OSI will not apply partial assessments on quarterly returns, those are included in the final assessment and will be applied as mentioned above;
- OSI will not apply credits or issue refunds for MIP credits that exceed the current year tax liability. Credits will not be carried forward into the next year unless a company has made an overpayment on their previous years' premium taxes or quarterly estimated taxes. They will only carry over funds due to overpayment for 3 years pursuant to Section 59A-6-5 (B) NMSA 1978.

**Bulletin 2015-027 Supersedes Bulletin 2015-14 Application of Medical Insurance Pool (MIP) Credits to Premium Tax Liability, NMSA 1978, Section 59A-54-10 (B)- Amended:** This bulletin included the language in Bulletin 2015-14 and added the following effective October 9, 2015:

- In the event a company receives a corrected MIP final assessment, they must amend their corresponding final premium tax return with the OSI.
- Companies must provide cancelled check copies to the OSI for interim MIP payments to receive the credit. Copies must display front and back of the check and there must be proof that MIP has deposited the check.

## **SUMMARY OF FINDINGS**

The findings noted as part of the special audit are detailed below. Refer to Appendix A for a breakout of findings by company. The OSI provided responses to each audit finding. Responses have not been audited or edited.

### **Finding 2017-001 Improper Application of MIP Credits**

**Condition:** During the review of MIP credits claimed by insurers, ER noted eleven taxpayers had erroneously applied MIP Credits. The MIP was established in 1987 by the New Mexico State Legislature as a not-for-profit entity. It is not a state agency. This pool was created to provide access to health insurance coverage to New Mexico residents who were denied health insurance or considered uninsurable. It was also intended to help those who have exhausted their COBRA



benefits and have no other portability options. There is very limited state funding for MIP. MIP is funded in a small part by premiums charged to members. There is another specific member population that receives State funding. The remaining amount of MIP funding is derived from annual assessments issued to participating insurers. Annual assessments are mandated by statute and are not optional for insurers. Insurance companies are eligible to deduct the annual assessment from taxable income for federal and state income tax purposes and are also eligible to deduct a percentage of the assessments from their premium taxes due to the State of New Mexico.

Each participating insurer's estimated share of the annual MIP assessment is the product of MIP's budgeted loss and each insurer's premium market share. MIP sends quarterly billing invoices, referred to as interim assessments, to certain large insurers. The quarterly billing invoices are not specifically required by statute. Instead statute permits MIP to operate as they deem necessary and MIP has determined that quarterly billings to large insurers are necessary to assist in meeting cash flow requirements. During the scope of our audit the invoiced amount was one-fourth of the insurer's estimated share of the annual assessment. An annual true-up is performed each year and is now completed by April 1<sup>st</sup>. Assessment true-up refunds, if applicable, are issued once collections are completed. Payments on all assessment invoices, including initial assessments, interim billings and final assessments, are due within 30 days. During the scope of the audit this annual true-up occurred after the April 15<sup>th</sup> annual tax premium tax return due date.

Per current statute, a fifty percent tax credit is allowed on the premium tax return for MIP assessments attributable to regular and low-income policyholder losses. A seventy-five percent tax credit is allowed on the premium tax return for the assessments attributable to MIP policyholders that receive state paid premiums, in whole or in part, through the Federal Ryan White CARE Act, the Ted R. Montoya Hemophilia Program at the University of New Mexico Health Sciences Center, the Children's Medical Services Bureau of the Public Health Division of the Department of Health, or other program receiving State funding or assistance. The premium tax credits for MIP assessment payments can be applied only once annually. MIP credits are distinct from credits created by overpayments. Per Section 59A-6-5 NMSA 1978, the Superintendent may permit overpayment credits to be carried forward for up to three years. There are no statutory provisions permitting MIP credits to be carried forward.

**Criteria:** 59A-54-10 NMSA 1978 addresses MIP assessments and allowed premium tax credits. The OSI issued Bulletin No. 2015-14 to further clarify this statute. Per this Bulletin, effective March 30, 2015, the OSI will accept application of MIP credits to final premium tax returns using the following guidelines:

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- MIP amounts recorded on the insurer's final MIP assessment for the preceding year will be applied to the return due the subsequent April;
- OSI will not apply partial credits to the final premium tax returns based on amounts recorded on the insurer's MIP "Interim Assessments"; those amounts are included and recorded on the insurer's MIP "Final Assessments" and will only be applied in the manner mentioned above;
- OSI will not apply credits or issue refunds for MIP credits that exceed the current year tax liability. Credits will not be carried forward into the next year unless an insurer has made an overpayment on their previous years' premium taxes or quarterly estimated taxes. They will only carry over funds due to overpayment for three years pursuant to 59A-6-5 (B) NMSA 1978.

Bulletin 2015-014 was updated with Bulletin 2015-027 on October 9, 2015. This bulletin included all the language in Bulletin 2015-14 and added the following effective October 9, 2015:

- In the event a company receives a corrected MIP final assessment, they must amend their corresponding final premium tax return with the OSI.
- Companies must provide cancelled check copies to the OSI for interim MIP payments to receive the credit. Copies must display front and back of the check and there must be proof that MIP has deposited the check.

**Cause:** Lack of clarity in 59A-54-10 NMSA 1978 leading to the issuance of Bulletins 2015-014 and 2015-027. Additionally, there has been a lack of oversight by the OSI to ensure MIP credits were being properly used by insurers. OSI procedures do not include comparing total amounts of MIP credit taken with the actual amount of MIP credit available.

**Effect:** During the review of MIP credits claimed by insurers, ER noted eleven taxpayers had erroneously applied MIP Credits resulting in a tax underpayment effect of \$37,993,243. Prior to the issuance of Bulletin 2015-14, it was noted insurers were utilizing their interim assessments and invoice payments in lieu of the annual MIP final assessments. The use of interim assessments and invoice payments led to issues such as taxpayer failure to account for and OSI failure to recognize, refunds issued by MIP as well as inappropriate allocations between premiums that qualified for a fifty percent tax credit and those that qualified for a seventy-five percent tax credit.

The most significant MIP credit issue was related to tax year 2014 and the application of Bulletin No. 2015-14. With the issuance of Bulletin No. 2015-14, the OSI instructed insurers to apply their final MIP assessment for the preceding year to the premium tax return due the subsequent April. Most of the insurers selected as part of this audit, who claimed MIP credits during tax year 2013, had previously claimed their 2013 MIP credits on their 2013 premium tax return utilizing their

interim assessments and invoice payments in lieu of the annual MIP final assessment. It was noted these same insurers then erroneously claimed the same 2013 MIP credits on their 2014 premium tax returns utilizing the 2013 MIP final assessment. Given the 2013 MIP credits were previously utilized in 2013, they were no longer available to be applied for tax year 2014. The effect was that more MIP credits were taken by insurers than were available. There was one insurer that did not apply its MIP credits in compliance with Bulletin No. 2015-14 until tax year 2015. The same issue previously discussed regarding the 2013 MIP credits was noted for this insurer with respect to its utilization of the 2014 MIP credits.

In addition, Bulletin No. 2015-14 clarified 59A-54-10 NMSA 1978 by stating the OSI will not apply credits or issue refunds for MIP credits that exceed the current year tax liability. It was noted multiple insurers applied MIP credits that exceeded the current year tax liability resulting in inaccurate overpayment credit balances.

**Recommendation:** The OSI should ensure insurance companies are utilizing MIP credits in compliance with 59A-54-10 NMSA 1978 and in accordance with Bulletin No. 2015-14 and Bulletin No. 2015-027. The total potential MIP credit should be compared with the actual amount taken by all taxpayers to ensure total amount taken does not exceed the total amount of the available credit. The OSI should also consider examining additional premium tax filings to ensure MIP credits were properly applied and not utilized in more than one tax year.

**Management's Response:** "OSI agrees with the auditor's recommendation that OSI should ensure insurance companies are utilizing MIP credits in compliance with 59A-54-10 NMSA 1978 and in accordance with Bulletin No. 2015-14 and Bulletin No. 2015-027. The OSI continues to work with the new MIP third party administrator (TPA) to improve the timing of the release of the MIP Final Report to the companies. OSI has already worked with the MIP TPA to include, on the MIP Final Report, the MIP Credits allowed to be taken by the companies so they do not have to calculate the credits themselves. This information is at the bottom of the MIP Final Report in boldface type for ease of identification. Audits of premium tax filings will include verification that MIP credits were properly applied. After the recommended new tools and methodology are established, all Financial Audit Bureau staff will be trained on the new tools and processes for verifying allowable MIP credits. Appropriate guidance will also be provided to companies on how to quantify the correct credit amount and how to report the credits on the Final Premium Tax Report."

**Finding 2017-002 Erroneous Political Subdivisions**

**Condition:** During the review of political subdivisions claimed by insurers, ER noted multiple political subdivisions that did not meet the definition of a political subdivision per 59A-6-2 NMSA 1978.

**Criteria:** In accordance with 59A-6-2 NMSA 1978, premiums attributable to insurance or contracts purchased by the state or a political subdivision for the state's or political subdivision's active or retired employees; and payments received by a health maintenance organization from the Federal Secretary of Health and Human Services pursuant to a contract issued under the provisions of 42 U.S.C. 1395 mm(g) are exempt from premium tax and health insurance premium surtax.

**Cause:** Lack of adequate oversight by the OSI to ensure political subdivisions claimed by insurers were in accordance with 59A-6-2 NMSA 1978.

**Effect:** Three insurers were found to have erroneously claimed political subdivisions that were not in accordance with 59A-6-2 NMSA 1978. In total, premium deductions totaling \$9,771,596 related to political subdivisions were deemed inappropriate and disallowed resulting in a tax underpayment effect of \$317,576.

**Recommendation:** The OSI should actively ensure insurance companies are taking deductions for political subdivisions in accordance with 59A-6-2 NMSA 1978. This verification should take place as part of FAB premium tax processing and audit procedures.

**Management's Response:** "OSI agrees with the auditor's recommendation that OSI should actively ensure insurance companies are taking deductions for political subdivisions in accordance with 59A-6-2 NMSA 1978. OSI will define the term "political subdivision" for premium tax purposes, and OSI will work to redesign the premium tax forms to include an attachment on which companies must provide a detailed list of the political subdivision exemptions claimed. The Financial Audit Bureau staff will then be trained on a process for verification of political subdivisions. Also, guidance will be provided to companies, and companies will be notified if a claimed political subdivision exemption is not acceptable."

**Finding 2017-003 Discrepancies in Premiums Reported**

**Condition:** ER noted multiple instances where premiums reported by insurers on their premium tax returns did not agree to the insurers' New Mexico State Business Page or Schedule T.

**Criteria:** In accordance with 59A-6-2 NMSA 1978, insurers are required to report annual premiums from policies within the State of New Mexico as reported on Schedule T of the insurers' annual statement filed with the OSI.

**Cause:** The majority of differences noted were due to insurers' failing to report a portion of their premiums. Subsequent amendments to Schedule T also resulted in minor differences between the premiums reported on insurers' premium tax returns and the premiums report on Schedule T of the insurers' annual statements. OSI has not developed policies and procedures designed to address amended Schedule T's.

**Effect:** Six insurers were found to have discrepancies in premiums reported. In total, \$1,247,578 in premiums were improperly reported resulting in a total tax underpayment effect of \$79,674.

**Recommendation:** The OSI should ensure insurance companies are reporting annual premiums from policies within the State of New Mexico that agree to the Schedule T of the annual statement filed with the OSI. This verification should take place as part of the FAB's premium tax processing and audit procedures. The OSI should also develop policies and procedures to confirm insurers file amended premium tax returns whenever they file an amended Schedule T with revisions to direct written premiums in the State of New Mexico. Requirements should be appropriately communicated to all insurers.

**Management's Response:** "OSI agrees with the auditor's recommendation that OSI should ensure insurance companies are reporting annual premiums from policies within the State of New Mexico that agree to the Schedule T of the annual statement filed with the OSI. OSI that agrees that it should develop policies and procedures to confirm insurers file amended premium tax returns when applicable. In October 2016, OSI began a preliminary process to develop policies and procedures to address issues that might arise. That preliminary process included input from the Financial Audit Bureau (FAB). The Examination Bureau will work with FAB to implement a process to inform FAB if any New Mexico domiciled companies have made an amendment to Direct Premium Written and if questions arise about a company's Business Page. Also, a process will be implemented for FAB to check companies that amended their Direct Premium Written that are not domiciled in the State of New Mexico and to request that such companies file an Amended Final Premium Tax Report."

#### **Finding 2017-004 Improper Surtax Exclusions**

**Condition:** During the review of the insurers' health insurance premium surtax calculations, ER noted multiple instances where insurers exempted premiums from their surtax calculation that were not in compliance with 59A-6-2 NMSA 1978.

**Criteria:** In 2004, 59A-6-2 NMSA 1978 was amended to impose a health insurance premium surtax of one percent of the gross health insurance premiums and membership and policy fees on health insurance or contracts, excluding disability income insurance or contracts, covering health risks within New Mexico. In 2004, the disability income plans were the only plans exempt from surtax.

In 2005, the New Mexico Legislature changed the text of 59A-6-2(C) NMSA 1978 to read that insurers "shall pay a health insurance premium surtax of one percent of the gross health insurance premiums and memberships and policy fees received by it on hospital and medical expense incurred insurance or contracts; nonprofit health care service plan contracts, excluding dental or vision only contracts; and health maintenance organization subscriber contracts covering health risks within this state during the preceding calendar year, less all return health insurance premiums, including dividends paid or credited to policyholders or contract holders and health insurance premiums received for reinsurance on New Mexico risks."

As noted above, Subsection C limits the types of health insurance exempt from surtax to nonprofit vision only plans and nonprofit dental only plans. Subsection E also exempts premiums attributable to insurance or contracts purchased by the state or a political subdivision for the state's or political subdivision's active or retired employees; and payments received by a health maintenance organization from the Federal Secretary of Health and Human Services pursuant to a contract issued under the provisions of 42 U.S.C. 1395 mm(g) from premium tax and health insurance premium surtax. Every other type of supplemental health insurance plan is considered "hospital or medical expense incurred insurance or contracts" as defined by Subsection C 59A-6-2 NMSA 1978.

**Cause:** A lack of clarity in 59A-6-2 NMSA 1978, specifically the definition of hospital or medical expense incurred insurance or contracts, as well as a lack of adequate oversight by the OSI to ensure premiums excluded from surtax by insurers were in accordance with 59A-6-2 NMSA 1978.

**Effect:** Two insurers were found to have claimed improper surtax exclusions. In total, \$71,000,102 in premiums were improperly exempted resulting in a total tax underpayment effect of \$710,001.

**Recommendation:** The OSI should ensure insurance companies are reporting premiums subject to surtax in accordance with 59A-6-2 NMSA 1978. The premium tax forms should be re-designed to include a formal attachment to provide a detailed listing of the surtax exemptions claimed. Surtax exemption verification should take place as part of the FAB's premium tax processing and audit procedures.

**Management's Response:** "OSI agrees with the auditor's recommendation that OSI should ensure insurance companies are reporting premiums subject to surtax in accordance with 59A-6-2 NMSA 1978. OSI will work to redesign the premium tax forms to include a formal request attachment from the companies to provide a detailed listing of the surtax exemptions claimed. OSI will included in the Financial Audit Bureau (FAB) procedures the verification process and will train all FAB staff regarding allowable surtax exemptions. Also, guidance will be provided to companies, and companies will be notified if a claimed surtax exemption is not allowed."

**Finding 2017-005 Errors Switching from Premiums Received to Direct Written Premium Basis**

**Condition:** It was noted that multiple insurers, when making the switch from a premium received basis to a direct written premium basis, reported their current year direct written premiums per Schedule T but failed to include the prior tax year's premiums receivable that was subtracted from the prior year direct written premium when calculating premiums received.

**Criteria:** In 2007, Section 59A-6-2(B) was amended, effective June 15, 2007, to impose the premium tax on gross premiums and membership and policy fees received or written by the insurer, as reported on Schedule T and supporting schedules of its annual financial statement. Prior to this amendment, Section 59A-6-2(B) imposed premium tax on gross premiums and membership and policy fees received by the insurer on insurance or contracts covering risks within the State of New Mexico.

During review of the insurers' premium tax returns, ER noted multiple insurers, prior to 2007, were reporting their premium on a premium received basis as opposed to a direct written basis as reported on the New Mexico State Business Page and Schedule T of insurers' annual statement filed with the OSI. In developing a balance for premiums received during a tax year, the insurers would begin with their direct written premium in the State of New Mexico for the current tax year, add the premiums receivable from the prior tax year, then subtract the premiums receivable for the current tax year.

**Cause:** Accounting oversights by the insurers as well as a lack of adequate monitoring by the OSI to ensure the premiums reported by insurers complied with this specific statutory change.

**Effect:** It was noted three insurers did not properly account for the switch from a premium received basis to a direct written premium basis. These errors resulted in the insurers failing to pay premium taxes on premiums totaling \$19,935,628 for a total tax underpayment effect of \$596,478.

**Recommendation:** The OSI should consider reviewing additional premium tax filings to ensure applicable insurance companies properly accounted for the change from a premium received to a direct written premium basis.

**Management's Response:** "OSI agrees with the auditor's recommendation that OSI should consider reviewing additional premium tax filings to ensure applicable insurance companies properly accounted for the change from a premium received to a direct written premium basis. After the audit/examination has been completed and the new tools and methodology have been reviewed, OSI will strive to provide appropriate guidance to companies on the correct process to ensure that amounts of Direct Premium Written on Schedule T are reported correctly for purposes of filing the Premium Tax Return."

**Finding 2017-006 Improper Exclusion of Dividends Paid or Credited to Policyholders Deduction**

**Condition:** ER noted two insurers failed to deduct dividends paid or credited to policyholders from their taxable premiums.

**Criteria:** In accordance with 59A-6-2 NMSA 1978, insurers can deduct from taxable premiums all return premiums including dividends paid or credited to policyholders or contract holders and premiums received for reinsurance on New Mexico risks.

**Cause:** Erroneous deductions by insurers for dividends paid or credited to policyholders were noted by the OSI. As a result, the column for dividends paid or credited to policyholders was removed from the New Mexico premium tax return by the OSI beginning in 2015.

**Effect:** Removal of the column for dividends paid or credited to policyholders from the New Mexico premium tax return resulted in insurers not being able to uniquely identify and deduct legitimate dividends paid or credited to policyholders from their taxable premiums in compliance with 59A-6-2 NMSA 1978. It was noted two insurers failed to deduct dividends paid or credited to policyholders from their taxable premiums. This resulted in tax overpayments totaling \$47,699.

**Recommendation:** Premium tax forms and their associated instructions should be designed to facilitate accurate tax filings. The OSI should immediately reestablish the column for dividends paid or credited to policyholders in its annual premium tax return so that insurers may again deduct these amounts in compliance with 59A-6-2 NMSA 1978. Premium tax filing forms and instructions should be reviewed by legal counsel and revised as needed to correctly accommodate all tax reporting requirements.

**Management's Response:** "OSI agrees with the auditor's recommendation that OSI immediately reestablish the column for dividends paid or credited to policyholders on the Premium Tax



Return. OSI intends to reestablish the column for dividends, have the forms and instructions reviewed by legal counsel, and train the FAB staff and provide appropriate guidance to companies on what amounts from the Annual Financial Statement Business Page are to be included on the Final Premium Tax Return.”

#### **Finding 2017-007 Erroneously Applied Overpayment Credits**

**Condition:** ER noted insurers had erroneously applied overpayment credits during the audit period, some of which resulted in erroneous refunds issued by the OSI.

**Criteria:** In accordance with 59A-6-5 NMSA 1978, the Superintendent may authorize refund of money erroneously paid as fees, licenses, penalties or taxes from the insurance department suspense fund under request for refund made within three years after the erroneous payment. In the case of premium taxes erroneously paid or overpaid in accordance with law, refund may also be requested as a credit against premium taxes due in annual or quarterly tax returns filed within three years of the erroneous or excess payment.

**Cause:** The erroneously applied overpayment credits noted by ER were a direct result of the findings identified during this audit and the subsequent adjustments to premium tax and health insurance premium surtax due on an annual basis.

**Effect:** It was noted three insurers erroneously applied overpayment credits resulting in additional premium tax and health insurance premium surtax due in the amount of \$24,957,746 which includes balances related to erroneous refunds issued to two insurers by the OSI totaling \$10,671,539.

**Recommendation:** The OSI should establish policies and procedures among all affected Bureau’s to ensure insurance companies are utilizing overpayment credits in accordance with 59A-6-5 NMSA 1978. Before issuing refunds for overpayments, overpayment balances should be reviewed, verified and approved prior to disbursing the funds. This verification should take place as part of the FAB’s premium tax processing and audit procedures.

**Management’s Response:** “OSI agrees with the auditor’s recommendation that OSI should establish policies and procedures among all affected Bureaus to ensure insurance companies are utilizing overpayment credits in accordance with 59A-6-5 NMSA 1978. OSI will ensure that a process is put into place with new policies and procedures for FAB that are designed to verify the accuracy of claimed overpayment credits prior to any disbursement based on a refund request. The FAB staff will be trained on the new tools and methodology to ensure that these policy and procedures are followed and understood before any overpayment refund is issued. Also, appropriate guidance will be provided to the companies in order to ensure a better understanding of the overpayment credit process.”

### **GENERAL OBSERVATIONS FOR OSI**

While performing the procedures previously outlined above, the following general observations were noted by ER that may have a significant impact on the OSI's ability to properly process, record and maintain New Mexico Premium Tax and Health Insurance Premium Surtax filings received from insurers:

#### ***Lack of Formal Processes and Procedures and Lack of an Adequate Automated System***

The current software for tracking premium tax activity (IDEAL) as well as the procedures documentation available with the OSI's customization is minimal, resulting in inefficiencies and inaccuracies in managing premium taxes. The following were noted:

- Lack of adequate tracking of data entry and modifications by user and lack of ability to provide a detailed audit trail for transaction history.
- No automatic process for establishing and tracking penalties.
- There is no automatic tracking ability for the processing of credits and refunds and the company accounts in IDEAL do not indicate when a refund has been issued to the insurer, making it possible for FAB staff to issue a refund that exceeds the company's actual credit balance.
- IDEAL is not tied out to the state's book of record.

#### ***Insufficient FAB Staffing to Perform its Necessary Tasks***

Many of the recommendations in this report refer to the FAB. Currently this bureau has four full-time employees, including the Bureau Chief, and one temporary employee. There is one vacancy. Based on our observations while performing our procedures onsite at the OSI, and through review of the premium tax files during our procedures, we do not believe there is adequate staffing for the volume of filings flowing through FAB. Currently, the Bureau Chief will perform some reviews, but the workload associated with each position does not allow the Bureau Chief to review all transactions.

#### ***Communication Between FAB, Financial Examinations Bureau and the Financial Analysis Department of the Financial Examinations Bureau Should be Further Developed***

Developing communication channels among FAB, Financial Examinations Bureau (FEB) and the Financial Analysis Department of the FEB would provide a more robust supervisory process over premium taxes. Both the Analysis and Examination functions should be made aware of any premium tax compliance issues noted by FAB during its reviews. The Analysis and Examination

functions could be utilized by FAB to follow-up with the insurers regarding the remediation of any issues identified.

***Political Subdivision is not Clearly Defined***

Statute Section 59A-6-2(E)(1) states “Exempted from the taxes imposed by this section are:

- (1) premiums attributable to insurance or contracts purchased by the state or a political subdivision for the state's or political subdivision's active or retired employees.”

There has been no Bulletin or guidance issued by the OSI to further define or clarify what is deemed a political subdivision for exemption purposes. This may lead to inconsistencies in reported and approved political subdivisions.

***Premium Tax Forms and Form Instructions are not Thoroughly Reviewed for Legal Compliance Prior to Publication***

The quarterly and annual premium tax form instructions are not thoroughly reviewed by the OSI legal function prior to publication. The instructions may contain errors or misinterpretations of statutes that could lead to errors in insurer filings. As an example, the 2016 and 2017 instructions for premium tax filings included a reference stating that Federal Exempt Premiums included Federal Flood. While Federal Flood is exempt, the National Flood Insurance Program (NFIP) allows insurers that issue “Write Your Own” NFIP flood policies that are not exempt from state premium tax.

In addition, the premium tax forms are not designed to distinctly capture required information. An example is the political subdivision column of the premium tax form. The premium tax forms do not specifically accommodate all eligible deductions such as the dividends paid or credited to policyholders and various nontaxable passthrough premiums received by insurers. As a result, the political subdivision column has become a “catch-all” for various deductions.

***Overpayment Credits May be Transferred Between Different Business Lines***

Current statutes do not provide the OSI authority to restrict transfer of overpayment credits between lines of business. Balances derived from property and vehicle insurance business are to be distributed to the fire protection fund, balances derived from fees imposed by subsections A and E of 59A-6-1 NMSA 1978 are to be distributed to the insurance operations fund, and the remaining balances derived from other sources to the General Fund. Because premium taxes are distributed to different funds based on line of business, overpayment credits transferred

between different lines of business may distort the amounts that should be distributed to a particular fund.

### ***Lack of Consistency in the FAB Review Process***

The lack of formally documented processes and procedures within FAB has created inconsistencies in how premium tax filings are reviewed and how statutes and guidelines are applied.

### ***Collection of Retaliatory Fees***

On July 9, 2009, the OSI issued Bulletin No. 2009-008 concerning retaliatory fees and reciprocal requirements. Per the Bulletin, retaliatory fees and reciprocal requirements are provided for under Article 6 of the Insurance Code, and the relevant section of the Article 6 provides that an insurer shall be subject to additional fees or charges, termed retaliatory or reciprocal requirements, whenever form or rate-filing fees in excess of those imposed by state law are charged to insurers in New Mexico doing business in another state or whenever a condition precedent to the right to issue policies in another state is imposed by the laws of that state over and above the conditions imposed upon insurers by the laws of New Mexico; in those cases, the same form or rate-filing fees may be imposed upon an insurer from another state transacting or applying to transact business in New Mexico so long as the higher fees remain in force in another state. If an insurer does not comply with the additional retaliatory or reciprocal requirement charges imposed under this subsection, the Superintendent may refuse to grant or may withdraw approval of the tendered form or rate filing.

While 59A-6-1 NMSA 1978 subjects insurers to retaliatory or reciprocal requirements, the Statute does not require the imposition of retaliatory fees or reciprocal requirements on insurers. Instead, the statute grants the discretion to the Superintendent to impose retaliatory fees or reciprocal requirements. Per Bulletin No. 2009-008, the Superintendent decided to no longer impose these fees or requirements due to the heavy administrative burden placed on the OSI.

ER recommends the OSI reconsider imposing retaliatory fees on insurers in compliance with 59A-6-1 NMSA 1978. A cost benefit analysis should be performed to determine the viability of reinstating these fees to include additional staffing requirements needed to assist current staff with the administrative burden.

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**EXIT CONFERENCE**

On October 18, 2017, ER, the OSI and OSA held an exit conference with the following individuals to discuss the results of the special audit and the findings:

**New Mexico Office of the Superintendent of Insurance**

John Franchini, Superintendent of Insurance  
Robert Doucette, Deputy Superintendent of Insurance  
Vicente Vargas JD, General Counsel  
Margaret Moquin JD, Staff Counsel  
Andy Romero, ARM, AIC, Division Director

**New Mexico Office of the State Auditor**

Sanjay Bhakta, CPA, CGFM, CFE, CGMA, Deputy State Auditor  
Sunalei Stewart, JD, CFE, Chief of Staff  
Sarita Nair, JD, MCRP, Chief Government Accountability Officer and General Counsel  
Elise Mignardot, CPA, Audit Manager

**Examination Resources, LLC**

Bradley Hazelwood, CPA, CFE, MCM, Director  
Susan Heath, CPA, Auditor  
Sigurd Proudfit, CFE, AMCM, Auditor

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NEW MEXICO OFFICE OF THE SUPERINTENDENT OF INSURANCE  
 APPENDIX A - FINDINGS BY COMPANY  
 FOR THE PERIOD JANUARY 1, 2003 THROUGH DECEMBER 31, 2016

Company	Finding 2017-001	Finding 2017-002	Finding 2017-003	Finding 2017-004	Finding 2017-005	Finding 2017-006	Finding 2017-007	Total	% of Total Underpayment
M	\$ (14,347,085)	\$ (301,232)	\$ 9,434	-	-	-	\$ (14,286,207)	\$ (28,925,090)	44.77%
F	(8,440,275)	-	(45,065)	-	-	-	-	(8,485,340)	13.13%
L	(8,167,648)	-	-	-	\$ (31,175)	-	-	(8,198,823)	12.69%
C	-	-	-	-	-	-	(6,948,263)	(6,948,263)	10.75%
R	(3,846,605)	-	-	-	-	-	-	(3,846,605)	5.95%
J	-	(3,941)	(72,764)	-	-	-	(3,723,276)	(3,799,980)	5.88%
E	(1,331,349)	-	-	-	-	-	-	(1,331,349)	2.06%
N	(1,231,871)	-	47,353	-	-	-	-	(1,184,518)	1.83%
K	(421,943)	-	-	\$ (708,289)	-	-	-	(1,130,232)	1.75%
B	-	-	-	-	(359,685)	-	-	(359,685)	0.56%
O	-	-	-	-	(205,618)	-	-	(205,618)	0.32%
Q	(75,455)	-	-	-	-	-	-	(75,455)	0.12%
H	(111,558)	-	-	-	-	\$ 41,951	-	(69,607)	0.11%
P	-	-	(26,627)	-	-	-	-	(26,627)	0.04%
A	(14,242)	-	-	-	-	-	-	(14,242)	0.02%
I	(5,211)	-	-	(1,712)	-	-	-	(6,923)	0.01%
D	-	(12,404)	7,994	-	-	-	-	(4,409)	0.01%
G	-	-	-	-	-	5,748	-	5,748	-0.01%
<b>Total</b>	<b>\$ (37,993,243)</b>	<b>\$ (317,576)</b>	<b>\$ (79,674)</b>	<b>\$ (710,001)</b>	<b>\$ (596,478)</b>	<b>\$ 47,699</b>	<b>\$ (24,957,746)</b>	<b>\$ (64,607,018)</b>	<b>100.00%</b>

Life and Health Insurers  
 Property and Casualty Insurers