

**REPORT OF  
MARKET CONDUCT EXAMINATION  
OF**

**LINCOLN DIRECT LIFE INSURANCE  
COMPANY**

Lincoln, Nebraska

**AS OF  
September 15, 2006**

**COMMONWEALTH OF PENNSYLVANIA**



**INSURANCE DEPARTMENT  
MARKET CONDUCT DIVISION**

**Issued: November 7, 2006**

# LINCOLN DIRECT LIFE INSURANCE COMPANY

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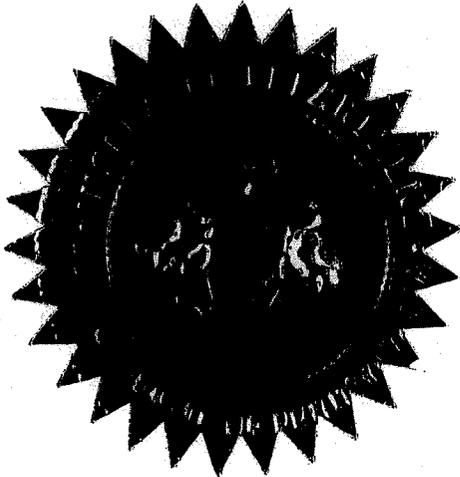
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BEFORE THE INSURANCE COMMISSIONER  
OF THE  
COMMONWEALTH OF PENNSYLVANIA

IN RE: The Act of April 9, 1929, P.L. 177, No. 175, known as The  
Administrative Code of 1929

AND NOW, this 29 day of April, 2002, Randolph L.

Rohrbaugh, Deputy Insurance Commissioner, is hereby designated as the  
Commissioner's duly authorized representative for purposes of entering in and executing  
Consent Orders. This delegation of authority shall continue in effect until otherwise  
terminated by a later Order of the Insurance Commissioner.



M. Diane Koken  
M. Diane Koken  
Insurance Commissioner

BEFORE THE INSURANCE COMMISSIONER  
OF THE  
COMMONWEALTH OF PENNSYLVANIA

IN RE:	:	VIOLATIONS:
	:	
LINCOLN DIRECT LIFE	:	Sections 641-A and 903(a) of the
INSURANCE COMPANY	:	Insurance Department Act, <u>as amended</u>
1526 K Street	:	<u>by</u> Act 147 of 2002 (40 P.S. §§310.41
Lincoln, NE 68508	:	and 323.3)
	:	
	:	Sections 354 and 405-A of the
	:	Insurance Company Law, Act of May
	:	17, 1921, P.L. 682, No. 284 (40 P.S.
	:	§§ 477b and 625-5)
	:	
	:	Title 31, Pennsylvania Code, Sections
	:	51.5, 83.4c, 83.55c, 89b.11(b),
	:	89b.11(c)(1), 146.5 and 146.6
	:	
	:	Title 18, Pennsylvania Consolidated
	:	Statutes, Section 4117(k)
	:	
Respondent.	:	Docket No. MC06-10-022

CONSENT ORDER

AND NOW, this *7<sup>th</sup>* day of *NOVEMBER*, 2006, this Order is hereby  
issued by the Deputy Insurance Commissioner of the Commonwealth of  
Pennsylvania pursuant to the statutes cited above and in disposition of the matter  
captioned above.

1. Respondent hereby admits and acknowledges that it has received proper notice of its rights to a formal administrative hearing pursuant to the Administrative Agency Law, 2 Pa.C.S. § 101, et seq., or other applicable law.

2. Respondent hereby waives all rights to a formal administrative hearing in this matter, and agrees that this Consent Order shall have the full force and effect of an order duly entered in accordance with the adjudicatory procedures set forth in the Administrative Agency Law, supra, or other applicable law.

3. Without admitting the allegations of fact and conclusions of law contained herein, Respondent neither admits nor denies that it violated any law or regulation of the Commonwealth.

#### FINDINGS OF FACT

4. The Deputy Insurance Commissioner finds true and correct each of the following Findings of Fact:

(a) Respondent is Lincoln Direct Life Insurance Company, and maintains its address at 1526 K Street, Lincoln, Nebraska 68508.

(b) A market conduct examination of Respondent was conducted by the Insurance Department covering the period from January 1, 2005, to December 31, 2005.

- (c) On September 15, 2006, the Insurance Department issued a Market Conduct Examination Report to Respondent.
  
- (d) A response to the Examination Report was provided by Respondent on October 13, 2006.
  
- (e) The Examination Report notes violations of the following:
  - (i) Section 903(a) of the Insurance Department Act, No. 285 (40 P.S. § 323.3), which requires every company or person subject to examination must keep all books, records, accounts, papers, documents and any or all computer or other recordings relating to its property, assets, business and affairs in such manner and for such time periods as the Department may require, in order that its representatives may ascertain whether the company has complied with the laws of the Commonwealth;
  
  - (ii) Section 641.1-A of Act 147 of 2002 prohibits any entity or the appointed agent of any entity from transacting the business of insurance through anyone acting without an insurance producer license (40 P.S. § 310.41a);
  
  - (iii) Section 354 of the Insurance Company Law (40 P.S. § 477b), which prohibits issuing, selling, or disposing of any policy, contract or certificate

until the forms have been submitted to, and formally approved by, the Insurance Commissioner;

(iv) Section 405-A of the Insurance Company Law, No. 284 (40 P.S. §625-5), which requires every insurer to institute and maintain internal audit and compliance procedures which provide for the evaluation of compliance with all statutes and regulations dealing with sales methods, advertising and filing and approval requirements for life insurance and annuities. These procedures shall also provide for the following:

- (a) periodic reviews of consumer complaints in order to identify patterns of improper practices;
- (b) regular reporting to senior officers and the board of directors or an appropriate committee thereof with respect to any significant findings;
- (c) the establishment of line of communication, control and responsibility over the dissemination of advertising and promotional materials, including illustrations and illustration explanations, with the requirements that such materials shall not be used without the approval by company employees whose compensation, other than generally applicable company bonus or incentive plans, is not directly linked to marketing and sales.

Each insurer shall make available for department inspection upon request its internal audit and compliance procedures which are instituted as required by this section;

- (v) Title 31, Pennsylvania Code, Section 51.5, which requires, together with the annual statement, a company to file a Certificate of Compliance executed by an authorized officer of the company, which states that to the best of his knowledge, information and belief, the advertisements which were disseminated by the company during the preceding statement year complied or were made to comply in all respects with the provisions of the insurance laws and regulations of this Commonwealth;
  
- (vi) Title 31, Pennsylvania Code, Section 83.4c, which requires the appropriate officer of each direct response or mail-order insurer shall certify, in conjunction with the annual statement of the insurer, that all written disclosure statements have been provided in accordance with this subchapter. Failure to do so certify shall constitute *prima facie* evidence that written disclosure statements have not been provided to prospective purchasers of life insurance;
  
- (vii) Title 31, Pennsylvania Code, Section 83.55c, which states if it is the practice of the insurer to mail the policy directly to the applicant, the appropriate officer of the insurer shall certify, in conjunction with the annual statement of the insurer, that in accordance with this subchapter surrender comparison index disclosures

have been included with policies at delivery or provided earlier upon request.

Failure to so certify shall constitute prima facie evidence that surrender comparison index disclosure have not been provided to prospective purchasers of life insurance;

- (viii) Title 31, Pennsylvania Code, Section 89b.11(b), which requires each form to contain a form number consisting of numbers, letters or both. The form number shall be adequate to distinguish the form from all others used by the insurer. The form number may be the same as that of a form to be replaced. However, if the form to be replaced was approved by or filed with the Department, it may not have been issued in this Commonwealth;
  
- (ix) Title 31, Pennsylvania Code, Section 89b.11(c)(1), which requires each form to contain a brief description or descriptive caption, which shall appear in prominent type on the first or cover page, or in the case of a policy, contract or certificate, on the specifications page if the brief description is visible without opening the form. The brief description shall contain at least the following information: A designation of the general type of the form, policy, contract, certificate, rider, endorsement, amendment, agreement, application or other general type;
  
- (x) Title 31, Pennsylvania Code, Section 146.5, which requires every insurer, upon receiving notification of a claim, shall within 10 working days,

acknowledge the receipt of such notice unless payment is made within such period of time. If an acknowledgement is made by means other than writing, an appropriate notation of such acknowledgement shall be made in the claim file of the insurer and dated;

- (xi) Title 31, Pennsylvania Code, Section 146.6 states that if an investigation cannot be completed within 30 days, and every 45 days thereafter, the insurer shall provide the claimant with a reasonable written explanation for the delay and state when a decision on the claim may be expected; and
- (xii) Title 18, Pennsylvania Consolidated Statutes, Section 4117(k), which requires all applications for insurance and all claim forms shall contain or have attached thereto the following notice: "Any person who knowingly and with intent to defraud any insurance company or other person files an application for insurance or statement of claim containing any materially false information or conceals for the purpose of misleading, information concerning any fact material thereto commits a fraudulent insurance act, which is a crime and subjects such person to criminal and civil penalties."

#### CONCLUSIONS OF LAW

5. In accord with the above Findings of Fact and applicable provisions of law, the Deputy Insurance Commissioner makes the following Conclusions of Law:

- (a) Respondent is subject to the jurisdiction of the Pennsylvania Insurance Department.
  
- (b) Respondent's violations of Section 641-A of Act 147 of 2002 are punishable by the following, under Section 691-A of Act 147 of 2002 (40 P.S. § 310.91):
  - (i) suspension, revocation or refusal to issue the certificate of qualification or license;
  - (ii) imposition of a civil penalty not to exceed five thousand dollars (\$5,000.00) for every violation of the Act;
  - (iii) an order to cease and desist; and
  - (iv) any other conditions as the Commissioner deems appropriate.
  
- (c) Respondent's violation of Section 354 of The Insurance Company Law is punishable by the following, under Section 354 of The Insurance Company Law (40 P.S. § 477b):
  - (i) suspension or revocation of the license(s) of Respondent;
  - (ii) refusal, for a period not to exceed one year thereafter, to issue a new license to Respondent;
  - (iii) imposition of a fine of not more than one thousand dollars (\$1,000.00) for each act in violation of the Act.

(d) Respondent's violations of Section 405-A of the Insurance Company Law, No. 284 (40 P.S. §625-5) are punishable by the following, under 40 P.S. § 625-10:

Upon determination by hearing that this act has been violated, the commissioner may issue a cease and desist order, suspend, revoke or refuse to renew the license, or impose a civil penalty of not more than \$5,000 per violation.

(e) Respondent's violations of Title 31, Pennsylvania Code, Sections 83.4c and 83.55c are punishable under Title 31, Pennsylvania Code, Section 83.6:

(i) For failing to insure adequate disclosure of basic information, after a hearing, a company may be subject to the penalties provided under 40 P.S. § 475, for violations of 40 P.S. §§ 472 through 474. In addition, failure to make the disclosure outlined in this subchapter may be considered a violation of 40 P.S. §§ 1171.1 through 1171.15.

(f) Respondent's violations of Title 31, Pennsylvania Code, Sections 89b.11(b) and 89b.11(e)(1) are punishable under Section 354 of the Insurance Company Law (40 P.S. § 477b) by suspension or revocation of the license(s) of Respondent; refusal, for a period not to exceed one year thereafter, to issue a new license to Respondent; or imposition of a fine of not more than one \$1,000.00 for each act in violation of the Act.

(g) Respondent's violations of Title 31, Pennsylvania Code, Sections 146.5 and 146.6 are punishable under Section 9 of the Unfair Insurance Practices Act (40 P.S. §§ 1171.9):

(i) cease and desist from engaging in the prohibited activity;

(ii) suspension or revocation of the license(s) of Respondent.

(h) In addition to any penalties imposed by the Commissioner for Respondent's violations of the Unfair Insurance Practices Act (40 P.S. §§ 1171.1 – 1171.5), the Commissioner may, under Sections 10 and 11 of the Unfair Insurance Practices Act (40 P.S. §§ 1171.10, 1171.11) file an action in which the Commonwealth Court may impose the following civil penalties:

(i) for each method of competition, act or practice which the company knew or should have known was in violation of the law, a penalty of not more than five thousand dollars (\$5,000.00);

(ii) for each method of competition, act or practice which the company did not know nor reasonably should have known was in violation of the law, a penalty of not more than one thousand dollars (\$1,000.00).

ORDER

6. In accord with the above Findings of Fact and Conclusions of Law, the Deputy Insurance Commissioner orders and Respondent consents to the following:

- (a) Respondent shall cease and desist from engaging in the activities described herein in the Findings of Fact and Conclusions of Law.
- (b) Respondent shall file an affidavit stating under oath that it will provide each of its directors, at the next scheduled directors meeting, a copy of the adopted Report and related Orders. Such affidavit shall be submitted within thirty (30) days of the date of this Order.
- (c) Respondent shall comply with all recommendations contained in the attached Report.
- (d) Respondent shall pay Thirty-Five Thousand Dollars (\$35,000.00) to the Commonwealth of Pennsylvania in settlement of all violations contained in the Report.
- (e) Payment of this matter shall be made by check payable to the Commonwealth of Pennsylvania. Payment should be directed to Sharon L. Fraser,

Administrative Assistant, Bureau of Enforcement, 1227 Strawberry Square,  
Harrisburg, Pennsylvania 17120. Payment must be made no later than thirty  
(30) days after the date of this Order.

7. In the event the Deputy Insurance Commissioner finds that there has been a breach of any of the provisions of this Order, based upon the Findings of Fact and Conclusions of Law contained herein may pursue any and all legal remedies available, including but not limited to the following: The Deputy Insurance Commissioner may enforce the provisions of this Order in the Commonwealth Court of Pennsylvania or in any other court of law or equity having jurisdiction; or the Deputy Insurance Commissioner may enforce the provisions of this Order in an administrative action pursuant to the Administrative Agency Law, supra, or other relevant provision of law.

8. Alternatively, in the event the Deputy Commissioner finds that there has been a breach of any of the provisions of this Order, the Deputy Commissioner may declare this Order to be null and void and, thereupon, reopen the entire matter for appropriate action pursuant to the Administrative Agency Law, supra, or other relevant provision of law.

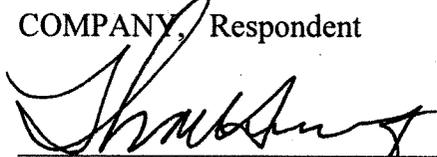
9. In any such enforcement proceeding, Respondent may contest whether a breach of the provisions of this Order has occurred but may not contest the Findings of Fact and Conclusions of Law contained herein.

10. Respondent hereby expressly waives any relevant statute of limitations and application of the doctrine of laches for purposes of any enforcement of this Order.

11. This Order constitutes the entire agreement of the parties with respect to the matters referred to herein, and it may not be amended or modified except by an amended order signed by all the parties hereto.

12. This Order shall be final upon execution by the Deputy Insurance Commissioner. Only the Insurance Commissioner or a duly authorized Deputy Insurance Commissioner is authorized to bind the Insurance Department with respect to the settlement of the alleged violations of law contained herein, and this Consent Order is not effective until executed by the Insurance Commissioner or a duly authorized Deputy Insurance Commissioner.

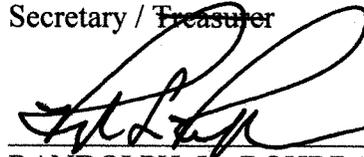
BY: LINCOLN DIRECT LIFE INSURANCE  
COMPANY, Respondent



\_\_\_\_\_  
President / Vice President



\_\_\_\_\_  
Secretary / Treasurer



\_\_\_\_\_  
RANDOLPH L. ROHRBAUGH  
Deputy Insurance Commissioner  
Commonwealth of Pennsylvania

## I. INTRODUCTION

The Market Conduct Examination was conducted on Lincoln Direct Life Insurance Company, hereafter referred to as "Company," at the Company's offices located in Lincoln, Nebraska, May 22, 2006, through June 7, 2006. Subsequent review and follow-up was conducted in the office of the Pennsylvania Insurance Department.

Pennsylvania Market Conduct Examination Reports generally note only those items, to which the Department, after review, takes exception. A violation is any instance of Company activity that does not comply with an insurance statute or regulation. Violations contained in the Report may result in imposition of penalties. Generally, practices, procedures, or files that were reviewed by Department examiners during the course of an examination may not be referred to in the Report if no improprieties were noted. However, the Examination Report may include management recommendations addressing areas of concern noted by the Department, but for which no statutory violation was identified. This enables Company management to review these areas of concern in order to determine the potential impact upon Company operations or future compliance.

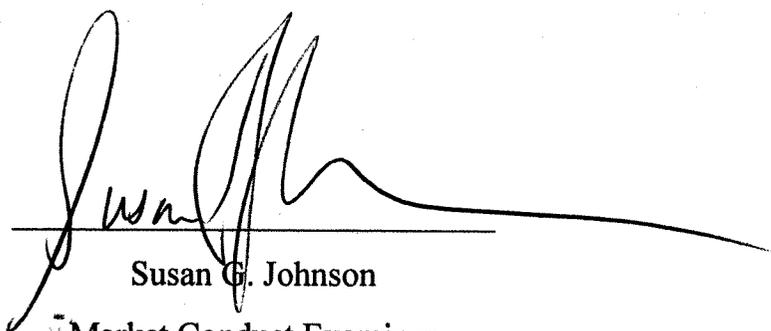
Throughout the course of the examination, Company officials were provided status memoranda, which referenced specific policy numbers with citation to each section of law violated. Additional information was requested to clarify apparent violations. An exit conference was conducted with Company officials to discuss the various types of violations identified during the examination and review written summaries provided on the violations found.

The courtesy and cooperation extended by the Officers and Employees of the Company during the course of the examination is acknowledged.

The undersigned participated in the Examination and in the preparation of this Report.

A handwritten signature in black ink, appearing to read 'Daniel Stemcosky', written over a horizontal line.

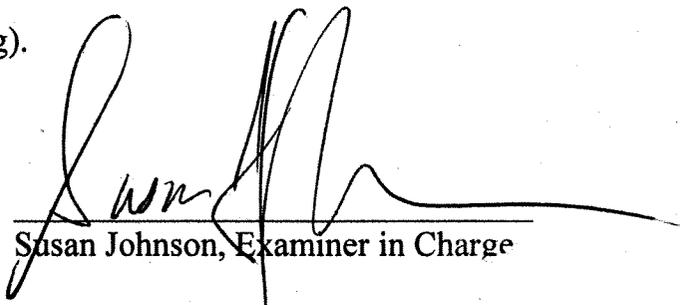
Daniel Stemcosky, AIE, FLMI  
Market Conduct Division Chief

A handwritten signature in black ink, appearing to read 'Susan G. Johnson', written over a horizontal line.

Susan G. Johnson  
Market Conduct Examiner

**VERIFICATION**

Having been duly sworn, I hereby verify that the statements made in the within document are true and correct to the best of my knowledge, information and belief. I understand that false statements made herein are subject to the penalties of 18 Pa. C.S. §4903 (relating to false swearing).

  
Susan Johnson, Examiner in Charge

Sworn to and Subscribed Before me

this 6 Day of September, 2006



Notary Public  
COMMONWEALTH OF PENNSYLVANIA  
NOTARIAL SEAL  
THERESA M. SENECA, Notary Public  
City of Harrisburg, Dauphin County  
My Commission Expires Aug. 15, 2010

## **II. SCOPE OF EXAMINATION**

The Market Conduct Examination was conducted pursuant to the authority granted by Sections 903 and 904 (40 P.S. §§323.3 and 323.4) of the Insurance Department Act and covered the experience period of January 1, 2005, through December 31, 2005, unless otherwise noted. The purpose of the examination was to determine compliance by the Company with Pennsylvania insurance laws and regulations.

The examination focused on the Company's operation in areas such as: Advertising, Consumer Complaints, Forms, Producer Licensing, Underwriting Practices and Procedures, and Claim Handling Practices and Procedures.

The Company was requested to identify the universe of files for each segment of the review. Based on the universe sizes identified, random sampling was utilized to select the files reviewed for this examination.

During the course of the examination, for control purposes, some of the review segments identified in this Report may have been broken down into various sub-categories by line of insurance or Company administration. These specific sub-categories, if not reflected individually in the Report, would be included and grouped within the respective general categories of the Examination Report.

### **III. COMPANY HISTORY AND LICENSING**

Lincoln Direct Life Insurance Company began operations in 1896, as Lincoln Mutual Life Insurance Company (LML) domiciled in Nebraska. In 2000, LML reorganized as a mutual holding company and the name of the operating company was changed to Lincoln Direct Life Insurance Company. In 2001, the Lincoln Mutual Holding Company merged with WFR Mutual Insurance Holding Company, also domiciled in Nebraska. On January 1, 2005, LDL merged with and into Assurity Life Insurance Company. Woodmen Accident and Life Insurance Company merged with and into Assurity Life Insurance Company on October 1, 2003. Assurity is a stock life insurance company ultimately controlled by its policyholders through Assurity Security Group, Inc., the consolidated holding company of Assurity and Security Financial Life which was effective on January 1, 2005.

Insurance was sold through a personal producing general agency distribution system through 1999. In 1997, Lincoln Direct Life Insurance Company began marketing its Direct Response Term products and in 2000, direct response became the sole distribution channel. Currently Lincoln Direct is marketing products as a sales division within Assurity under the marketing name of Assurity Direct. The products currently being marketed are same products offered as Lincoln Direct, namely a 10 year level term product, a modified benefit whole life product, several whole life products and a few riders.

As of their December, 2004, annual statement for Pennsylvania, The Lincoln Direct Life Insurance Company reported direct premium for ordinary life insurance and annuities in the amount of \$740,425. As of December, 2005, Assurity Life

**Insurance Company reported direct premium for ordinary life insurance and annuities in the amount of \$4,682,992 and direct premium for accident and health in the amount of 6,894,990.**

#### **IV. ADVERTISING**

Title 31, Pennsylvania Code, Section 51.2(c) provides that “Any advertisements, whether or not actually filed or required to be filed with the Department under the provisions of this Regulation may be reviewed at any time at the discretion of the Department.” The Department, in exercising its discretionary authority for reviewing advertising, requested the Company to provide copies of all advertising materials used for solicitation and sales during the experience period.

The Company provided a list of 9 pieces of advertising utilized in the Commonwealth during the experience period. The advertising consisted of: Letters, Direct Mailers, Envelopes, Brochures. All 9 pieces of advertising was requested, received and reviewed. The advertising materials and the Company’s web site were reviewed to ascertain compliance with Act 205, Section 5 (40 P.S. §1171.5), Unfair Methods of Competition and Unfair or Deceptive Acts or Practices and Title 31, Pennsylvania Code, Chapter 51 and Chapter 89. The following violation was noted:

##### **1 Violation – Title 31, Pennsylvania Code, Section 51.5**

Each company required to file an annual statement which is now or which hereafter becomes subject to this chapter shall file with the Department with its Annual Statement a Certificate of Compliance executed by an authorized officer of the company wherein it is stated that to the best of his knowledge, information and belief the advertisements which were disseminated by the company during the preceding statement year complied or were made to comply in all respects with the provisions of the insurance laws and regulations of this Commonwealth. Evidence that the Certificate of Compliance was filed with the Pennsylvania Department of Insurance could not be established.

## V. FORMS

The Company was requested to provide a list and copies of all policy forms, conversion contracts, applications, riders, amendments and endorsements used during the experience period. Throughout the course of the examination, all underwriting files were reviewed to identify the policy contracts, riders, endorsements and applications used in order to determine compliance with requirements of Insurance Company Law, Chapter 2, Section 354 (40 P.S. §477b). Applications and claim forms were reviewed to determine compliance with Title 18, Pennsylvania Consolidated Statutes, Section 4117(k).

During the onsite review of the underwriting files, an underwriting procedure was identified. The procedure involved the issuance of a deemer rather than an amendment in cases where the date of application was missing, a beneficiary designation was either missing or insurable interest of the beneficiary designated was in question, or the amount of insurance was not indicated on the application.

The Company was requested to provide the Department with a list of all Pennsylvania residents issued a life policy with a deemer attached during the experience period. The Company provided a list of 83 policies issued with deemers. The following violations were noted:

### **1 Violation - Title 18, Pennsylvania Consolidated Statutes, Section 4117(k)**

All applications for insurance and all claim forms shall contain or have attached thereto the following notice:

“Any person who knowingly and with intent to defraud any insurance company or other person files an application for insurance or statement of claim containing any

materially false information or conceals for the purpose of misleading, information concerning any fact material thereto commits a fraudulent insurance act, which is a crime and subjects such person to criminal and civil penalties.”

The CHILD PLUS Benefit Program application form did not contain the required fraud statement.

**83 Violations – Title 31, Pennsylvania Code, Section 89b.11(b)**

Each form shall contain a form number consisting of numbers, letters, or both. The form number shall be adequate to distinguish the form from all others used by the insurer. The form number may be the same as that of a form to be replaced. However, if the form to be replaced was approved by or filed with the Department, it may not have been issued in this Commonwealth and shall be withdrawn from any issuance in this Commonwealth. The form titled “Deemer” and made a part of the application upon issuance of the policy in the 83 files noted did not contain a form number.

**83 Violations - Insurance Company Law, Section 354 (40 P.S. §477b)**

It shall be unlawful for any insurance company, doing business in the Commonwealth of Pennsylvania, to issue, sell, or dispose of any policy, contract, or certificate, covering life insurance, or use application, riders, or endorsements, in connection therewith, until the forms have been submitted to, and formally approved by, the Insurance Commissioner. The form titled “Deemer” and made a part of the application upon issuance of the policy in the 83 files noted was not filed for approval.

## VI. PRODUCER LICENSING

The Company was requested to provide a list of all producers active and terminated during the experience period. Section 671-A (40 P.S. §310.71) of the Insurance Department Act prohibits agents from doing business on behalf of any entity without a written appointment from that entity. Section 641.1-A (40 P.S. §310.41a) of the Insurance Department Act prohibits a company from accepting insurance applications or securing any insurance business through anyone acting without a license. Section 671.1 (40 P.S. §310.71a) of the Insurance Department Act requires the Company to report all producer terminations to the Department.

The Company provided a list of 5 producers. All 5 producers were compared to departmental records of agents to verify appointments, terminations and licensing. The following violations were noted:

### **4 Violations –Insurance Department Act, No. 147, Section 641.1-A (40 P.S. §310.41a)**

(a) Any insurance entity or licensee accepting applications or orders for insurance or securing any insurance business that was sold, solicited or negotiated by any person acting without an insurance producer license shall be subject to civil penalty of no more than \$5000 per violation in accordance with this act. This section shall not prohibit an insurer from accepting an insurance application directly from a consumer or prohibit the payment or receipt of referral fees in accordance with this act.

The 4 individuals noted were listed as representatives for the Company; however, Department records do not identify these individuals as holding a Pennsylvania insurance license during the experience period.

<u>Last Name</u>	<u>First Name</u>
Hardesty	Karen
Konen	Shelley
Monismith	Linda
Redwine	Dora

## VII. CONSUMER COMPLAINTS

The Company was requested to identify all consumer complaints received during the experience period and provide copies of their consumer complaint logs for 2001, 2002, 2003, and 2004. The Company identified 6 written consumer complaints and provided complaints logs for 2001, 2002, 2003 and 2004. All 6 consumer complaints identified, were forwarded from the Department. The 6 consumer complaint files were requested, received and reviewed.

The Department's list of written consumer complaints that were forwarded to the Company during the experience period was compared to the Company's complaint log. The complaint files and the 4 years of complaint logs were reviewed for compliance with the Unfair Insurance Practices Act, No. 205 (40 P.S. §1171). Section 5(a)(11) of the Act requires maintenance of a complete record of all complaints received during the preceding four (4) years. The record shall indicate the total number of complaints, their classification by line of insurance, the nature of each complaint, the disposition of the complaint and the time it took to process each complaint. Written complaint files involving claims were also reviewed for compliance with Title 31, Pennsylvania Code, Section 146.5(b) and 146.5(c), Unfair Claims Settlement Practices. No violations were noted.

## **VIII. UNDERWRITING**

The Underwriting review was sorted and conducted in 8 general segments.

- A. Underwriting Guidelines
- B. Term Life Policies Issued
- C. Juvenile Whole Life Policies Issued
- D. Ordinary Life Policies Issued
- E. Individual Life Policies Declined
- F. Life Policies Terminated
- G. Life Policies Not-Taken
- H. Term Life Conversions

Each segment was reviewed for compliance with underwriting practices and included forms identification and agent identification. Issues relating to forms or producer licensing may appear in those respective sections of the Report and are not duplicated in the Underwriting portion of the Report.

### **A. Underwriting Guidelines**

The Company was requested to provide copies of all established written underwriting guidelines in use during the experience period. Underwriting guidelines were reviewed to ensure guidelines were in place and being followed in a uniform and consistent manner and no underwriting practices or procedures were in place which could possibly be considered discriminatory in nature, or specifically prohibited by statute or regulation. No violations were noted.

The following guides were provided and reviewed:

1. Underwriting Guidelines, Bulletins and Declination Procedures for all products.
  - New Business Procedures for Entering Applications
  - Buyer's Guide and Procedures
  - Replacement Procedures
  - Procedures for Declining an Application
  - Statement Regarding Underwriting Guidelines

#### **B. Term Life Policies Issued**

The Company identified a universe of 674 term life policies issued during the experience period. A random sample of 50 policy files was requested, received and reviewed. The policy files were reviewed to determine compliance to issuance, underwriting, and replacement statutes and regulations. The following violations were noted:

#### **3 Violations - Insurance Department Act, Section 903 (40 P.S. §323.3)**

(a) Every Company or person subject to examination in accordance with this act must keep all books, records, accounts, papers, documents and any or all computer or other recordings relating to its property, assets, business and affairs in such manner and for such time periods as the department, at its discretion, may require in order that its authorized representatives may readily ascertain whether the Company or person has complied with the laws of this Commonwealth. Pertinent information was missing in the 3 files noted.

**50 Violations – Title 31, Pennsylvania Code, Section 83.4c**

The appropriate officer of each direct response or mail-order insurer shall certify, in conjunction with the annual statement of the insurer, that all written disclosure statements have been provided in accordance with this subchapter. Failure to so certify shall constitute prima facie evidence that written disclosure statements have not been provided to prospective purchasers of life insurance. The 50 files noted indicated that disclosure statements had been delivered by mail with no evidence of a certification of disclosure by an officer of the Company.

**C. Juvenile Whole Life Policies Issued**

The Company identified a universe of 12 juvenile whole life policies issued during the experience period. All 12 policy files were requested, received and reviewed. The policy files were reviewed to determine compliance to issuance, underwriting, and replacement statutes and regulations. The following violations were noted:

**12 Violations – Title 31, Pennsylvania Code, Section 83.4c**

The appropriate officer of each direct response or mail-order insurer shall certify, in conjunction with the annual statement of the insurer, that all written disclosure statements have been provided in accordance with this subchapter. Failure to so certify shall constitute prima facie evidence that written disclosure statements have not been provided to prospective purchasers of life insurance. The 12 files noted indicated that disclosure statements had been made by mail with no evidence of a certification of disclosure by an officer of the Company.

**12 Violations – Title 31, Pennsylvania Code, Section 83.55c**

If it is the practice of the insurer to mail the policy directly to the applicant, the appropriate officer of the insurer shall certify, in conjunction with the annual statement of the insurer, that in accordance with this subchapter surrender comparison index disclosures have been included with policies at delivery or provided earlier upon request. Failure to so certify shall constitute prima facie evidence that surrender comparison index disclosures have not been provided to prospective purchasers of life insurance. The 12 files noted indicated that delivery of the comparison index disclosures had been made by mail with no evidence of a certification of disclosure by an officer of the Company.

**2 Violations - Insurance Company Law, Section 354 (40 P.S. §477b)**

It shall be unlawful for any insurance company, doing business in the Commonwealth of Pennsylvania, to issue, sell, or dispose of any policy, contract, or certificate, covering life insurance, or use application, riders, or endorsements, in connection therewith, until the forms have been submitted to, and formally approved by, the Insurance Commissioner. The form titled “Deemer” and made a part of the application upon issuance of the policy in the 2 files noted was not filed for approval.

#### **D. Ordinary Life Policies Issued**

The Company identified a universe of 70 ordinary life policies issued during the experience period. A random sample of 50 ordinary life policy files was requested, received and reviewed. The policy files were reviewed to determine compliance to issuance, underwriting, and replacement statutes and regulations. The following violations were noted:

##### **50 Violations – Title 31, Pennsylvania Code, Section 83.4c**

The appropriate officer of each direct response or mail-order insurer shall certify, in conjunction with the annual statement of the insurer, that all written disclosure statements have been provided in accordance with this subchapter. Failure to so certify shall constitute prima facie evidence that written disclosure statements have not been provided to prospective purchasers of life insurance. The 50 files noted indicated that disclosure statements had been made by mail with no evidence of a certification of disclosure by an officer of the Company.

##### **50 Violations – Title 31, Pennsylvania Code, Section 83.55c**

If it is the practice of the insurer to mail the policy directly to the applicant, the appropriate officer of the insurer shall certify, in conjunction with the annual statement of the insurer, that in accordance with this subchapter surrender comparison index disclosures have been included with policies at delivery or provided earlier upon request. Failure to so certify shall constitute prima facie evidence that surrender comparison index disclosures have not been provided to prospective purchasers of life insurance. The 50 files noted indicated that delivery of the comparison index disclosures had been made by mail with no evidence of a certification of disclosure by an officer of the Company.

**35 Violations – Title 31, Pennsylvania Code, Section § 89b.11(b)**

Each form shall contain a form number consisting of numbers, letters, or both. The form number shall be adequate to distinguish the form from all others used by the insurer. The form number may be the same as that of a form to be replaced. However, if the form to be replaced was approved by or filed with the Department, it may not have been issued in this Commonwealth and shall be withdrawn from any issuance in this Commonwealth. The application form in the 35 files noted did not contain a form number.

**28 Violations – Title 31, Pennsylvania Code, Section § 89b.11(c)(1)**

Each form, except an insert page, shall contain a brief description or descriptive caption. This brief description or descriptive caption shall appear in prominent type on the first or cover page of the form, or, in the case of a policy, contract or certificate, on the specifications page if the brief description or descriptive caption is visible without opening the form. The brief description or descriptive caption shall contain at least the following information: A designation of the general type of the form, that is, policy, contract, certificate, rider, endorsement, amendment, agreement, application or other general type. A description of the form could not be established in the noted files.

**36 Violations - Insurance Company Law, Section 354 (40 P.S. §477b)**

It shall be unlawful for any insurance company, doing business in the Commonwealth of Pennsylvania, to issue, sell, or dispose of any policy, contract, or certificate, covering life insurance, or use application, riders, or endorsements, in connection therewith, until the forms have been submitted to, and formally approved by, the Insurance Commissioner. Verification of application form approval could not be established in the 36 files noted.

### **E. Life Policies Declined**

The Company was requested to provide a list of all policies declined during the experience period. The Company identified 47 individual life policies declined. A random sample of 25 files was requested, received and reviewed. The files were reviewed to ensure declinations were not the result of any discriminatory underwriting practice and the proper return of any unearned premium. No violations were noted.

### **F. Life Policies Terminated**

The Company was requested to provide a list of all policies terminated during the experience period. The Company identified a universe of 970 life policies terminated. A random sample of 25 files was requested, received and reviewed. The policies were reviewed to ensure compliance with contract provisions, termination laws and regulations and proper return of any unearned premium. No violations were noted.

### **G. Life Policies Not-Taken**

The Company was requested to provide a list of all policies not-taken during the experience period. The Company identified 13 life policies not-taken. All 13 policy files were requested, received and reviewed. A not-taken policy by definition is a contract that is issued and the insured requests cancellation. The files were reviewed to ensure compliance with the free-look provisions of the contract. No violations were noted.

## **H. Term Life Conversions**

The Company identified a universe of 49 term life conversion policies issued during the experience period. A random sample of 25 conversion files was requested, received and reviewed. The files were reviewed to determine compliance to issuance and underwriting statutes and regulations. The following violations were noted:

### **25 Violations – Title 31, Pennsylvania Code, Section 83.4c**

The appropriate officer of each direct response or mail-order insurer shall certify, in conjunction with the annual statement of the insurer, that all written disclosure statements have been provided in accordance with this subchapter. Failure to so certify shall constitute prima facie evidence that written disclosure statements have not been provided to prospective purchasers of life insurance. The 25 files noted indicated that disclosure statements have been made by mail with no evidence of a certification of disclosure by an officer of the Company.

### **25 Violations – Title 31, Pennsylvania Code, Section 83.55c**

If it is the practice of the insurer to mail the policy directly to the applicant, the appropriate officer of the insurer shall certify, in conjunction with the annual statement of the insurer, that in accordance with this subchapter surrender comparison index disclosures have been included with policies at delivery or provided earlier upon request. Failure to so certify shall constitute prima facie evidence that surrender comparison index disclosures have not been provided to prospective purchasers of life insurance. The 25 files noted indicated that delivery of the comparison index disclosures has been made by mail with no evidence of a certification of disclosure by an officer of the Company.

**25 Violations – Title 31, Pennsylvania Code, Section 89b.11(b)**

Each form shall contain a form number consisting of numbers, letters, or both. The form number shall be adequate to distinguish the form from all others used by the insurer. The form number may be the same as that of a form to be replaced. However, if the form to be replaced was approved by or filed with the Department, it may not have been issued in this Commonwealth and shall be withdrawn from any issuance in this Commonwealth. The application form in the 25 files noted did not contain a form number.

**25 Violations – Title 31, Pennsylvania Code, Section 89b.11(c)(1)**

Each form, except an insert page, shall contain a brief description or descriptive caption. This brief description or descriptive caption shall appear in prominent type on the first or cover page of the form, or, in the case of a policy, contract or certificate, on the specifications page if the brief description or descriptive caption is visible without opening the form. The brief description or descriptive caption shall contain at least the following information: A designation of the general type of the form, that is, policy, contract, certificate, rider, endorsement, amendment, agreement, application or other general type. The required form explanation was not evident in the 25 files noted.

**25 Violations - Insurance Company Law, Section 354 (40 P.S. §477b)**

It shall be unlawful for any insurance company, doing business in the Commonwealth of Pennsylvania, to issue, sell, or dispose of any policy, contract, or certificate, covering life insurance, or use application, riders, or endorsements, in connection therewith, until the forms have been submitted to, and formally approved by, the Insurance Commissioner. Verification of application form approval could not be established in the noted files.

## **IX. INTERNAL AUDIT AND COMPLIANCE PROCEDURES**

The Company was requested to provide copies of their internal audit and compliance procedures. The audits and procedures were reviewed to ensure compliance with Insurance Company Law, Section 405-A (40 P.S. §625-5). Section 405-A provides for the establishment and maintenance of internal audit and compliance procedures, which provides for the evaluation of compliance with all statutes and regulations dealing with sales methods, advertising, and filing and approval requirements for life insurance and annuities. The procedures shall also provide for the following:

- (1) Periodic reviews of consumer complaints in order to determine patterns of improper practices.
- (2) Regular reporting to senior officers and the board of directors or an appropriate committee thereof with respect to any significant findings.
- (3) The establishment of lines of communication, control and responsibility over the dissemination of advertising and promotional materials, including illustrations and illustration explanations, with the requirement that such materials shall not be used without the approval by company employees whose compensation, other than generally applicable company bonus or incentive plans, is not directly linked to marketing or sales.

The following violations were noted:

### **1 Violation – Insurance Company Law, Section 405-A (40 P.S. §625-5)**

Establishment of Internal Audit and Compliance Procedures.

- (a) Every insurer shall institute and maintain internal audit and compliance procedures which provide for the evaluation of compliance with all statutes and regulations dealing with sales methods, advertising and filing and approval

requirements for life insurance and annuities. These procedures shall also provide for the following:

- (1) Periodic reviews of consumer complaints in order to identify patterns of improper practices.
  - (2) Regular reporting to senior officers and the board of directors or an appropriate committee thereof with respect to any significant findings.
  - (3) The establishment of line of communication, control and responsibility over the dissemination of advertising and promotional materials, including illustrations and illustration explanations, with the requirements that such materials shall not be used without the approval by company employees whose compensation, other than generally applicable company bonus or incentive plans, is not directly linked to marketing and sales.
- (b) Each insurer shall make available for department inspection upon request its internal audit and compliance procedures which are instituted as required by this section.

The Company failed to provide verification of the establishment of internal audits and compliance procedures.

## X. CLAIMS

The claims review consisted of a review of the Company's claim manuals and a review of the claim files. The Company was requested to provide copies of all procedural guidelines including all manuals, memorandums, directives and any correspondence or instructions used for processing claims during the experience period. The Company provided one claim manual title, "Procedural Guidelines". The claim manual was reviewed for any inconsistencies, which could be considered discriminatory, specifically prohibited by statute or regulation, or unusual in nature. No violations were noted.

The Claim file review consisted of 1 area:

### A. Life Claims

The claim files sampled were reviewed for compliance with requirements of the Unfair Insurance Practices Act, No. 205 (40 P.S. §1171) and Title 31, Pennsylvania Code, Chapter 146, Unfair Claims Settlement Practices. The claims were additionally reviewed for compliance with Insurance Company Law, Section 411B, Payment of Interest (40 P.S. §511b).

## **A. Life Claims**

The Company was requested to provide a list of all claims received during the experience period. The Company identified 20 life claims. All 20 claim files were requested, received and reviewed. The claim files were reviewed for compliance with Title 31, Pennsylvania Code, Chapter 146 and Insurance Company Law, Section 411B, Payment of Interest (40 P.S. §511b). The following violations were noted:

### **1 Violation - Title 31, Pennsylvania Code, Section 146.5**

Every insurer, upon receiving notification of a claim, shall within ten working days, acknowledge the receipt of such notice unless payment is made within such period of time. If an acknowledgement is made by means other than writing, an appropriate notation of such acknowledgment shall be made in the claim file of the insurer and dated. The Company failed to acknowledge the claim noted within 10 working days.

### **3 Violations - Title 31, Pennsylvania Code, Section 146.6**

Every insurer shall complete investigation of a claim within 30 days after notification of a claim, unless the investigation cannot reasonably be completed within the time. If the investigation cannot be completed within 30 days, and every 45 days thereafter, the insurer shall provide the claimant with a reasonable written explanation for the delay and state when a decision on the claim may be expected. The Company failed to provide a timely status letter for the 3 claims noted.

## **XI. RECOMMENDATIONS**

The recommendations made below identify corrective measures the Department finds necessary as a result of the number of some violations, or the nature and severity of other violations, noted in the Report.

1. The Company must review and revise internal control procedures to ensure compliance with requirements of Title 31, Pennsylvania Code, Chapter 146, Unfair Claims Settlement Practices.
2. The Company must review and revise Licensing procedures to ensure compliance with Section 641.1-A of the Insurance Department Act of 1921 (40 P.S. §§310.41a, 310.71 and 310.71a).
3. The Company must implement procedures to ensure advertising certification requirements of Title 31, Pennsylvania Code, Chapter 51.
4. The Company must review internal control procedures to ensure compliance with disclosure requirements of Title 31, Pennsylvania Code, Chapter 83.
5. The Company must review internal control procedures to ensure compliance with forms requirements of Title 31, Pennsylvania Code, Chapter 89.
6. The Company must review internal control procedures to ensure compliance with forms filing and approval requirements of Section 354 of the Insurance Company Law of 1921 (40 P.S. §477b).
7. The Company must implement internal audit and compliance procedures to ensure compliance with Section 405-A of the Insurance Company Law of 1921 (40 P.S. §625-5).
8. The Company must implement procedures to ensure compliance with the fraud statement notice requirements of Title 18, Pennsylvania Consolidated Statutes, Section 4117(k).

## **XII. COMPANY RESPONSE**



**Assurity**  
Life Insurance Company

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October 12, 2006

Daniel A. Stemcosky, AIE, FLMI  
Market Conduct Division Chief  
Bureau of Enforcement  
Pennsylvania Insurance Department  
1321 Strawberry Square  
Harrisburg, PA 17120

Re: *Response to the Report of Market Conduct Examination Warrant: 05-M26-071*

Dear Mr. Stemcosky:

On behalf of Lincoln Direct Life Insurance Co. and Assurity Life Insurance Company (collectively "Assurity" or the "Company"), please allow this letter to serve as our response to the Report of the Market Conduct Examination Warrant Number 05-M26-071 (the "Report"), which was received with your cover letter dated September 15, 2006. We have reviewed the Report and respectfully submit this response.

This response will address the Recommendation section at the conclusion of the Report. The recommendations made in the Report identify measures that the Department believes are necessary as a result of the number or the nature of the alleged violations noted in the Report. With respect to the other exceptions covered in the Report, but not addressed in the recommendations or within this response, Assurity wishes to note that the remaining areas typically involve a single or statistically insignificant number of unique errors and not a trend. Those exceptions are a reflection of human error or deviation from Assurity's established procedures and practices and do not require material institutional corrective actions. Assurity has nonetheless taken steps to minimize the recurrence of these issues in the future.

We have organized our response in relation to the recommendations set forth in the Report as follows:

- 1. The Company must review and revise internal control procedures to ensure compliance with requirements of Title 31, Pennsylvania Code, Chapter 146, Unfair Settlement Practices.**

The Company has reviewed its claim handling standards and written procedures and revised to incorporate specific written requirements of Title 31, Pennsylvania Code, Chapter 146, Unfair Claims Settlement Practices. It is noted, however, that Pennsylvania timeframes mandated within Chapter 146 are less restrictive timeframes than were included within the prior written claim procedures. Employees have been or are in the process of being trained as to documentation procedures and acknowledgement of receipt and understanding of the written claim handling policies and procedures. In addition, written self-audit and monitoring procedures have been further implemented with designated department staff who will be auditing a random percentage of claims for compliance with established policies and procedures. The self-audit reports are ultimately directed to senior management and the appropriate Board committee at regular intervals as part of the Company's overall compliance program.

- 2. The Company must review and revise licensing procedures to ensure compliance with Section 641.1-A of the Insurance Department Act of 1921 (40 P.S. §§310.41a, 310.71 and 310.71a).**

The Company has amended its processes in the Assurity Direct marketing unit at issue in this report so that: 1) one employee in the unit currently holds a Pennsylvania insurance producer license, and 2) if a consumer calls with a question regarding completion of the application or the suitability of an Assurity product for a specific individual, the call is immediately transferred to this licensed agent. We have begun the process of licensing an additional individual in the unit so that we will always have a licensed person in the unit to take these consumer calls. The employees in the unit have been trained on the new process, and we will monitor their compliance with it.

- 3. The Company must implement procedures to ensure advertising certification requirements of Title 31, Pennsylvania Code, Chapter 51.**

Assurity has audited its Certificate of Compliance (relating to the Company's advertising) filing processes as part of its annual statement filing requirements, and has determined that this was a singular oversight on its part. We have confirmed that documented filing processes include the filing of the required Certificate of Compliance.

- 4. The Company must review internal control procedures to ensure compliance with disclosure requirements of Title 31, Pennsylvania Code, Chapter 83.**

Assurity has audited its Certificate Regarding Disclosure Statements filing processes as part of its annual statement filing requirements, and has determined that this

was a singular oversight on its part. We have confirmed that documented filing processes have been revised to address this Certificate.

**5. The Company must review internal control procedures to ensure compliance with forms requirements of Title 31, Pennsylvania Code, Chapter 89.**

The Company has filed an Application Amendment which includes a form number with the Department for approval. Until the Application Amendment is approved by the Department, we are not issuing policies including incomplete applications. We have also filed a Term Conversion application which the DOI approved on September 20, 2006. The Company suspended its marketing of term conversions until this form was approved.

**6. The Company must review internal control procedures to ensure compliance with forms filing and approval requirements of Section 354 of the Insurance Company Law of 1921 (40 P.S. §477b).**

As a result of this examination, the Company has conducted an audit of the Assurity Direct forms used in connection with the issuance and processing of insurance policies. We have ceased the use of any form without a form number. We have also reviewed our procedures and have implemented a process designed to prevent our I.T. Department from coding our policy administration system to generate unapproved forms as policy pages. The employees who code the policy administration system to generate policy pages have been trained on this new process. We will also institute a monitoring process addressing these issues.

**7. The Company must implement internal audit and compliance procedures to ensure compliance with Section 405-A of the Insurance Company Law of 1921 (40 P.S. §625-5).**

The Company had historically established market conduct internal audit and compliance procedures prior to the examination period but had not conducted self-audits specifically relating to Assurity Direct processes which could be presented to the DOI. The Company's overall compliance program complies with Section 405-A of the Insurance Company Law of 192 (40 P.S. 625-5) and includes procedures which provide for the evaluation of compliance with statutes and regulations and company policies and procedures addressing sales distribution methods, advertising, filing and approval requirements, consumer claims and complaints as follows:

(a) Periodic reviews of consumer complaints in order to identify patterns of improper practices.

(b) Regular reporting to senior officers and the Audit Committee of the Board of Directors of any significant findings regarding the periodic reviews of consumer

complaints. The compliance program includes regular reporting to senior management at least quarterly as to trends, practices and compliance matters. We will document such reporting in the future.

(c) The Company has revisited its documented procedures regarding the approval of marketing and sales materials and revised them accordingly. This includes specific communication channels for directives and controls for prior approval of advertising materials, including illustrations and illustration explanations, by company employees and the Legal Department, whose compensation, other than generally applicable company bonus or incentive plans, is not directly linked to marketing or sales.

**8. The Company must implement procedures to ensure compliance with the fraud statement notice requirements of Title 18, Pennsylvania Consolidated Statutes, Section 4117(k).**

The Company has refiled the CHILD PLUS Benefit Program application form containing the required fraud statement. In the meantime, we have suspended marketing of this program and are not using this form.

Thank you for your consideration on this matter and for providing us with an opportunity to respond to the Report. We wish to offer our sincere gratitude to the Department and each individual examiner for the courtesies granted to us throughout the course of this very professionally conducted examination.

Sincerely,

A handwritten signature in black ink that reads "Carol S. Watson". The signature is written in a cursive, flowing style.

Carol S. Watson