

**STATE OF VERMONT  
DEPARTMENT OF BANKING, INSURANCE, SECURITIES  
& HEALTH CARE ADMINISTRATION**

In re: Bankers Life and Casualty )  
Company ) DOCKET NO. 04-022-I  
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**ORDER ADOPTING REPORT OF EXAMINATION**

NOW COMES John P. Crowley, Commissioner of the Vermont Department of Banking, Insurance, Securities and Health Care Administration, and hereby issues the following Order adopting the Market Conduct Examination Report in the above referenced docket number, subject to the exceptions and qualifications discussed below.

**FINDINGS OF FACT**

1. Pursuant to the authority granted by Vermont law including, but not limited to, that contained in 8 V.S.A. §§ 10-13, 18, 3564-3574 and 4726, the Commissioner of the Department of Banking, Insurance, Securities and Health Care Administration (“the Department”) is charged with administering and enforcing the insurance laws and regulations of the State of Vermont and is authorized to conduct examinations of insurers and licensees to determine whether they are in compliance with said laws and regulations.

2. Bankers Life and Casualty Company (the “Company”) is authorized to transact business in Vermont under Certificate of Authority 1091 P.

3. On February 20, 2003, a final market conduct examination report was issued by examiner Charles Piasecki entitled REPORT OF EXAMINATION OF THE MARKET CONDUCT AFFAIRS OF BANKERS LIFE AND CASUALTY COMPANY BY VERMONT DEPARTMENT OF BANKING, INSURANCE, SECURITIES AND HEALTH CARE ADMINISTRATION (hereinafter “the Report”).

4. In accordance with the requirements of 8 V.S.A. § 3574(b), the Report was transmitted to the Company and the Company was afforded a reasonable period of time to submit a formal written response to the findings of the Report. The Company submitted a formal written response addressing issues raised in the Report (the “Response”), discussed issues with the Department and provided additional information requested by the Department.

5. Pursuant to 8 V.S.A. § 3574(c), the undersigned Commissioner has fully considered the Report, the Company’s Response, and additional information provided.

#### **CONCLUSIONS OF LAW**

6. The Company has suggested numerous changes to the Report. To the extent this Order does not expressly adopt changes suggested by the Company, those suggested modifications are not adopted. Unless specified otherwise, the Department adopts the examiner’s report and recommendations as written.

7. The Company suggests the language contained in the Forward of the Report (page 5) which refers to the New Hampshire market conduct exam be removed because the New Hampshire exam was not completed at the time of the Report. As such the Company asserts that New Hampshire’s concerns which led to the Vermont exam may not ultimately be supported by New Hampshire’s findings.

The undersigned declines the Company's suggestion. The Report simply notes how the Department chose to examine the Company and does not lend undue support to New Hampshire's concerns about the Company at that time.

8. In the Response (pages 1-2), the Company suggests numerous changes to the Executive Summary. (Report at page 7.) To the extent not specifically addressed herein, the Company's suggested changes are not adopted. To the extent the Company argues some of the examiner's conclusions were not supported by the findings, these arguments are addressed in detail below. The Company suggests some language be added to the fourth paragraph of the Executive Summary. The undersigned adds the following language to the end of the fourth paragraph of the Executive Summary: "It should be noted that after discovery by the examiner, the Company took corrective action regarding the producer designed sales aid and the pre-approach letter." Finally, the undersigned does not adopt the sixth paragraph of the Executive Summary and it shall be considered deleted.

9. On page 8 of the Report, in the **PERTINENT FACTS OF THE CURRENT EXAMINATION – I. Replacement regulation violations** section, the examiner details the Company's lack of compliance with Vermont's Replacement Regulation (Regulation I-2001-03) for the six sample files which involved replacement policies. The examiner notes that none of these files contained the appropriate forms and that the none of the policyholders interviewed had received a copy of the required disclosure form. The examiner recommends the Company explain how it was "able to completely overlook implementing the requirements of the Regulation I-2001-03", verify that it is now in compliance with the Regulation, explain how it came to be in compliance

and explain what procedures it has implemented which will ensure that the Company does not overlook new Vermont regulations. (Report at page 8, Recommendation No. 1 at Report page 18.)

The Company does not address the substance of the examiner's conclusion that the Company failed to comply with Vermont's replacement regulation, Regulation I-2001-03. The Company requests the addition of language indicating it was in compliance with the replacement regulations prior to March 1, 2002. The Company asks the word "completely" be replaced with "inadvertently" in the examiner's recommendation. (Response at page 3.) The Company asks that the second recommendation not be adopted<sup>1</sup> because the Company has taken steps to come into compliance with the replacement regulation on August 21, 2002.

Finally, the Company notes that it has a "full time Compliance/Legal Department" which "has the responsibility of tracking and reporting regulatory developments." (Response at page 3.) The Company asserts that this was one isolated regulatory oversight and that procedures in place are already adequate to ensure Company awareness of new regulatory developments.

Upon consideration, the undersigned adopts this portion of the Report unchanged and adopts the examiner's recommendation, subject to the one modification discussed below. The Company has requested the inclusion of an affirmative assertion that it was in compliance with Vermont's replacement requirements prior to March 1, 2002.

However, there is no evidence supporting this assertion either in the Report or in the

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<sup>1</sup> In its Response, the Company requests recommendations be deleted. However, the Report exists as drafted by the examiner. The Department then chooses whether or not to adopt the Report, including the recommendations contained therein. Therefore, although the Company may have asked that a recommendation be deleted, this Order shall use the term "adopt" consistent with existing Vermont procedure.

Company's Response. Further, the undersigned finds this portion of the Report sufficiently focused to avoid misleading the reader concerning the breadth of the Company's noncompliance.

The undersigned declines to replace the word "completely" with the word "inadvertent" as suggested by the Company (*see* Recommendation No. 1.1 at Report page 8, Recommendation No. 1.2 at Report page 18). However, the undersigned agrees that the word "completely" is superfluous and it should be considered deleted.

The undersigned adopts the second and third recommendations (Recommendation Nos. 1.2 and 1.3 at Report page 8, Recommendations Nos. 1.1 and 1.3 at Report page 18). The Company asserts compliance with the second recommendation (that it has implemented procedures to comply with the recommendation and that it has described those procedures to the Department). The undersigned has reviewed the Company's regulatory bulletin and, if implemented by Company representatives, it appears the Company shall be in compliance with the Regulation. To that end, written verification that the bulletin attached as Appendix A to the Report has been distributed to all relevant Company employees and representatives and that such bulletin procedures are being followed shall be sufficient to satisfy Recommendation Nos. 1.2 and 1.3, Report, page 8. Such written verification shall be provided to the Department no later than December 20, 2004.

Regarding the fourth recommendation (Recommendation No. 1.3 at Report pages 8 and 18), the undersigned finds that further specific description is warranted regarding the procedures in place to ensure general regulatory compliance. Such description shall include a more detailed description of the staffing of the Compliance/Legal Department

and the responsibilities of the Compliance/Legal Department. In satisfying the obligations imposed by this recommendation, the Company should focus on information which will provide the Department with enough information for the Department to verify that no additional steps need be taken and that the Company can reasonably be anticipated to be aware of applicable new Vermont regulations and statutes adopted in the future.

Regulation I-2001-03 § 8C requires that when an insurer has failed to comply with the Regulation, as in this case, the insurer shall “provide the policy owner an in force illustration if available or policy summary for the replacement policy or available disclosure document for the replacement contract and the appropriate notice” required under the Regulation. As such, the Company is obligated to provide this information to those customers buying replacement policies from March 1, 2002 until the Company came into compliance with the Regulation. The Company shall provide the Department with written confirmation that such information has been provided. This written confirmation shall be provided to the Department no later than December 20, 2004.

Finally, the undersigned finds the Company’s failure to comply with the Regulation I-2001-03 appropriate for the imposition of a \$10,000 administrative penalty.

10. In the **PERTINENT FACTS OF THE CURRENT EXAMINATION – II. Unfair Trade Practices Violations – 1. Sales aid comparing annuity to mutual funds** section (Report at page 9) the examiner notes the use of a sales aid used in the sale of an annuity. The sales aid contained three specific misrepresentations about the annuity which was the subject of the sale. Further, the examiner notes that it was impossible to

assess the extent of use of this sales aid or similar such aids because sales materials were not retained and client files were not maintained in a central location.

The examiner recommends that: 1) the Company prohibit the use of this specific sales aid; 2) the Company implement a program to review all sales aids used by its producers;<sup>2</sup> 3) the Company require that a copy of all sales material used with clients be kept in the client folder so the material can be reviewed by the Company and regulatory authorities; and 4) the Company require that all client files be kept at the Company's regional office. (Report at page 9, Recommendation No. 2 at Report page 18.)

In its Response (pages 3-4 and pages 11-12), the Company generally asserts that the use of the sales aid in question was one isolated incident. The Company notes the producer which used the sales aid was reprimanded for the use of the material and attaches a memo in support of that assertion. Further, the Company notes it presently requires all sales aids to be approved by the Company and attaches various documents to its Response pertaining to its internal sales material approval procedures. The Company also attaches its standard contract used with its producers, which indicates that it is a breach of the contract for a producer to use unapproved materials.

The Company requests none of the examiner's four recommendations be adopted because use of the sales aid was in violation of Company practice and additional measures have been implemented to increase compliance. The Company also notes that prior to March 1, 2002 it had no obligation to maintain centrally located client files containing sales materials used.

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<sup>2</sup> During the time period covered by this exam, Chapter 113 of Title 8 was significantly revised. "Agents" are now referred to as "producers". See 8 V.S.A. § 4791(6). For ease of reference, the term "producer" shall be used in this Order to refer to agents as the examiner and Company use that term in the Report and Response.

Upon consideration, the undersigned adopts this portion of the Report and the examiner's recommendations. Although the documents provided by the Company indicate that the Company has policies in place which prohibit the use of unauthorized sales materials, it is undisputed that the Company had no ability to assess producer compliance with its procedures. Because the Company not only did not monitor sales aids used by its producers, but had no ability to do so until the examination was underway, the Company cannot establish this was an isolated incident. The producer in question has been a representative of the Company for a number of years. Further, the Company is mistaken that it was under no obligation to retain sales material used. Regulation 99-1, effective June 15, 2000, obligates the Company to maintain marketing records such that they are readily available to the Commissioner. Without the retention of sales materials used, or even any client files, it is impossible for the Company or the Department to assess the Company's marketing activities.

The examiner's four recommendations are adopted. It appears the first recommendation has been satisfied and no additional action is necessary on the part of the Company. Regarding the second recommendation, the Company shall provide the Department with a detailed description of its procedures for reviewing sales materials used by producers no later than December 20, 2004.<sup>3</sup>

The examiner's third recommendation is that the Company require copies of all sales materials used with clients be kept in the client folder. The Company indicates that it "requires documentation of all sales material used during the sale." Although this may

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<sup>3</sup> The Company has submitted materials which it claims satisfy this recommendation. See Response at page 4. However, the examiner recommends the company implement procedures to review sales aids used by producers. The Company has provided its internal advertising approval procedures. The procedures submitted with the Response do not address Company procedures to review marketing materials used in the field by producers.

be sufficient to satisfy the examiner's recommendation, the Company must provide a more detailed description of what "documentation" it requires. No later than December 20, 2004, the Company must verify that it requires all sales aids used in a subject sale (or attempted sale) to be kept in the specific client's file. Further, the Company shall explain what steps it has taken to implement this procedure.

The examiner's fourth recommendation (Report at page 9) suggests that the Company keep all client folders at the regional office. The examiner notes that such steps are necessary to allow the Company to assess producer compliance with applicable law and company procedures relating to advertising materials. The Company states that such recommendation has been satisfied because "the branch sales manager agreed to keep individual folders containing sales material used by the agent at the local office." (Response at page 4.) Although it is encouraging that the branch sales manager has agreed to keep "individual folders containing sales material" in the branch office, this does not entirely meet the requirements of the recommendation. It is the Company's responsibility to implement procedures in Vermont whereby all producers understand that each client must have an individual file and that file, in addition to all other pertinent documents, must also include sales materials. Further, the Company must implement a policy whereby all such client files shall be stored in a central location. This procedure must be implemented at the Company level. The Company shall provide a detailed description of the new policy regarding client file retention, how it is being implemented and what steps the Company intends to take to verify that the new procedures are being followed by the Company's producers. Such description shall be provided to the Department no later than December 20, 2004.

Finally, the undersigned finds the use of the improper sales aid appropriate for the imposition of a \$2,000 penalty. This penalty includes a \$1,000 penalty for the one discovered violation of the Unfair Trade Practices Act and \$1,000 penalty for failing to comply with Regulation 99-1 as it relates to marketing materials.

11. In the **PERTINENT FACTS OF THE CURRENT EXAMINATION – II. Unfair Trade Practice Violations – 2. Pre-approach sales letter 98-A006** section of the Report (pages 9-10), the examiner describes the Company’s use of sales letter 98-A006 (see Appendix C, Report at page 24), which misrepresented a Company product in violation of the Unfair Trade Practices Act, 8 V.S.A. § 4721 *et seq.* The examiner also notes that the Department received three complaints indicating that specific consumers had, in fact, been misled by the sales letter in question.

The examiner recommends that the Company: 1) describe the procedures it has in place to ensure that sales materials comply with Vermont law; 2) describe how it failed to determine the sales aid in question was misleading and in violation of the law; and 3) indicate what procedures it has in place presently to ensure that no additional misleading sales materials will be approved for use by the Company. (Report at page 10, Recommendation No. 3 at Report page 18.)

In response, the Company requests that none of the recommendations be adopted. The Company acknowledges that the pre-approach letter “should have been more clear and should not have been authorized for use” (Response, page 5), but notes that it has procedures in place to ensure sales material complies with Vermont law.<sup>4</sup>

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<sup>4</sup> It should be noted that the sales material in question most likely fails to comply with the laws of any state. The sales material misrepresented the product. This is specifically prohibited in most, if not all, states.

Upon consideration, the undersigned adopts this portion of the Report and the examiner's recommendations. Although the Company has provided materials describing the internal procedures used to process proposed marketing materials, the documents provided are silent concerning the actual analysis applied by the responsible Company division. In this instance, a sales aid was approved which was not appropriate. What the Department needs to understand is the type of analysis applied by the Company to assess compliance and sales material approval. A review of the analysis will allow the Department to determine if changes need to be made to the existing procedures. Further, the Company has not provided any specific explanation of how the sales aid in question was approved. A detailed explanation of how the specific sales aid at issue was approved, despite obvious shortcomings, will assist the Department in its assessment of the existing advertisement approval procedures employed by the Company. The Company shall provide the information required by the examiner (Recommendations Nos. 1-3 at Report, page 10) no later than December 20, 2004.

Further, the undersigned finds this matter is appropriate for the imposition of a \$5,000 administrative penalty.

12. In the **PERTINENT FACTS OF THE CURRENT EXAMINATION – II. Unfair Trade Practice Violations – 3. Annuity Applications** section of the Report (page 10), the examiner notes that of the 50 sample annuity files reviewed, five contained the following statement in the remarks section of the application: “This annuity will cause no harm to the annuitant.” The remarks section is above the applicant's signature. The applicant signs to certify that the above information is correct to the best of his/her belief. The examiner notes this statement is inaccurate and misleading and, as such, a

violation of the Unfair Trade Practice Act. 8 V.S.A. § 4724. The examiner recommends the Company implement a review procedure to monitor producer statements that are used on the applications and provide a description of such procedure to the Department.

(Report at page 11, Recommendation No. 4 at page 18.)

In response, the Company disputes the statement is misleading and a violation of 8 V.S.A. § 4724. The Company explains: “The original intent of the statement was to convey that the applicant had other assets available for their use.” (Response at page 5.) The Company further notes that the withdrawal penalties and other risks associated with the annuity product are disclosed in other portions of the policy materials. Nonetheless, the Company has instructed its producers not to use the statement “in the remarks section” and indicates underwriters “will monitor the remarks section of the applications to assure agents do not include this statement in the application.” (Response at page 5.)

The undersigned rejects the Company’s assertion this statement does not violate 8 V.S.A. § 4724. That the applicant may have other assets has nothing whatsoever do with whether the purchase of the product could cause harm to the applicant. The placement of the statement above the applicant’s signature and the fact that it is handwritten on the application by the producer indicates it is intended as a factual representation about the product in question. Yet, the products in question is not without at least some risk. For example, one of the customers purchased the Form LA-04P annuity. This product includes surrender charges as high as 7.2% and is subject to surrender charges until the ninth year.<sup>5</sup> As such, if the customer in question required access to the funds within 9 years of purchase, financial harm could occur. As such, the statement is misleading and constitutes a clear violation of 8 V.S.A. § 4724.

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<sup>5</sup> The customer was 76 years old at the time of purchase.

The undersigned adopts this portion of the Report and the examiner's recommendations contained therein. The Company has indicated that it has instructed its producers to not use the statement in the remarks section. The undersigned directs the Company to confirm, in writing, that it has instructed its producers to not use the statement at any part of the sale.<sup>6</sup> Such confirmation must be provided no later than December 20, 2004. The Company shall also confirm that, as indicated in its Response, it is complying with the examiner's recommendation pertaining to the implementation of a review procedure of producer statements contained on applications, contained in the Remarks section or otherwise. (Recommendation No. 4 at Report page 18.)

The undersigned further finds these violations appropriate for the imposition of a \$5,000 administrative penalty. This penalty reflects \$1,000 penalty per misrepresentation discovered by the examiner. The Company shall note that if the Department discovers use of this, or substantially similar, language in the future, the Department may allege that such use is willful.

13. In the **PERTINENT FACTS OF THE CURRENT EXAMINATION – II. Unfair Trade Practice Violations – 4. Sales Brochure – Retirement Activity** section of the Report (pages 12 - 13), the examiner discusses use of sales brochure Retirement Annuity # 10573 (9/97), where the company compares an annuity to a three month certificate of deposit (CD) interest rate to illustrate that the annuity earns a better interest rate. The brochure states "Single premium tax-deferred annuities are becoming even more popular because of \* \* \* [t]he simple historical fact that annuity interest rates normally exceed the popular one year CD rates." (Appendix E, Report at page 27.) The

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<sup>6</sup> If the Company ever markets a product that has zero risk to the consumer, the Company may request the Department's permission to use the statement in the sale of such product.

brochure then goes on to compare the annuity return to a three month CD return. The examiner notes the three month CD rate is the lowest rate for a CD and comparing it to an annuity is misleading. The examiner recommends that the company stop using the three month CD rate in this comparison. (Report at page 12, Recommendation No. 5 at page 18.)

In response, the Company disputes that the comparison is misleading. (Response at pages 5-6.) The Company notes the Board of Governors, Federal Reserve System does not publish one year CD rates and that the rates in question are the average annual rates for a 3 month CD.

The undersigned rejects the Company's argument and adopts this portion of the Report. The three month CD rate is not an appropriate comparison when the brochure text refers to the one year CD rate. The fact that the three month CD rate has been averaged out over the year is not the point – it is still the lowest rate for a CD. The examiner's recommendation is adopted; the Company is ordered to stop using the sales brochure in question and to further refrain from using the three month CD rate of return in a manner that may indicate such rate is actually the one year CD rate. The Company shall provide written confirmation of compliance with this recommendation no later than December 20, 2004.

Finally, the undersigned finds the use of this misleading chart appropriate for the imposition of a \$5,000 administrative penalty.

14. In the **PERTINENT FACTS OF THE CURRENT EXAMINATION – II. Unfair Trade Practice Violations – 5. Sales Brochure – The Key to the Golden Retirement Activity** section of the Report (pages 12 - 13), the examiner discusses the

Company's use of a chart on the back of brochure #12680 (10/96) which compares annuity returns before taxes imposed upon withdrawal to CD returns that are taxed yearly, but not at withdrawal. (Appendix F, Report at page 33.) Specifically, the examiner objects to the Company's assertion in the brochure that the annuity will earn \$35,331 more than the CD, when in fact, the \$35,331 doesn't reflect taxes which must be deducted from earnings at withdrawal. The examiner notes in another Company brochure, the Company provides a third comparison which describes the annuity returns after taxes and "gives the customer a complete picture." (Report at page 12.) The examiner recommends a third chart be added to brochure #12680 which includes the annuity returns after taxes have been deducted and that the Company implement procedures to insure similar misleading charts are not included in future sales materials. (Report at page 13, Recommendation No. 6 at Report page 19.)

In response, the Company disputes the comparison at issue is misleading. (Response at pages 6-7.) The Company notes the brochure is supposed to be used only with the assistance of a producer and as such, the potential purchaser will have reviewed all of the qualifications regarding the annuity returns which are contained inside the brochure, before reviewing the chart on the back of the brochure. Thus, the Company states, by the time the client reviews the potentially misleading chart, the "client is aware there will be tax consequences when money is disbursed." (Response at page 6.) Further, the Company notes that the purpose of the chart is to show growth of both products, not actual return. The Company states: "We are comparing accumulations for 25 years." Thus, the \$35,331 difference is a difference in accumulation and is not intended to be presented as a difference in actual return. The Company also notes that in

bold print, under the chart, the brochure states “you pay no taxes on your interest until you take it out.” (Appendix F, Report at page 33.)

Upon consideration, the undersigned rejects the Company’s argument and concludes the brochure is sufficiently misleading to constitute a violation of 8 V.S.A. §4724. The undersigned adopts this portion of the Report and the examiner’s recommendation contained therein. Despite the Company’s attempt to draw a distinction between accumulation and return, most customers may not readily grasp such a distinction. More importantly, the chart itself focuses on the \$35,331 “annuity advantage”. By highlighting the difference in growth and emphasizing it as the relevant comparison, the brochure significantly de-emphasizes the very distinction the Company is attempting to make to justify the comparison.

The undersigned specifically rejects the Company’s argument that because the brochure is used by a producer to sell a product, the consumer will be that much less likely to be misled because they will have gone through the whole brochure by the time they get to the back. The exam has uncovered questionable marketing techniques used by some of the Company’s producers. More significantly, until recently, the Company was not sufficiently monitoring sales practices of its producers. As such, the undersigned declines to rely on the Company’s producers to provide additional explanation in order to ensure the chart is not misconstrued. Moreover, in general, sales material should be sufficiently clear to stand on its own, whether or not a producer is intended to walk through the material with the customer; the Department does not condone sales materials that are sufficiently unclear as to be misleading absent an accompanying verbal explanation.

The Company shall verify to the Department no later than December 20, 2004 that it has ceased to use the chart in question and that in the future it will avoid the use of similarly misleading comparisons.

The undersigned finds this violation does warrants the imposition of a \$2,000 administrative penalty. This nominal penalty appears warranted in light of the Company's apparent good faith use of the misleading material.

15. In the **PERTINENT FACTS OF THE CURRENT EXAMINATION – II. Unfair Trade Practice Violations – 6. Sales Brochure – Equity Indexed Annuity** (Report at page 13), the examiner notes the Company's insert # 14405 contains a chart which purports to illustrate a hypothetical cash value of the Company's Equity 1 annuity product compared to the S&P 500. (Appendix G, Report at page 34.) The examiner notes the chart uses an index value based on an 80% participation rate. However, the Company's annual average participation rate has never exceeded 75.83%. As such, the examiner concludes the brochure contains a misleading projection and in violation of 8 V.S.A. § 4724. The examiner recommends that the Company change the participation rate used in the sales material to reflect realistic projections of future participation rates. (Report at page 13, Recommendation No. 7 at Report page 19.)

In its Response (page 7), the Company asserts that its use of the 80% participation rate is not misleading. The Company notes "the purpose of this illustration is not to imply that such growth is likely to happen. It is to show the customer what happens when there are fluctuations in the S&P 500." (Response at page 7.) Further, the Company notes that the average participation rate for 2000 and 2001 was 75.84%, but

that it was “76.25% for year 2002 to August.”<sup>7</sup> (Response at page 7.) Further, the Company notes for the 41 month period from April 1999 through August 2002, the participation rate was 80% in 26 of the months. Additionally, the Company notes the insert indicates that the rate is set yearly and the chart is labeled “Hypothetical Cash Value Accumulation” and clearly states that participation rates are not guaranteed. Thus, the Company argues, it does not misrepresent the benefits of the product.

Upon consideration, the undersigned adopts this portion of the Report. The undersigned rejects the Company’s argument and concludes the use of the 80% participation rate in the brochure is a violation of 8 V.S.A. § 4724. The chart is clearly intended to illustrate the performance of the Company product, as compared to the S&P 500. Although the chart is intended to provide only a hypothetical comparison, that comparison must be reasonably based on previously occurring events. In this situation, the Company had chosen to use an annual participation rate which has limited, if any, basis in reality. If the Company were allowed to use an 80% rate as its sample annual participation rate, when in fact it has never actually had an annual average of 80%, then what is to prevent the Company from using 90%? The participation rate should be no higher than the previous average annual participation rates.

The Company shall confirm no later than December 20, 2004 that it no longer uses this advertisement and will further confirm that it will not use statistics for product comparison unless those statistics are based on actual previously occurring events which are presented in a manner that is not misleading. The Company shall specifically note that return rates and similar statistics used in sales materials must be reasonably

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<sup>7</sup> Presumably this means that the average participation rate for January 2002 to August 2002 was 76.25%, although that is not entirely clear from the Response. The Response is dated December 2002.

supported by actually occurring historical events. That the Company has previously achieved an 80% participation rate inconsistently, and has not exceeded that rate, fails to reasonably support the use of such a figure for comparison purposes in an advertisement.<sup>8</sup>

Finally, the undersigned finds this appropriate for the imposition of a \$10,000 administrative penalty.

16. In the **PERTINENT FACTS OF THE CURRENT EXAMINATION – II. Unfair Trade Practice Violations – 7. Unsuitable Sales** section of the Report (page 13-14), the examiner describes two incidents in which the Company’s producer sold unsuitable policies and complaints were filed with the Department. In both situations, the Company refunded the money. The examiner refrains from making recommendations in this section of the Report because the remainder of the Report details improvements implemented by the Company and the examiner’s thoughts about the specifics of those improvements.

In it’s Response (pages 7-8), the Company requests this portion of the Report not be adopted because the producers who sold the suitable policies “believed, at the time of sale that the product they presented and sold was suitable for the clients [sic] needs.” (Response at page 8.)

Upon consideration, the undersigned adopts this section of the Report. The sales in question were unsuitable. Although evidence may exist to support the Company’s assertion that the producers in question reasonably believed the sales were suitable, the Company does not provide any such evidence.

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<sup>8</sup> For example, presumably the S&P return rate used in the comparison used was the annual average – not the highest return rate achieved in a portion of unidentified and isolated months.

The undersigned finds, in light of the Company's restitution to the consumer, no administrative penalty is warranted under these particular circumstances.

17. On page 15 -16, in the **III. COMPANY IMPROVEMENTS – 1. Suitability Training** section of the Report, the examiner notes that the Company implemented significant improvements in the area of suitability. The new suitability training instructs producers to determine whether a customer meets four specific guidelines before selling a policy. Although the Report indicates the guidelines are excellent, the examiner has concerns about how the producers are being trained to implement the use of the guidelines.

The first two guidelines require that the producer determine that the customer needs the insurance and that the proposed coverage fit that need. (Report at page 15.) To ascertain the necessary information to satisfy these two guidelines, the producers are instructed to fill out the Company's Needs Assessment form (See Appendix H, Report at pages 36-39). However, the examiner states the Needs Assessment form was "not designed to get a complete and accurate picture of the prospect's situation." (Report at page 15.) The examiner recommends the form be expanded to obtain a complete picture of the prospect's financial picture, including all assets, liabilities, income and expenses. Further, the forms should elicit information about personal objectives, risk tolerance, customer's age, investment sophistication and tax issues. (Report at page 15, Recommendation No. 8 at Report page 19.)

The third guideline which the Company instructs its producers to apply when assessing suitability is establishing whether or not the customer can afford the insurance. The examiner notes that the Company indicated it provides no training to its

producers regarding establishing the liquidity needs of prospective clients. The examiner notes that without assessment of the liquidity needs of a prospect, producers cannot determine whether the insurance is affordable, nor can the Company determine whether the sale was suitable. This is particularly true, the examiner notes, in light of the Company's business practice of focusing on sales to the elderly.

The examiner recommends the Company provide training in assessing affordability and set standards for producers to follow regarding prospective customers' liquidity needs. (Report at page 16, Recommendation No. 9 at Report page 19.)

Finally, the Company's fourth suitability guideline directs producers to establish that in a replacement situation, the proposed new coverage is better for the prospect considering benefits gained and benefits lost. The examiner notes that this guideline applies to only those situations where an annuity product, as opposed to another investment, is being replaced and that this limitation undercuts the effectiveness of the fourth guideline. The examiner notes that many customers replace other investments (such as certificates of deposit or mutual funds) when replacing an annuity. As such, a producer "must consider using the test of the benefits gained and benefits lost for all replacement policies." (Report at page 16.) The examiner recommends the Company expand its training to instruct producers to analyze benefits lost and benefits gained when purchasing any Company product, not just replacing an existing annuity. (Report at page 16, Recommendation No. 10 at Report page 19.)

The examiner notes another problem associated with training Company producers to implement the fourth suitability guideline lies in the fact that producers are not given any training regarding the benefits offered by the investments that are being replaced

when the customer purchases the annuity. Producers cannot give reliable advice regarding the suitability of a proposed product if they don't understand what is being replaced.

Regarding training producers concerning the implementation of the fourth guideline, the examiner recommends that the Company instruct producers to advise their prospective clients to check with their current financial advisor before changing investments or, in the alternative, the Company provide training to their producers sufficient to allow producers to adequately advise prospective clients concerning the benefits lost when replacing an existing non-annuity investment with an annuity. (Report at page 16, Recommendation No. 11 at Report page 19.)

In its Response (page 8), the Company asks that the Report be amended to clarify that the Company's compliance has not improved as it relates to the sale of suitable products, but simply to its documentation of suitability. The Company provides no rationale for this proposed amendment.

The Company defends its Needs Assessment form<sup>9</sup> by noting that various areas where the examiner believes additional information should be gathered (such as assets, liabilities, income, age, risk tolerance) are already covered by the form.

Regarding the examiner's concern that the Company is not training its producers sufficiently to assess the liquidity needs of prospective clients, the Company again reiterates that producers do uncover sufficient information by using the Needs Assessment form and further notes that the producers are trained about the specific

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<sup>9</sup> The Company and the materials it has attached to the Response refer to the Company's "fact finder". See Response at pages 8-9 and attachments. It appears the "Needs Assessment" form (Appendix H of the Report) is one fact finder. However, Company materials refer to several others. Because "fact finders" are not labeled as such, it's unclear if the Company provided all of the fact finders it uses.

product benefits offered by the Company. Additionally, the Company requests that information about certain products be added to the first paragraph on page 16 of the Report to clarify that some products offered by the Company have minimal penalties associated with early withdrawal and thus, presumably, customer liquidity needs are not relevant when assessing suitability of the product. Finally, the Company asks that the examiner's recommendation requiring additional training in affordability not be adopted.

Regarding the examiner's recommendations that the Company provide additional training for its producers, the Company asserts that its training is already adequate and asks the examiner's recommendations not be adopted. The Company notes that in addition to the fact finder training provided in which producers are taught how to gather relevant data for suitability analysis, producers must also complete a "Suitability, Replacement and Disclosure" course, the Company provides detailed training on each of its products and the Company has made additional training available on line for its producers.<sup>10</sup> (Response at page 9.)

The Company objects to the examiner's recommendation that it provide additional training regarding other types of investments. The Company asserts that there is no proof that their producers do not understand CD's or mutual funds. Further, the Company notes the replacement regulation only applies to the replacement of annuities. Regulation I-2001-03. Finally, the Company objects to the examiner's recommendation that the Company advise prospective clients to consult with their

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<sup>10</sup> According to the attachments to the Response, producers are offered access to the following courses: Introduction to Long Term Care, Introduction to Annuities, Introduction to Life Insurance, and Introduction to Medicare. Further, it appears producers are provided with links to a variety of public sources of information about related topics, such as the "official U.S. Government site for people with Medicare."

financial advisor before making a decision or train their producers about the investments which prospective clients are being counseled to replace with a Company product.

Upon consideration, the undersigned adopts this section of the Report and the examiner's recommendations, subject to the following modifications. Regarding the examiner's recommendation that additional information be elicited regarding the prospect's entire financial picture and income needs (Report at page 15 and Recommendation No. 8 at Report page 19), the undersigned acknowledges the Financial Needs form appears to seek all of the relevant information identified by the examiner and to that end, modifications are not necessary except as explicitly provided herein. Specifically, the form does not provide sufficient space or level of detail concerning the prospect's existing financial picture and to that end, the Company shall expand that portion of the form (see Report at page 38). Further, the Company shall add a question to the form which seeks to specifically ascertain the prospect's present and anticipated liquidity needs. The Company shall provide such revised form to the Department for review and approval no later than December 20, 2004. Additionally, the Company shall confirm that all other "fact finder" forms intended to assist producers in ascertaining suitability of Company products shall contain sufficient questions about the customers financial and liquidity needs.

Regarding the examiner's recommendation that the Company provide training to further assist producers in assessing the affordability of a specific product for a prospective customer (Report at page 16, Recommendation No. 9 at Report page 19), the undersigned orders the Company to expand that portion of its training. The training

materials provided do not appear to address liquidity needs. The target audience for the Company's products (the elderly) typically have specific liquidity needs and ascertaining such needs is a vital element of establishing which of the Company's products are suitable for a specific prospect or client. The Company shall provide a written description of how it has expanded its training to address assessing liquidity needs, with relevant supporting documentation, to the Department no later than December 20, 2004.

Regarding the examiner's recommendation that producers apply a benefits lost to benefits gained analysis to all sales, not only those involving the replacement of annuities (Report at page 16, Recommendation No. 10 at Report page 19), the undersigned rejects the Company's argument that the recommendation should not be adopted because Regulation I-2001-03 only applies to annuities. The important point of the examiner's recommendation is that only suitable policies are sold to clients. Although the specific requirements of Regulation I-2001-03 only apply to the replacement of existing life insurance and annuity products (*see* Regulation I-2001-03 § 1(A)(2)), pursuant to 8 V.S.A. § 4724(16), all unsuitable sales are prohibited. To that end, the analysis of benefits gained to benefits lost is a necessary focus for the sale of any product. The Company shall confirm to the Department in writing, no later than December 20, 2004, that it has instructed its producers that every sale must be suitable and that part of the suitability analysis necessarily involves an assessment of benefits lost versus benefits gained.

Finally, the undersigned adopts the examiner's recommendation that producers instruct clients to consult with their financial advisor or that the Company provide its

producers with training regarding other investments (Report at page 16, Recommendation No. 11 at page 19). The Company notes that the Needs Assessment form already asks if a client has a financial advisor. This is not the same as advising the client to consult that person.<sup>11</sup> In order to ensure that only suitable sales occur, if producers are going to provide financial advice or tax advice, such advice should ideally be verified by a professional licensed to discuss those aspects of the transaction. In the alternative, the Company may provide additional training focusing on the more common investments clients often replace with annuities. The Company shall provide the Department with a detailed written description of what steps it has taken, with appropriate supporting documentation, to the Department no later than December 20, 2004.

Finally, the undersigned rejects the Company's argument that because the statutes do not specifically provide detailed guidelines for what constitutes a suitable sale (Response at page 10), the Company cannot be directed to take specific steps to ensure suitability because other companies in the marketplace have no such specific obligations. The statute does not precisely define the necessary prerequisites for a sale to be "suitable" in order to give carriers, such as the Company, maximum flexibility. Such flexibility promotes economic efficiency and encourages creative product development. However, by allowing carriers to develop and define their products and sales techniques, the Department is not prevented from stopping those sales techniques that fail to adequately assess suitability needs of prospective clients.

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<sup>11</sup> The Company also notes that some point of sales material already advise a prospect to consult with an attorney, accountant or tax advisor. (Response at page 9.) To satisfy this recommendation, the Company can provide a detailed list that indicates each product is sold with such an advisory.

Other insurers are obligated to only sell suitable products. Other insurers have and will continue to be directed to take certain steps, within the specific parameters of their target populations, business practices and available product lines, to ensure suitability needs of clients. As a result of the examiner's review of the Company's target population, business practices and available product lines, the recommendations contained herein are the most appropriate way to address the Company's suitability obligations.

18. On pages 16-17, in the **COMPANY IMPROVEMENTS – Suitability Questionnaires** section of the Report, the examiner notes the Company started using suitability questionnaires in July of 2002; the examiner indicates the questionnaires are a good start to ensure suitability needs are adequately addressed. However, the examiner notes that although Company procedures provide that a policy should not be issued without the managers signature on the suitability questionnaire, seven out of seventeen policy sales did not include a manager's signature on the suitability questionnaire. The examiner recommends the Company take additional steps to ensure compliance with its internal requirement that a branch manager sign the questionnaire before a policy is issued. (Report at page 17, Recommendation No. 12 at Report page 20.)

The examiner also notes that the suitability questionnaire does not contain the four points identified in the Company's suitability training guidelines which are necessary to assess the suitability of a sale.<sup>12</sup> As such, the examiner recommends the suitability questionnaire ask the producer to answer the four questions that the training recommends. (Report at page 17, Recommendation No. 13 at Report page 20.)

In response, the Company notes that the Needs Assessment form already contains all of the relevant questions necessary to assess the four suitability guidelines identified in the training. (Response at page 10.)

Upon consideration, the undersigned adopts this portion of the Report, including the examiner's recommendations, subject to the following modifications. The Company

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<sup>12</sup> These are: Is there a need? Does the policy meet the need? Can the customer afford the policy? If a replacement, are benefits gained better than benefits lost?

shall provide a written description of how it has modified its internal procedures to comply with Recommendation No. 12 (Report page 20). Regarding the change to the suitability questionnaire recommended by the examiner, the Company is instructed to incorporate these guidelines into the suitability form. The Company argues that incorporating the four suitability guidelines into the suitability questionnaire is unnecessary because the suitability analysis is done when the prospect and producer fill out the various fact finder forms. However, the fact finder forms allow the analysis to take place. The suitability questionnaire acts as a final suitability checklist. The information necessary to perform the analysis may be gathered and assessed at the fact finding part of the transaction. The suitability checklist will allow a final check to ensure that adequate analysis was performed regarding all four suitability guidelines identified by the Company. The new questions can provide for a simple yes or no response. Details supporting those responses shall be noted in the fact finder forms filled by the customer and producer.

The Company shall provide the revised forms to the Department for review and approval no later than December 20, 2004.

### **ORDER**

Based upon the Findings of Fact and Conclusions of Law set forth above, **IT IS THEREFORE ORDERED** by the Commissioner of the Department of Banking, Insurance, Securities and Health Care Administration that the REPORT OF EXAMINATION OF THE MARKET CONDUCT AFFAIRS OF BANKERS LIFE AND CASUALTY COMPANY BY VERMONT DEPARTMENT OF BANKING, INSURANCE, SECURITIES AND HEALTH CARE ADMINISTRATION (which is incorporated herein by reference) shall be and hereby is adopted with the following modifications and clarifications:

19. As discussed above in Paragraph 6 above, the undersigned rejects any proposed changes to the Report which are not expressly adopted below.

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20. As discussed in Paragraph 8 above, the following changes are made to the Report. The fourth paragraph of the Executive Summary (Report at page 7) shall include the following statement at the end: “It should be noted that after discovery by the examiner, the Company took corrective action regarding the producer designed sales aid and the pre-approach letter.” The sixth paragraph of the Executive Summary is not adopted and shall be considered deleted.

21. As discussed in Paragraph 9 above, addressing the **I. Replacement regulation violations** section of the Report, the undersigned does not adopt the word “completely” as used in the examiner’s first recommendation (Recommendation No. 1.1 at Report page 8, Recommendation No. 1.2 at Report page 18). Subject to that modification, the three recommendations on pages 8 and 18 are adopted. As described more fully in Paragraph 9 above, the Company shall provide a written explanation of how it failed to implement Regulation I-2000-03 (Recommendation No. 1.1 at Report page 8, Recommendation No. 1.2 on Report page 18). The Company shall confirm in writing that the “Regulatory Bulletin” attached as Appendix A to the Report has been distributed to all relevant Company employees and representatives and that the procedures outlined in the “Regulatory Update” are being followed (Recommendation No. 1.2 at Report page 8, Recommendation No. 1.1 at Report page 18). As described more in depth in Paragraph 9 above, the Company shall expand on its explanation of how it maintains compliance with Vermont statutes and regulations as such are passed and promulgated (Recommendation No. 1.3 at Report pages 8 and 18). Finally, as discussed above in Paragraph 9, the Company shall also provide the information required by Regulation I-2001-03 § 8C to those in-force policyholders who purchased replacement policies from

the Company on or after March 1, 2002 through the date of this Order. If the Company asserts such policyholders have received this information previously, the Company shall not provide the information again, but shall so indicate to the Department. Compliance with this portion of the Order shall require a spreadsheet (preferably in Excel format) noting the policyholders, policy number, policy dates and information provided to comply with this section. The actions detailed in this paragraph shall be completed and provided to the Department no later than December 20, 2004.

22. As discussed more fully in Paragraph 9 above, the undersigned finds the Company's failure to implement Vermont Regulation I-2001-03 warrants the imposition of a \$10,000 administrative penalty.

23. As discussed in Paragraph 10 above, the section of the Report entitled **PERTINENT FACTS OF THE CURRENT EXAMINATION – II. Unfair Trade Practices Violations – 1. Sales aid comparing annuity to mutual funds** is adopted, including the examiner's recommendations. The Company shall provide the information discussed in Paragraph 10 to the Department no later than December 20, 2004.

24. As discussed above in Paragraph 10, the undersigned finds the Company's producer's violation of the Unfair Trade Practices Act and the Company's failure to follow Regulation 99-1 pertaining to record retention warrants the imposition of a \$2,000 penalty.

25. As discussed in Paragraph 11 above, the section of the Report entitled **PERTINENT FACTS OF THE CURRENT EXAMINATION – II. Unfair Trade Practice Violations – 2. Pre-approach sales letter 98-A006** and the examiner's recommendations contained therein are adopted. As more fully described above, the

Company shall provide the information required to the Department, in writing, no later than December 20, 2004.

26. As noted in Paragraph 11 above, the Company's approval of misleading sales material, sales letter 98-A006, warrants the imposition of a \$5,000 administrative penalty.

27. As discussed above in Paragraph 12, the section of the Report entitled **PERTINENT FACTS OF THE CURRENT EXAMINATION – II. Unfair Trade Practice Violations – 3. Annuity Applications** is adopted, along with the examiner's recommendations contained therein. As described above, the Company shall confirm that it has instructed producers to not use the misleading statement in question and shall further provide the Department with written confirmation that it has implemented (and follows) procedures for monitoring producers statements contained on product applications. Such confirmation shall be provided to the Department in writing no later than December 20, 2004.

28. As discussed above in Paragraph 12, the undersigned finds the misleading statements contained on the annuity applications warrants the imposition of a \$5,000 administrative penalty.

29. As discussed in Paragraph 13 above, the undersigned adopts the portion of the Report, and the examiner's recommendation contained therein, entitled **PERTINENT FACTS OF THE CURRENT EXAMINATION – II. Unfair Trade Practice Violations – 4. Sales Brochure – Retirement Activity**. As discussed, the Company shall cease using sales brochure Retirement Annuity # 10573 (9/97) and shall not use a three month CD interest rate when the text of a sales aid refers to a one year

rate. The Company shall provide written confirmation of compliance with the requirements of this Paragraph to the Department no later than December 20, 2004.

30. As discussed above in Paragraph 13, the Company shall pay a \$5,000 administrative penalty for violating the Unfair Trade Practices Act by using Retirement Annuity # 10573 (9/97).

31. As discussed in Paragraph 14 above, the undersigned adopts the portion of the Report entitled **PERTINENT FACTS OF THE CURRENT EXAMINATION- II. Unfair Trade Practice Violations – 5. Sales Brochure – The Key to Golden Retirement Activity** and the examiner's recommendation contained therein. As more fully described above, the Company shall provide written confirmation that it has ceased using the subject brochure and it shall not utilize similarly misleading materials in the future. Such confirmation shall be provided to the Department no later than December 20, 2004.

32. As more fully discussed above in Paragraph 14, the undersigned finds the use of the chart on the back of brochure #12680 to warrant the imposition of a \$2,000 administrative penalty.

33. As discussed in Paragraph 15 above, discussing the **PERTINENT FACTS OF THE CURRENT EXAMINATION – II. Unfair Trade Practice Violations – 6. Sales Brochure – Equity Indexed Annuity** section of the Report, the Company shall cease using Company insert # 14405 and shall not use unsupportable comparison statistics in the future. Written confirmation of the compliance with this Paragraph, as more fully described in Paragraph 15 above, shall be provided to the Department no later than December 20, 2004.

34. As discussed in Paragraph 15, the Company's use of insert # 14405 warrants the imposition of a \$10,000 administrative penalty.

35. As discussed in Paragraph 16 above, the undersigned adopts the portion of the Report entitled **PERTINENT FACTS OF THE CURRENT EXAMINATION – II. Unfair Trade Practice Violations – 7. Unsuitable Sales.**

36. As more fully discussed in Paragraph 17 above, pertaining to the **III. COMPANY IMPROVEMENTS – 1. Suitability Training** section of the Report, the undersigned adopts this portion of the Report and the examiner's recommendations, subject to the following modifications. Regarding Recommendation No. 8 (Report page 19), the Company shall expand the Needs Assessment form as specifically described and shall confirm in writing that all such "fact finder" forms used in Vermont are similarly revised. Regarding Recommendation No. 9 (Report page 19), the Company shall expand the portion of its producer training concerning assessing affordability of a specific product for a particular prospect, specifically as such training relates to assessing liquidity needs. Regarding Recommendation No. 10 (Report page 19), the Company shall confirm in writing that it has instructed its producers that all product sales must be suitable and that part of a suitability analysis involves assessing benefits lost versus benefits gained. Regarding Recommendation No. 11 (Report page 19), the Company's producers must instruct prospects to consult with their financial advisor prior to purchasing a product or, in the alternative, provide increased training concerning investments which are typically sold or otherwise replaced by a Company product. Written confirmation of compliance with this Paragraph (as more fully explained above in Paragraph 17) shall be provided to the Department no later than December 20, 2004.

37. As discussed in Paragraph 18 above, the undersigned adopts the portion of the Report, including the examiner's recommendations, entitled **COMPANY IMPROVEMENTS - Suitability Questionnaires**, subject to the modifications discussed herein. The Company shall provide the Department with a written description of how it has modified its internal procedures to ensure a manager's signature is obtained on each suitability questionnaire prior to a sale (Recommendation No. 12, Report at page 20). The Company is further ordered to incorporate the four suitability questions into its suitability form (Recommendation No. 13, Report at page 20). The Company shall confirm compliance with this portion of the Order and provide amended forms to the Department for review no later than December 20, 2004.

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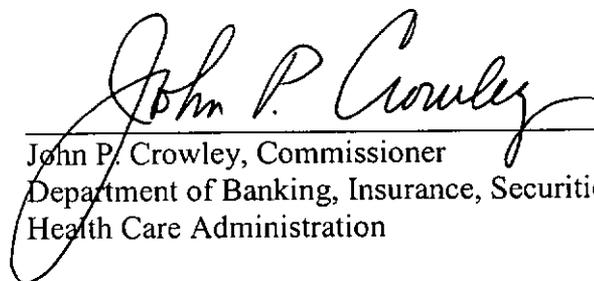
38. All penalties described above shall be paid to the Department no later than 10 days after the expiration of the appeal deadline of this Order, or other administrative or judicial order as appropriate.

**PURSUANT TO 8 V.S.A. § 3574(c), THIS ORDER AND REMEDIAL ACTION SET FORTH HEREIN MAY BE APPEALED TO THE COMMISSIONER BY FILING AN ADMINISTRATIVE APPEAL WITHIN THIRTY (30) DAYS OF THE DATE SET FORTH BELOW. FURTHER REMEDIAL ACTIONS AND PENALTIES ORDERED UPON RECEIPT OF INFORMATION ORDERED HEREIN MAY BE APPEALED WITHIN THIRTY (30) DAYS OF SUBSEQUENT DECISIONS BY THE UNDERSIGNED.**

Dated at Montpelier, Vermont this 20<sup>th</sup> day of October, 2004.

Department of Banking, Insurance,  
Securities and Health Care Administration

By:

  
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John P. Crowley, Commissioner  
Department of Banking, Insurance, Securities and  
Health Care Administration