

DOCKET CLOSING SUMMARY

Docket Number: 04-051-I Date Opened: 11/10/04

Case Name: Lincoln Benefit Life

Your Name: Rebecca Heintz

Type of Matter: market conduct

Statutory Provisions at issue/violated: 8 VSA 4724~~(F)~~,  
subchapter, regulation 91-1315, 8 VSA §3165,  
8 VSA 48311,

Department Final Disposition: Order adopting examination

Order Entry Date: 7/20/05

Sanctions:

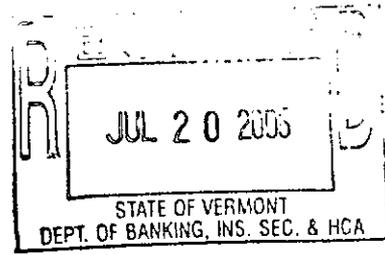
Fine:	\$	<u>\$1,000</u>
Costs:	\$	<u>          </u>
Rescission:	\$	<u>          </u>
Restitution:	\$	<u>          </u>

Other Conditions/Sanctions:  
Some remedial action by October '05

Appeal:  Yes  No

Disposition on Appeal:

Date Closed: 9/2/05



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

In Re: Lincoln Benefit Life  
Company  
NAIC # 65595

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DOCKET NO. 04-051-I

**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. Lincoln Benefit Life Company (the “Company”) is authorized to transact business in Vermont under Foreign Company License No. 1841 P.

3. On December 19, 2003, a final target<sup>1</sup> market conduct examination report was issued by examiners Robbie L. Kriplean and James Montgomery entitled MARKET CONDUCT EXAMINATION REPORT OF LINCOLN BENEFIT LIFE COMPANY LINCOLN, NEBRASKA AS OF AUGUST 31, 2002 BY VERMONT DEPARTMENT OF BANKING, INSURANCE, SECURITIES AND HEALTH CARE ADMINISTRATION (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 Report. The Company submitted a formal response (the "Response") addressing the issues raised in the Report. The Department has undertaken additional investigation, sought additional information from the Company and negotiated with the Company concerning issues contained herein.

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

#### **CONCLUSIONS OF LAW**

6. To the extent comments made by the Company are not discussed below, such comments are expressly rejected by the undersigned. The examiners' Report, including recommendations, is adopted unless noted below.

7. In the CONSUMER COMPLAINTS section of the Report (pages 7 - 8), the examiners note that it appears the Company has not filed annual complaint reports with the Department as required by Regulation 76-1 § 5 from 1999 to 2002.

The examiners reviewed the two complaints which the Company had received during the time period covered by the examination. One of the complaints involved a

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<sup>1</sup> The market conduct examination focused primarily on marketing and sales, claims processing and replacement procedures from January 1, 1999 to August 31, 2002. (Report at page 5.)

woman who had purchased a policy after being quoted a “preferred elite” rate at the time the application was written. However, the Company issued the policy at a higher rate than originally quoted because of medical reasons, and effected the change by means of a Home Office Endorsement. The applicant claimed to have never received a policy and had no way of discovering the increase in premium until the preauthorized premium payment was made by automatic withdrawal from her bank account. The applicant indicated she would not have replaced her existing policy if she had known the premium was going to be higher. However, by the time she made the discovery, the “free look” period had expired. The Company did not provide relief to the complainant.

The examiners note that such a procedure failed to comply with the policy provisions contained in item B. of the **DECLARATIONS** provision of the Company’s application approved by the Department. Failure to comply with filed forms constitutes a violation of 8 V.S.A. § 4724(19). The examiners point out the Company has no procedures in place to obtain a written agreement (as required by the policy language) in every case where a Home Office Endorsement was used to make changes to the benefits, payment class or age at issue (as required by the policy). (Report at page 8.)

The examiners recommend that the Company go back and identify every case where it failed to obtain written consent to changes made by Home Office Endorsements. In instances where such changes were to the insured’s disadvantage, the examiners recommend such insured be provided with the policy for which the insured had originally applied, in addition to compensation for the costs the insured incurred as a result of the unauthorized changes. (Recommendation No. 1, Report at page 21.)

In response, the Company indicates it now requires an “amendment anytime that a rate is changed from the rate applied for by the applicant.” (Response at page 1.) Further, the Company voluntarily completed an internal audit and identified 43 policies in Vermont where a change in rate caused an increase in premium which was issued with an endorsement rather than an amendment. The Company has proposed a remediation program to address the problems associated with these 43 policies. The Department has reviewed this proposed remediation program and approved it.

The undersigned finds that it appears the Company has aggressively addressed the problem discovered by the examiners. The Company has been cooperative with the Department staff in devising a fair and appropriate solution for the impacted policyholders. However, it is unclear that the new procedures proposed in the Response directly addresses the issue identified by the examiners. The Company indicates it will require an “amendment” from the customer “anytime that a rate is changed from the rate applied for by the applicant.” (Response at page 1.) However, what the Company must do to comply with the subject policy language is ensure that a “written agreement” is obtained from the customer if there is a change in “insurance amount, benefits, payment class or age at issue.” The Company shall confirm in writing no later than October 15, 2005, that its proposed change will comply with the policy language. The Company shall further confirm, no later than October 15, 2005, that it has completed the remediation program negotiated with the Department.

Upon consideration, the undersigned finds the discovered violations warrant no penalty. Although the statutes provide for a potentially large penalty in this situation, the

Company has been proactive in seeking to address the outstanding issue and has cooperated with the Department. As such, no penalty is warranted at this time.

8. In the **SALES AND MARKETING – SUITABILITY – Violation with Regulation 88-3 § 3** section of the Report (page 9), the examiners note that although the Company wrote variable life products during the course of the examination, it failed to establish and maintain Standards of Suitability as required by Vermont Regulation I-88-3, Article III, § 3. (Report at page 9.) As such, the examiners recommend the Company establish and maintain such standards. (Recommendation No. 2, Report at page 21.)

In its Response, the Company states it “has established and now maintains a written statement specifying the Standards of Suitability to be used as required by Vermont Regulation” I-88-3, Article III, § 3. (Response at page 1.)

Upon consideration, the undersigned adopts this portion of the Report and the examiners’ recommendation. It is not clear that the Company has adequately complied with the examiners’ recommendation. No later than October 15, 2005, the Company shall provide to the Department for review the Standards of Suitability developed to comply with the Regulation and further indicate how it is monitoring compliance with such standards.

9. In the **SALES AND MARKETING – SUITABILITY – Compliance with Statutes and Regulations Governing Suitability** section of the Report (pages 9 – 10), the examiners note that the Company indicated it did not have a monitoring system in place to ensure that its appointed producer, working through financial services firms, were complying with its suitability standards. The examiners recommend that the Company establish suitability guidelines and procedures for the contracted financial services firms and

establish a monitoring system to ensure that all appointed producers are following these guidelines. (Recommendation No. 3, Report at page 21.)

In its Response (page 1), the Company disputes that it is responsible for ensuring the financial services firms and producers selling its products follow the law.

Nonetheless, the Company indicates that it has implemented new procedures, such as customer surveys for all new customers purchasing through the contracted financial services firms, in order to establish whether the customer and the financial services representative discussed issues pertinent to suitability. (Response at pages 1 – 2.)

Upon consideration, the undersigned adopts this portion of the Report and the examiners' recommendation. The undersigned notes that the Company is mistaken that it has no legal obligation to ensure its appointed producers' compliance with Vermont's suitability guidelines. As an appointed producer selling the Company's products, the Company must ensure that those Company products are only sold when suitable.<sup>2</sup>

Nonetheless, it appears that the Company is taking, or plans on taking, proactive steps to ensure compliance going forward. To that end, the Company is instructed to more fully expand on the explanation provided in its Response to the Department for approval. For example, the Company should provide the Department with a sample of the revised customer survey and written confirmation that such survey is being utilized and results are being actively reviewed by Company personnel. Similarly, the Company shall expand on what it means by "using freelook and complaint reports" to monitor producer

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<sup>2</sup> Whether the Company would have a contractual action for indemnification against the financial services firm arising out of the sale of unsuitable products is a matter of contract law and outside the scope of this exam. However, the existence of a potential cause of action does not insulate the Company from compliance with the laws in the state in which its products are sold.

suitability compliance. Such explanation and confirmation shall be provided to the Department, in writing, no later than October 15, 2005.

10. In the **ADVERTISING** section of the Report (page 10), the examiners note that brochure LBL-2717-Rev. 10/00 states “Preferred loans are at zero net cost.” The examiners indicate that such statement is misleading because loaned portions of the policy earn less interest than unloaned portions of the policy.

In its Response, the Company disputes that the language is misleading, but indicates it has ceased using the brochure in question. (Response at page 2.)

Upon consideration, the undersigned adopts this portion of the Report and the examiners’ recommendation. The Company shall confirm in writing, no later than October 15, 2005 that it will not use the statement “Preferred loans are at zero net cost” in future advertising unless the loaned portion of the policy will earn the same interest as the unloaned portion. The undersigned further concludes that no administrative penalty is warranted under these circumstances.

11. In the **ADVERTISING – Long Term Care** section of the Report (pages 11 – 12), the examiners discuss the Company’s use of the “Think Everyday” FIN 77-2 brochure which includes the statement that 50% of people will spend some portion of time in a nursing home. The examiners note that this statistic is misleading because 50% of the people that will qualify for its long term care product will likely not spend time in a nursing home because the Company underwrites its coverage. Further, the examiners note that this advertising was not filed for approval with the Department. The examiners recommend the Company discontinue use of the subject brochure and other advertising

using similarly misleading wording. The examiners also recommend the Company develop procedures to ensure compliance with Vermont Regulation 91-1 § 15.

In response, the Company disputes the advertising in question is misleading, but indicates that it has discontinued its use. (Response at page 2.)

Upon consideration, the examiner adopts this portion of the Report and the examiners recommendations. No later than October 15, 2005, the Company shall provide a written description of the procedures it has implemented to ensure compliance with Regulation 91-1 § 15.

The undersigned concludes that use of the advertising in question does not warrant imposition of an administrative penalty for the content of the advertising because the undersigned finds the misleading nature of the language was not sufficiently egregious to warrant imposition of a penalty. However, the imposition of a \$1,000 administrative penalty is warranted for the Company's failure to file the advertising with the Department for approval.

12. In the **FAILURE TO PROVIDE SIGNED ILLUSTRATION** section of the Report (page 12) the examiners note that a policy failed to contain the signed illustration form in violation of I-98-1 § 7 D.

The Company does not respond to this section of the Report.

Upon consideration, the undersigned adopts this portion of the Report. However, it appears this was a single oversight and no further action by the Company or penalties are warranted.

13. In the **MARKET VALUE ADJUSTMENTS (MVA)** section of the Report (page 12), the examiners note that in light of the complexity of the MVA product, the Company

should include illustrations with the sales materials which illustrate the range of adjustments that have occurred in the past during differing market conditions.

(Recommendation No. 6, Report at page 21.)

In its Response, the Company indicates that inclusion of sample adjustments “will be considered as marketing materials are revised and developed.” (Response at page 2.)

Upon consideration, the undersigned concludes the product in question is sufficiently complex that such failure to provide illustrations of the product performance may constitute a violation of 8 V.S.A. § 4724(1)(A). The Company shall confirm in writing, no later than October 15, 2005, that it has developed sample illustrations of the MVA product and that such samples will be used to assist customers to understand the product at the time of potential sale.

14. In the **IMPROPER REFERENCE TO SEARS ROEBUCK & COMPANY** section of the Report (page 12), the examiners note that the Company’s individual flexible premium deferred annuity application contains the following statement above the applicant’s signature: “I am a customer of Sears, Roebuck & Company or one of its subsidiaries or affiliates.” This language was originally developed and used for group products covering Sears customers, but has been used for other products. The examiners recommend the Company amend its application forms by deleting the reference to Sears.

(Recommendation No. 7, Report at page 22.)

In its Response, the Company indicates it “is in the process of amending its application forms to delete the reference to Sears & Roebuck” and that such applications shall be filed with the Department for approval. (Response at page 2.)

Upon consideration, the undersigned adopts this portion of the Report and the examiners' recommendation. Despite the Company's claims that it is "in the process" of amending its forms, the Department has no record of any such filings. The Company shall provide to the Department for approval, no later than October 15, 2005, form filings seeking to remove inappropriate references to Sears Roebuck. It is the position of the undersigned that such amendment should be a priority to be accomplished as promptly as reasonably possible.

15. In the **REPLACEMENTS** section of the Report (pages 14-16), the examiners discuss a variety of violations of Vermont's replacement regulations.<sup>3</sup> The examiners recommend that the Company review its procedures so as to ensure compliance with the replacement regulations and take care to list only replacement transactions in its replacement register. (Recommendations Nos. 8 and 9, Report at page 22.)

In its Response, the Company indicates that replacement "procedures have been validated and quality checks have increased to assure that replacement regulations are followed" and that it has "reviewed its process to assure that only replacement policies are listed in the replacement register." (Response at page 3.)

Upon consideration, the undersigned adopts this portion of the Report and the examiners' recommendations. The Company has indicated it is complying with the examiners' recommendations and no additional action is necessary.

16. In the **CLAIMS PROCEDURES AND PROCESSING** portion of the Report (page 17), the examiners note that of the five paid life claim files during the examination period, three of them were not paid in compliance with 8 V.S.A. § 3665 in that interest was not

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<sup>3</sup> For policies issued prior to March 1, 2002, the examiners reviewed compliance with Vermont Replacement Regulation I-88-2. For policies issued after that date, the examiners assessed compliance with Vermont's current replacement regulation, Regulation I-2001-3.

paid as required. The examiners recommend the Company revise its claims processing procedures so as to comply with 8 V.S.A. § 3665. (Recommendation No. 10, page 22.)

In its response, the Company indicates that it finds 8 V.S.A. § 3665 somewhat ambiguous, but has nonetheless compensated the three policyholders noted in the exam and revised its claims payment procedures effective February 2, 2003.

Upon consideration, the undersigned adopts this portion of the Report, including the examiners recommendations. It appears the Company has complied with the recommendations and no additional action is necessary. In light of the Company's proactive steps to rectify the claims payment problems discovered by the examiners, the undersigned concludes an administrative penalty is not warranted.

17. In the **PRODUCER LICENSING** section of the Report, the examiners note one instance where a producer solicited Company business before being appointed.

In response, the Company notes that under current law, effective July 1, 2002, producers did not need to be licensed or appointed to solicit business. The Company states it is "currently following the licensing and appointment requirements" which are presently effective.

The undersigned expressly rejects the Company's interpretation of current Vermont insurance producer licensing laws. All persons must be licensed as producers prior to any solicitation. Further, to the extent an individual is holding him or herself out as an agent of the Company, that individual must be appointed by the Company.

8 V.S.A. § 48131.

The undersigned adopts this portion of the Report. The Company shall confirm in writing to the Department no later than October 15, 2005 that it is complying with

Vermont licensing laws and that it has revised its procedures to the extent necessary to correct its misinterpretation of the law.

18. In the **INTERNAL AUDITS** portion of the Report (page 19), the examiners note that although the Company provided them with a list of all internal audits conducted by the Company, the Company declined to provide the actual audit results. The Company based this refusal on the work product doctrine, the attorney-client privilege and the “insurance compliance self-evaluative privilege.” (Report at page 19.) The examiners recommend Department counsel review the Company’s stated grounds for refusal.

The Company does not respond to this portion of the Report.

Upon consideration, the undersigned adopts this portion of the Report. The undersigned notes that additional facts other than those provided in the Report would be required to support the Company’s assertion that such audits are not subject to review.<sup>4</sup> As the Company must be aware, the work product doctrine only prevents the disclosure of documents prepared in anticipation of litigation. Further, the attorney client privilege does not apply in all situations where an action involves counsel. Finally, as of yet there is no such thing as the “insurance compliance self-evaluative privilege” in Vermont. Nonetheless, the Department has no interest in discouraging any effort taken by insurers to candidly assess compliance with the law. To that end, the undersigned does not request additional information. The examiners reviewed the list of self audits and nothing contained on that list appeared sufficiently relevant to the examiners to further pursue the issue with the Company. It should be noted for future reference that the

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<sup>4</sup> It is possible such additional information was provided to the examiners who note “The Company also included a more detailed discussion of their position as summarized above.” (Report at page 19.)

examiners and the Department have the authority to treat such documents as confidential and exempt from public disclosure. *See, e.g.*, 8 V.S.A. §3574(d)(4).

19. In the **FINES, PENALTIES & FORFEITURES** section of the Report (page 20), the examiners note the Company failed to file a list of reportable actions for 1999, 2000 and 2001 as required by Bulletin 30. The examiners note that a review of regulatory actions against the Company during the time period does not indicate any consistent pattern or intentional or serious consumer abuse.

The Company does not respond to this section of the Report.

The undersigned adopts this portion of the Report. The undersigned further orders the Company to provide written confirmation that it has implemented procedures to ensure future compliance with Bulletin 30. Such confirmation shall be provided no later than October 15, 2005.

### **ORDER**

20. The Report is adopted in its entirety without modification unless expressly stated to the contrary herein.

21. As discussed more fully in Paragraph 7 above, the Company shall complete its remediation program and confirm in writing, no later than October 15, 2005, that it has done so. Further, the Company will provide a written confirmation that the proposed procedural changes will comply with the policy language as discussed above. Such confirmation shall be provided no later than October 15, 2005.

22. As more fully discussed in Paragraph 8 above, no later than October 15, 2005, the Company shall provide the Department with the Standards of Suitability required by I-

88-3, Article III, § 3, and shall further provide a written explanation of how it is monitoring compliance with the Standards of Suitability.

23. As more fully discussed in Paragraph 9 above, the Company shall provide to the Department, for review and approval, no later than October 15, 2005, an expanded explanation of the procedures it has implemented, or intends to implement, to ensure that Company products sold through financial services firms are only being sold when the sale is suitable for the needs of the purchaser.

24. As more fully discussed in Paragraph 10 above, the Company shall provide the Department with written verification no later than October 15, 2005 that it will not use the statement "Preferred loans are at zero net cost" in future advertising unless such statement is accurate, as described in Paragraph 10 above.

25. As discussed in Paragraph 11 above, addressing the **ADVERTISING – Long Term Care** section of the Report, the Company shall provide for the Department's review and approval, a written description of the procedures in place to ensure compliance with Regulation 91-1 § 15. Such description shall be provided no later than October 15, 2005.

26. As discussed in Paragraph 11 above, the Company's failure to file its long-term care advertisement for approval warrants the imposition of a \$1,000 administrative penalty.

27. As discussed in Paragraph 13 above, addressing the **MARKET VALUE ADJUSTMENTS** section of the Report, the Company shall provide the Department with confirmation no later than October 15, 2005 that it has developed sample illustrations for use with the MVA product and will be using those illustrations in the sale of the MVA product.

28. As discussed above in Paragraph 14, discussing the **IMPROPER REFERENCE TO SEARS ROEBUCK & COMPANY** section of the Report, the Company shall file amended forms for review removing any inappropriate references to Sears Roebuck no later than October 15, 2005.

29. As discussed above in Paragraph 17, the Company shall confirm in writing to the Department no later than October 15, 2005 that it is complying with Vermont's licensing laws and that it has revised its procedures to the extent necessary to correct its previous misinterpretation of the law relating to producer licensing.

30. As discussed above in Paragraph 19, the Company shall provide the Department with written confirmation that it will implement procedures to ensure future compliance with the Department's Bulletin 30. Such confirmation shall be provided no later than October 15, 2005.

31. All penalties described above shall be paid to the Department no later than ten 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**

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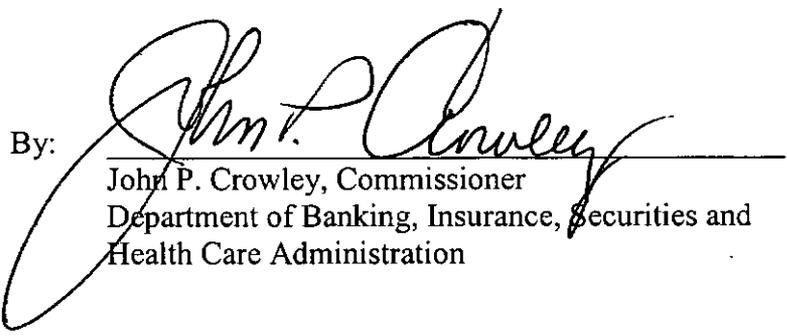
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**THIRTY (30) DAYS OF THE DATE SET FORTH BELOW. FURTHER  
REMEDIAL ACTIONS AND PENALTIES ORDERED UPON RECEIPT OF  
INFORMATION ORDERED HEREIN MAY BE APPEALED WITHIN THIRTY  
(30) DAYS OF SUBSEQUENT DECISIONS BY THE UNDERSIGNED.**

Dated at Montpelier, Vermont this 20<sup>th</sup> day of July, 2005.

Department of Banking, Insurance,  
Securities and Health Care Administration

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