

MARKET CONDUCT EXAMINATION REPORT

of

**THE MANUFACTURERS LIFE INSURANCE COMPANY
(U.S.A.)**

of

BLOOMFIELD HILLS, MICHIGAN

As of

December 31, 2003

By

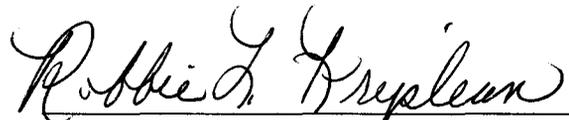
**VERMONT DEPARTMENT OF BANKING,
INSURANCE, SECURITIES AND HEALTH CARE
ADMINISTRATION**



CERTIFICATION

James R. Montgomery III, AIE, FLMI, MAAA, Robbie L. Kriplean, CIE, AIRC and Jennifer E. Greenway, AIRC participated in this examination.

I, Robbie L. Kriplean, CIE, AIRC, being duly sworn, do hereby affirm that the foregoing report of the Market Conduct Examination of the Manufacturers Life Insurance Company (U.S.A.) is true and correct to the best of my knowledge and belief.


Robbie L. Kriplean, CIE, AIRC

Notary Seal

Subscribed and sworn to before me this 4th day of October, 2005.


NOTARY PUBLIC

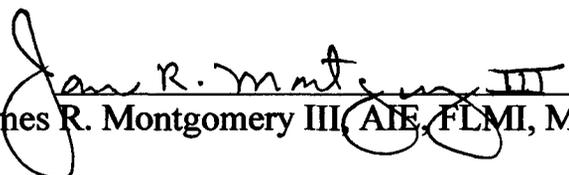


My commission expires 5/5/09

CERTIFICATION

James R. Montgomery III, AIE, FLMI, MAAA, Robbie L. Kriplean, CIE, AIRC and Jennifer E. Greenway, AIRC participated in this examination.

I, James R. Montgomery III, AIE, FLMI, MAAA, being duly sworn, do hereby affirm that the foregoing report of the Market Conduct Examination of the Manufacturers Life Insurance Company (U.S.A.) is true and correct to the best of my knowledge and belief.


James R. Montgomery III, AIE, FLMI, MAAA

Notary Seal

Subscribed and sworn to before me this 13 day of October, 2005.


NOTARY PUBLIC

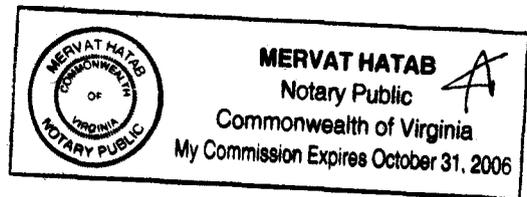
 **Jamie White**
Commission # DD475111
Expires September 22, 2009
Bonded Troy Fain - Insurance, Inc. 800-385-7019

CERTIFICATION

James R. Montgomery III, AIE, FLMI, MAAA, Robbie L. Kriplean, CIE, AIRC and Jennifer E. Greenway, AIRC participated in this examination.

I, Jennifer E. Greenway, being duly sworn, do hereby affirm that the foregoing report of the Market Conduct Examination of the Manufacturers Life Insurance Company (U.S.A.) is true and correct to the best of my knowledge and belief.


Jennifer E. Greenway, AIRC



Notary Seal

Subscribed and sworn to before me this 12th day of October, 2005.

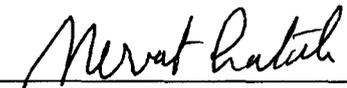

NOTARY PUBLIC

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October 6, 2005

**The Honorable John Crowley
Commissioner
Vermont Department of Banking, Insurance,
Securities and Health Care Administration
89 Main Street, Drawer 20
Montpelier, Vermont 05620**

Dear Commissioner Crowley:

Pursuant to your instructions and in compliance with the provisions of 8 V.S.A. § 3565 et seq. and procedures promulgated by the National Association of Insurance Commissioners, an examination of the market conduct activities has been conducted of:

The Manufacturers Life Insurance Company (U.S.A.), NAIC # 65838

**Mail Address:
P.O. Box 640
Buffalo, New York 14201-0640**

**Statutory Home Office:
38500 Woodward Avenue
Bloomfield Hills, Michigan 48304**

**Main Administrative Office:
200 Bloor Street East
Toronto, Ontario, Canada M4W 1E5**

The report thereon, as of December 31, 2003, is respectfully submitted.

FOREWORD

This target market conduct examination report is written generally by exception and additional practices, procedures and files subject to review during the examination were omitted from the report if no improprieties were observed.

The Manufacturers Life Insurance Company (U.S.A.) is referred to throughout this report as the “Company” or “Manulife (U.S.A.)”, unless specifically mentioned by name. The Vermont Department of Banking, Insurance, Securities and Health Care Administration is referred to as the “Department” or the “Vermont Department”.

The Company’s responses, with respect to the findings of this examination, will be made available upon written request to the Vermont Department.

The examiners wish to acknowledge the exceptional cooperation of the Company’s Director & U.S. Division Compliance Coordinator, Ingrid Bastaldo, in facilitating the examination process.

SCOPE OF EXAMINATION

EXAMINATION AUTHORITY

The examination of The Manufacturers Life Insurance Company (U.S.A.) was conducted pursuant to applicable Vermont statutes and regulations.

TIME FRAME

The examination generally covers the period from January 1, 2001 through December 31, 2003.

SAMPLING METHODOLOGY

The examiners used random sampling techniques, utilizing ACL software.

EXAMINATION SITUS

The Company's statutory home office is located at, 38500 Woodward Avenue, Bloomfield Hills, Michigan 48304; however, this examination was conducted entirely off-site. Information, documents and other materials were provided directly to the examiners in hard copy and/or computer diskettes.

MATTERS EXAMINED

- Replacements
- Claims administration

PREVIOUS EXAMINATIONS

PRIOR REPORT SUMMARY AND CONCLUSIONS

The Vermont Department did not conduct an examination of the Company during the last five years.

EXECUTIVE SUMMARY

Replacements

The reviews by the examiners revealed a total of ninety (90) violations of replacement regulations. The types of reviews and nature of the various violations are described in detail below and in the text of this report. It should be noted that the absence of a replacement form from a file results in multiple violations of the regulations.

The examiners' review of replacement files revealed a total of seventy-four (74) violations, in the annuity files, out of forty-six (46) life and annuity files reviewed. There were nineteen (19) annuity files having at least one (1) violation, which represents 41% of the total replacement files reviewed. The violations which appeared most frequently were violations of Regulation 2001-3 § 3 B and § 5 A (1). Regulation 2001-3 § 3 B requires a notice signed by both the applicant and producer attesting that the notice has been read aloud by the producer or that the applicant did not wish the notice to be read aloud. Regulation 2001-3 § 5 A (1) requires the Company to verify that the required forms were received and are in compliance with the regulation.

In eleven (11) instances on annuity contracts (24% of the files reviewed) the Company failed to provide contract owners with notices advising them of their right to return the contract within thirty (30) days of delivery and receive a refund as required by Regulation 2001-3 § 5 A (4). While the Company did furnish "free look" notices, such notices provided for ten (10) or twenty (20) days rather than the required thirty (30) days. Since there is no way of determining how many of these persons would have availed themselves of this opportunity had they been aware of the full thirty (30) days in which to do so, the examiners are recommending that the Company offer them a new "free look" period equal to the difference between thirty (30) days and the ten (10) or twenty (20) days they were originally allowed. Such premium refunds would be as described in the text of this report.

The examiners conducted an additional review consisting of a sample of fifty (50) annuity files and thirty-three (33) life insurance files for a total sample of eighty-three (83) files of contracts/policies issued during the examination period for compliance with Regulation 2001-3, which became effective on March 1, 2002, or Regulation 88-2, which was in effect prior to that date.

There was a total of sixteen (16) miscellaneous violations out of the total sample of eighty-three (83) files reviewed. Ten (10) of the files had at least one violation. The various types of violations are described in the body of this report.

In view of the large percentage of violations identified in the annuity files, the examiners recommend that the appropriate staff, including producers, be re-trained regarding compliance with the requirements of Regulation 2001-3. The examiners further

recommend that the Company assign, to one or more responsible persons, specific accountability for the review of every annuity replacement file and responsibility for completing and signing a checklist before each file is finally closed.

During the examination process the Company's response to the examiners' criticisms was as follows:

Corrective Action: The Annuity Operations will make the necessary enhancements to their current procedures/training material to facilitate compliance with Regulation 2001-3. Applicable staff will be reminded and re-educated regarding the importance of compliance with the requirements of Regulation 2001-3 to avoid future clerical errors. When required, forms under Regulation 2001-3 will be reviewed to ensure they are received in good order and at the time the application is taken. When applicable, we will ensure that a signed statement regarding existing policies or contract is obtained.

There was one instance described in the report where the Company refunded \$128,929.25 under the "free look" provision of an annuity contract. The examiners contend that the Company should have refunded \$136,498.53 (a difference of \$7,569.28) inasmuch as the contract was never delivered to the applicant and therefore never became effective.

Claims Administration

The Company's system for a closed block of claims (Claim Unit 2) does not identify the state of issue in all cases. Thus, the examiners have recommended that the Company go back and verify the state of issue for these claims so as to make accurate information available to the Vermont Department.

The examiners reviewed all of the claims which the Company stated were paid during the examination period. Initially, the examiners were furnished eighteen (18) claim files, of which ten (10) were disallowed as the state of issue was not Vermont. Five (5) of the remaining eight (8) files, i.e. 62.5%, contained violations involving the payment of insufficient interest on death claims. The Company became aware of its failure to pay Vermont's statutorily required rate of 6% interest on "some of the claims" as stated in the Company's preliminary examination data response dated February 20, 2004. Corrective action was taken March 24, 2004, in that the Company paid the affected beneficiaries the balance of interest owing including the penalty rate of 12%.

Additionally, the Company's written procedures did not reflect the penalty rate of 12% in the event a claim was not paid within thirty (30) days of receipt of proof of loss per 8 V.S.A. § 3665 (d). Further, a chart provided to the examiners, which displays the Company's claim payment history with respect to the interest rate applied to death claims proceeds, shows that from January 1, 1987 until January 26, 2004, the interest rate paid on death claims was less than 6%, in violation of 8 V.S.A. § 3665 (c) (2).

The Company stated that they have undertaken efforts to correct their practices and written procedures so as to bring them into compliance with Vermont statutes and regulations.

The examiners pointed out to the Company that their reporting of death claims contained some errors in their Annual Statements (as explained in the report) for the years 2001 and 2003. The Company indicated that they have called this to the attention of the appropriate employees and enhanced their valuation systems so as to avoid future discrepancies.

COMPANY PROFILE

HISTORY

Manulife (U.S.A.) is a wholly owned subsidiary of The Manufacturers Investment Corporation, which is an indirect wholly owned subsidiary of The Manufacturers Life Insurance Company, Ontario, Canada, which in turn is a wholly owned subsidiary of Manulife Financial Corporation.

Manulife (U.S.A.) was incorporated on September 6, 1955, under the laws of Maine as the Maine Fidelity Life Insurance Company and commenced business on January 31, 1956. The present title was adopted in 1990 and in 1992 the Company was redomesticated to Michigan.

As a result of a corporate reorganization, the business of two other companies of the Manulife group in the United States were transferred to the Company on January 1, 2002.

The Company is licensed to transact business in the District of Columbia and all states except New York, in addition to Guam, Puerto Rico and the U.S. Virgin Islands.

STATUTORY HOME OFFICE

38500 Woodward Avenue
Bloomfield Hills, Michigan 48304

MAIN ADMINISTRATIVE OFFICE

200 Bloor Street East
Toronto, Ontario, Canada M4W 1E5

VERMONT REPORTED PREMIUMS

Direct written premiums in Vermont for the years indicated are as follows:

	2001	2002	2003
Ordinary Life	4,688,789	4,752,073	5,201,738
Individual Annuities	0	10,027,761	7,527,505
Group Annuities	0	33,365,165	38,449,464
Other	26,928,864*	0	0
Totals	31,617,653	48,144,999	51,178,707

* The considerations reported by the Company as "Other" for 2001 were reported as group annuities for 2002 and 2003. The Company informed the examiners that these are group annuity contracts of their Group Pensions Department sold to trustees of profit-sharing and pension plans qualified under Section 401 (a) of the Internal Revenue Code or to trustee eligible deferred compensation plans of state and local governments described in s. 457 of the Internal Revenue Code.

(I) REPLACEMENTS

The examination period for this report runs from January 1, 2001 to December 31, 2003. Vermont Regulation 2001-3 became effective on March 1, 2002, and replaced Regulation 88-2, which was in effect prior to that time. Tests were performed in order to determine compliance with these regulations as described below.

(A) REPLACEMENT REVIEW

The Company's replacement register contained a total of fifteen (15) individual life policies and a total of forty-four (44) individual annuity contracts, which were subject to the review. This test was conducted by reviewing all of the files listed in the replacement register, except for those which were duplicates of files contained in the issued life and annuity sample.

The following chart (Chart I) identifies violations of Vermont's replacement regulations. The numbers in the right hand column represent violations of various sections of the replacement regulations, which are keyed to the Legend immediately following the chart. The Legend contains citations to the various sections of the regulations in addition to a brief description of each type of violation.

CHART I

Violations from replacement sample:

Annuity Replacements

Contract Number	Violations (Numbers are keyed to legend)
2279999	1,2,3,4,6
2280709	3
2284754	1,3,5,6 Outdated Repl. Form
2284757	1,3,5,6 Outdated Repl. Form
2284758	1,3,5,6 Outdated Repl. Form
2286188	1,2,3,4,6
2279126	1,2,3,4,6
2283414	1,5,6 New York Repl. Form
2288873	1,2,3,4,6
2286186	1,2,3,4,6

2283412	1,5,6	New York Repl. Form
2283413	1,5,6	New York Repl. Form
2283565	1,3,4,5,6	Outdated Repl. Form
2295077	1,2,3,4,6	
2312193	1,2,4,6	
8007655	4	
2335931	1,2,4,6	
8011504	1,4,5,6	Outdated Repl. Form
2348286	1,2,4,6	

LEGEND

- 1** Failure to verify that the required forms were received and are in compliance with the Regulation- Reg. 2001-3 § 5 A (1).
- 2** Unable to produce copies of the notification of replacement- Reg. 2001-3 § 5 A (3).
- 3** Failure to provide to the contract owner notice of the right to return the contract within thirty (30) days of the delivery of the contract and receive an unconditional full refund of all premiums or in the case of variable contracts, a payment of the cash surrender value provided under the contract plus fees and other charges-Reg. 2001-3 § 5 A (4).
- 4** No evidence that the producer provided a signed statement identifying any preprinted or electronically presented company approved sales materials used- Reg. 2001-3 § 3 E or a statement that the producer used only company-approved sales materials-Reg. 2001-3 § 5 C (1).
- 5** Notice does not conform to Reg. 2001-3 (Appendix A).
- 6 *** No notice signed by both applicant and producer attesting that the notice has been read aloud by the producer or that the applicant did not wish the notice to be read aloud-Reg. 2001-3 § 3B.
- *** This violation is under *Duties of Producers* in the Reg.

(1) Summary of Violations

It can be determined from Chart I that there was a total of seventy-four (74) violations out of forty-six (46) replacement files reviewed. This is an average of 1.60 violations per replacement. There were nineteen (19) files having at least one (1) violation, which represents forty-one (41) percent of the forty-six (46) total replacement files reviewed.

The types of violations which appear most frequently in Chart I are those designated by the numbers "1" and "6". These two (2) types of violations appear a total of seventeen (17) times each.

It should be noted that the absence of a replacement form from a file results in multiple violations of the regulations.

(2) Violations of Regulation 2001-3 § 5 A (1)

Number "1" denotes violations of Regulation 2001-3 § 5 A (1) from annuity files, indicating that the Company failed to verify that the required forms were received and were in compliance with the Regulation. Although, in some cases, the Company was able to furnish notes indicating that the agent was contacted for Vermont replacement paperwork, the fact that required documents are missing from the files serves as prima facie evidence that the Company's verifications were not adequate to satisfy the requirement of Regulation 2001-3 § 5 A (1).

(3) Violations of Regulation 2001-3 § 3 B

The type of violations designed by the number "6" represent instances where the Company's files did not contain a notice signed by both the applicant and the producer, attesting that the notice has been read aloud by the producer or that the applicant did not wish to have the notice read aloud (Reg. 2001-3 § 3 B).

(4) Recommendation

In view of the large percentage of violations identified in the annuity files, the examiners recommend that the appropriate staff, including producers, be re-trained regarding compliance with the requirements of Regulation 2001-3. The examiners further recommend that the Company assign, to one or more responsible persons, specific accountability for the review of every annuity replacement file and responsibility for completing and signing a checklist before each file is finally closed.

During the examination the Company's response to the examiners' criticisms was as follows:

Corrective Action: The Annuity Operations will make the necessary enhancements to their current procedures/training material to facilitate compliance with Regulation 2001-3. Applicable staff will be reminded and re-educated regarding the importance of

compliance with the requirements of Regulation 2001-3 to avoid future clerical errors. When required, forms under Regulation 2001-3 will be reviewed to ensure they are received in good order and at the time the application is taken. When applicable, we will ensure that a signed statement regarding existing policies or contracts is obtained.

(5) Right to Return Contracts

Chart I also shows that there were eleven (11) instances where the Company failed to provide the contract owners with notices advising them of their right to return the contract within thirty (30) days of delivery and receive a refund as required by Regulation 2001-3 § 5 A (4). This represents 24% of the replacement files reviewed.

While the Company did furnish “free look” notices in these eleven (11) instances, the notices provided “free look” periods of less than the required thirty (30) days. In some cases the period was only ten (10) days and others showed twenty (20) days.

There is no way of determining which of these persons, if any, would have returned their contracts for a refund of premiums had they been notified of the proper thirty (30) day “free look” period required by Regulation 2001-3 § 5 A (4). In the interest of making these persons whole, the examiners recommend that they be afforded a new “free look” period equal to thirty (30) minus the number of days that they were originally afforded. During the new “free look” period they should be allowed an opportunity to return their contracts and receive refunds as prescribed by the regulation. For example, if the contract were a variable annuity issued with an original ten (10) day “free look” period, the annuitant should be granted a new twenty (20) day period during which he or she could return the contract and receive the full current cash surrender provided under the contract plus surrender charges and any other fees or charges.

The Company stated that contracts issued after August 1, 2002, did provide the appropriate thirty (30) day “free look” to applicants for replacement policies.

(B) ISSUED LIFE AND ANNUITY REVIEW

The tests performed by the examiners involved reviewing a sample of fifty (50) annuity files, out of a population of three hundred and seventy (370) and all the issued life policies, which was a total of thirty-three (33). The samples represented those policies/contracts that were issued within the examination period and were reviewed for compliance with Vermont Regulation 2001-3, effective on March 1, 2002, or Regulation 88-2, which was in effect prior to that time.

The following chart (Chart II) identifies violations of Vermont's replacement regulations. The numbers in the right hand column represent violations of various sections of the replacement regulations, which are keyed to the Legend immediately following the chart. The Legend contains citations to the various sections of the regulations in addition to a brief description of each type of violation.

Chart II

Violations from issued life and annuity sample:

Issued Annuities

Contract Number	Violations (Numbers are keyed to legend)
2317524	4
2279998	1,2,3,5,6
2304910	3
2304146	1,2,6
2313007	5
2321135	3
8007656	6
2341102	3

Issued Life

Policy Number	Violations (Numbers are keyed to legend)
58916438	7
59005942	7

LEGEND

- 1 Failure to verify that the required forms were received and are in compliance with the Regulation- Reg. 2001-3 § 5 A (1).
- 2 Unable to produce copies of the notification of replacement- Reg. 2001-3 § 5 A (3).
- 3 No statement signed by both the applicant and the producer as to whether the applicant has existing policies or contracts-Reg. 2001-3 § 4 C.
- 4 Failure to have applicant and producer sign the notice regarding replacements **at the time the application is taken**- Reg. 2001-3 § 3 B.
- 5 Failure to provide to the contract owner notice of the right to return the contract within thirty (30) days of the delivery of the contract and receive an unconditional full refund of all premiums or in the case of variable contract, a payment of the cash surrender value provided under the contract plus fees and other charges-Reg. 2001-3 § 5 A (4).
- 6 No evidence that the producer provided a signed statement identifying any preprinted or electronically presented company approved sales materials used- Reg. 2001-3 § 3 E or a statement that the producer used only company-approved sales materials-Reg. 2001-3 § 5 C (1).
- 7 No signed statement by the agent as to whether replacement is involved – Reg. 88-2 § 6 A (2).

(1) Summary of violations

Chart II reflects that there were a total of sixteen (16) violations out of eighty-three (83) files reviewed. There were ten (10) files having at least one (1) violation.

(2) Violations of Regulation 88-2 § 6 A (2)

Two (2) violations of Regulation 88-2 § 6 A (2), which are cited in Chart II and designated as “7” on the Legend, are instances where the life files did not contain a signed statement by the agent as to whether replacement is involved. These violations were cases in which the agent neglected to answer the questions on the agent’s section of the application which reads: *To the best of your knowledge, is this insurance intended to replace, or will it cause a change in, or involve a loan under any insurance or annuity policy on the life of any Proposed Life Insured or in any insurance or annuity policy owned by the Owner?*” Regulation 88-2 § 6 A (2) requires “a signed statement as to whether the agent or broker knows replacement is or may be involved in the transaction”.

The Company contends that, although the agent failed to answer the replacement question on the “Agent’s Statement” portion of the application, the agent signed the application in which the applicant answered the replacement question, therefore they did not violate the regulation.

By signing the application, the agent was not signing any stated assertions. The signed statement concerning replacement, pursuant to the regulation, is contained in the “Agent’s Statement” section of the application. Since this question was not answered in these two (2) instances, these cases represent violations of Regulation 88-2 § 6 A (2).

(3) Violations of Regulation 2001-3 § 5 A (4)

Chart II also shows that there were two (2) instances where the Company failed to provide the contract owners with notices advising them of their right to return the contract within thirty (30) days of delivery and receive a refund pursuant to Regulation 2001-3 § 5 A (4). While the Company did furnish “free look” notices in these two (2) instances, the notices provided “free look” periods of less than the required thirty (30) days. As discussed in this section of the report, under the heading, (A) (5) “**Right to Return Contracts**”, in the interest of making those persons whole, the examiners recommend that they be afforded a new “free look” period equal to thirty (30) minus the number of days that they were originally afforded. During the new “free look” period they should be allowed an opportunity to return their contracts and receive refunds prescribed in the regulation.

As previously mentioned, the Company asserted that their annuity operations made the necessary procedural changes, in conformity with the requirements of Regulation 2001-3 § 5 A (4), to provide the full thirty (30) day “free look” to applicants of replacement policies after August 1, 2002.

(4) Recommendation

As also stated in the section entitled **Replacement Review**, in view of the large percentage of violations identified in the annuity files, the examiners recommend that the appropriate staff, including producers, be retrained regarding compliance with the requirements of Regulation 2001-3. The examiners further recommend that the Company assign, to one or more responsible persons, the specific responsibility for reviewing every annuity replacement file and completing and signing a checklist before each file is finally closed. Company verification is specifically required by Regulation 2001-3 § 5 A (1) as discussed above.

The Company responded that all applicable staff will be reminded and re-educated regarding the importance of compliance with the requirements of Regulation 2001-3 to avoid future clerical errors. When required, forms under Regulation 2001-3 will be reviewed to ensure they are received in good order and at the time the application is taken. When applicable we will ensure that a signed statement regarding existing policies or contracts is obtained.

(C) REVIEW OF “FREE LOOK” POLICY FILES

The examiners found one instance where the Company returned \$7,569.28 less than the applicants were entitled. The circumstances surrounding this case are explained below.

The Company was asked to furnish copies of the policies and/or contracts that were returned during the “free look” period pursuant to Regulation 2001-3 § 5 A (4). Included in the Company’s response was a copy of the file on annuity contract# 2287854 for which a husband and wife applied for a “Venture Vantage” annuity contract on May 6, 2002. This was to be a replacement of their annuity with another life insurance company.

On May 30, 2002, a check in the amount of \$81,398.53 was issued to Manulife (U.S.A.) by the other company for crediting to the new annuity. The applicants sent a separate check to Manulife, in the amount of \$57,500 on June 6, 2002. Thus, the total amount of the deposit paid to Manulife (U.S.A.) toward the annuity for which the applicants applied was \$138,898.53.

On July 15, 2002, the applicants wrote to the Company indicating that they still had not received an annuity contract and requested their money back. They further stated that they were informed that the contract had a seven-year (7) surrender charge period, which they subsequently learned was for nine years (9).

On August 5, 2002, the agent admitted in writing that he still had the contract even though he had previously claimed to have delivered it to the applicants back in June. The agent further stated to the Company “I will straighten out this mess. Sorry for the problem.”

The applicants had elected an “income plan” option on their application whereby they were to receive monthly withdrawals of their contract value in the amount of \$1,200.00 per month. The Company did make two such withdrawals and transferred a total of \$2,400.00 to the applicants by electronic funds transfer.

On August 13, 2002, the Company issued a check to the applicants in the amount of \$128,929.25. This was \$7,569.28 less than the \$138,898.53 that they had paid for the annuity contract, less the \$2,400.00, which had been withdrawn.

The Company contends that the fact that the agent had not delivered the contract does not void the contract. However, the examiners maintain that since the agent had not delivered the contract it was never binding.

The Company explained that they were unable to determine when the “free look” period began because the agent failed to deliver the contract. They decided to permit the applicants to exercise their right to return the policy under the “free look” provision of the contract and refunded to them the value of the contract on July 16, 2002 (\$135,179.68) less the bonus enhancements added to the contract by the Company (6,250.43). The right to return the contract as explained in Regulation 2001-3 § 5 A (4) begins after delivery of the policy. Therefore, since the contract was never delivered, it was never binding and the “free look” period never commenced. Regulation 2001-3 § 5 A (4) would not apply when determining the amount due to the applicants.

The Company maintains that the contract was “constructively delivered to the Contract Owners by virtue of delivery to the agent”. This would be true if the agent was an agent of the contract owners, but the agent is an agent of the Company. Therefore, the policy was never delivered to the applicants.

As mentioned, the applicants had elected an “income plan” option on their application whereby they received monthly withdrawals from their contract value in the amount of \$1,200.00 per month. The Company had made two such withdrawals and transferred a total of \$2,400.00 to the applicants by electronic funds transfer. The Company pointed out that the applicants exercised their rights under the contract by electing a partial surrender of \$2,400.00. However, since the Company set up these automatic withdrawals pursuant to an option elected by the applicants at the time of their original application, such payments could not represent acceptance of the contract by the applicants by virtue of exercising their rights under the contract

The Company also asserts that if one of the contract owners had died after the contract was issued but before delivery could occur, the Company would have paid any death claim payable under the contract. Although the examiners have no reason to believe that the Company would not have paid a death claim in this situation, their contention is purely hypothetical and has no bearing on whether a valid contract was established. Furthermore, the Company states that the contract became effective immediately upon issuance of the policy documents. The examiners contend that a valid contract requires

mutual assent. In this case, the applicants had never even seen the policy since it was never delivered. The Company cannot bind the applicants to a contract without allowing them to see the contract.

Since the contract was never delivered to the applicants, it could not have been legally binding, in which case the applicants should have received a full refund of their deposit of \$138,898.53 that they had paid to the Company, less the \$2,400.00 which had been withdrawn.

The examiners recommend that the Company return the additional \$7,569.28 to which the applicants are entitled.

(II) CLAIMS PROCEDURES AND PROCESSING

(A) CLAIMS PROCESSING UNITS

The Company's life claims are processed through two (2) separate units and are identified as Claims Unit 1-Individual Life Claims and Claims Unit 2-Closed Block of Individual Life Claims.

Claims Unit 1

Claims Unit 1 processes the Company's life claims through its customer service center in Buffalo, NY.

Claims Unit 2

On December 30, 1982, the Manufacturers Life Insurance Company acquired control of Maine Fidelity Life Insurance Company and continued to carry on business under the name of Maine Fidelity Life Insurance Company until July 31, 1990 when its name was changed to The Manufacturers Life Insurance Company (U.S.A.). Effective May 3, 1994, Manulife (U.S.A.) entered into service and indemnity coinsurance agreements with Protective Life Insurance Company under which Protective Life assumed, on a 100% indemnity coinsurance basis, a closed block of Manulife (U.S.A.) individual life policies (previously Maine Fidelity). Pursuant to the terms of the agreement, Protective Life assumed responsibilities for the full servicing of the insurance policies ceded by Manulife (U.S.A.), including the claims handling function. Therefore, Claims Unit 2 processes claims pursuant to the closed block of life policies described above, through "Life Benefits", a division of Protective Life Insurance Company, located in Brentwood, Tennessee.

(B) REVIEW OF INDIVIDUAL PAID LIFE CLAIMS

(1) Issue State

The examiners requested a listing of all the individual life claims which were paid during the examination period (There were no reported group life claims). Upon review of the claim files, it was determined that a revised listing was in order, as half the claims from Unit 1 and Unit 2 represented policies that were not issued in Vermont and therefore, not subject to the review. The revised listing from Unit 2 again contained discrepancies in that the heading entitled "Issue State" indicated that the issue state was Vermont, however, the manual review of the claim files contained policies that were not issued in Vermont. The Company responded that "if there is no issue state field on the system" the Company would default to the policyholder's current state of residence as the issue state. Thus, it is possible that claims subject to Vermont law were not included in the listing

and therefore not reviewed for compliance with appropriate Vermont statutes and regulations.

It is recommended that the Company go back and verify the state of issue for the closed block of business (Claim Unit 2), so that accurate information would be available to the Vermont Department.

(2) Violations of 8 V.S.A. § 3665 (c) (2)

Subsequently, the examiners reviewed all the claims that the Company stated were paid during the examination period. Initially, the examiners were furnished eighteen (18) claim files, of which ten (10) were disallowed as the state of issue was not Vermont (Refer to the preceding discussion). It should be noted that five (5) of the eight (8) claim files subject to the review contained violations of Vermont statutes as described below.

The following table identifies claims which were found to be in violation of 8 V.S.A. §3665 (c) (2):

Policy #	Comments
24600801	Did not apply 6% interest as required by 8 V.S.A. § 3665 (c) (2)
51195204	Did not apply 6% interest as required by 8 V.S.A. § 3665 (c) (2)
M10994618 **	The numbers of days used in the calculations were incorrect. The Company paid interest based on 17 days, but should have paid interest based on 20 days. Date of death: 12-19-01, check date 1-7-02 (20 days)
26015875	Did not apply 6% interest as required by 8 V.S.A. § 3665 (c) (2)
17700659	Did not apply 6% interest as required by 8 V.S.A. § 3665 (c) (2)

It should be noted that the Company became aware of its failure to pay Vermont’s statutorily required rate of 6% interest on “some of the claims” as stated in the Company’s preliminary examination data response dated February 20, 2004. The Company added that corrective action would be taken in that the Company would pay the balance of interest owing the affected beneficiaries along with the penalty rate of 12% interest. This was accomplished on March 24, 2004.

****** The Company was criticized for incorrectly calculating the number of days used in applying the death claim interest for policy #M10994618. The Company stated in response to the examiners' criticism on July 22, 4002, that "A check will be issued to the beneficiary for an additional 3 days interest."

(C) NON-COMPLIANCE OF WRITTEN PROCEDURES & PRACTICES

As previously discussed under section **II (B) (2) Violations of 8 V.S.A. § 3665 (c) (2)**, the Company's response to a preliminary examination data request dated February 20, 2004, revealed the Company's failure to comply fully with 8 V.S.A. § 3665.

In addition to the violations of 8 V.S.A. § 3665 (c) (2), as detailed in the referenced section, the Company's written procedures did not reflect the penalty rate of 12% in the event a claim is not paid within thirty (30) days of receipt of proof of loss, contrary to 8 V.S.A. § 3665 (d). The Company stated in the February 20, 2004, response that going forward claim procedures would reflect the 12% penalty rate. In a letter dated July 22, 2004, the Company provided an exhibit containing the revised procedures which reflect compliance with Vermont statutes and regulations. The revision is dated July 19, 2004.

Additionally, the Company furnished charts displaying its claim payment history with respect to the interest rate applied to death claim proceeds from January 1, 1987, through January 26, 2004, in response to the preliminary data request dated February 20, 2004. The chart for Claim Unit 1 indicates that from January 1, 1987 until January 26, 2004, the death claim interest rate was less than 6% in violation of 8 V.S.A. 3665 (c) (2). The chart for Claims Unit 2 (Closed Block of Individual Life (effective April 1, 1994) reflects that the correct rate of 6.00% interest was paid from April 1, 1994 to current date. A copy of the chart for Claim Unit 1 is duplicated below.

Claims Unit 1-Individual Life and Group Life Business:

Period	Death Claim Interest Rate
Jan 1, 1987 to Dec 31, 1992	5.50%
Jan 1, 1993 to Mar 14, 2003	3.50%
Mar 15, 2003 to June 30, 2003	2.10%
July 1, 2003 to Jan 25, 2004	1.80%
Jan 26, 2004 to Current date	6.00%

The Company added in their response, that "the appropriate claims procedures have been revised to ensure the correct rate of interest will be applied to comply with Vermont regulations."

The examiners recommend that the Company go back as far as the Vermont Department deems appropriate and perform an audit of individual life claims in order to ensure that the statutorily required rate of 6% interest was afforded to each of the beneficiaries.

(D) DEATH CLAIMS REPORTING

Vermont Reported Death Benefits Paid (Individual Life)

Year	Death Benefits
2001	44,690
2002	121,087
2003	635,392

The examiners observed an irregularity with the Company's Annual Statements' Exhibits (Direct Business in the State of Vermont) for the years 2001 and 2003. The reported paid death claims and the reported incurred death claims could not be reconciled.

The death benefits paid during 2001 as shown above, were \$44,690, whereas the incurred death claims were reported as only \$16,295 and there was no amount shown as unpaid at December 31 of the prior year. The Company responded that four (4) claims totaling \$28,584 from Claim Unit-2 Closed Block of Individual Life, had been "inadvertently left out". Further, the Company added that appropriate employees have been reminded about the inclusion of information of those policies serviced by Protective Life.

Similarly, in the Exhibit for the year 2003, the death benefits paid during the year were reported as \$635,392, whereas the incurred death claims were reported to be only \$320,392 again with no amounts reported as unpaid at December 31 of the prior year. The Company stated that the incurred death claims failed to include a \$315,000 claim because the policy was originally issued in New Jersey (See the following discussion of the Company's method of reporting death claims). The Company further stated that they have enhanced their valuation systems so the applicable numbers for the current state of residence can be reported to avoid future discrepancies.

The Company's method of reporting death benefits paid and incurred on the State Pages are based upon the payee's current state of residence at the time the benefit is paid. Thus, for accounting data in the State Pages, the Company allocates business to each state using the same method as in Schedule T, which is generally according to the current residence of the policy owner.

(E) UNCLAIMED FUNDS/CLAIMS PROCEDURES

The examiners inquired as to whether the Company had formal written procedures by which they could identify those policies where the insured may not be living and for which no claim had been filed. For example, situations where the policy had been paid up and on the books for an unusually long period of time and those cases where the insured has attained, or would have attained if he or she were living, the limiting age under the mortality table on which the reserve is based. Refer to 27 V.S.A. § 1210.

The Company responded, at the inception of the examination, that while Claims Unit 1 did not have a formal written procedure in place, they relied on any return/undelivered mail resulting from the annual mailing of policyholders' annual statements to begin a search process. Additionally, "If the insured is no longer alive, it is hoped that the anniversary statement would prompt the filing of a death claim. There have been no resulting situations for Vermont insureds."

Further, the Company stated that effective July 7, 2004, formal written procedures were implemented and added to their claims manual (Claims Unit 1). The examiners reviewed the exhibits provided, which represent the newly implemented procedures, and concluded that they are in compliance with 27 V.S.A. § 1210 (Vermont's Unclaimed Property Laws).

SUMMARY OF RECOMMENDATIONS

1.

Pages 10-12 & 14-17

In view of the large percentage of violations of replacement regulations identified in the annuity files, the examiners recommend that the appropriate staff, including producers, be re-trained regarding compliance with the requirements of Regulation 2001-3. The examiners further recommend that the Company assign, to one or more responsible persons, specific accountability for the review of every annuity replacement file and responsibility for completing and signing a checklist before each file is finally closed.

2.

Pages 13 & 16

It is recommended that those persons whose policies were replaced and who were notified of "free look" periods less than thirty (30) days be afforded a new "free look" period equal to thirty (30) days minus the number of days that they were originally afforded during the new "free look" period. They should be allowed an opportunity to return their contracts and receive refunds prescribed in the regulation.

3.

Pages 17-19

In view of the fact that annuity contract # 2287854 was never delivered to the applicants, the Company should refund the additional amount of \$7,569.28 to which the applicants are entitled.

4.

Pages 20 & 21

It is recommended that the Company go back and verify the state of issue for the closed block of business (Claim Unit 2), so that accurate information would be available to the Vermont Department.

5.

Pages 21, 22 & 23

The examiners recommend that the Company go back as far as the Vermont Department deems appropriate and perform an audit of individual life claims in order to ensure that the statutorily required rate of 6% interest was afforded to each of the beneficiaries.