



State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

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Sean Dilweg, Commissioner

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Notice of Adoption and Filing of Examination Report

Take notice that the proposed report of the market conduct examination of the

AMERICAN FAMILY LIFE INSURANCE COMPANY  
6000 AMERICAN PKY  
MADISON WI 53783

dated NOVEMBER 6, 2009, and served upon the company on SEPTEMBER 10, 2010, has been adopted as the final report, and has been placed on file as an official public record of this Office.

Dated at Madison, Wisconsin, this 6TH day of OCTOBER, 2010:

Sean Dilweg  
Commissioner of Insurance

**STATE OF WISCONSIN  
OFFICE OF THE COMMISSIONER OF INSURANCE  
MARKET CONDUCT EXAMINATION**

**OF**

**AMERICAN FAMILY LIFE INSURANCE COMPANY  
MADISON, WISCONSIN**

**OCTOBER 19 - NOVEMBER 6, 2009**

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State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

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November 6, 2009

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Honorable Sean Dilweg  
Commissioner of Insurance  
Madison, WI 53702

Commissioner:

Pursuant to your instructions and authorization, a targeted market conduct examination was conducted October 19 to November 6, 2009 of:

AMERICAN FAMILY LIFE INSURANCE COMPANY  
Madison, Wisconsin

and the following report of the examination is respectfully submitted.

#### I. INTRODUCTION

American Family Life Insurance Company was incorporated on November 21, 1957 and received its certificate of authority from the state of Wisconsin on December 30, 1957. American Family Life Insurance Company is domiciled in the state of Wisconsin. American Family Life Insurance Company is a stock company, wholly owned by American Family Mutual Insurance Company, a multiple-line carrier formed in 1927 through its downstream holding company, AmFam Incorporated. The holding company, AmFam Inc was formed by American Family Mutual for the purpose of holding the stock of the American Family subsidiaries, which in addition to American Family Life Insurance Company, includes the property/casualty insurers American Standard Insurance Company of Wisconsin, American Standard Insurance Company of Ohio and American Family Insurance Company. Collectively, American Family Mutual Insurance Company and subsidiaries are known as the American Family Mutual Insurance Group.

American Family Life Insurance Company's operations are conducted through the parent company's field management personnel on a state director and district manager basis through approximately 4,000 multiple-line exclusive agents. The company markets participating whole life, term life, fixed and variable universal life and fixed and variable annuity products. American Family Life Insurance Company also writes structured settlement business and small amounts of group life insurance which is issued to American Family Mutual Insurance Company employees. During the Office of the Commissioner of Insurance's (OCI's) last market conduct examination in February, 2000, American Family Life Insurance Company indicated that it was phasing out of the credit life and disability insurance business. According to the company's annual reports in 2008 and 2007, the company did not report any business in credit life and disability insurance

American Family Life Insurance Company first began marketing variable life and annuity products in September of 2000. As of May 29, 2009, American Family Life Insurance Company no longer solicited and sold new variable products. The company doesn't plan to relinquish its authority to issue variable products as it may engage in future sales of variable products if future economic conditions warrant.

The company obtained its license in Georgia in 2008 to bring the states it is licensed to write in to 27 states.

The following table summarizes the total direct national premium written in 2008 and 2007 as compared it to the total direct premium written in Wisconsin.

### National Direct Business to Wisconsin Direct Business Summary

| 2008                                |                         |                        |                    |                      |                          |
|-------------------------------------|-------------------------|------------------------|--------------------|----------------------|--------------------------|
|                                     | Life Insurance Premiums | Annuity Considerations | Deposit Type Funds | Other Considerations | Total (Sum of 4 Columns) |
| Wisconsin                           | \$ 69,843,259           | \$ 7,645,338           | \$ 2,244,725       | \$ 0                 | \$ 79,733,322            |
| National                            | \$ 372,462,344          | \$ 41,284,091          | \$ 2,244,725       | \$ 0                 | \$ 415,991,160           |
| <i>Wisconsin As a % of National</i> | <i>18.75%</i>           | <i>18.52%</i>          | <i>100%</i>        | <i>0%</i>            | <i>19.17%</i>            |
|                                     |                         |                        |                    |                      |                          |
| 2007                                |                         |                        |                    |                      |                          |
|                                     | Life Insurance Premiums | Annuity Considerations | Deposit Type Funds | Other Considerations | Total (Sum of 4 Columns) |
| Wisconsin                           | \$ 70,318,158           | \$ 9,231,928           | \$ 4,553,615       | \$ 0                 | \$ 84,103,701            |
| National                            | \$ 369,769,907          | \$ 48,907,400          | \$ 4,553,615       | \$ 0                 | \$ 423,230,922           |
| <i>Wisconsin As a % of National</i> | <i>19.02%</i>           | <i>18.88%</i>          | <i>100%</i>        | <i>0%</i>            | <i>19.87%</i>            |

In 2008 and 2007, American Family Life Insurance Company had premium written in life insurance and annuity business. The majority of the premium written by the company in 2007 and 2008 was life insurance. The company's ranking of market share in Wisconsin for 2008 was third with a 3.5% share of the market. In 2008, American Family Life Insurance Company ranked as the 77<sup>th</sup> writer of annuities in the state of Wisconsin and held a 0.1% share of the market. In 2007, the company ranked as the third writer of life insurance with a market share of 3.3%. For annuity business in 2007, the company ranked 64<sup>th</sup> in Wisconsin and held a 0.2 % share of the market.

The following tables summarize the company's Wisconsin premium written and benefits paid for 2008 and 2007, broken down by line of business.

**Wisconsin Life Insurance Business**

| 2008  | Ordinary     | Credit Life | Group       | Industrial | Total        |
|---|--------------|-------------|-------------|------------|--------------|
| <b>Direct Premiums &amp; Annuity Considerations</b> |              |             |             |            |              |
| Life Insurance                                      | \$67,653,661 | -           | \$2,189,598 | -          | \$69,843,259 |
| Annuity Considerations                              | \$ 7,645,338 | -           | \$0         | -          | \$ 7,645,338 |
| Deposit Type Funds                                  | \$ 2,244,725 | -           | -           | -          | \$ 2,244,725 |
| Other Considerations                                | -            | -           | -           | -          | -            |
| Total (Sums of Lines 1 to 4)                        | \$77,543,724 | -           | \$2,189,598 | -          | \$79,733,322 |
| <b>Direct Claims &amp; Benefits Paid</b>            |              |             |             |            |              |
| Death Benefits                                      | \$17,386,904 | -           | \$1,051,500 | -          | \$18,438,404 |
| Annuity Benefits                                    | \$ 2,589,764 | -           | \$0         | -          | \$2,589,764  |
| All Others  | \$28,196,079 | -           | \$0         | -          | \$28,196,079 |
| Totals  | \$48,172,747 | -           | \$1,051,500 | -          | \$49,224,247 |

| 2007  | Ordinary     | Credit Life | Group       | Industrial | Total        |
|---|--------------|-------------|-------------|------------|--------------|
| <b>Direct Premiums &amp; Annuity Considerations</b> |              |             |             |            |              |
| Life Insurance                                      | \$66,497,065 | -           | \$3,821,093 | -          | \$70,318,158 |
| Annuity Considerations                              | \$ 9,231,928 | -           | \$0         | -          | \$ 9,231,928 |
| Deposit Type Funds                                  | \$ 4,553,615 | -           | -           | -          | \$ 4,553,615 |
| Other Considerations                                | -            | -           | -           | -          | -            |
| Total (Sum of Lines 1 to 4)                         | \$80,282,608 | -           | \$3,821,093 | -          | \$84,103,701 |
| <b>Direct Claims &amp; Benefits Paid</b>            |              |             |             |            |              |
| Death Benefits                                      | \$16,127,168 | -           | \$1,604,000 | -          | \$17,731,168 |
| Annuity Benefits                                    | \$ 2,317,061 | -           | \$0         | -          | \$ 2,317,061 |
| All Others  | \$29,750,469 | -           | -           | -          | \$29,750,469 |
| Totals  | \$48,194,698 | -           | \$1,604,000 | -          | \$49,798,698 |

The amount of ordinary life insurance premiums written in 2008 increased by \$1,156,596 over the amount written in 2007. However, the amount of annuity considerations decreased from 2007 to 2008 by \$1,586,590.

The Office of the Commissioner of Insurance received 16 complaints against the company between January 1, 2007 through August 31, 2009. A complaint is defined as 'a written communication received by the Commissioner's Office that indicates dissatisfaction with an insurance company or agent. The following table categorizes the complaints received

against the company by type of policy and complaint reason. There may be more than one type of coverage and/or reason for each complaint. Ten of the 16 complaints were policyholder service related and involved policy change delays, failure to promptly respond to inquiries, premium notice/billing problems and/or cancellation/nonrenewal problems.



### Complaints Received

| As of August 20, 2009 |       |            |              |            |                   |            |        |            |                      |            |       |            |
|-----------------------|-------|------------|--------------|------------|-------------------|------------|--------|------------|----------------------|------------|-------|------------|
| Reason Type           | Total |            | Underwriting |            | Marketing & Sales |            | Claims |            | Policyholder Service |            | Other |            |
|                       | No.   | % of Total | No.          | % of Total | No.               | % of Total | No.    | % of Total | No.                  | % of Total | No.   | % of Total |
| Life                  |       | %          |              | %          |                   | %          |        | %          |                      | %          |       | %          |
| Individual Life       | 4     | 100%       |              | %          |                   | %          |        | %          | 4                    | 100%       |       | %          |
| Group Life            |       | %          |              | %          |                   | %          |        | %          |                      | %          |       | %          |
| Individual Annuity    |       | %          |              | %          |                   | %          |        | %          |                      | %          |       | %          |
| Group Annuity         |       | %          |              | %          |                   | %          |        | %          |                      | %          |       | %          |
| Credit Life           |       | %          |              | %          |                   | %          |        | %          |                      | %          |       | %          |
| All Others            |       | %          |              | %          |                   | %          |        | %          |                      | %          |       | %          |
| Total                 | 4     | 100%       |              |            |                   |            |        |            | 4                    | 100%       |       |            |

| 2008               |       |            |              |            |                   |            |        |            |                      |            |       |            |
|--------------------|-------|------------|--------------|------------|-------------------|------------|--------|------------|----------------------|------------|-------|------------|
| Reason Type        | Total |            | Underwriting |            | Marketing & Sales |            | Claims |            | Policyholder Service |            | Other |            |
|                    | No.   | % of Total | No.          | % of Total | No.               | % of Total | No.    | % of Total | No.                  | % of Total | No.   | % of Total |
| Life               |       | %          |              | %          |                   | %          |        | %          |                      | %          |       | %          |
| Individual Life    | 7     | 100%       | 4            | 100%       |                   | %          |        | %          | 3                    | 100%       |       | %          |
| Group Life         |       | %          |              | %          |                   | %          |        | %          |                      | %          |       | %          |
| Individual Annuity |       | %          |              | %          |                   | %          |        | %          |                      | %          |       | %          |
| Group Annuity      |       | %          |              | %          |                   | %          |        | %          |                      | %          |       | %          |
| Credit Life        |       | %          |              | %          |                   | %          |        | %          |                      | %          |       | %          |
| All Others         |       | %          |              | %          |                   | %          |        | %          |                      | %          |       | %          |
| Total              | 7     | 100%       | 4            | 57%        |                   |            |        |            | 3                    | 43%        |       |            |

| 2007               |       |            |              |            |                   |            |        |            |                      |            |       |            |
|--------------------|-------|------------|--------------|------------|-------------------|------------|--------|------------|----------------------|------------|-------|------------|
| Reason Type        | Total |            | Underwriting |            | Marketing & Sales |            | Claims |            | Policyholder Service |            | Other |            |
|                    | No.   | % of Total | No.          | % of Total | No.               | % of Total | No.    | % of Total | No.                  | % of Total | No.   | % of Total |
| Life               |       | %          |              | %          |                   | %          |        | %          |                      | %          |       | %          |
| Individual Life    | 5     | 100%       | 2            | 100%       |                   | %          |        | %          | 3                    | 100%       |       | %          |
| Group Life         |       | %          |              | %          |                   | %          |        | %          |                      | %          |       | %          |
| Individual Annuity |       | %          |              | %          |                   | %          |        | %          |                      | %          |       | %          |
| Group Annuity      |       | %          |              | %          |                   | %          |        | %          |                      | %          |       | %          |
| Credit Life        |       | %          |              | %          |                   | %          |        | %          |                      | %          |       | %          |
| All Others         |       | %          |              | %          |                   | %          |        | %          |                      | %          |       | %          |
| Total              | 5     |            | 2            | 40%        |                   |            |        |            | 3                    | 60%        |       |            |

## II. PURPOSE AND SCOPE

The examination was conducted to determine compliance with recommendations made in OCI's previous market conduct examination dated February 2, 2000, and to determine whether the company's practices and procedures comply with the Wisconsin insurance statutes and rules. The examination focused on the period from January 1, 2007 through August 31, 2009. In addition, the examination included a review of any subsequent events deemed important by the examiner-in-charge during the examination.

Legislation, which went into effect on November 1, 2004, pertaining to the suitability of annuity sales required that the sale of an individual annuity to a person age 65 and older be suitable for the consumer based on the person's financial situation and needs. The law, s. 628.347, Wis. Stat., was amended effective October 1, 2008, to apply to the sale of an individual annuity to a person of any age. The law requires an insurer to establish and maintain a system to supervise the recommendations of its insurance producers.

In addition to determining compliance with recommendations made in the previous market conduct examination, the examination was conducted to determine whether the company has sufficient oversight and supervisory control over the company's appointed agents, as required by s. 628.347, Wis. Stat., to ensure that annuity sales to consumers are appropriate and suitable for their needs.

The examination covered individual life and individual annuity business in Wisconsin and included a review of company operations & management, marketing, sales & advertising, policy forms, policyholder service and complaints, producer licensing, and underwriting which includes new business, replacement business and suitability.

The report is prepared on an exception basis and comments on those areas of the company's operations where adverse findings were noted.

### III. PRIOR EXAMINATION RECOMMENDATIONS

The previous market conduct examination of the company, as adopted February 2, 2000, contained 15 recommendations. Following are the recommendations and the examiners' findings regarding the company's compliance with each recommendation.

#### Agents

1. It is recommended American Family Life increase the exchange of information between the agent data base at the agency services department and the CyberLife system at American Family Life to a daily basis. This increase in the exchange of information must be an automatic exchange between the two systems and not depend on a manual system.

**Action:** Compliance

#### Marketing, Sales & Advertising

2. It is recommended American Family Life require its agents to submit their personal web sites for approval by the company prior to use as required by s. Ins 2.16 (29) (b), Wis. Adm. Code, and that the company maintain a copy of such advertisements in its advertising file as required by s. Ins 2.16 (30), Wis. Adm. Code.

**Action:** Compliance

3. It is recommended American Family Life include a notation of the extent of distribution in the individual advertisement files as required by s. Ins 2.16 (30), Wis. Adm. Code.

**Action:** Compliance

4. It is recommended American Family Life clearly identify on its brochures and advertisements which products are offered only through American Family Life in compliance with s. Ins 2.16 (5), Wis. Adm. Code.

**Action:** Compliance

5. It is recommended American Family Life include a form number on each published advertisement as required by s. Ins 2.16 (28), Wis. Adm. Code.

**Action:** Compliance

6. It is recommended American Family Life give a separate and unique form number to each advertisement created by an individual agent as required by s. Ins 2.16 (28), Wis. Adm. Code.

**Action:** Compliance

7. It is recommended American Family Life keep a notation in the web site's advertising file indicating the form number of the policy advertised on the company's web site as required by s. Ins 2.16 (30), Wis. Adm. Code.

**Action:** Compliance

### **Policy Forms**

8. It is recommended American Family Life revise and refile with the Office of the Commissioner of Insurance for approval within 30 days of the adoption of this report, language in American Family Life's individual life applications, form numbers L-51E (WI) Ed. 1/99, L-51 (WI) Ed. 6/98, L-52 (WI) Ed. 6/98, L-447 Ed. 8/84, and L-10426 Ed. 3/87 to comply with s. 631.90, Wis. Stat., and s. Ins 3.53, Wis. Adm. Code, which pertain to AIDS questions, and to comply with s. 631.20, Wis. Stat., with respect to other questions on the applications.

**Action:** Compliance

### **Policyholder Service & Complaints**

9. It is recommended American Family Life respond to complainants on complaints received from Office of the Commissioner of Insurance within 10 days as requested in the OCI 51-11 letter.

**Action:** Compliance

### **Underwriting**

10. It is recommended American Family Life develop procedures to ensure that the company's agents follow the company's own written procedures which requires an agent to complete a replacement form prior to taking an application and then send the replacement form along with the application to the company, if replacement is involved, as required by s. Ins 2.07 (4) (b), Wis. Adm. Code, and that American Family Life secure a properly completed replacement form with the application prior to commencing any underwriting as required by s. Ins 2.07 (5) (a) 4a, Wis. Adm. Code.

**Action:** Compliance

11. It is recommended American Family Life require its agents to use the Wisconsin replacement form as specified in s. Ins 2.07 (3) (b), Wis. Adm. Code, for Wisconsin business, and that the company obtains the correct replacement form with the application as required by s. Ins 2.07 (5) (a) 4a, Wis. Adm. Code.

**Action:** Compliance

12. It is recommended American Family Life as required by s. Ins 2.07 (5) (a), Wis. Adm. Code, develop procedures to inform and ensure that its agents answer the agent's replacement question on the application, sign and date the application by the agent replacement question, properly complete the replacement form prior to taking an application, and submit it to the company with the application, and keep a copy in their file, as required by s. Ins 2.07 (4), Wis. Adm. Code.

**Action:** Compliance

13. It is recommended that American Family Life develop procedures to ensure that it obtains both the applicant's and the agent's statements regarding whether replacement is involved as required by s. Ins 2.07 (5) (a) 1, Wis. Adm. Code.

**Action:** Compliance

14. It is recommended American Family Life develop procedures to ensure that notification is provided to the other insurance company of the replacement or possible replacement within 5 calendar days of receipt of the application and prior to commencing any underwriting as required by s. Ins 2.07 (5) (a) 4b, Wis. Adm. Code.

**Action:** Compliance

15. It is recommended American Family Life develop procedures to ensure its agents give a copy of the Wisconsin Notice and Consent for Human Immunodeficiency Testing form to the person who signed it as required by s. Ins 3.53 (4) (c), Wis. Adm. Code.

**Action:** Compliance

#### IV. CURRENT EXAMINATION FINDINGS

##### **Company Operations and Management**

The examiners reviewed the company's response to the company operations and management interrogatory.

American Family Life Insurance Company is a member of the Insurance Marketplace Standards Association (IMSA). American Family Life Insurance Company became a member of IMSA in 1997. The company recertified in 2001, 2004, and 2007.

American Family Life Insurance Company first began marketing variable life and annuity products in September of 2000. American Family Life Insurance Company marketed its variable products through American Family Securities, LLC. The company marketed two variable products, a variable universal life insurance policy and a variable annuity. On May 12, 2009, American Family Life Insurance Company informed its field agents who are registered representatives with its affiliated broker-dealer, American Family Securities that it will cease solicitation and sale of new variable products in 2009. As of May 29, 2009, American Family Life Insurance Company ended the solicitation and sale of new variable products in all states except Idaho, Nevada, South Dakota and Utah. All sales efforts in the remaining four states ceased on September 30, 2009. The company doesn't plan to relinquish its authority to issue variable products as it may engage in future sales of variable products if future economic conditions warrant. American Family Life Insurance Company is working with the Financial Industry Regulatory Authority (FINRA) to de-register agents who are currently registered representatives. The company expects the de-registration to be completed by the end of 2009. American Family Securities, in coordination with FINRA, has established a Securities Service Center which is based at American Family Life Insurance Company's home office. The Securities Service Center is staffed by registered representatives who took over the duties currently performed by the field agents. As the field agents are de-registered, their customers

will be transferred to the Securities Service Center for servicing. The Securities Service Center will not market new products and will not be responsible for servicing any non-variable product. In addition, American Family Life Insurance Company began in-house administrative servicing of variable products after eight years of using a third-party vendor.

American Family Life Insurance Company has a non-marketing third-party administrator agreement with Alliance-One Services, Inc. and its parent company, Computer Sciences Corporation. Alliance-One Services, Inc. provides the automated workflow and record-keeping systems used by American Family Life Insurance Company for all of its variable universal life and variable annuity policy files and Alliance-One Services will also continue to process the daily trades within American Family Life Insurance Company's various sub-accounts as initiated by the policyholders. American Family Life Insurance Company has a contract with Alliance-One Services, Inc. through March 31, 2013.

The examiners reviewed six internal audits done between April, 2007 and July, 2009. No significant findings were noted in the examiners' review of the internal audit reports. American Family Life Insurance Company has an Internal Audit Department which assists the Audit Committee and management of American Family Mutual Insurance Company by identifying and analyzing major risks throughout the organization and identifying and evaluating the related internal controls.

Audits in the form of investigations of potential agent misconduct or fraud, including possible financial improprieties, are handled by the Corporate Compliance Department which is headed by the Compliance and Ethics Director. The Compliance Department investigates all allegations or concerns of wrongdoing which are initiated as a result of concerns identified by District Managers or referred by the Consumer Affairs Department, which handles consumer complaints. The Corporate Legal Department is consulted during the course of these investigations. After completing the investigation, the Compliance Department prepares written

findings of its investigations and a determination is made on what, if any, action is taken against the agent.

The company monitors NILS, which offers daily updates on the state and federal insurance laws via email and over the web, on a weekly basis for newly enacted laws, regulations and bulletins, and determines if applicable to the company. Once a law or regulation is found to be applicable to the company, a rough draft of the Compliance Mandate Impacts & Solutions and Mandate Procedure Document, that incorporates the new law or regulation into company policy and procedures, is referred to the core life mandate team to finalize the draft. Once the draft is finalized, a release is sent to the appropriate areas of the company and to the field force concerning the impacts of the mandate and the effective date. The company is also notified of changes in the insurance laws and regulations through ACLI alerts and the company's internal Government Affairs and Corporate Legal departments.

No exceptions were noted.

### **Marketing, Sales & Advertising**

The Marketing Division in American Family Mutual Insurance Company is responsible for marketing, sales and advertising for American Family Life Insurance Company. The Marketing Division is made up of the following departments: Advertising, Digital Marketing, Customer Experience and Satisfaction, Planning and Administration, Consumer and Market Research, Customer Relationship Marketing, Market Development, Strategy and Integration, and Product Portfolio Marketing.

The Advertising Department is responsible for the creation of advertising, maintenance and management of the existing advertising and the advertising files, and administration of agent advertising programs. Digital Marketing is responsible for the amfam.com website, developing and executing e-commerce objectives by providing tools and best practices to connect with customers, the district managers' and agents' websites and



position agents as local trusted advisors and deploy tactics that drive prospects directly to agents. The Customer Experience and Satisfaction Department provides input to help improve the customer's experience, develops and provides programs for employees and agents on behaviors and activities that increase customer satisfaction, and analyzes a wide variety of customer satisfaction data to look for ways for improvement. The Planning and Administration Department leads the divisional business planning and manages the execution of the Marketing Plan and is the Marketing division's liaison to the Corporate Compliance Department. Consumer and Market Research is responsible for the analysis of research data and identifying opportunities for improvement, provides insights, recommendations and answers to business questions based on research data, and measures customer satisfaction with company products, service and processes. The Customer Relationship Marketing Department develops personalized marketing strategies for prospective and current customers to increase business growth, develops, produces and distributes direct marketing programs, manages the agent marketing web portal through which agents purchase direct marketing programs, advertising and other promotional items such as key chains, pens etc. to market their agencies, and develop and implement events, sponsorships of events or other personalized marketing activities for American Family Mutual Insurance Company. The Market Development, Strategy and Integration Department is responsible for developing and implementing programs that help agents market locally; implementing, administering and measuring promotional programs, awards and sales campaigns; and develops market plans and programs that help expand the company's market presence and growth in designated multicultural markets. The Product Portfolio Department develops and implements the company's corporate product strategy, designs and implements new products, and monitors the company's corporate existing products. The Agency Sales department within the Executive Administration Division is responsible for the management of agent contracts, appointments and terminations. The Life Sales Support Team within the company's Life Division is staffed by a group of individuals with

advanced life expertise. The Life Sales Support Team provides field management and agents with life insurance technical expertise and sales support through an internal sales support hotline, occasionally will visit agents in the field and host videoconferences and teleconferences with field management and agents.

The Customer Relationship Marketing Department sends direct mail pieces to policyholders that have American Family Insurance to solicit leads. The policyholders may or may not have life insurance with American Family Life Insurance Company. American Family Mutual Insurance Company also provides agents with a number of direct marketing materials that can be ordered and mailed to policyholders and prospects. The agent's name and telephone number are on the direct marketing items for the policyholder or prospect to call or the policyholder or prospect can respond by returning the business reply card. If the policyholder or prospect returns the business reply card, the business reply card is sent to a vendor, Progressive Impressions International. Progressive Impressions International tracks and distributes the leads to the agents. In addition, the Customer Relationship Marketing Department collects leads at the various events in which American Family Insurance participates. The company has a specific lead card which is to be used at all local agent and corporate events. All lead cards completed are separated and the top copy is given to the agents who worked the event. This will allow the agents an opportunity for follow-up. The bottom copy is sent to Data Dimensions, the vendor the company has contracted with to do data entry and storage of the lead cards. After the data is entered, Data Dimensions sends the data back to the company so that the leads can be sent back out to the agents who worked the event for additional follow-up if desired. Once data is a year old, Data Dimensions will notify American Family Mutual Insurance Company to determine if the leads should be continued to be stored or if the leads can be destroyed. Data Dimensions will not destroy any lead cards without prior permission from American Family Mutual Insurance Company. The final source of leads is through the company's website by indicating the prospect's interest on an online "Quote

Request Form". The prospect can choose a particular agent to whom the lead is to be sent, or can ask the system to assign an agent. Once the form is completed and submitted, the lead is sent to the American Family Mutual Insurance Company's Agency Notification System. The agent receives an email to check the Agency Notification System which will then provide the lead information. The Agency Notification System is an internal system with no vendor involvement.

American Family Mutual Insurance Company has two advertising filing systems. Most company provided advertisements are paper files and the agent custom advertisements, policyholder newsletter and website advertisement use an electronic advertising review and tracking system. The paper advertising files are organized by line of business and then the unique ad identification number. Current advertising files are located in the Advertising Department. Older and obsolete files are sent to American Family Mutual Insurance Company's Records Retention Department. Paper advertising files are kept for a minimum of 10 years. Agent created advertisements, Policyholder Newsletter and website advertisements have electronic advertising files. American Family Mutual Insurance Company's electronic ad tracking system assigns a unique advertising identification number to each advertisement and the electronic files are organized by number. The system also captures data fields such as agent name, agent/district code, line of business being advertised, states in which the item will be used, media type and approval status. The required documentation for a life and annuity electronic advertising tracking file is the same as for the paper advertising file.

American Family Mutual Insurance Company has company approved American Family Life Insurance advertisements that agents are encouraged to use. To use company pre-approved advertisements, the agent goes to the agent's company website, chooses the advertisement and the agent's personal information is automatically added to the advertisement. The advertisement can't be changed or altered in any way. At any time, the company can run a report on an advertisement to determine how much the advertisement is used, by whom and

where the advertisement was used. However, if an agent has a need to create his/her own advertisement, company policy requires that the agent submit the proposed advertisement to the Advertising Department for review and approval before using the advertisement. To encourage the use of company approved advertisements, American Family Insurance offers a local media reimbursement advertising program for agents that offers a 50% reimbursement of qualified advertising costs. Agents are required to submit copies of advertisements they placed along with reimbursement submissions. Advertisements created by the agents do not qualify for reimbursement.

American Family Insurance Company's agent website policy states that individual agent created websites are prohibited. The company does not have any formal program to monitor for agent created websites, however, there have been occasional projects since the implementation of the company's website policy to look for individual agent created websites. Individuals within the company and in the field have discovered agent created websites and referred them to either the Digital Marketing or Advertising departments who have contacted the agents and required removal of the website.

The American Family Insurance company website, [www.amfam.com](http://www.amfam.com), contains company approved individual agent pages. The agent pages are pre-filled with company originated information. Agents have the option to do minor customization of their sites to include information such as professional background, education and honors. When agents submit information for customized portions of the agent web pages, it is reviewed by the company's Digital Marketing Department and inaccurate or inappropriate content is rejected. Agents also have the option to obtain a customized website address, known as a "vanity URL" which is typically a variation of the name of the agent and then ".com". The customized website address will redirect a user to the agent's individual agent page contained within the [www.amfam.com](http://www.amfam.com) company site.

The examiners reviewed the company's response to the marketing, sales & advertising interrogatory, the online database for advertisements, and the company's paper advertising files.

The examiners reviewed a sample of 60 advertising files including 10 webpage advertisements. No exceptions were noted.

### **Policy Forms**

The Product Design Department is responsible for product development, regulatory form filings, risk selection guidelines, compliance related projects, industry and regulatory surveys, state expansion strategies for market research and sales support.

When new policy forms are released for use or when policy forms are being discontinued, a Life Forms Disposition Notification is completed, reviewed and stored on EDMS in Life/Health Product Design. Once the new policy form or the discontinued policy form is placed on the EDMS in Life/Health Product Design, the Product Design Department sends electronic notification to all necessary personnel in the company, including field personnel, noting the effective date of the release or discontinuation. The company expects the notification to be sent one week prior to implementation.

The examiners reviewed the company's response to the policy forms interrogatory, compliance with s. Ins 6.85, Wis. Adm. Code that requires an insurer to notify its insureds of their right to file a complaint, and verified that all 58 policy forms currently in use by the company in Wisconsin were, in fact, approved or filed for use in Wisconsin. The examiners also reviewed all 16 of the company's life policy forms and both of the company's annuity policy forms which were marketed during the period of review. Twelve of the 16 life policies are whole life, 10, 20, and 30 year pay whole life, 10, 20, 30 level term life insurance policy forms and 15 and 30 year decreasing term life insurance policies. The whole life policies do not have a surrender charge period. The other 4 of the 16 life policies, including 2 flexible premium

universal life policies and 2 flexible premium variable universal life policies, have surrender charge periods which range from 14 years to 19 years. Of the 4 life policies that have surrender charge periods, the flexible premium variable universal life policy with a surrender period of 14 years, is ranked third of all the policies issued during the period of review. However, this policy is no longer being marketed because the company stopped selling variable policies as of May 29, 2009. The other three life insurance policies with surrender charge periods rank 12 or lower out of the 16 life insurance policies marketed during the period of review. Both of the annuity policies, including the flexible premium deferred annuity and the variable annuity policy, have surrender charge periods of 9 years. The company does not offer bonuses or issue any riders or endorsements on either of the annuity policies.

The sale of term life insurance policies accounted for 13,077 (60.30%) of the 21,688 total life insurance policies issued during the period of review. Three of the top-five policy forms issued during the period of review are term life insurance policies with rankings of 1, 2 and 5 in the top-five policy forms issued. The two variable universal life policies made up 2,643 (12.19%) and the whole life and universal life insurance policies made up 5,968 (27.52%) of the 21,688 total life insurance policies issued during the period of review. The variable annuity policies accounted for 783 (72.77%) of the 1,076 total annuity policies issued during the period of review. During the period of review, the sale of variable life and annuity policies that American Family Life Insurance Company decided to stop selling on May 29, 2009, accounted for 3,426 (15.05%) of the total 22,764 life and annuity policies issued.

The examiners also reviewed the 3 policy forms listed for the period of review that were submitted to the Office of the Commissioner of Insurance under file and use.

No exceptions were noted.

## **Policyholder Service and Complaints**

The company's Consumer Affairs Department is responsible for the handling of complaints received from the Office of the Commissioner of Insurance and complaints made directly to the company. The company has expanded its definition of a complaint to not only include written communication of a problem but also include complaints received by phone calls and from persons who walk into the company's headquarters to verbally file a complaint. The complaint handling processes are the same for complaints received from the Office of the Commissioner of Insurance and for complaints received directly from an insured. Every complaint received by the company is logged into and tracked by the Consumer Affairs Complaint Management System (CACM). The company's Unified Complaint Log is part of the Consumer Affairs Complaint Management System. Individual business areas of the company with expertise in the complaint subject matter prepare responses to the complaint. The responses are sent to the Consumer Affairs Department for review to ensure that the responses address all the complainant's concerns, comply with relevant statutes and regulations and the company's policies and procedures, and that responses are timely after the response is sent to OCI and insureds. Complaints involving variable products are handled by the Broker/Dealer Operations Manager and staff with assistance from American Family Securities.

The Life Product Design Unit conducts a quarterly review of each complaint received regarding American Family Life Insurance Company policies. The Life Product Design Unit categorizes the complaints, identifies any outstanding patterns or trends and drafts a brief summary report which is shared with the Product Design administrators and the Compliance and Ethics Director.

The Life Sales Department monitors complaints against agents and agents with multiple complaints. A Life/Health Marketing and Sales Complaint Report is prepared quarterly and reviewed by the Life Product Design Unit. The Life/Health Marketing and Sales Complaint Report is used to summarize which sales districts have the highest number of complaints and to

note if any agent has more than one complaint in a quarter. The report is broken down by product type such as individual health, individual life, individual annuity, variable annuity and variable universal life. Under each product type, the report is broken down by sales area of each state, district number and agent number. The number of complaints is listed by both district and agent. The report clearly indicates which districts and agents have complaints. If a high number of complaints or a pattern of complaints associated with a particular agent is observed, the matter is referred to the agent's District Manager and the Life Sales Department for further action. Allegations of misconduct or misrepresentation by agents are referred to Corporate Compliance for investigation. The company told the examiners that to date, the results of the quarterly review have not identified the need to track complaints about an individual agent on an annual or a multi-year history basis. American Family Securities, LLC handles the variable product complaints. American Family Securities receives a Daily Complaint Report run by the Consumer Affairs Department to identify and investigate complaints involving a registered agent and if necessary, takes appropriate follow up action. A summary of all the complaint reports, called the American Family Life Insurance Company Complaints Report, is prepared quarterly and reviewed by the Product Design Administrators and the Compliance and Ethics Director. The American Family Life Insurance Company Complaints Report gives the total number of complaints nationwide and of that total, how many were insurance department complaints. The report also breaks down the complaints by state, region, complaint reason, number of complaints by product type, and whether the response to the complaints was within the company's time parameters. The American Family Life Insurance Company Complaints report has a conclusion which summarizes the complaint information and includes recommendations based on the complaint information.

All fixed and variable annuity complaints alleging suitability concerns are logged into the Consumer Affairs Complaint Management (CACM) database and referred to the Broker/Dealer Operations Manager for handling. The new business file and all of the supporting



documents are reviewed by a member of the Broker/Dealer Operations staff who was not involved in the initial review when the policy was issued.

The examiners reviewed the company's response to the policyholder service and complaint interrogatory, company complaint reports, and all 73 complaints recorded in the company's Unified Complaint Log. These 73 complaints included 16 received from the Office of the Commissioner of Insurance and 57 complaints that were filed directly with the company. Ten (62.5%) of the 16 Office of the Commissioner of Insurance complaints were policyholder service related and involved policy change delays, failure to promptly respond to inquiries, premium notice/billing problems and/or cancellation/nonrenewal problems. Six (37.5%) of the 16 Office of the Commissioner of Insurance complaints involved agent handling. All of the Office of the Commissioner of Insurance complaints involved life insurance. Also, 31 (54.38%) of the 57 complaints that were filed directly with the company, were policyholder service related complaints and involved policyholder service delays, premium notice/billing problems, cancellation/nonrenewal problems and/or agent change requests. Examiners noted that 37 (50.68%) of the 73 complaints recorded in the company complaint log involved policyholder service complaints. Of the 57 complaints filed directly with the company, 18 (31.58%) involved what the company labeled as agent/insurance producer handling and 3 (5.26%) of the 57 complaints filed directly with the company were alleged misleading statement or misrepresentation.

No exceptions were noted.

## **Producer Licensing**

The Agency Sales Department is responsible for the management and oversight of agent contracts, agent appointments and termination processes, agent compensation, and agent support programs and services provided to three sales regions, designated as East, Central and West regions. The Agency Sales Department works closely with Corporation Compliance and Sales Management to monitor agent compliance with internal programs and policies, industry association standards, and regulatory statutes.

The Agency Sales East Region manages and oversees the agents in Wisconsin along with agents in Georgia, Illinois, Indiana and Ohio. All agents are supervised by a local District Sales Manager who reports to a Sales Director. The Sales Director reports to the Agency Sales Regional Vice President. Wisconsin is divided into two sales areas (east and west) and therefore has two Sales Directors, each of whom supervises eight District Sales Managers. The American Family Life Insurance Company's Executive Vice President, the Agency Sales Regional Vice President and the two Sales Directors make up the Sales Management team.

American Family Life Insurance Company considers its agents, who sell American Family Insurance products exclusively, to be independent contractors rather than employees of American Family. All agents have signed the American Family Agent Agreement covering American Family Life Insurance, American Family Mutual Insurance and American Standard Insurance of Wisconsin companies. Agents are assigned to a particular district but may sell insurance in any area, territory or state that they are properly licensed and appointed in. Each agent may hire his or her own employees, who are usually licensed, but does not have the authority to appoint another individual as an American Family agent. American Family Life does not accept brokered business.

American Family Insurance has partnered with SourceRight Solutions to assist with recruitment efforts for agents. Agent candidates are either recruited by SourceRight Solutions or by American Family District Sales Managers. SourceRight conducts the initial screening processes on American Family's behalf ensuring that all candidates meet the company's Agent Appointment Standards. If candidates meet the company's Agent Appointment Standards, they must complete an online assessment which is supplied by the company's vendor, HR Chally. Candidates are also requested to complete a Market Opinion Survey, supplied by LIMRA, which is used to give the candidates a realistic job preview. Successful candidates are then entered into the tracking pool which the company uses to manage candidates through the hiring process. District Sales Managers are then able to view the candidate information online and schedule interviews.

Every agent is required to attend the entire New Agent Training Program which is run by the Education Division. The company stated that the New Agent Training Program was designed to standardize training and educate new agents about American Family's products and services. The New Agent Training Program is a seven-week training program which usually takes place within 30 days of the agent's appointment to American Family Insurance. The New Agent Training Program is an in-depth curriculum covering topics ranging from basic business management to product knowledge, sales skills, replacement, and suitability. The agent training program also includes field days in which the agent participates in on-the-job training, working with the District Sales Manager and/or other agents in a sales office or on sales calls. American Family Insurance pays the agent a training allowance for the time they are in the New Agent Training Program.

Agent communications regarding new or changes to Wisconsin insurance laws and regulations, new or changes to company procedures and policies, and new or changes in products are done by email. The email program is referred to as Message Central. E-mails are sent every Tuesday and Thursday to all agents. Agents go to the Message Central and select

their state to read the all agent and state specific messages. The company also produces a monthly agent publication called the *All American* which is in written form and can also be accessed online. The *All American* includes information on program and product announcements, regulatory changes, sales ideas, messages from top management, agent interviews, and agent recognition.

American Family Insurance offers various classes throughout the year to help its agents complete their continuing education requirements. The Education Division tracks agent completion of company sponsored continuing education courses but doesn't track the continuing education courses agents take from the numerous outside vendors or online providers. The Agency Sales Regional Support monitors Sircon for continuing education completion, however, the company considers it the agents' responsibility to make sure they complete the state continuing education requirements. Agents receive a license renewal reminder from the Agency Sales Regional Support 60 days prior to renewal date. The Agency Sales Regional Support monitors Sircon monthly to identify whether or not agents have paid their renewal fee and/or completed their continuing education requirements. As appropriate, Agency Sales Regional Support will send agents an email or letter reminding them of the need to take care of their license renewal.

American Family Life Insurance Company participates in various incentive programs sponsored by American Family Mutual Insurance Company and sponsors some of its own incentive programs. The incentive programs can be for a single line of business or for all lines of business. Points are awarded for sales and agents must reach a certain point level in order to qualify for the incentive program. Points are tied to the amount of premium and are awarded based only on first year premium, not renewal premiums. Both external and internal replacements are considered new business. However, first year premium on internal replacements is the difference between the first year premium paid on the new policy and the first year premium on the replaced policy, and points are awarded based on that difference.

The examiners reviewed the company's response to the producer licensing interrogatory, appointment and termination procedures, and 100 agent files that included 50 active and 50 terminated agents, to determine if the company's practices and procedures related to the appointment and termination of its agents comply with Wisconsin insurance statutes and rules. The agent files and data lists provided by the company were also compared to the records maintained by the Office of the Commissioner of Insurance.

In the comparison of the company's list to the Office of the Commissioner of Insurance's list, the examiners found that one agent on the company's list was licensed in Wisconsin but not appointed with the company. The agent submitted 25 applications, all of which were issued, to the company from December 30, 2004 through May 3, 2007 without being appointed with the company. The agent was terminated on May 31, 2007. In response, the company stated it appeared that an individual mistakenly indicated that the agent was appointed with the company in the agent system when in fact no company appointment was ever submitted to the Office of the Commissioner of Insurance. The company admitted that it should have discovered the error during the annual reconciliation of the OCI appointment listing and corrected the problem.

- 1. Recommendation:** It is recommended that the company follow its established procedures for not accepting any business from an agent until the agent has been properly appointed with the company as required by s. Ins 6.57(5), Wis. Adm. Code.

During the review of the 50 terminated agent files, the examiners found 19 terminated agents, who were Customer Service Representatives (CSR), did not receive a termination letter from the company or the letter was not included in the agent's file. The Customer Service Representative works in the office of the agent and obtains an insurance license to allow the Customer Service Representative to help the agent with his clients. According to the company, a Customer Service Representative is not an employee of American Family, does not sign an agent contract with the company, and doesn't receive any

commissions. The Customer Service Representative's file is included in the agent's file, and American Family does appoint a Customer Service Representative with the company. The company stated that a Customer Service Representative is an employee of the agent and American Family does not normally send termination letters to the Customer Service Representative. The task is usually performed by the agent.

American Family considers District Managers and in-house appointed agents employees of American Family and not producing agents. District Managers and in-house appointed agents don't sign an agent contract and do not have an agent file. They have an employment agreement and a job description which is kept in Human Resources. However, American Family does appoint and terminate the non-producers in Sircon but does not keep a file of the appointment and termination verifications from Sircon for the non-producers. The company stated that since the non-producers are employees, it does not send a termination letter to the non-producers unless Human Resources officially terminate their employment.

2. **Recommendation:** It is recommended that the company amend its established procedures to provide all agents whose appointment to represent the company has been terminated with a written notice stating that the agent is no longer a representative of the company and that he or she may not act as its representative and which includes a formal demand for the return of all indicia of agency to include the Customer Service Representatives and non-producers as required by s. Ins 6.57(2), Wis. Adm. Code.

## **Underwriting**

### **New Business**

The Life New Business Policy Services in the Life Operations Department is responsible for processing life applications and issuing life policies. Life New Business Policy Services enters the non-electronic applications into the App Entry Wizard system and once all of the information is entered, a policy number is issued and the information is then entered into the Cyberlife system which is an administration system that is used in processing and tracking of applications. Electronic applications receive a policy number when the agent submits the

application and it is automatically in the App Entry Wizard system and then has to be entered into the Cyberlife system. Once the application is in the Cyberlife system, Life New Business Policy Services reviews the answers on the application and accompanying paperwork, reviews the forms received to ensure that the correct forms were received and completed properly, and requests additional information that underwriting may require. The application is then sent to Life Underwriting for review. If Life Underwriting approves the application, Life New Business Policy Services issues and mails the policy. If Life Underwriting does not approve the application for issue, Life Underwriting will send a decline letter to the applicant.

Variable life and annuity products and fixed annuities are processed the same. Applications are scanned into the Automated Workflow (AWD) system, given a policy number and then the information is entered into the Cyberlife system. The application and accompanying paperwork is reviewed to determine if the requirements are in good order or not in good order. If the applications are in good order, a suitability review is conducted and then referred to Life Underwriting. If Life Underwriting approves the application, Life New Business Policy Services issues and mails the policy.

To ensure that the company's underwriting guidelines and procedures are being followed, senior underwriters complete an audit of 10 cases for each Life and Associate underwriter per quarter. Each audit includes a review of an underwriter's internal and external communication skills; determines whether the underwriter's decisions, actions, and resources were appropriate and documented; that the underwriter correctly interpreted, verified and investigated information from the Medical Information Bureau; and whether the underwriter verified that the correct state specific application was used, all of the appropriate documents were submitted with the application, and that the agent was properly licensed. The audit results are used to help assess individual performance as well as individual and department training needs.

American Family Life Insurance Company currently allows agents to submit business electronically through the LP2000 system. Signatures are obtained by the use of an electronic signature pad which is connected to the agent's computer. At the time the agent submits the electronic application, the application receives a policy number and it is automatically in the App Entry Wizard system ready to be entered into the Cyberlife system for the application process to begin.

The company does not allow nor does the company have any future plans to allow consumers to apply for coverage online and submit applications electronically. However, American Family Life Insurance Company is researching the possibility of allowing existing policyholders the capability of submitting an application electronically for additional coverages. The company is still working through the legal and compliance issues such as signatures, underwriting and notification requirements.

The following chart shows the total number of policies issued for each of the top-seven life insurance forms sold by agents during the period of review.

| <b>Policy Form Number</b> | <b>Number of Life Insurance Policies Issued during Period of Review</b> | <b>Percentage of Total Life Insurance Policies Issued during Period of Review</b> |
|---------------------------|---|---|
| L-34(WI) Ed. 3/07         | 5,337   | 24.61%  |
| L-33 (WI) Ed. 3/07        | 2,350   | 10.83%  |
| L-97 VUL (WI) Ed. 3/01    | 2,339   | 10.78%  |
| L-24 (10) (WI) Ed. 1/05   | 2,058   | 9.49%   |
| L-34 (WI) Ed. 1/05        | 2,000   | 9.22%   |
| L-60 (WI) Ed. 1/05        | 1,904   | 8.78%   |
| L-35 (WI) Ed. 3/07        | 1,827   | 8.42%   |

The top-seven life policy forms accounted for 17,815 (82.14%) of the 21,688 total life policies issued during the period of review. Four of the top-seven life policy forms [L-34(WI) Ed. 3/07, L-33(WI) Ed. 3/07, L-34(WI) Ed. 1/05 and L-35(WI) Ed.3/07] are term life insurance policies which accounted for 11,514 (53.09%) of the 21,688 total life policies issued during the



period of review. The term life insurance policies have level premiums ranging from 10 years to 30 years. Two of the top-seven are whole life policy forms [L-24(10)(WI) Ed. 1/05 and L-60(WI) Ed. 1/05] which accounted for 3,962 (18.27%) of the 21,688 total life policies issued. The third-ranked of the seven policy forms was a variable universal life policy (L-97 VUL(WI) Ed. 3/01) which accounted for 2,339 (10.78%) of the 21,688 total life policies issued. The data provided by the company indicated that sales of variable universal life insurance policies accounted for 2,643 (12.19%) of the 21,688 total life policies issued during the period of review.

The following chart shows the total number of contracts issued for each of the two annuity policy forms sold by agents during the period of review.

| <b>Policy Form Number</b> | <b>Number of Annuity Contracts Issued during Period of Review</b> | <b>Percentage of Total Annuity Contracts Issued during Period of Review</b> |
|---------------------------|---|---|
| L-A10 VA(WI) Ed. 3/01     | 783   | 72.77%  |
| L-A10(WI) Ed. 1/04        | 293   | 27.23%  |

The variable annuity contract [L-A10 (WI) Ed. 3/01] accounted for 783 (72.77%) of the 1,076 total annuities issued during the period of review. The other annuity contract [L-A10(WI) Ed. 1/04] is a flexible premium deferred annuity which had 293 (27.23%) contracts issued during the period of review. During the period of review, the sale of variable life and annuity products accounted for 3,426 (15.05%) of the total 22,764 life and annuity policies issued by the company. As mentioned earlier, the company decided to stop selling variable products on May 29, 2009.

The following chart, based on the information from the data call which was provided by the company, provides information regarding the issue ages of the annuity contracts issued by American Family Life Insurance Company in Wisconsin during the period of review.

|                                 | Under<br>65 | 65 - 74 | 75 and<br>older | Total |
|---------------------------------|-------------|---------|-----------------|-------|
| 2007                            |             |         |                 |       |
| From Replacement File           | 65          | 3       | 1               | 69    |
| From Non Replacement File       | 427         | 7       | 1               | 435   |
| 2007 Totals                     | 492         | 10      | 2               | 504   |
|                                 |             |         |                 |       |
| 2008                            |             |         |                 |       |
| From Replacement File           | 38          | 3       | 0               | 41    |
| From Non Replacement File       | 322         | 9       | 2               | 333   |
| 2008 Totals                     | 360         | 12      | 2               | 374   |
|                                 |             |         |                 |       |
| 2009                            |             |         |                 |       |
| From Replacement File           | 11          | 6       | 1               | 18    |
| From Non Replacement File       | 173         | 4       | 3               | 180   |
| 2009 Totals                     | 184         | 10      | 4               | 198   |
|                                 |             |         |                 |       |
| Total From Replacement File     | 114         | 12      | 2               | 128   |
| Total From Non Replacement File | 922         | 20      | 6               | 948   |
| Totals                          | 1,036       | 32      | 8               | 1,076 |

According to the data, the company issued a total of 1,076 annuity contracts during the period of review. From 2007 to 2008, the company had a decrease in its total sale of annuity contracts by 130 (-25.79%). Of the 1,076 annuity contracts issued, 1,036 (96.28%) were issued to individuals under the age of 65, 32 (2.97%) annuity contracts were issued to individuals age 65 through age 74, and 8 (.74%) annuity contracts were issued to individuals age 75 and older. Of the 40 contracts issued to individuals 65 and older, 14 (35%) involved replacement and of the 8 contracts sold to individuals age 75 and older, 2 (25%) involved replacement.

The issue ages for American Family Life Insurance annuities are age 0 to a maximum issue age of 80. If the annuitant on the application is over age 80, only a fixed single premium immediate annuity can be offered. The issue ages for a fixed single premium immediate annuity are age 25 to age 90. The company will not accept any application for any type of annuity if the applicant is over age 90.

The examiners reviewed the company's response to the New Business and Underwriting interrogatory. The examiners also reviewed 50 new business life files of which 6 were variable life new business files and 50 new business annuity files of which 26 were variable annuity new business files.

No exceptions were noted.

## **Underwriting**

### **Replacement**

The examiners reviewed the company's response to the Replacement interrogatory.

American Family Life Insurance Company defines external replacement as any transaction where the company receives an application for an individual life insurance policy or annuity with American Family Life Insurance Company and the applicant owns an existing life insurance policy or annuity with another company that will be canceled, exchanged, lapsed, surrendered, changed to reduce or eliminate benefits, reduced in value or face amount, and/or a loan or dividend withdrawal will be taken in order to purchase the new policy or annuity. An internal replacement is when the existing life insurance policy or annuity that the applicant owns is with American Family Life Insurance Company.

Examiners had difficulty reconciling the replacement data the company provided in response to the examination interrogatory for replacement with the data provided in the examination's data call and the data reported in the Market Conduct Annual Statements (MCAS) that the company filed with OCI. Subsequent to when the examiners were onsite, the company provided corrected numbers of total sales of life and annuity policies and total number of life and annuity replacements. The company stated that its policy administration system does not carry a replacement indicator for all product types and therefore the company could not provide internal and external replacement numbers strictly from the administration system. To explain why the data provided in the response to the interrogatory, and the data provided in the

data call and the Market Conduct Annual Statements did not agree, the company explained that its current replacement report system produces data that is unrelated to new sales involving actual replacements, and that data inflated the number of replacements. An example the company provided was that in 2008, 20% of all life applications were closed out or not taken and no money was received by the company. However, under the current replacement report system if the same individual applied for another American Family Life policy and it was issued within the next 13 months, it is considered a replacement. The company stated that it had already undertaken a Life Replacement Report Renovation project to eliminate the excess data generated by the current life replacement reports.

The corrected numbers provided by the company indicated that the total number of life replacements for 2007 was 641 (7.06%) of the 9,076 total life business in Wisconsin for that year. The total number of life replacements for 2008 was 526 (6.87%) of the 7,652 total life business in Wisconsin for that year. The total number of life replacements for the period of January 1, 2009 through August 31, 2009 was 376 (7.77%) of the 4840 of the company's total life business in Wisconsin for that period.

Using the revised numbers provided by the company, the total number of annuity replacements for 2007 was 146 (28.51%) of the 512 total annuity business in Wisconsin for that year. The total number of annuity replacements for 2008 was 70 (17.72%) of the 395 total annuity business in Wisconsin for that year. The total number of annuity replacements for the period of January 1, 2009 through August 31, 2009 was 18 (9.09%) of the 198 total annuity business in Wisconsin for that period. The company stated that the yearly percentages of annuities that are replacements are higher than the corresponding percentages for life replacement because the percentage of annuity sales involving replacement becomes more pronounced due to the low total number of annuities issued. The company stated that it waives the surrender charges if a replacement is completed from universal life to universal life, universal life to variable universal life and fixed annuity to variable annuity. The company

indicated that it does not waive surrender charges if the replacement is from variable universal life or universal life to whole life or from variable annuity to fixed annuity. The company does not impose surrender charges on its whole life products.

The company pays commission to agents based on first year premium and renewals. There is no adjustment made to the commission to agents for external replacements. However, the company does make adjustments to the commission payable for internal replacements. The agent's first year compensation is reduced by the amount of the first year compensation that the agent received on the original policy for internal replacement of permanent policies. For term to term policy replacements, the compensation adjustment is one half of the adjustment that is done for the internal replacement of permanent policies.

The company provides specific replacement training to its agents through the mandatory New Agent Training Program that is described in the Producer Licensing section of this report. In addition, American Family Life Insurance Company has online the company's Life Reference Manual that provides agents instruction on replacement in all of the states in which the company is licensed. Included in the replacement section of the Life Reference Manual is the company's Statement of Principle that promotes the conservation of in-force life insurance policies and opposes activities aimed at replacement of existing policies. The company bases its position on the understanding that the highest value to policyholders is generally provided by the existing policy as opposed to any new replacement policy. Among the considerations supporting this position, that agents are instructed to consider before replacing an existing policy are that premiums generally increase with age which means the replacement usually results in higher premiums, cash values and/or dividends generally increase faster on older policies, surrender charges may be assessed against cash value removed from an existing policy, incontestable and suicide periods start over, often existing coverage provides more favorable contract provisions, selling costs are charged largely against the initial years' premium

resulting in duplicating the selling costs for the policyholder with replacement, and if the existing policy is cancelled before the new policy is issued, the applicant could be significantly harmed if the new policy is declined or issued substandard. The Statement of Principle promotes policyholder value in developing long-term client relationships that are compromised by replacement based selling. However, the company understands that replacement may sometimes be appropriate and has instructed its agents to help the policyholder make an informed decision and evaluation of the positives and negatives of a replacement.

In order to monitor the percent of business involving replacement both company wide and by individual agents, the company developed and began using a Data Warehouse system in late 2004 that pulls information from the company's other systems to capture replacement transactions. Because the company anticipated that the majority of the states in which American Family Life Insurance Company is licensed would be adopting the NAIC definition of replacement, the rules engine for identifying replacement activity uses the NAIC definition of replacement. The Data Warehouse system uses an insured/owner matching routine to also determine if an undisclosed replacement has taken place. The company runs reports that provide information, by district, on the total number of replacements, percent of replacements to total sales, total disclosed replacements both internal and external, and total non-disclosed replacements, both internal and external. This report allows the company to monitor replacement activity by district, by state, and by sales regions. Reports are also run that provide replacement information by agent, replacing policy number, policyholder's name, replaced policy number and replaced company. This report allows the company to monitor the replacement activity of each individual agent.

In response to questions in the Replacement interrogatory, the company described its compliance with Wisconsin's new replacement rule which went into effect on July 1, 2009 with an implementation date of November 1, 2009. According to the company, internal department managers were informed of the change in September in order to set the procedures

for implementation on November 1, 2009. The company stated that the New Business Life employees were advised of the new replacement rules on October 6, 2009, and in mid-October, agents, District Managers and all employees will receive a field communication advising them of Wisconsin's new replacement rules. The field communication will announce Wisconsin's adoption of the NAIC definition of replacement and explain that the new replacement notice is to be completed whether replacement is occurring or not. The replacement section in the Life Reference Manual will be updated as of November 1, 2009. The company stated that it already offers a 30-day free-look period which is in compliance with the new replacement rules and therefore there is no need to make any changes to the company's policy forms.

The examiners also reviewed 50 new business life replacement files of which 12 were variable life replacement new business files and 50 new business annuity replacement files of which 39 were variable annuity replacement new business files.

No exceptions were noted.

## **Underwriting**

### **Suitability**

In response to questions in the Suitability interrogatory, American Family Life Insurance Company described its procedures for complying with s. 628.347, Wis. Stat. with regards to the suitability of annuity sales to consumers. The company stated that its suitability requirements apply to all issue ages and to the sale of all annuities. The company stated that while the initial responsibility for ensuring recommendations are suitable rests with the writing agent, the company is responsible for and has developed a suitability review process for monitoring the recommendations made by its agents. Prior to January of 2009, the company had different suitability questionnaires for fixed annuity and variable annuity sales that the agents had to complete when taking an application. In January of 2009, the fixed annuity suitability questionnaire was again revised to be the same as the suitability questionnaire used

for variable annuities. The suitability questionnaire contains information obtained from the applicant such as marital status, and occupation information including length of employment, tax status, financial status (such as annual income, available and type of liquid assets, retirement assets, and net worth), source of funds for the purchase of the annuity, investment objectives (including the reason for purchasing the annuity, and if the annuity will meet the applicant's financial objectives). The questionnaire also asks how many years before the applicant plans to withdraw funds from the annuity, whether the applicant has a retirement plan through an employer and whether the applicant understands that the annuity being applied for has a surrender charge and penalties for early withdrawal. The suitability questionnaire requires the signature of both the applicant and agent confirming that based on the financial information provided by the applicant, the purchase is suitable for the applicant's needs and/or financial objectives. For variable products, the agent must complete a Risk Tolerance Questionnaire which is signed by both the applicant and the agent, and if replacement is involved, a Variable Annuity Switch Form in addition to completing the suitability questionnaire and the Agent Report for Annuities. The Variable Annuity Switch Form requests information about the date of purchase of the existing annuity, current age of the applicant, value of existing annuity, amount of surrender charge or contingent deferred sales charge, the surrender charge as a percentage of the existing contract value, years remaining until the end of the surrender period, how long the applicant expects to keep American Family Life variable annuity, and the initial amount to be invested in the new variable annuity. The form also requires a side-by-side comparison of the current fees, charges and features of the existing annuity to the American Family Life variable annuity. All of the fees, charges and features of the American Family Life variable annuity are filled in as part of the form except the amount of the guaranteed death benefit. In addition, the applicant must complete a section which requires an explanation of why the applicant is replacing the existing policy, whether the applicant replaced another variable annuity within the past 36 months and if the agent did or did not make the recommendation to replace the existing.



The agent has to explain why replacement is in the best interest of the applicant, why the existing annuity no longer meets the applicant's objectives, and what the disadvantages or consequences are to the applicant if the applicant doesn't replace the existing annuity. Both the applicant and agent must sign the Variable Annuity Switch Form with the agent again stating that the sale is suitable.

The variable and fixed annuity applications are scanned into the Automated Workflow (AWD) system, given a policy number and then the information is entered into the Cyberlife system. As part of the process of entering the information in the Cyberlife system, there is a suitability information section and suitability question screens which require entry of information from the suitability questionnaire. When all of the required documents are received and entered, the application is sent via the Cyberlife system to the suitability review team. The suitability review team is in the Broker/Dealer Operations Unit which is in the Life Operations Department. The suitability review team not only reviews the suitability of variable annuity sales but also the fixed annuity sales. The suitability review team members, who have been trained for suitability review, review all of the documents using a suitability review checklist. The company workflow was designed to ensure that all annuity applications have been reviewed and signed-off on by the suitability review team. If the annuity application has not been signed-off, an error message is posted on the Cyberlife system and the application can't continue to be processed until the suitability review team has reviewed and signed-off on the application. The suitability review team meets weekly with individuals from Broker/Dealer Compliance, Life Sales and the Training Principal to discuss suitability cases and trends in the applications submitted and reviewed for suitability.

The Broker/Dealer, American Family Securities LLC, audits the suitability review of the variable annuity new business by the suitability review team monthly for compliance with the company's suitability guidelines. There is no additional review of the fixed annuity suitability at this time.

All new agents go through the required New Agent Training Program which includes educating the agent about the company's philosophy, policies, and procedures regarding suitability of coverage. Information in the Life Reference Manual, which is on the agent web portal on the company's website, also contains the company's philosophy, policies, and procedures regarding suitability. The company also makes available 94 educational life and annuity courses to its agents through on-line, instructor-led training using webinar, instructor-led and job-aid training. At least 14 of these courses include instruction on replacement and suitability of coverage as of December 2008. The company stated that its applications, questionnaires, and forms are designed to complement the policies and procedures in place to ensure that an agent makes recommendations based upon relevant information and that fixed annuity, variable annuity and variable life insurance policy sales are suitable. The questionnaires and forms used to determine suitability are pre-issue requirements.

The company reviews all annuities, both variable and fixed, and variable universal life insurance applications for suitability. The company is not able to segregate Wisconsin applications from those received from other states. Companywide, 2,748 variable annuity applications, 1,102 fixed annuity applications, and 10,070 variable universal life applications were reviewed by the suitability review team in 2007. In 2008, 1,938 variable annuity applications, 621 fixed annuity applications, and 7,269 variable universal life applications were reviewed by the suitability review team. From January 1, 2009 through May 2009, the suitability review team reviewed 517 variable annuity applications, 919 fixed annuity applications, and 1,831 variable universal life applications. Of the 2,748 variable annuity applications reviewed companywide, 58 (2.11%) of the applications were rejected due to suitability in 2007. In 2008, 33 (1.70%) of the variable annuity applications were rejected by the suitability review team out of the 1,938 total variable annuity applications reviewed. From January 1, 2009 through May 2009, the suitability review team rejected 7 (1.35%) of the variable annuity applications out of 517 total variable annuity applications received, and rejected 18 (1.96%) of the 919 total fixed

annuity application received up to the end of May. The company stated that prior to January 1, 2009, the company did not have a formal rejection report for fixed annuity applications. In 2007, the suitability review team rejected 86 (.84%) of the 10,070 total variable universal life applications reviewed. In 2008, 47 (.65%) of the variable universal life applications reviewed by the suitability review were rejected out of 7,269 total variable universal applications reviewed. From January 1, 2009 through May 2009, the suitability review team rejected 11 (.60%) out of 1,831 total variable universal life applications received.

The company's Suitability Rejection Report identifies the agent, applicant, policy number, rejection date, reason for rejection, and the member of the suitability review team who reviewed the application. This report allows the company to monitor any patterns or trends in the reasons for rejection, and to monitor the reasons for rejection and number of rejections for individual agents.

As previously mentioned, the examiners reviewed 50 new business annuity files, 50 new business life files, 50 replacement annuity files, and 50 replacement life files as part of the exam. During their review, examiners checked the files for the suitability questionnaire and found that all 200 new business files included the suitability questionnaire. No exceptions were noted.

### **Market Conduct Annual Statement**

Wisconsin participates in the NAIC's Market Conduct Annual Statement (MCAS). The company meets the minimum premium threshold for life and annuity business and therefore is required to file a Market Conduct Annual Statement in Wisconsin. When attempting to reconcile the number of life and annuity policies involving replacement, the examiners reviewed the company's Market Conduct Annual Statements for 2007 and 2008, and found that the company had reported having zero annuity replacements in 2007 and 2008, and a relatively small but the same number of life replacements in both years. These numbers did not agree

with the numbers of life and annuity replacements the company reported in response to the examination interrogatory for replacement or the examination data call. In fact, the 2008 MCAS contained identical data as the company's 2007 MCAS except for a very few data elements. American Family Life Insurance Company stated that the inconsistencies were due to human error and that responsibility for completing the Market Conduct Annual Statement has been reassigned to Corporate Compliance and workpapers have been developed to guide and direct the preparation of future Market Conduct Annual Statement submissions including assorted tie-outs to annual financial statements and a comparison of data between years for reasonableness. The Market Conduct Annual Statement requires that an officer of the company submitting the filing certify that he or she is knowledgeable of the information required to be provided in the Market Conduct Annual Statement and that to the best of his or her knowledge and belief, the filing along with necessary related exhibits, schedules, and explanations contained in, or annexed or referred to therein, represent a full and accurate statement of the information required in accordance with the filing instructions. The required certification of accuracy, signed by an officer of the company, was included with both the 2007 and 2008 Market Conduct Annual Statement filings made by the company. Section 628.34(1), Wis. Stat. states that no person on behalf of an insurer may make or cause to be made any communication relating to the insurance business which contains false or misleading information, including information misleading because of incompleteness. Filing a report with a false entry in the report is a communication within the meaning of this statute. Subsequent to the onsite examination and at the request of the examiners, the company refiled a corrected MCAS for 2007 and 2008 in Wisconsin. The company also contacted the other participating MCAS states in which the company is licensed and refiled a corrected MCAS for 2008 in each state for which incorrect data was submitted.

3. **Recommendation:** It is recommended that the company develop, document and implement procedures to accurately report to the Commissioner required information about the company's business in Wisconsin, including but not limited to the information provided in the Market Conduct Annual Statement, as required by s. 628.34(1), Wis. Stat.

## V. CONCLUSION

The market conduct examination of American Family Life Insurance Company was conducted by the Wisconsin Office of the Commissioner of Insurance to determine compliance with the prior recommendations made in the market conduct examination report adopted February 2, 2000 and to verify that the company has established an effective system of supervision to ensure that its agents' recommendations to consumers to purchase or exchange an annuity are appropriate and suitable for their customers' financial situation and needs.

The examiners found that the company has complied with all 15 recommendations made in the previous market conduct examination report adopted February 2, 2000.

During the current examination, the examiners found that the company's program for monitoring the suitability of annuity sales includes the New Agent Training Program which educates the new agent about the company's philosophy, policies and procedures regarding suitability; and a suitability review team that reviews the suitability of all annuity sales. The company also uses the same consumer suitability questionnaire for both fixed and variable annuities. The company's Suitability Rejection Report allows the company to monitor patterns or trends in the reasons for rejection, reasons for rejection and the number of rejections for each agent.

American Family Life Insurance Company first began marketing variable life and annuity products in September of 2000. As of May 29, 2009, American Family Life Insurance Company no longer solicited and sold new variable products. American Family Securities, in coordination with FINRA, has established a Securities Service Center which is based at American Family Life Insurance Company's home office. The Securities Service Center is staffed by registered representatives who took over the duties previously performed by the field agents. The company doesn't plan to relinquish its authority to issue variable products as it may engage in future sales of variable products if future economic conditions warrant.

The examiners made two new recommendations in the area of producer licensing. Pertaining to the first recommendation, the examiners found that one agent was licensed in Wisconsin but not appointed with the company. This agent submitted 25 applications, all of which were issued, to the company without being appointed with the company. The company did not follow its established procedures for not accepting business from an agent until the agent has been properly appointed with the company.

During the review of the company's terminated agent files, the examiners found that Customer Service Representatives (CSR) did not receive a termination letter from the company when terminated. The company does not consider the Customer Service Representative an employee of American Family, however, American Family does appoint the Customer Service Representative with the company. Also, examiners found that District Managers and in-house appointed agents are considered employees of American Family and not producing agents. District Managers and in-house appointed agents do not sign an agent contract and do not have an agent file. They have an employment agreement and a job description which is kept in Human Resources. Although American Family Life Insurance Company does appoint and terminate the non-producing agents, it does not send a termination letter to non-producing agents unless Human Resources officially terminates their employment. The company needs to amend its established procedures to provide a written notice to all agents, including customer service representatives and non-producing agents whose appointment to represent the company has been terminated, that states the agent is no longer a representative of the company and that he or she may not act as its representative and which includes a formal demand for the return of all indicia of agency.

After reviewing the company's Market Conduct Annual Statements for 2007 and 2008, examiners found significant errors in the data that was reported to OCI. The company must develop, document and implement procedures to accurately report to the Commissioner

required information about the company's business in Wisconsin, including but not limited to the information provided in the Market Conduct Annual Statement.



## VI. SUMMARY OF RECOMMENDATIONS

### Producer Licensing

Page 26 1. It is recommended that the company follow its established procedures for not accepting any business from an agent until the agent has been properly appointed with the company as required by s. Ins 6.57(5), Wis. Adm. Code.

Page 27 2. It is recommended that the company amend its established procedures to provide all agents whose appointment to represent the company has been terminated with a written notice stating that the agent is no longer a representative of the company and that he or she may not act as its representative and which includes a formal demand for the return of all indicia of agency to include the Customer Service Representatives and non-producers as required by s. Ins 6.57(2), Wis. Adm. Code.

### Market Conduct Annual Statement

Page 42 3. It is recommended that the company develop, document and implement procedures to accurately report to the Commissioner required information about the company's business in Wisconsin, including but not limited to the information provided in the Market Conduct Annual Statement, as required by s. 628.34(1), Wis. Stat.

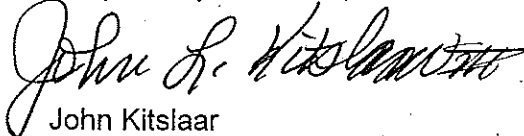
VII. ACKNOWLEDGEMENT

The courtesy and cooperation extended to the examiners during the course of the examination by the officers and employees of the company is acknowledged.

In addition, to the undersigned, the following representatives of the Office of the Commissioner of Insurance, state of Wisconsin, participated in the examination.

| <u>Name</u>   | <u>Title</u>       |
|---------------|--------------------|
| John Pegelow  | Insurance Examiner |
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Respectfully submitted,



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