

DELAWARE DEPARTMENT OF INSURANCE
MARKET CONDUCT EXAMINATION REPORT
LIFE INSURANCE COMPANY OF THE SOUTHWEST

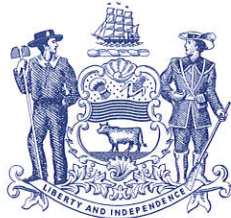
NAIC # 65528

1 National Life Dr.
Montpelier, VT 05604

As of

June 30, 2011

Karen Weldin Stewart, CIR-ML
Commissioner



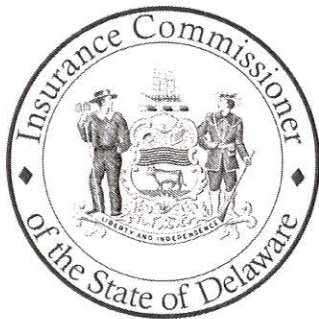
Delaware Department of Insurance

I, Karen Weldin Stewart, Insurance Commissioner of the State of Delaware, do hereby certify that the attached REPORT ON EXAMINATION, made as of June 30, 2011 on

Life Insurance Company of the Southwest

is a true and correct copy of the document filed with this Department.

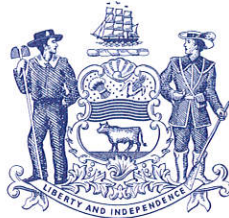
Attest By: *Janet News*



In Witness Whereof, I have hereunto set my hand and affixed the official seal of this Department at the City of Dover.

Karen Weldin Stewart
Karen Weldin Stewart, CIR-ML
Insurance Commissioner

Karen Weldin Stewart, CIR-ML
Commissioner



Delaware Department of Insurance

REPORT ON EXAMINATION
OF THE
Life Insurance Company of the Southwest
AS OF
June 30, 2011

The above-captioned Report was completed by examiners of the Delaware Department of Insurance.

Consideration has been duly given to the comments, conclusions and recommendations of the examiners regarding the status of the Company as reflected in the Report.

This Report is hereby accepted, adopted and filed as an official record of this Department.

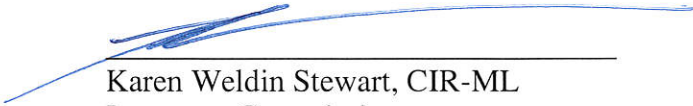

Karen Weldin Stewart, CIR-ML
Insurance Commissioner

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Honorable Karen Weldin Stewart CIR-ML
Insurance Commissioner
State of Delaware
841 Silver Lake Boulevard
Dover, Delaware 19904

Dear Commissioner Stewart:

In compliance with the instructions contained in Certificate of Examination Authority Number 65528-11-709, and pursuant to statutory provisions including 18 Del. C. §318-322, a market conduct examination has been conducted of the affairs and practices of:

Life Insurance Company of the Southwest

The examination was performed as of June 30, 2011. Life Insurance Company of the Southwest, hereinafter referred to as the "Company", was incorporated under the laws of Delaware. The examination consisted of two phases, an on-site phase and an off-site phase. The on-site phase of the examination was conducted at the following Company location:

15455 Dallas Parkway, Suite 800
Addison, TX 75001

The off-site examination phase was performed at the offices of the Delaware Department of Insurance, hereinafter referred to as the "Department" or "DDOI," or other suitable locations.

The report of examination herein is respectfully submitted.

EXECUTIVE SUMMARY

Life Insurance Company of the Southwest (the "Company") incorporated in Texas in March 7, 1955. The Company's main administrative offices are located in Addison, Texas.

On the Company's 2010 annual statement filed with the Department, Life Insurance Company of the Southwest reported Delaware direct premium of annuity contracts in the amount of \$13,596,096, of which \$13,593,696 were ordinary annuity considerations and the subject of the examination.

The examination was announced as part of an examination series on companies in the Annuity marketplace in Delaware. The examination focused on the Company's annuity business in the following areas of operation: Company Operations/Management; Complaint Handling, Marketing/Sales, Producer Licensing, Producer Oversight, Terminations, Surrenders, Replacements and Underwriting. This effort is being conducted to ensure compliance with 18 Del. Admin. Code 1214 Senior Protection in Annuity Transactions, 18 Del. Admin. Code 1204 Replacements, 18 Del. C. §1716 Notification to Insurance Commissioner of Termination.

The following exceptions were noted in the areas of operation reviewed:

- Company Operations and Management - 2 Exceptions - 18 Del. C. §2712. Filing, approval of forms.
 - Failure to file two forms with the Department prior to use.
- Complaint Handling - 2 Exceptions – 18 Del. C. §2304 (17) Failure to maintain complaint handling procedures.
 - Failing to identify and list two complaints on the Company's complaint log.
- Marketing and Sales - 1 Exceptions – 18 Del. C. §2304. Unfair methods of competition and unfair or deceptive acts or practices defined.
 - Utilizing policy forms which contained a report of assets without the amount of the insurer's liabilities being reported.
- Marketing and Sales - 3 Exceptions – 18 Del. C. §2304. Unfair methods of competition and unfair or deceptive acts or practices defined.
 - Failing to provide a reference of the source of statistics used in three marketing forms.
- Underwriting and Rating - 10 Exceptions - 18 Del Admin. Code 1204 §7.1. Replacement of Life Insurance.
 - Failing to provide a notice of replacement to the insurer being replaced.

SCOPE OF EXAMINATION

The Market Conduct Examination was conducted pursuant to the authority granted by 18 *Del. C.* §318-322 and covered the experience period of January 1, 2010, through June 30, 2011. The purpose of the examination was to determine the Company's compliance with Delaware insurance laws and regulations related to the annuity market place.

The examination was a target market conduct examination of the Company's Senior Annuity business in the following areas of operation: Company Operations and Management; Complaint Handling, Marketing and Sales, Producer Licensing and Underwriting and Rating.

METHODOLOGY

This examination was performed in accordance with Market Regulation standards established by the Department and examination procedures suggested by the NAIC. While the examiners' report on the errors found in individual files, the general business practices of the Company are also reviewed.

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

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

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

COMPANY HISTORY AND PROFILE

Life Insurance Company of the Southwest was incorporated in the State of Texas on March 7, 1955. The Company is currently licensed in 49 states, the District of Columbia. Life Insurance Company of the Southwest is a wholly owned subsidiary of the National Life Group.

On the Company's 2010 annual statement filed with the Department, Life Insurance Company of the Southwest reported Delaware direct premium of annuity contracts in the amount of \$13,596,096, of which \$13,593,696 were ordinary annuity considerations and the subject of the examination.

COMPANY OPERATIONS AND MANAGEMENT

Internal Audit and Compliance Procedures

The Company provided a list of all internal audits performed in the last five years. The Company provided a listing of seventy (70) internal audits that were performed during the examination period.

No exceptions were noted.

Policy Forms

The Company provided a list and copies of all policy and/or member forms, conversion contracts, applications, riders, amendments and endorsements used during the experience period. The forms provided and additional forms from various underwriting sections of the exam were reviewed to ensure compliance with 18 Del. C. §2712, Filing, approval of forms. The following exceptions were noted.

(2)Exceptions – 18 Del. C. §2712. Filing, approval of forms.

(a) No basic insurance policy or annuity contract, form, or application form where written application is required and is to be made a part of the policy or contract or printed rider or endorsement form or form of renewal certificate shall be delivered or issued for delivery in this State, unless the form has been filed with the Commissioner.

Form numbers 5776 and 7775 were not filed with the Department, as required by 18 Del. C. §2712.

Recommendation: It is recommended that the Company immediately cease using form numbers 5776 and 7775 until the form has been submitted and approved by the Delaware Department of Insurance as required by 18 Del. C. §2712.

CONSUMER COMPLAINTS

The Company identified all consumer complaints received during the experience period and noted that none had been received by Delaware Consumers.

During the review of the Issued files provided by the Company, the examiners found a complaint in the issued file. The complaint was not recorded in the Company's complaint log. Included in 18 Del. Admin. Code 902 is a requirement for maintenance of a complete record of all complaints received during the experience period. The record shall indicate the total number of complaints, their classification by line of insurance, the nature of each complaint, the disposition of the complaint and the time it took to process each complaint. The Company is found to be in violation of 18 Del. Admin. Code 902 §1.2.1.2.

The following exceptions were noted.

(2) Exceptions – 18 Del. C. §2304 (17) Failure to maintain complaint handling procedures.

Failure of any person to maintain a complete record of all the complaints which it has received since the date of its last examination as otherwise required in this title. This record shall indicate the total number of complaints, their classification by line of insurance, the nature of each complaint, the disposition of these complaints and the time it took to process each complaint. For purposes of this subsection, "complaint" shall mean any written communication primarily expressing a grievance.

Two complaints were not listed as complaints by the Company but were found within the Company's documented policy issue files.

Recommendation: It is recommended that the Company log all complaints and not just the ones deemed to be formal complaints in the Company's complaint log. The complaint log must be in compliance with 18 Del. Admin. Code 902 .

PRODUCER LICENSING

The Company provided a list of all producers who were either active or terminated during the examination period, in addition to the Company's policies and procedures regarding the following activities:

- Appointment Procedures
- Producer Terminations
- Accuracy of application information
- Alteration Procedures

- Internal Replacements
- Background Checks for Producers
- Allegations of Misconduct/Misrepresentation against Producers

The policies and procedures were received and reviewed. The Company provided a list of 128 active producers and 52 terminated producers. Each active and terminated producer was compared by name to Delaware Department of Insurance records to verify appointments and terminations.

In addition, the producers from the replacement policy sample were reviewed for licensing and appointments. Any finding related to the replacement files will be noted in that section of this report.

No exceptions were noted.

MARKETING AND SALES

The Company provided a list of all advertising materials available for use during the experience period. The Company provided a list of 55 pieces of Company produced advertising materials. The Company indicated that all pieces of advertising were produced internally with no agent or producer generated materials.

3 Exceptions – 18 Del. C. §2304. Unfair methods of competition and unfair or deceptive acts or practices defined.

(2) False information and advertising generally. -- No person shall make, publish, disseminate, circulate or place before the public, or cause, directly or indirectly, to be made, published, disseminated, circulated or placed before the public, in a newspaper, magazine or other publication, or in the form of a notice, circular, pamphlet, letter or poster, or over any radio or television station, or in any other way, an advertisement, announcement or statement containing any assertion, representation or statement with respect to the business of insurance or with respect to any person in the conduct of the insurance business, which is untrue, deceptive or misleading.

The marketing and sales advertising exceptions resulted from the Company referencing statistics without a reference of the source for marketing form numbers 9493, 10271, 10478, which could result in misleading or deceptive statements or assertions.

Recommendation: It is recommended that the Company reference the source of all statistics used in their advertising to avoid possible misrepresentation and comply with 18 Del. C. §2304(2).

1 Exception – 18 Del. C. §2304. Unfair methods of competition and unfair or deceptive acts or practices defined.

(11) False statements and entries. --

c. No person shall advertise the capital or assets of any insurer without in the same advertisement setting forth the amount of the insurer's liabilities.

One exception resulted from policy form number 7955 and marketing form number 9529 which contained a report of assets without the amount of the insurer's liabilities being reported.

Recommendation: It is recommended that the Company include the insurer's liabilities where a report of assets is used in any marketing or policy form. 18 Del. C. §2304(11)c.

UNDERWRITING AND RATING

A) Issued Annuities

The Company identified a universe of 167 new accumulator annuity contracts issued by Life Insurance Company of the Southwest during the experience period. A random sampling of 50 annuity contracts was reviewed. The following violations were noted:

10 Exceptions - 18 Del. Admin. Code 1204 §7.1 Replacement of Life Insurance

Each insurer that uses an agent of broker in a life insurance or annuity sale shall:

7.1.2 Where a replacement is involved:

7.1.2.2 Send to each existing insurer a written communication advising of the replacement or proposed replacement of the policy. The communication should include the information obtained pursuant to section 7.1.2.1 above and a Summary or Ledger Statement describing the proposed new policy. This written communication shall be made within 7 working days of the date the application is received in the replacing insurer's home office, or the date the proposed life insurance policy or annuity contract is issued, whichever is sooner.

The written communication advising of the replacement to the existing insurer was not provided as required as required by 18 Del. Admin. Code 1204 §7.1.

Recommendation: It is recommended that the Company ensure notification to existing insurers of a pending replacement in compliance 18 Del. Admin. Code 1204 §7.1.

B) Terminated/Cancelled Annuities

The Company provided a list of all Annuity Policies terminated during the experience period. The Company identified a universe of 20 terminated annuities. The policies were reviewed. The files were reviewed to ensure that terminations were not the result of any discriminatory underwriting practices. The files terminated due to death were reviewed for compliance with 18 *Del. Admin. Code* 902 and 903.

There were no exceptions noted during the file review.

C) Not Taken Annuities

The Company provided a list of all annuity contracts not taken during the experience period. The Company indicated one (1) annuity contract was issued and not taken at delivery. The annuity not-taken file was reviewed to ensure compliance with the free-look provisions of the contract and applicable statutory requirements, as applicable.

No exceptions were noted.

D) Surrendered Annuities

The Company provided a list of all annuity contracts surrendered during the experience period. The Company identified a universe of 19 surrendered annuities during the exam period. The annuities were reviewed to ensure that the surrenders were properly handled. The surrenders were reviewed for compliance with 18 *Del. Admin. Code* 902 and 903.

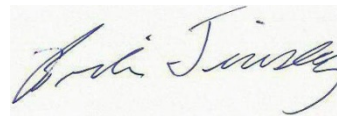
No exceptions noted.

CONCLUSION

The recommendations made below identify corrective measures the Department finds necessary as a result of the exceptions noted in the Report. Location in the Report is referenced in parenthesis.

1. It is recommended that the Company immediately cease using form numbers 5776 and 7775 until the form has been submitted and approved by the Delaware Department of Insurance as required by 18 Del. C. §2712.(Company Operations and Management: Policy Forms)
2. It is recommended that the Company review its procedures to ensure that all complaints are identified and logged in compliance with 18 *Del. C.* §2304 (17). (Consumer Complaints)
3. It is recommended that the Company ensure the source is identified when using statistics in their marketing forms to avoid misleading or deceptive statements or assertions in order to comply with 18 *Del. C. Code* §2304(2). (Marketing and Sales)
4. It is recommended that the Company include the insurer's liabilities where a report of assets is used in any marketing or policy form in accordance with 18 *Del. C.* §2304 (11) (c), Unfair methods of competition and unfair or deceptive acts or practices defined. (Marketing and Sales)
5. It is recommended that the Company ensure notification to existing insurers of a pending replacement in compliance 18 *Del. Admin. Code* 1204 §7.1. (Issued Annuities)

The examination conducted by Shelly Schuman, Brian Tinsley, Steve Misenheimer, and John Rucidlo, is respectfully submitted.



Brian Tinsley, AIE, MCM
Examiner-in-Charge
Market Conduct
Delaware Department of Insurance