

STATE OF MICHIGAN
DEPARTMENT OF INSURANCE AND FINANCIAL SERVICES



MARKET CONDUCT EXAMINATION

NUMBER 2015C-0097

October 7, 2016

TARGETED MARKET CONDUCT EXAMINATION REPORT

OF

MEMBERS LIFE INSURANCE COMPANY

WAVERLY, IOWA

NAIC COMPANY CODE 86126

For the Period January 1, 2014 through December 31, 2014

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I. EXECUTIVE SUMMARY

Members Life Insurance Company (the Company) is an authorized Iowa domiciled company. This targeted examination was conducted by the Michigan Department of Insurance and Financial Services (DIFS) in conformance with the National Association of Insurance Commissioners (NAIC) *Market Regulation Handbook* (2014) (*Handbook*) and the Michigan Insurance Code, MCL 500.100 et seq. (the Code).

DIFS conducted this examination in accordance with statutory authority of MCL 500.222 et seq. All Michigan laws, regulations, and bulletins cited in this report may be viewed on the [DIFS website](http://www.michigan.gov/difs) at www.michigan.gov/difs, or on the [Michigan Legislature website](http://www.legislature.mi.gov) at <http://www.legislature.mi.gov>. Note: Code citations may be sans specific statutory language when a statute is significantly long or a chapter is applied broadly to one or more standards (“et seq.” will then be used). However, statutory language may be included with certain citations, when and if there are findings, observations or discussion points within the report or management letter that benefit from specific reference.

This is a targeted examination of the Company’s individual variable annuity line of business, conducted remotely, as a result of analysis of the Company’s NAIC Market Conduct Annual Statement (MCAS) 2014 submission. The examination was called for January 1, 2013 through December 31, 2014; however, only 2014 data was ultimately reviewed as there were no surrenders or other concerns with 2013 data.

The purpose of the exam is to evaluate the compliance of the Company with applicable Michigan statutes, NAIC guidelines, and DIFS regulations. The scope of market conduct examination includes the Company’s activities related to the handling of: (1) Marketing and Sales, (2) Underwriting and Rating, and (3) Producer Licensing. The examination team consisted of Sherry J. Bass-Pohl, Examiner-in-Charge, and Christopher Gleason, Market Analyst.

This summary of this targeted market conduct examination of the Company is intended to provide a high-level overview of the examination results. The body of the report provides the Company responses, findings, and DIFS recommendations.

DIFS considers a substantive issue one in which a “finding” or violation of Code was found to have occurred, or one in which corrective action on the part of the Company is deemed advisable.

Findings:

There are no findings.

Recommendations:

There are no recommendations.

II. EXAMINATION FINDINGS AND RECOMMENDATIONS

The examination followed a pre-determined protocol of interrogatories developed by the DIFS subject matter expert (SME) for all variable annuity companies identified through specific MCAS analysis. The interrogatories were designed to assess risk and evaluate compliance in the areas specifically related to the identified MCAS ratios, with an increased focus on suitability and suitability oversight programs and producer licensing. The questions and the Company's responses to those questions are reproduced below.

A. MARKETING AND SALES

Standard 1: All advertising and sales materials are in compliance with applicable statutes, rules and regulations. NAIC *Handbook*, Chapter 16.

MCL 500.2007:

The following are defined as unfair methods of competition and unfair and deceptive acts or practices in the business of insurance: Making, publishing, disseminating, circulating, or placing before the public, or causing, 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 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 his insurance business, which is untrue, deceptive or misleading.

Standard 2: Regulated entity internal producer training materials are in compliance with applicable statutes, rules and regulations. NAIC *Handbook*, Chapter 16.

Standard 3: Regulated entity communications to producers are in compliance with applicable statutes, rules and regulations. NAIC *Handbook*, Chapter 16.

Standard 5: The insurer has suitability standards for its products, when required by applicable statutes, rules and regulations. NAIC *Handbook*, Chapter 19.

Standard 9: Insurer rules pertaining to producer requirements with regard to suitability in annuity transactions are in compliance with applicable statutes, rules and regulations. NAIC *Handbook*, Chapter 19.

MCL 500.4160(1):

(1) A producer shall not solicit the sale of an annuity unless the producer has adequate knowledge of the product to recommend the annuity and the producer is in compliance with the insurer's standards for product training.

A producer may rely on insurer-provided product-specific training standards and materials to comply with this subsection.

(2) A producer who engages in the sale of annuities shall complete a 1-time 4-credit training course approved by the commissioner and provided by an insurance producer program of study registered under chapter 12. ...

Standard 10: Insurer rules pertaining to suitability in annuity transactions are in compliance with applicable statutes, rules and regulations. NAIC *Handbook*, Chapter 19.

Standard 11: The insurer has procedures in place to educate and monitor compliance with insurer-specific education and training requirements and with applicable statutes, rules and regulations regarding the solicitation, recommendation and sale of annuity products. NAIC *Handbook*, Chapter 19.

Standard 12: The insurer has product-specific training standards and materials designed to provide producers with adequate knowledge of the annuity products recommended prior to soliciting the sale of annuity products. The insurer must also have reasonable procedures in place to require its producers to comply with applicable producer training requirements. NAIC *Handbook*, Chapter 19.

The following statutes apply to *Handbook* Chapter 16, Standards 1, 2, and 3, as well as *Handbook* Chapter 19, Standards 5, 9, 10, 11, and 12:

MCL 500.4158(1):

An insurer shall establish a supervision system that is reasonably designed to achieve the insurer's and its producers' compliance with this chapter, including, but not limited to, all of the following:

(a) Maintain reasonable procedures to inform its producers of the requirements of this chapter and incorporate the requirements of this chapter into relevant producer training manuals. (b) Establish standards for producer product training and maintain reasonable procedures to require its producers to comply with section 4160. (c) Provide product-specific training and training materials that explain all material features of its annuity products to its producers.

(b) Establish standards for producer product training and maintain reasonable procedures to require its producers to comply with section 4160.

(c) Provide product-specific training and training materials that explain all material features of its annuity products to its producers.

(d) Maintain procedures for review of each recommendation before issuance of an annuity that are designed to ensure that there is a reasonable basis to determine that a recommendation is suitable. Review procedures may apply a screening system for the purpose of identifying

selected transactions for additional review and may be accomplished electronically or through other means, including, but not limited to, physical review. An electronic or other system may be designed to require additional review only of those transactions identified for additional review by the selection criteria.

(e) Maintain reasonable procedures to detect recommendations that are not suitable. This may include, but is not limited to, confirmation of consumer suitability information, systematic customer surveys, interviews, confirmation letters, and programs of internal monitoring. This subdivision does not prevent an insurer from complying with this subdivision by applying sampling procedures or by confirming suitability information after issuance or delivery of the annuity.

(f) Annually provide a report to senior management, including to the senior manager responsible for audit functions, that details a review, with appropriate testing, reasonably designed to determine the effectiveness of the supervision system, the exceptions found, and corrective action taken or recommended, if any.

1. The MCAS data indicates that 100% of the Company's total surrendered individual variable annuity contracts are surrendered less than ten (10) years in force (Ratio #4). This exceeds the Michigan average of 62.31%. Please provide an explanation as to why the Company has this percentage of surrendered contracts less than ten (10) years in force and why its average is higher than the state average. Describe what plans, if any, you have in place to bring this number down. [Note: This statistic was inadvertently cited incorrectly. The Michigan average is actually 29.3%.]

Company Response:

The Company reported one variable annuity surrendered less than 10 years in force. As noted in our cover letter, MEMBERS Life Insurance Company is currently only marketing one annuity contract and sales of that contract commenced in the last half of 2013. As such we would anticipate that any surrenders in the next ten years will impact this ratio, making it appear higher than the matured blocks of business it is being compared to held by industry peers.

DIFS' Comment on Company Response:

DIFS accepts the Company's explanation that only one product is offered and it has been offered for a brief period which would result in all surrenders being under ten years. There are no concerns at this time.

Findings:

There are no findings.

Recommendations:

There are no recommendations.

2. Please give a brief description of the product development process currently in place in the Company. Describe what measures you take during the product development phase to help ensure that the products developed will be sold to suitable clients.

Company Response:

The product development process involves several areas throughout the company including representatives from marketing/sales, legal/compliance and operations/administration. The development process consists of multiple phases which include but are not limited to:

1. Product Concept & Market Research - New product concepts are developed and tested against available market research. Target market(s) are identified and evaluated for size/scale, customer value, and profitability. Suitability considerations relative to the target market identification (e.g. min/max issue ages, Internal Revenue Code considerations, distribution channel, etc.) are assessed.
2. Business Case Development - The consumer need (e.g. protected retirement accumulation, outliving one's assets in retirement, etc.) to be met by the product is clearly defined. The target market and financial viability of the product are analyzed and further clarified. Strategic fit within the retail annuity product portfolio is confirmed.
3. Product Planning/Development - Product specifications are developed and product success measures created and the following plans are developed: (1) overall implementation, (2) IT, (3) operations, (4) filing, (5) marketing, (6) sales and (7) staff and producer training. Suitability is directly addressed within the Operations, Filing Strategy and Training Plans.
4. Launch - Product is made available for sale to consumers after receipt of regulatory approval, delivery of producer training, system implementations, updates to operational processes, staff training and suitability standards which satisfy annuity recommendations to consumers defined in Michigan Code 500.4151 – 500.4165.

DIFS' Comment on Company Response:

The Company states it considers suitability factors, and in what ways it considers these factors when developing new products. Based on the Company's statement, DIFS is satisfied with the measures outlined.

Findings:

There are no findings.

Recommendations:

There are no recommendations.

3. Does the Company allow the sale of an annuity if the applicant refuses to provide the necessary suitability information on the application? Please explain and attach the Suitability form that the Company uses for variable annuity sales in Michigan.

Company Response:

Michigan Insurance Code 500.4158 allows insurers to contract with a third party to establish and maintain a system of supervision that is reasonably designed to ensure suitability sales. Michigan Code 500.4165 provides a safe harbor provision which states that sales made in compliance with FINRA requirements will satisfy the requirements outlined in the Michigan Code. The MEMBERS Zone annuity product is a registered product, and therefore, subject to FINRA requirements. FINRA rules do not require suitability determinations for unsolicited sales of variable annuities. The Company contracts with distribution partners to establish and maintain a FINRA compliant system of supervision for the MEMBERS Zone annuity product. A customer's refusal to provide suitability information for an unsolicited sale is acceptable if the Broker/Dealer principal review approves the application as an unsolicited sale. Each distribution partner has their own set of forms; therefore, we do not require an internal suitability questionnaire in order to avoid duplicative forms.

DIFS' Comment on Company Response:

DIFS reviewed documents including the Company's 2014 Report for CMFG Life Insurance Company and MEMBERS Life Insurance Company Annuity Policies and Procedures (Report to Senior Management) and 2014 Suitability in Annuity Transactions Procedures. DIFS is satisfied with documentation that the Company has sufficient policies and procedures for ensuring suitability in place. The Company has contractual relationships with entities that perform suitability review; however, the Company appropriately notes in its Report to Senior Management that it maintains supervision over the third party entities, and a review of the Company's processes for ensuring third party distributors perform suitability oversight of producers are adequate.

Findings:

There are no findings.

Recommendations:

There are no recommendations.

4. Does the Company currently create a report to senior management with regards to the internal annuity suitability supervision system in Michigan? If so, attach a copy of the most recent report. If not, attach a copy of the most recent internal audit report relevant to this line of business in Michigan. In this case, detail why the Company does not currently produce a report to senior management for Michigan. Include if the Company has plans to generate this report in the future.

Company Response:

MEMBERS Life Insurance Company complies with Michigan Insurance Code 500.4158 by providing an annual report of the testing of the Company's annuity products compliance with annuity suitability regulations. The report provides an in-depth explanation of requirements, findings, and issues for annuity transactions for the previous year. The purpose of this report is to test and verify that the Company's supervisory procedures are reasonably designed to achieve compliance with applicable state laws/regulations and to determine the effectiveness of its' supervision system. See attached 2014 report.

DIFS' Comment on Company Response:

The 2014 report was reviewed and does include internal annuity suitability supervision measures. This report includes recommendations which, if put in place, will strengthen the Company's annuity suitability supervision.

Findings:

There are no findings.

Recommendations:

There are no recommendations.

5. Describe how the Company provides product-specific training to producers in Michigan.

Company Response:

Currently, the company utilizes the RegEd Annuity Training Platform for delivery of company product-specific training. The Annuity Product Team occasionally provides classroom/webinar sessions for delivery of the product-specific training as an alternative method of delivering the product specific training as well.

DIFS' Comment on Company Response:

DIFS is satisfied that the Company provides contracted and in-house product training. Additionally, the Company states in its Report to Senior Management that instances where producers did not complete training prior to submitting applications, resulted in the applications being rejected.

Findings:

There are no findings.

Recommendations:

There are no recommendations.

6. Does the Company require continuing education with regard to the products offered? Describe your supervision system that ensures that requirements are met, and that the

producers are adequately explaining the terms and conditions of an annuity before submitting the application.

Company Response:

Producers who engage in the sale of annuity products in Michigan must complete state specific education/training requirements before soliciting sales of annuity products. Producers who wish to sell MEMBERS annuity products in Michigan must complete 4 hours of one-time annuity training before selling annuity products, as well as complete MEMBERS product-specific annuity training. When there is a new annuity product development or significant changes to existing annuity products, producers must complete new product training modules. Producers are also required to disclose information about annuity contracts to protect consumers and foster consumer education. The Company will not accept annuity applications unless all required state annuity suitability education/training has been completed and the product disclosure document signature page has been received with the application to confirm the [sic] the consumer has been reasonably informed of the various features of the annuity.

DIFS' Comment on Company Response:

The training outlined by the Company, and which it states is monitored via application review by the Compliance Team, would comply with producer training required by MCL 500.4158(1). Recommendations outlined in the Senior Report, if enacted, would strengthen supervision.

Findings:

There are no findings.

Recommendations:

There are no recommendations.

7. Please describe the commission structure used to pay producers who sell individual variable annuities for the Company. Include if the commissions vary depending on type of product sold or the manner in which it is funded, e.g. deferred versus immediate, 1035 exchange, etc.

Company Response:

The Members products are distributed through two distribution systems. One is via CBSI, an affiliated broker dealer that has financial service networking agreements in place with more than 300 credit unions. CBSI receives the same level of commissions as an independent broker dealer. The CBSI producers are compensated based on overall Gross Dealer Concession (GDC) production. The CBSI producers receive higher payouts as total production increases according to production breakpoints. The compensation they receive for a specific annuity transaction depends on their total production from sales of all products.

External Broker Dealers receive a commission per product based on the commission rate applied per product as set in their dealer agreements. Commissions vary by product and may vary based on the owner's age. Early surrenders may be subject to commission chargebacks. There are no commission adjustments for 1035 exchanges.

DIFS' Comment on Company Response:

The Company's response reflects there are no commission incentives to market this product inappropriately to older individuals, such as increase in commission with increase in age of applicant. Likewise, commission is not increased with funding from sources which may incur surrender charges. DIFS accepts the Company's explanation of its commission structure.

Findings:

There are no Findings.

Recommendations:

There are no Recommendations.

8. Describe how advertising pieces for individual variable annuities are created by the Company or by the Company's producers. If created by producers, describe the approval process utilized by the Company to ensure compliance with Michigan rules and regulations, including the Michigan Insurance Code, MCL 500.001 et seq. Include web site approval of producers if Company products are mentioned.

Company Response:

Advertising materials for individual variable annuities are created by the Wealth Accumulation Marketing department. The Governance, Risk & Assurance (GRA) department oversees a process that ensures all marketing materials meet the requirements of our regulators. All marketing materials undergo a compliance review and approval before they are used with the public. This includes any material or medium used to promote interest in annuity products. Producers are not permitted to create advertising pieces for variable annuities.

DIFS' Comment on Company Response:

The review of advertising materials outlined and prohibition of producer-created advertising the Company states it has in place, comply with Michigan statute.

Findings:

There are no Findings.

Recommendations:

There are no Recommendations.

B. UNDERWRITING AND RATING

Standard 5: All forms, including contracts, riders, amendments, endorsement forms and certificates are filed with the insurance department, if applicable. NAIC *Handbook*, Chapter 16.

MCL 500.4111:

The filing requirements applicable to modified guaranteed annuities are those filing requirements otherwise applicable under existing statutes and regulations of this state concerning individual and group life insurance and annuity contract form filings, to the extent appropriate, provided, however, filings shall include a demonstration in a form satisfactory to the commissioner that the nonforfeiture provisions of the contract comply with section 4115.

The examiners requested a description of all individual variable annuity products available for purchase in Michigan during the exam period. This listing was used to verify that all products had been properly filed for use with DIFS.

9. Please provide a brief description for each of the Company's individual variable annuity products available in Michigan during the exam period. Include each product's target demographic, any surrender period and penalties, deferment periods, and fees and interest rates for each. Also include the most recent SERFF Tracking Number proving that each annuity sold here has been approved for sale in Michigan.

Company Response:

The Company's only annuity sold in Michigan is the MEMBERS Zone product filed as a Modified Guaranteed Annuity (A071.002) on November 19, 2012, approved for sale on February 8, 2013. The SERFF tracking number is CUNA-128763673.

The MEMBERS Zone is a Single Premium Deferred Modified Guaranteed Index Annuity with the assets held in an insulated, non-unitized separate account, and is registered as a security with the SEC. The contract has two periods, the accumulation period and the payout period. It is marketed as a retirement savings vehicle for issue ages 0-85 for a minimum qualified or non-qualified purchase payment of \$5,000. Applicants allocate the purchase payment between two risk control accounts, the Secure Account and the Growth Account according to their level of risk selecting from a 5, 7, or 10 year initial index period. The risk control accounts earn interest based on the performance of an external index. Each risk control account has its own index interest rate cap and associated index interest rate floor. The index interest rate floor for the Secure Account is 0.0% while the Growth Account has an index interest rate floor of -10.0% which offers more upside potential in the form of a higher index interest rate cap. The index interest cap is guaranteed for one year; subject to change thereafter, and will not fall below the minimum rate cap of 1.0%.

During the initial index period, 10% of the beginning of year contract value each year is available for withdrawal without a surrender charge or market value adjustment. The market value adjustment may increase or decrease the amount withdrawn. The surrender charge schedule for each initial index period is as follows:

Contract Year	1	2	3	4	5	6	7	8	9	10
Charge (10yr)	9%	9%	8%	7%	6%	5%	4%	3%	2%	1%
Charge (7yr)	9%	9%	8%	7%	6%	5%	4%	0%	0%	0%
Charge (5yr)	9%	9%	8%	7%	6%	0%	0%	0%	0%	0%

Surrender charges and the market value adjustment are not applied to death proceeds and are waived for hardships (nursing home/hospital confinement or terminal illness) as described in the contract.

DIFS' Comment on Company Response:

The MEMBERS Zone annuity is appropriately filed in compliance with MCL 500.4111. Product features do not raise any concerns.

Findings:

There are no findings.

Recommendations:

There are no recommendations.

C. PRODUCER LICENSING

Standard 1: Regulated entity records of licensed and appointed (if applicable) producers and in jurisdictions where applicable, licensed company or contracted independent adjusters agree with insurance department records. NAIC *Handbook*, Chapter 16.

MCL 500.1208a(1):

An insurance producer shall not act as an agent of an insurer unless the insurance producer becomes an appointed agent of that insurer. An insurance producer who is not acting as an agent of an insurer is not required to become appointed.

Standard 2: The producers are properly licensed and appointed and have appropriate continuing education (if required by state law) in the jurisdiction where the application was taken. NAIC *Handbook*, Chapter 16.

10. Please provide a list of all producers from whom the Company accepted applications for Michigan products during the exam period. The list shall include, at

least, the following information for each appointed producer: name, address, NPN, appointment date, and date the Company first accepted business from the producer.

Company Response:

Note: The Company provided an Excel spreadsheet containing the requested data.

File Data	Population Size	Maximum Number of Failures Permitted in Sample	Stage 1 Sample Size	Date Sample Pulled	Errors Found
Michigan producers from whom the Company accepted business during the examination period	50	n/a	n/a	n/a	0

The examiner conducted a census review of all Michigan producers from whom the Company accepted business during the examination period by comparing Company-provided data against the DIFS internal producer licensing database.

DIFS Comment on Company Response:

The review outlined above was conducted and there were no violations of MCL 500.1208a for unappointed activity.

Findings:

There are no Findings.

Recommendations:

There are no Recommendations.

III. ACKNOWLEDGEMENT

This examination report of Members Life Insurance Company is respectfully submitted to the Director of the Department of Insurance and Financial Services, State of Michigan.

The courteous cooperation and assistance of the officers and employees of the Company extended to the examiners during the course of the examination is hereby acknowledged.

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In addition to the undersigned, Christopher Gleason, Market Conduct Analyst, participated in the examination.

Sherry J. Bass-Pohl, AMCM
Examiner-in-Charge
Department of Insurance and Financial Services
Market Conduct Section