

STATE OF MICHIGAN
DEPARTMENT OF INSURANCE AND FINANCIAL SERVICES



MARKET CONDUCT EXAMINATION

NUMBER 2014C-0069

June 5, 2015

TARGETED MARKET CONDUCT EXAMINATION

OF

NATIONAL WESTERN LIFE INSURANCE COMPANY

DENVER, CO

NAIC COMPANY CODE 66850

For the Period January 1, 2012 through December 31, 2012

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I. EXECUTIVE SUMMARY

National Western Life Insurance Company (the Company) is an authorized Colorado 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* (2012) (*Handbook*) and the Michigan Insurance Code, MCL 500.100 et seq. (the Code).

The interrogatory covers the period January 1, 2012 to December 31, 2012. The interrogatory was conducted under the supervision of Sherry J. Bass-Pohl, Manager of the Market Conduct Company Examination Unit.

This is a targeted risk assessment interrogatory, conducted via mail, as a result of analysis of the NAIC Market Conduct Annual Statement (MCAS) submission. There are no Findings or Recommendations.

II. INTERROGATORY TO COMPANY

Following is each interrogatory provided to the Company, followed by the Company response:

1) Please provide a written description of each of National Western Life Insurance Company's (the Company) Individual Fixed Annuities that were offered during the last three years. Be sure to describe any surrender period and penalties, deferment periods, fees and interest rates for each.

Company Response:

Attached please find "Highlight Sheets" for each individual fixed annuity offered for sale in Michigan during the last three years, which contain the information you have requested, including but not limited to withdrawal charges, contract term, and guaranteed interest rates.

Examiner's Note: The Company provided all information as requested. This information is not reproduced in this report.

DIFS' Comment on Company Response:

DIFS has no comment in connection with this question.

2) Please provide a written description of the underwriting processes in place during the exam period. How do you ensure that all annuities sold by the Company are suitable? How do you ensure that multiple contracts are not sold to individual annuity owners? Please attach the Suitability form that the Company uses for Individual Fixed Annuities.

Company Response:

Attached please find our Suitability Department's internal and external suitability guidelines. The PDF entitled "National Western Life Practical Suitability Guidelines" is a basic checklist for our producers. It does not address all circumstances but is designed to address some of the most common questions raised by producers. The document entitled "Annuity Suitability Analyst Guidelines for Corrections on Annuity Suitability Questionnaire" is used internally only and serves as the Suitability Department's guidelines for making suitability determinations.

National Western will allow more than one annuity to be sold to a consumer if, at a minimum, it is part of a planning strategy that aids in meeting a financial or estate planning objective and if each annuity meets the suitability criteria as outlined in our guidelines and set forth by the Company. All annuity sales are reviewed on an individual basis to ensure that each is an overall benefit to the consumer.

Attached please find form DM-1174, which is the Company's Annuity Suitability Questionnaire for All Applicants.

DIFS' Comment on Company Response:

The suitability factors on the Suitability Questionnaire meet the requirements of the Michigan Insurance Code, specifically those factors required in MCL 500.4151(e).

The checklist for approval seems to adequately account for mistakes without obviously allowing unsuitable sales.

3) The MCAS data also indicate that approximately 85% of the Company's total surrendered contracts are surrendered in less than 10 years from the effective date. Is this accurate? Can you please provide an explanation as to why the Company has so many surrendered contracts? Does this raise any suitability concerns at the Company underwriting level? What plans do you have in place to bring this number down?

Company Response:

The Company's Accounting Department has confirmed that the 2012 MCAS data that you referenced in your letter is accurate. Please note that some of our products have contract terms of ten years or less.

National Western has a wide variety of annuity contracts to offer to prospective purchasers with varying benefits and features. One feature that is fairly standard throughout is the liquidity of our products. Most products allow annuitization after five years for a minimum of five years, without withdrawal charges. A consumer's financial situation and needs may change over time, and the ability to surrender in less than ten years is a beneficial feature. The Company is pleased to be able to provide consumers with flexible products that meet their needs.

In addition, a third party may contribute to a consumer's decision to surrender a National Western annuity and replace it with a product from another company. While we would be happy to retain the consumer's business and continue servicing his or her needs, National Western is contractually obligated to comply with its policyholders' surrender requests and does not employ high pressure "conservation" tactics to influence their decision.

Additional contributing factors to the surrender rate could be based on the changing insurance environment as companies release more competitive products. Over the past several years, these products increasingly include substantial premium bonuses that can recapture the surrender charges the consumer may incur as a result of the replacement. National Western also has a number of products that offer such premium bonuses. Further, due to the more competitive market, severe market fluctuation, and other well-known insurance institutions merging or selling off books of business, consumers are also diversifying their assets more. Diversification can range from a full replacement to a moving a 10% penalty-free amount to take advantage of additional premium bonuses offered with other companies' products.

A consumer's decision to surrender his or her annuity does not indicate that the purchase of that product was not suitable at the time of application but rather evidences a variety of other possibilities, such as change in circumstances, third party influence, market fluctuation, product competition, etc. It should be noted that National Western continues to review and if necessary modify its suitability guidelines and performs a variety of audit measure, such as client surveys and annual reviews, to ensure that suitability determinations are proper and that the Company's procedures are effective.

The Company does not intend to make concerted efforts to reduce the surrendered contracts percentage but rather intends to focus efforts on continuing to provide products that allow for flexibility and financial security, while maintaining our customer service standards and meeting any and all contractual obligations and regulatory requirements.

DIFS' Comment on Company Response:

DIFS agrees that surrenders can be caused by extenuating factors and does not automatically mean a sale was unsuitable.

4) Please describe in detail the commission structure used to pay producers who write Individual Fixed Annuities for the Company. Does the commission 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:

Commissions are paid based on a Company-approved rate per product per producer record. These rates are provided to the producers, via commission schedule, at time of onboarding with the Company. For example, a producer may be appointed with us to sell annuities and set up with a level 1 commission level, which pays 4% First Year commission on issue ages 0-75 on the NWL IMPACT 10® product. Other rates per product are reflected on the commission schedule as well. Attached please find a sample of the commission schedule the producer would have received in the example stated above.

Please note that the commission rates do vary by product, but it is based more specifically on how the pricing was determined, set, and approved by the Actuarial Department rather than the type of product or method of receipt by the Company, such as deferred versus immediate or 1035 exchange.

DIFS' Comment on Company Response:

DIFS has no comment in connection with this question.

5) Please detail the Company's training methods used to educate producers on the products that the Company offers. Does the Company require any continuing education with regard to the products offered? How does the Company make sure that producers have the appropriate level of knowledge of the Company's specific annuity products?

Company Response:

National Western requires that all producers who sell the Company's annuity products complete our Product-Specific Training. This training program is designed to provide our producers with knowledge of the types of annuity products offered by the Company as well as specific features that each product provides.

National Western currently uses QuestCE, a continuing education provider, to facilitate this training program. QuestCE houses our program content, and we validate each producer's completion of this training via information received from QuestCE daily or by direct query of the QuestCE database. The information is queried using the producer's social security number as key search criterion. The information returned from the query includes the producer's name, social security number, affiliated company/national marketing organization, the date registered, date completed, and the course name, title, and code.

In addition to Product-Specific Training, the Company also conducts in-person and web-based training for producers and Independent Marketing Organizations that focuses on describing product features and explaining in more detail how the products generally operate.

DIFS' Comment on Company Response:

The Company response is satisfactory as required in MCL 500.4160.

6) Are the advertising pieces for Individual Fixed Annuities created by the Company or by the Company's producers? If created by producers, please describe the approval process utilized by the Company to ensure compliance with the Insurance Code of the State of Michigan, MCL 500.0001 et seq.

Company Response:

National Western has advertising pieces that are created by the Company as well as producer-submitted advertising.

Our producers are contractually obligated to comply with our Rules and Regulations, which include the advertising approval process utilized by the Company for advertising pieces created by producers. The Company's approval process requires that all advertising that a producer creates be submitted to the Company for review prior to its use or dissemination. Please find attached an excerpt from the Agent Procedure Manual (Rules and Regulations) detailing the Advertising Approval Procedures and Guidelines.

Please note also that National Western sends a Compliance Bulletin annually to producers reminding them that all advertising must be submitted to the Company for review prior to use or dissemination and that written approval from the Company is required, as well as reiterating that failure to comply with our advertising procedures could result in termination. A copy of the Compliance Bulletin that went to producers in 2014 is attached.

DIFS' Comment on Company Response:

DIFS has no comment in connection with this question.

Recommendations and Conclusion:

There are no recommendations or findings in connection with this interrogatory. The Company appears to be in compliance with the relevant sections of the Michigan Insurance Code.

III. ACKNOWLEDGEMENT

This targeted examination report of National Western Life Insurance Company is respectfully submitted to the Commissioner 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 examiner during the course of the examination is hereby acknowledged.

In addition to the undersigned, Zachary Dillinger, Senior Market Conduct Examiner, participated in the examination.

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