



REPORT ON  
EXPANSION APPLICATION TO LIFT RESTRICTIONS  
AND  
ALLOW NEW BUSINESS SALES

OF

*Capitol Life Insurance Company*  
(NAIC Company Code 61581)

*as of*

*May 27, 2021*

*State of Rhode Island*  
*Department of Business Regulation*  
**Insurance Division**



**State of Rhode Island  
DEPARTMENT OF BUSINESS REGULATION  
1511 Pontiac Avenue, Bldg. 69-2  
Cranston, Rhode Island 02920**

**Insurance Division**

**ADOPTION ORDER**

The attached Report on Expansion Application to Lift Restrictions and Allow New Business Sales (“Report”) as of May 27, 2021 of Capitol Life Insurance Company, was recently completed by duly qualified examiners pursuant to the provisions of the Rhode Island General Laws.

Due consideration has been given to the comments of the examiners regarding the operation of the Company and its affairs, as reflected in the report.

It is therefore ORDERED that said Report be, and it is hereby, adopted and filed and made an official record of this Department as of this date subject to the following conditions:

- That a Consent Agreement between the Company and the Insurance Division be executed requiring the Company to implement the corrective actions identified in the Report’s Conclusion and to provide the Insurance Division with all requested follow-up information and procedures, as outlined in the Report’s Conclusion.
- That upon the execution of that Consent Agreement, Capitol Life Insurance Company’s license will be reactivated to begin conducting business in Rhode Island again.
- And that monitoring of the Company’s business activity in Rhode Island by the Insurance Division be continued thorough performance of annual MARS analysis until this is no longer deemed necessary.

DEPARTMENT OF BUSINESS REGULATION

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Elizabeth Kelleher Dwyer  
Superintendent of Insurance

Dated September 7, 2021

## **Company Request to Re-Enter Rhode Island Marketplace**

Capitol Life Insurance Company (cocode 61581) (the “Company”) applied to reactivate its license in January 2018 in order to conduct business in the Rhode Island marketplace. In response, the Market Conduct Unit of the Rhode Island Department of Business Regulation (the “Department”) reviewed the Company’s national MCAS data as well as the data for its affiliated company, Liberty Bankers Life Insurance Company (cocode 68543), to review the market activities of the related company in recent years. Based on that cursory review, the Department informed the Company that they should withdraw their application. The Company asked for further information and discussion, and the Company and the Department had several interactions during March and April 2019. The Company asked that the Department take a more robust look at their business operations and sales history, essentially to look beyond the Market Conduct Annual Statement (“MCAS”) metrics.

The initial review of the Department included a review of the national MCAS scores of the combined companies, from 2015 through 2017, and noted that those ratios were more than 80% above the national averages in numerous areas.

- Individual Annuity Ratio 1 (replacements issued to contracts issued);
- Individual Annuity Ratio 2 (replacements for annuitants age > 80 total replacements);
- Individual Annuity Ratio 3 (deferred contracts issued to annuitants age > 80 to total deferred contracts issued);
- Individual Life Ratio 2 (replacements where insureds age > = to total replacements);
- Individual Life ratio 5 (claims paid beyond 60 days from the date of due proof to claims paid); and
- Individual Life ratio 6 (claims denied, resisted, or compromised to claims closed).

From 2015 through 2018, the combined companies also reported:

- 344 of 691 annuity contracts issued (49.78%) were replacements,

- 70 of 344 annuity replacements (20.34%) were issued to individuals aged 80 years or older;
- 94 of 677 deferred annuity contracts (13.88%) were issued to individuals aged 80 years or older;
- 57 of 141 total life insurance replacements (40.42%) were issued to individuals aged 65 or older;
- 37 of 129 life insurance claims closed (28.68%) were paid more than 60 days from date of due proof to claim paid; and
- 32 of 161 claims closed during the period (19.88%) were denied, resisted, or compromised.

These ratio outliers show an unusually high proportion of new business qualifying as replacements, an unusually high proportion of new senior business qualifying as replacements, an unusually high proportion of claims denied, and an unusually high proportion of delayed payments on claims. The trends in replacements are concerning to regulators because annuity replacements present a greater risk of consumer harm than other sales. Laws and regulations require insurers and producers to perform additional work and scrutiny in reviewing and approving those replacement applications. The trends and claims denied and delayed payments on claims are also concerning in that it could be indicative of general practices in which the insurer is not fulfilling its financial obligations to its customers.

In response to these numbers, the Company identified that its Third-Party Administrator (“TPA”) had overreported replacements in MCAS metrics. The Department initially suggested that the Company try to improve upon their national MCAS scores and come back to the Department to discuss again in a couple years. Alternatively, the Department offered that the state could perform more detailed testing on the Company to determine whether or not it should be authorized to sell again in Rhode Island; but that time the Market Conduct unit would spend

on the company would be paid for by the company. In May 2019, the Company requested that the Department perform this additional testing.

### **Sampling and Testing Procedures**

In June 2019, the Company provided a listing of 136 Texas annuity replacements and 44 Massachusetts annuity replacements from 2015 through 2017 (plus 2 Texas annuity replacements from 2018). Using ACL, a sample size of 64 with two tolerable errors was determined by using the Record sample fields and entering a 95% confidence level, a population of 180, an upper error limit of 10% (based upon the standard NAIC benchmark for non-claims testing) and an expected error rate of 2.5% (based upon the Acceptance Samples Table (“AST”) per the Market Regulation Handbook). The items in the population were listed as 1 through 180, and ACL’s random number generator determined which of the 180 replacements would be selected for the sample of 64 files.

In June 2019, the Department requested for each of the sampled replacement contracts: (a) the completed application (including suitability information, reasons for the client’s purchase, an explanation of why the replacement is being recommended, signed paperwork when the client is ignoring a recommendation, etc.) and (b) policy details (including paperwork, when available) for both the original contract and the replacement contract (including guaranteed and estimated interest rates). The Company provided the documentation as requested without delay.

Beginning July 2019, data elements were identified and reviewed by the Department’s examiners for each of the sampled replacements. The following data elements were identified and captured by examiners for analysis:

- *Annuitant Age, Replacement (Y/N),*
- *External or Internal Replacement,*
- *Surrender Charge Period for New Product,*

- *Does net worth of applicant exceed \$1 million? (Y/N),*
- *Is there supporting information in the file substantiating the net worth? (Y/N),*
- *Was there a surrender charge? (Y/N),*
- *Did company notify existing insurer within 5 business days on receipt of application and maintain copies of notice? (Y/N),*
- *Was the replacement form filled out correctly and signed by the applicant and producer? (Y/N), and*
- *Was the replacement transaction sales material certification statement filled out correctly and signed by the producer? (N/A).*

During the testing process, the Company responded to several questions related to its plans in Rhode Island if the Department were to authorize it to write new business. In response to these questions, the Company indicated that “The Capitol Life is planning to offer fixed bank channel annuities...[it has] no plans to offer its traditional brokerage channel annuities in Rhode Island (those are the files you are currently reviewing). Nor [is it] aware of any plans for The Capitol Life to offer its ordinary life / final expense products or home service life in Rhode Island.”<sup>1</sup>

### **Results of Testing**

Examiners noted the following during the Department’s review:

1. The testing indicated that many of the items identified by the Company as “replacements” were not actually replacements. Specifically, the examiners determined that 15 of 64 sampled items (23.44%) were not replacements.
2. In 6 of 49 replacements (12.24%), the Company made errors related to the Massachusetts replacement forms. According to 211 CMR 34.04(2)(a), the replacement form must include three spots for marking “Company/Contract No.”

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<sup>1</sup> Note that the Company has undergone a name change from “The Capitol Life Insurance Company” to “Capitol Life Insurance Company,” but at the time of the quoted response, the name was correctly used.

Instead, the Company's replacement form only has one spot listed as "Company" and no notation asking for contract number. Additionally, 211 CMR 34.04(2)(b) states that the application must include "a list of all existing life insurance and annuity to be replaced identified by name of insurer, the insured and contract number. If a contract number has not been assigned by the existing insurer, alternative identification, such as an application or receipt number, shall be listed." Six (6) of the six (6) errors related to not having a contract number (for the replaced contract) listed, six (6) of the six (6) errors related to not listing the insured for the replaced contracts, and one (1) of the six (6) errors related to not having a company (for the replaced contract) listed. Additionally, all six (6) contracts were instances in which the documentation lacked a sales material certification statement filled, though such a sales form does not appear to be a requirement in Massachusetts.

3. In 32 of 64 sampled items (50%), the client was noted to have a net worth of one million dollars (\$1,000,000) or more. None of those files included any substantiation of wealth, as the Department has often found in its prior reviews of annuity sales. [Note: The Company has explained that in Texas and Massachusetts, the two states focused on in the testing, the Company's predominate business plan involves issuing supplemental annuities to high-net worth applicants that have maxed-out the Liberty Bankers Life Insurance Company's non-jumbo limit of \$500,000.]
4. In 37 of 49 replacements (75.51%), the annuitant was at least 65-years old at the time of replacement issuance.

5. The examiners noted a) the lack of a section in the contract replacement comparisons regarding mortality and expense fees, investment advisory fees, and potential charges for and features of riders and b) relatively brief written descriptions of the reasons for the replacement transactions. In Rhode Island, 230-RICR-20-25-1.6(A) requires the producer to have reasonable information in order to believe the replacement transaction is suitable when taking into account whether or not the transaction would result in the consumer “be[ing] subject to increased fees, investment advisory fees or charges for riders and similar product enhancements,” and Massachusetts and Texas have similar requirements (see 211 CMR 96.05(2) and Texas Code Section 1115.51(5)(A)). However, the examiners also noted that the Company captures numerous suitability questions and information in its paperwork.
6. None of the 40 external replacements included copies of contracts for the replaced annuities.
7. In several instances, the documentation indicated that a “financial planner” provided assistance, though it is unclear from the files the identity of the actual financial planners, or whether the producers represented themselves as financial planners.

Testing indicates that the Company has performed satisfactorily in its handling of Texas and Massachusetts replacements. All but one of the replacement transactions did not involve surrender charges, and the clients were generally of a high net worth and benefited overall based upon the multi-year interest rate guarantees of the annuities being offered.

## **Other Inquiries Made of the Company**

During the review process, the Department asked a series of other questions of the Company. Those questions focused on the annual Reports for Senior Management regarding the suitability supervision system, the Company's oversight of its TPA, written replacement and suitability procedures, documentation showing a suitability review of each file, and how (or if) the Company's suitability team takes into account the liquidity needs of clients.

### Guidelines for Suitability Reviews

In August 2019, the Company provided internal working guidelines for suitability reviews as per a version dated January 9, 2019 and a Suitability Analysis Agent User Guide, a description of the suitability approval process (including an example of detailed discussions among various Company employees), and details regarding how liquidity is considered when determining suitability. In November 2020, the Company provided details regarding newly-added procedures such as all suitability reviews (beginning January 1 for at least a year, in order to gain comfort with new laws) going through the Senior Vice President Compliance's office (instead of just the exceptions as determined by the business team).

### Annual Suitability Reports for Senior Management

With respect to the annual suitability reports, the Company identified that the reports since 2016 had been made orally to senior management and the board and were not captured in writing. Information regarding prior reports may have been available in the email of the former compliance manager, but that step was not requested of the Company. The Department believes that suitability reports must be prepared and presented to Senior Management in writing.

The Rhode Island Annuity Suitability Regulation requires that “[a]n insurer shall establish a supervision system that is reasonably designed to achieve the insurer's and its

insurance producers' compliance with the Regulation..." The suitability regulation also requires "The insurer shall annually provide a report to senior management, including to the senior manager responsible for audit functions, which 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." Based on the Company's responses, the examiners determined that during the review period the Company was not in compliance with at least the former of these requirements. However, the Company has since provided to the Department a written update on suitability that was part of its 2020 annual board meeting, plans for monthly senior management meetings on suitability, and a copy of a bank channel annual suitability certification form that will be used on a going-forward basis.

#### Oversight of its TPA

With respect to questions about the TPA, the Company admitted to having trouble with data coming from its TPA, and the Company stated that the TPA handles the Company's underwriting and issuance of annuities. The Company said that they were implementing changes to more properly identify replacements, and the Department believes this faulty data was a primary driver of several of the extreme MCAS scores. Per the Company on July 25, 2019:

"I know there was a period of time historically, before the Replacement indicator fields were available for Annuities in QL, that the assumption was made that if the External Transfer field was marked (meaning we were requesting funds from External companies via 1035 Exchange and Trustee to Trustee transfer) then we counted the policy as a replacement as we had no other way to extract this data. Since that time however, the proper replacement fields have been in use and we have no longer had to use the external transfer field as a replacement count."

The review of files did not detect the data was more correct from a certain date forward, but the Department has no reason to disbelieve that the Company through a concerted effort can ensure that it appropriately reports replacements.

## **Conclusion**

In concluding its review, the Market Conduct Unit recommends that the Superintendent of Insurance authorize the Company to reactivate its license and begin conducting business in Rhode Island under the following conditions:

1. Before marketing annuities in Rhode Island, the Company must provide to the Department written procedures in compliance with 230-RICR-20-25-4.4 to ensure that a) replacement forms are filled out correctly and signed by the applicant and producer and b) sales material certification statements are filled out correctly and signed by the producer. In addition, the Company must provide all copies of its replacement forms and sales certification forms utilized by the Company in compliance with 230-RICR-20-25-4.4.
  - a. The Company has already provided the requested updated written procedures.
2. Within 12 months, the Company must develop and provide to the Department written procedures in compliance with 230-RICR-20-25-4.6(A) to more proactively monitor timeliness issues between application date and issue date.
  - a. The Company has already provided the requested written confirmation of compliance with this requirement.
3. Before it begins to market annuities in Rhode Island, the Company must confirm to the Department that it has adopted a system in compliance with 230-RICR-20-25-1.6(G)(6) to provide senior management a written report regarding its suitability supervision system, the audits and tests that it has conducted of the system.
4. Before it begins to market annuities in Rhode Island, the Company must provide to the Department written procedures outlining the Company's system to monitor and detect

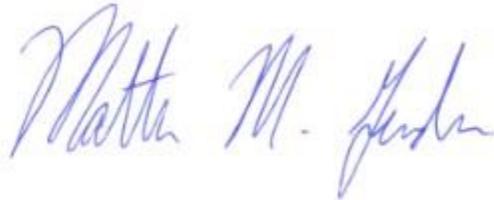
twisting and churning, as required by R.I. Gen. Laws § 27-29-4.7. [Note: this recommendation is based upon a market wide push for compliance in this area and is not being included due to a specific finding with the Company.]

5. Within 12 months, the Company must perform and provide to the Department an internal audit to confirm that the Company's improved processes are properly identifying replacement contracts.
  - a. The Company has provided a small description of this audit and represented that this description contains the entirety of the audit findings regarding replacements and suitability.
6. Within 12 months, the Company must provide to the Department its updated policies and procedures implemented to ensure that its MCAS data reported to the NAIC is accurate and reliable.
  - a. The Company has agreed to provide this information as proscribed.
7. If the Company's business plan changes in the next thirty-six (36) months to add a distribution channel in Rhode Island other than the bank-channel, the Company will affirmatively notify the Department of such change via email within sixty (60) calendar days of the change.
8. The notification requirement in part 7 (above) will trigger discussions between the Department and the Company over what procedural adjustments will be needed in order to gain the Department's approval of an additional distribution channel.

Assisting in the examination with the undersigned was Sarah Neil, PIR, MCM Principal Insurance Analyst, Segun Daramola, MPAc, AIE, APIR, AIRC, ALMI Senior Insurance

Examiner, Brian Werbeloff, MSA, CIE, ALMI, APIR, AIRC Senior Insurance Examiner, and  
Brett Bache, CIE, PIR, MCM, AIRC, ALMI Principal Insurance Examiner.

Respectfully submitted,

A handwritten signature in blue ink that reads "Matthew M. Gendron". The signature is written in a cursive style with a horizontal line underneath it.

Matthew Gendron, Esq.  
General Counsel & Chief of Regulatory Compliance  
Rhode Island Insurance Division



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Capitol Life Insurance Company, NAIC 61581

**June 2, 2021**

Rhode Island Insurance Division  
c/o Matthew Gendron  
1511 Pontiac Avenue, Bldg. 69-2  
Cranston, RI 02920

Re: Capitol Life Insurance Company ("Capitol Life") Expansion Application  
NAIC UCAA Tracking Number 69531

Dear Rhode Island Insurance Division:

In response to your Report on Expansion Application to Lift Restrictions and Allow New Business Sales of Capitol Life Insurance Company dated May 27, 2021, Capitol Life Insurance Company ("Capitol Life") offers the following clarifications for Rhode Island:

Sampling and Testing Procedures (page 3): During June 2019, since Rhode Island was testing based on the 2015 to 2017 MCAS reports, Capitol Life provided Rhode Island with the populations used for those MCAS reports (not annuity replacements). On August 28, 2019, the verified annuity replacements were sent to Rhode Island showing a total of 57 replacements for all 3 years combined, and again providing the TPA's explanation for the approximately 300 false positives reported for MCAS purposes.

Results of Testing (page 5): Capitol Life understands this to mean that Rhode Island is referencing technical deficiencies in the Massachusetts replacement notice form in use during the period under review (2015 to 2017), specifically that the form had a single line instead of 3 lines, and did not have a column subheading for contract number.

Capitol Life demonstrated its compliance with replacement regulations by providing Rhode Island with the following documents:

1. The transfer form obtained at the time of application requiring:
  - a. name of the company being replaced;
  - b. contract number being replaced; and
  - c. applicant's signature on the transfer form.

2. The replacement notices sent to the companies whose contracts were being replaced at the time of application.

Annual Suitability Reports for Senior Management (page 7): Capitol Life disagrees with Rhode Island that it failed to provide sufficient reporting on suitability during the period of review by Rhode Island. It appears that Rhode Island is possibly referencing Rhode Island's request for *written* reports for the 2015 to 2017 time period, and the undersigned confirms that, if *written* reports did exist for the 2015 to 2017 period, the reports would most likely be in predecessors' e-mails. To clarify, for the 2015 to 2017 period under review by Rhode Island: (1) verbal reports were (and still are) made at the monthly senior management staff meetings, and (2) verbal reports were also made at the annual board meeting (note: senior management attends the annual board meeting). Capitol Life is aware that Rhode Island did just amend its suitability law in 2021 to include a new requirement for a written report.

Conclusion 1.b. & 5. As previously indicated, Capitol Life's Compliance Department currently conducts 100% manual review of suitability, including replacements and advertising certification. The Compliance Review is in addition to the New Business review that verifies the case is "in good order". However, Capitol Life is aware of issues that can result from human error, and Capitol Life is now in the process of implementing an automated system where new business cases may only be submitted to Capitol Life after all replacement and sales certification requirements have been met. Capitol Life anticipates implementation will be completed during 2021, and would apply to its Rhode Island business.

Conclusion 3. As of today's date, Capitol Life has a variety of written reports that range in frequency depending on the distribution channel and regulatory requirements. For its anticipated bank channel distribution in Rhode Island, Capitol Life:

1. previously provided Rhode Island with a copy of a bank channel annual suitability certification;
2. would then conduct a compliance audit at least annually that includes a written report; and



**Rhode Island Insurance Division**

**Re: Capitol Life Insurance Company ("Capitol Life") Expansion Application  
UCAA Tracking Number 69531**

**June 2, 2021**

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3. would likely also conduct general audits of the bank channel distribution that are designed to detect deficiencies.

Conclusion 4. Capitol Life appreciates that Rhode Island has qualified that it found no instances of twisting or churning during testing. Capitol Life anticipates it would require something similar to Attachment 1 for its Rhode Island bank channel distribution.

Conclusion 6. Capitol Life now has a centralized database that captures data in a consistent manner across the various operating systems use to administer its business that Capitol Life uses for its data queries, including future MCAS reporting.

Please advise if Rhode Island requires any additional information. Otherwise, Capitol Life thanks Rhode Island for the considerable resources expended on the multi-year effort toward Capitol Life having the opportunity to increase the competitive insurance products available to Rhode Island consumers.

Sincerely,



Janet Gustafson

Senior Vice President, Compliance

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1605 Lyndon B Johnson Freeway Suite 700, Dallas, TX 75234  
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Preamble: This, document is a form of certification that may be used to satisfy R.I. Gen. Laws § 27-29-4.7.

\_\_\_\_\_ (“Broker/Dealer”) certifies to **CAPITOL LIFE INSURANCE COMPANY (“CLIC”)** that the Broker/Dealer, for the period of January 1, 2021 through December 31, 2021, THAT Broker/Dealer maintains a system to supervise recommendations to consumers by or through the Broker/Dealer or its affiliates regarding the purchase or exchange of annuities issued by the Insurer, which system is reasonably designed to achieve compliance with unfair trade practices, including:

- A. documenting an objectively reasonable basis for believing that a replacement or extraction will result in an actual and demonstrable benefit to the policyholder;
- B. monitoring for fraudulent, deceptive, or otherwise misleading recommendations, including deceptive omissions;
- C. when applicable, informing the applicant when the policy values, including cash values, dividends, and other assets of the existing policy or contract will be reduced, forfeited, or used in the purchase of the replacing or additional policy or contract;
- D. when applicable, informing the applicant that the replacing or additional policy or contract will not be a paid-up policy or that additional premiums will be due or that a new contestable period will apply and explaining the impact of these differences.

The Broker/Dealer acknowledges and agrees that CLIC may periodically review the compliance of the Broker/Dealer with this Certification.

The undersigned represents that he/she (i) is a senior manager of the Broker/Dealer who, in conjunction with others, has responsibility for overseeing the suitability of annuity sales, (ii) has a reasonable basis on which to make this Certification, and (iii) is authorized to provide this Certification on behalf of the Broker/Dealer.

\_\_\_\_\_  
Broker/Dealer

\_\_\_\_\_  
Print Name

By: \_\_\_\_\_

Title: \_\_\_\_\_

Date: \_\_\_\_\_