

Report On
Market Conduct Examination

Of The

THE PRUDENTIAL INSURANCE COMPANY OF AMERICA (Life Company)
751 BROAD STREET
NEWARK, NEW JERSEY 07101
TELEPHONE (908) 412-4000
NAIC COMPANY CODE 68241

AS OF
DECEMBER 31, 1992

DEPARTMENT OF BUSINESS REGULATION
INSURANCE DIVISION
STATE OF RHODE ISLAND

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Honorable Michael Bucci
Insurance Commissioner
State of Rhode Island
Providence, Rhode Island 02903

July 6, 1994

Sir:

In compliance with your instructions, and pursuant to Title 27, Chapter 13 and 13.1 of the Insurance Laws of the State of Rhode Island, a Market Conduct Examination has been performed on the Rhode Island business for:

The Prudential Insurance Company of America (Life Company)

751 Broad Street

Newark, New Jersey 07101

Hereinafter, generally referred to as "The Life Company", our report is submitted as follows:

FOREWORD

The report of the market conduct examination, in general, is a report by exception. Any additional practices, procedures and/or files subject to review during the examination may have been omitted from the report if no exceptions and/or improprieties were indicated.

SCOPE OF EXAMINATION

The examination, as stated in the salutation, was conducted in accordance with Title 27 Chapters 13 and 13.1 of the Insurance Laws of the State of Rhode Island. The examination commenced on May 3, 1993 and covered the period from January 1, 1990 to December 31, 1992.

The primary purpose of the examination was to determine the Life Company's compliance with statutes, regulations, and policy provisions relative to the Life Company, A.A.R.P. (American Association of Retired Persons), and Large Group Life Accident and Health Insurance activities within the State of Rhode Island.

The examination was performed in conformance with procedures as prescribed by the National Association of Insurance Commissioners. Accordingly, certain schedules, reviews and analyses were prepared and evaluations performed on principle segments of the Life Company, A.A.R.P. and Large Group Life Accident and Health.

The examination included but was not limited to a testing of Certificates of Authority, Consumer or Other Related Complaints, Sales and Advertising, Licensing of Agents, Agencies and Brokers, Policy Forms, Underwriting and Rating and Claims Practices for the following lines of business:

- . Individual Life
- . Group Life
- . Group Accident and Health

The results of the testing satisfied the primary purpose of the examination and formed the basis for the findings and recommendations presented in the report. These findings and recommendations related to the Life Company's life, health and accident business with the exclusion of AARP, which was found to have no exceptions noted.

COMPANY OVERVIEW

History

The Prudential Insurance Company of America was founded as the Prudential Friendly Society in Newark, New Jersey, in 1875. The objective of the company's founder, John Fairfield Dryden, was to make insurance protection available to the working class.

The company's subsidiaries offer Life and Health and Property/Casualty Insurance; Securities Brokerage Services; Mutual Funds; Mortgage Loans; Residential Realty Brokerage; Bank Savings Accounts and Credit Cards. It also provides a broad range of financial services to institutions, including Employee Benefits Programs, Capital Funding, Asset Management, Investment Banking, Reinsurance, Real Estate, Estate Development and Employee Relocation Assistance.

Still headquartered in Newark, New Jersey, the company has more than 100,000 employees in the United States and 20 other countries. Regional offices are located in Jacksonville, Florida; Minneapolis, Minnesota; Woodland Hills, California; and Fort Washington, Pennsylvania. Prudential's Canadian operations are based in Scarborough, Ontario and other key international activities are conducted in Japan, Great Britain, Hong Kong, Taiwan, South Korea, Belgium, Spain and Italy.

Company Operations and Management

The Prudential is a Mutual Company owned by its policyholders.

The company markets its products through one of the largest sales forces in the financial services industry. This force includes more than 23,000 insurance agents, 6,000 Prudential Securities Financial Advisors, and nearly 25,000 Prudential affiliated Realty Sales Associates, operating out of approximately 2,400 offices in North America and abroad.

When established in 1875, it was the first company in the United States to make Life Insurance available to the working class people by selling small policies with weekly premiums. Later, it introduced the concept of family life insurance and spear-headed the development of Variable Annuities and Flexible Premium Life Insurance. The Prudential also pioneered Major Medical Group Insurance and was an industry leader in

establishing and managing Health Maintenance Organizations (HMO's).

The Prudential holds a claim-paying rating of AA+ (as of 6/93) from Standard and Poors; a financial strength rating of Aa2 (as of 2/93) from Moody's Investor Service and an A++ (as of 5/93) claims paying rating from A.M. Best Company.

More than 200 subsidiaries currently operate under the Prudential name, including Prudential Securities, New York, NY; Prudential Mortgage Company, St. Louis, MO; The Prudential Real Estate Affiliates, Costa Mesa, CA; Prudential Mutual Fund Management Company, New York, NY; Prudential Relocation Management, White Plains, NY; and the Prudential Bank and Trust Company, Atlanta, GA.

The direct premiums for the Life Company for calendar year 1992 were \$14,044,322,396. Rhode Island's portion of those premiums amounted to \$29,038,183, which represents .2% percent of the Life Company's total direct premiums. The following schedule outlines the Life Company's life, accident and health lines of business direct premiums in the State of Rhode Island for 1992:

<u>LIFE INSURANCE</u>	<u>IN-FORCE PREMIUM</u>
1) Ordinary	\$17,787,268
2) Credit (Group & Ind)	\$145,479
3) Group	\$2,149,830
4) Annuity	\$356,668

5) Group Annuity	<u>\$437,192</u>
Total Life Insurance	<u>\$20,876,437</u>

ACCIDENT AND HEALTH

1) Group Policies	\$7,526,708
2) Credit (Group & Ind)	\$138,774
3) Non-Cancellable (Ind)	\$265,388
4) Non-Renewable (Ind)	\$221,222
5) Guaranteed Renewable	<u>\$9,654</u>
Total Accident and Health	<u>\$8,161,746</u>

The source of all figures presented in the above schedule is the 1992 Annual Statement.

CERTIFICATE OF AUTHORITY

A review of the Certificate Of Authority in conjunction with the operations of the Life Company was performed to determine the Life Company's compliance with Rhode Island Insurance Law 27-2-11, Foreign Insurance Company License.

The examiners determined from the results of the review that the Life Company is properly licensed in the State of Rhode Island to write life, accident and health lines of insurance and that the certificate was in

compliance with the authority granted them.

Therefore, no violation of Rhode Island Insurance Law 27-2-11 was noted by the examiners.

POLICYHOLDER TREATMENT

Consumer or Other Related Complaints

For the period under examination, the examiners performed a review and evaluation of the Company's Consumer or Other Related Complaints procedures and documentation to determine the Company's compliance with Rhode Island Insurance Laws and Regulations.

During the initial phase of the examination, the Company provided the examiners with a copy of their complaint register. The examiners identified a total of one hundred forty-seven (147) complaints. Fifty of the one hundred forty-seven complaints were first sent to the Rhode Island Insurance Division (the Division) and then forwarded by the Division to the Company.

The examiners requested the Company provide them with all the files corresponding to the above mentioned complaints. The Company, however, was unable to locate four (4) of the files. The Company's inability to produce these files are a violation of Rhode Island Insurance Law 27-

13.1-4(B), Examinations-Appointment of examiners; conduct of examination.

On the basis of the examiners' review of the files as provided, six of the files lacked sufficient documentation to determine the final outcome of each complaint. The Company's inability to provide complete file documentation is a violation of Rhode Island Insurance Law 27-2-19, Foreign Insurance Companies-Examinations.

Finally, the examiners determined from their file review that a pattern of misrepresentation by one of the Company's agents existed during the period under examination. Nine separate complaints of a similar nature were filed against the agent. The common grievance expressed in each complaint was that the agent had misrepresented information to the complainant. According to each complainant, the agent had instructed them erroneously to use dividend funds from one whole life policy to pay premium on a new whole life policy with no additional premium payments required. Therefore, each complaint presents a violation of Rhode Island Insurance Laws 27-4-5, Life Insurance Policies And Reserves-Misrepresentation and 27-29-4, Unfair Competition And Practices-"Unfair and Deceptive Acts".

It is therefore recommended based on the above findings that:

- 1) The Life Company review their present complaint records retention procedures to determine why the four (4) files could

not be located. Once the Life Company identifies the reason for the files' misplacement, the Life Company must make a determination whether to retain their current procedures or develop new ones to assure access to all complaint files.

- 2) The Life Company develop a checklist to assure that pertinent documents necessary to enable a complete reconstruction of the complaint handling is present within the file.
- 3) The Life Company send a letter of final complaint disposition to the complainant, retain a copy of the letter in the file, and record the appropriate information on the checklist.
- 4) The Life Company perform an investigation of all the business activity conducted by the agent in question on the Life Company's behalf. The Life Company should provide the Rhode Island Insurance Division with a full accounting of the outcome of the investigation and what the Life Company's intended resolution regarding the agent will be. The Division will then review the resolution to determine if further action is necessary.

MARKETING

Sales and Advertising

A test sample of various sales and advertising material used by the Life Company during the period under examination was reviewed to determine the Life Company's compliance with Rhode Island Insurance Laws 27-4-5, Life Insurance Policies and Reserves - Misrepresentations and 27-29-4, Unfair Competition and Practices - "Unfair and Deceptive Acts".

The review resulted in no exceptions noted.

UNDERWRITING AND RATING

The Life Company's Underwriting and Rating practices were reviewed to determine and evaluate the Life Company's treatment of applicants and handling of their corresponding applications and to verify that such practices are in compliance with Rhode Island Insurance Laws and Regulations.

To accomplish the purpose of the review, as stated above, the examiners selected a sample of two hundred-four (204) underwriting files and performed various examination procedures on them.

The performance of these procedures resulted in the following findings:

- 1) Four (4) underwriting files contained inadequate documents in violation of Rhode Island Regulation XXIX, Section 7C2, Replacement Of Life Insurance - Duties of replacing insurers-

Replacement: Accuracy of information.

- 2) Forty-four (44) underwriting files were in violation of Rhode Island Regulation XXIX, Section 7C4, Replacement Of Life Insurance- Duties of replacing insurers- Replacement: Three working day rule. Each file contained evidence that the three day rule on the deliverance of certain specified documents to the existing insurer had been violated.

- 3) Eight (8) underwriting files were not located at the time of the examination. The inability of the Life Company to provide these files not only violates Rhode Island Insurance Regulation XXIX, Section 7C7, Replacement Of Life Insurance- Duties of replacing insurers- Replacement: Maintenance of documents, but also the Rhode Island Insurance Law 27-13.1-4B, Examinations-Appointment of examiners; conduct of examination. The regulation deals with the retention of specific documents whereas the law deals with the retention of the entire file.

Based on the above findings, the examiners provide the following recommendations:

- 1) The Life Company review its current procedures for processing replacement business in light of the numerous violations to Rhode Island Regulation XXIX, Section 7C, Replacement Of Life Insurance-Duties of replacing insurers, and provide written

verification to the Rhode Island Insurance Division of the corrective action it has taken to eliminate further occurrences.

- 2) The Life Company provide all personnel involved in the processing of replacement business with a copy of Rhode Island Insurance Regulation XXIX, Replacement Of Life Insurance and inform them of the importance of adherence to its directives.
- 3) Due to an apparent breakdown in internal controls relative to record retention and retrieval of underwriting files, the Life Company review their record retention and retrieval procedures and implement corrective measures to ensure compliance with Rhode Island Insurance Regulation XXIX, Section 7C7, Replacement Of Life Insurance-Duties of replacing insurers- Replacement: Maintenance of documents and also the Rhode Island Insurance Law 27-13.1-4B, Examinations-Appointment of examiners; conduct of examination.

CLAIMS PRACTICES

The Life Company's Claims Practices were reviewed to determine and evaluate the Life Company's treatment of claimants relative to their respective claims and to verify that such practices are in compliance with Rhode Island Insurance Laws 27-4-26, Life Policies And Reserves-Interest on life insurance proceeds and 27-13.1-4(B), Examinations-

Appointment of examiners; conduct of examination, specifically, and various other Rhode Island Insurance Laws and Regulations, where applicable.

According to the statistical sampling methodology, the examiners were required to make a random sample selection of eighty-three (83) claim files and perform various examination procedures on them. The performance of these procedures resulted in the following findings:

- 1) Twenty-two (22) claim files contained information evidencing violation of Rhode Island Insurance Law: 27-4-26, Life Insurance Policies And Reserves-Interest on life insurance proceeds. According to the Law, the Life Company is required to pay the beneficiary interest on the proceeds at the rate of nine percent (9%) per annum from the date of death of an insured to the date of payment. Due to the potential magnitude of the violation, the examiners performed additional testing and determined that the Life Company has been violating this Law since the Law's inception on May 11, 1984.
- 2) The Life Company was unable to locate seven (7) claim files at the time of the examination for the examiners to review. The Life Company's inability to produce the files is a violation of Rhode Island Insurance Law: 27-13.1-4B, Examinations-Appointment of examiners; conduct of examination.

It is therefore recommended based on the findings that:

- 1) The Life Company review their internal claims handling practices relative to the Rhode Island Insurance Law: 27-4-26, make changes where necessary, and confirm in writing to the Rhode Island Insurance Division their adherence to the Law.
- 2) The Life Company pay to the beneficiaries of the twenty-two (22) claim files noted above the difference between the original interest paid and the nine percent (9%) due from the date of death to the date of payment plus nine percent (9%) from the original date to date of documented corrective action by the Life Company.
- 3) The Life Company produce a list of Rhode Island Death Claim beneficiaries who received interest payments of less than nine percent (9%) from the inception date of the Rhode Island Insurance Law 27-4-26 on May 11, 1984 to the date the Life Company began to fully comply with the statute. The Rhode Island Insurance Division will review the list to determine what further action should be taken.
- 4) Due to an apparent breakdown in controls relative to the record retention and retrieval of files, the Life Company management reviews its present record retention and retrieval procedures and implement corrective measures to ensure the

Life Company's compliance with Rhode Island Insurance Law: 27-13.1-4B, Examinations-Appointment of examiners; conduct of examination.

SUMMARY OF RECOMMENDATIONS

Page

- 8 1) The Life Company review their present complaint records retention procedures to determine why the four (4) files could not be located. Once the Life Company identifies the reason for the files' misplacement, the Life Company must make a determination whether to retain their current procedures or develop new ones to assure access to all complaint files.
- 8 2) The Life Company develop a checklist to assure that pertinent documents necessary to enable a complete reconstruction of the complaint handling is present within the file.
- 9 3) The Life Company send a letter of final complaint disposition to the complainant, retain a copy of the letter in the file, and record the appropriate information on the checklist.
- 8 4) The Life Company perform an investigation of all the business activity provided by the agent in question on the Life

Company's behalf. The Life Company should provide the Rhode Island Insurance Division with a full accounting of the outcome of the investigation and what the Life Company's intended resolution regarding the agent will be. The Division will then review the resolution to determine if further action is necessary on their part.

- 11 1) The Life Company review its current procedures for processing replacement business in light of the numerous violations to Rhode Island Regulation XXIX, Section 7C, Replacement Of Life Insurance-Duties of replacing insurers, and provide written verification to the Rhode Island Insurance Division of the corrective action it has taken to eliminate further occurrences.
- 12 2) The Life Company provide all personnel involved in the processing of replacement business with a copy of Rhode Island Insurance Regulation XXIX, Replacement Of Life Insurance, and inform them of the importance of adherence to its directives.
- 12 3) Due to an apparent breakdown in internal controls relative to record retention and retrieval of underwriting files, the Life Company review their record retention and retrieval procedures and implement corrective measures to ensure compliance with Rhode Island Insurance Regulation XXIX, Section 7C7, Replacement Of Life Insurance-Duties of replacing insurers-

Replacement: Maintenance of documents, and also the Rhode Island Insurance Law 27-13.1-4B, Examinations- Appointment of examiners; conduct of examination.

- 13 1) The Life Company review their internal claims handling practices relative to the Rhode Island Insurance Law: 27-4-26, make changes where necessary, and confirm in writing to the Rhode Island Insurance Division their adherence to the Law.
- 14 2) The Life Company pay to the beneficiaries of the twenty-two (22) claim files noted above the difference between the original interest paid and the nine percent (9%) due from the date of death to the date of payment, plus nine percent (9%) from the original date to date of documented corrective action by the Life Company.
- 14 3) The Life Company produce a list of Rhode Island Death Claim beneficiaries who received interest payments of less than nine percent (9%) from the inception date of the Rhode Island Insurance Law 27-4-26 on May 11, 1984 to the date the Life Company began to fully comply with the Statute. The Rhode Island Insurance Division will review the list to determine what further action should be taken.
- 14 4) Due to an apparent breakdown in controls relative to the record retention and retrieval of files, the Life Company

management review their present record retention and retrieval procedures and implement corrective measures to ensure the Life Company's compliance with Rhode Island Law: 27-13.1-4B, Examinations- Appointment of examiners, conduct of examination.

Acknowledgement

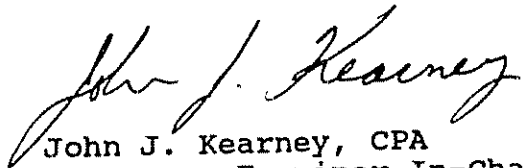
Acknowledgement is made of the courteous cooperation extended by the Company's officers and employees during the course of the examination.

In addition to the undersigned, Ronald R. Radtke, Senior Market Conduct Examiner and Carl E. Sanderson, Market Conduct Examiner participated in the examination, as well as, the preparation of the report.

Respectfully submitted,



Robert G. Arrow, F.L.M.I.
Senior Market Conduct Examiner
State of Rhode Island



John J. Kearney, CPA
Insurance Examiner-In-Charge
State of Rhode Island