

STATE OF NEW YORK INSURANCE DEPARTMENT

REPORT ON EXAMINATION

OF THE

FIRST SUNAMERICA LIFE INSURANCE COMPANY

AS OF

DECEMBER 31, 1999

DATE OF REPORT:

JANUARY 11, 2001

EXAMINER:

PATRICIA O'ROURKE

TABLE OF CONTENTS

<u>ITEM</u>	<u>PAGE NO.</u>
1. Executive summary	2
2. Scope of examination	3
3. Description of Company	4
A. History	4
B. Holding company	5
C. Management	7
D. Territory and plan of operation	10
E. Reinsurance	10
4. Significant operating results	11
5. Financial statements	14
A. Assets, liabilities, capital, surplus and other funds	14
B. Condensed summary of operations	16
C. Capital and surplus account	17
6. Market conduct activities	18
A. Advertising and sales activities	18
B. Underwriting and policy forms	21
C. Treatment of policyholders	21
7. Allocation of expenses	23
8. Corporate records	24
9. Prior report summary and conclusions	25
10. Summary and conclusions	28



STATE OF NEW YORK
INSURANCE DEPARTMENT
25 BEAVER STREET
NEW YORK, NEW YORK 10004

January 11, 2001

Honorable Gregory V. Serio
Superintendent of Insurance
Albany, New York 12257

Sir:

In accordance with instructions contained in Appointment No. 21562, dated July 21, 2000 and annexed hereto, an examination has been made into the condition and affairs of First SunAmerica Life Insurance Company, hereinafter referred to as "the Company," at its home office located at 733 Third Avenue, New York, New York, 10017.

Wherever "Department" appears in this report, it refers to the State of New York Insurance Department.

The report indicating the results of this examination is respectfully submitted.

1. EXECUTIVE SUMMARY

Effective October 31, 1997, John Alden Life Insurance Company of New York (“JANY”) merged with and into the Company. As of November 30, 1997, the life and accident and health business acquired in the JANY merger was sold to Bankers Life Insurance Company of New York (“Bankers”). (See item 3A of this report)

Effective January 1, 1999, SunAmerica, Inc. (“SunAmerica”), the Company’s parent, was acquired by American International Group, Inc. (“AIG”) in a stock for stock transaction. (See item 3A of this report)

Effective July 1, 1999, the Company acquired through an assumption reinsurance agreement, the New York business of Mutual Benefit Life Assurance Corporation (“MBL”). (See item 3A of this report)

The examiner’s review of a sample of transactions did not reveal any differences which materially affected the Company’s financial condition as presented in its financial statements contained in the December 31, 1999 filed statement. (See item 5 of this report)

The Company violated Section 1505(d) of the New York Insurance Law for making payments to five affiliates without notifying the Superintendent. (See item 3B of this report)

The Company violated Section 44.8(c) of Department Regulation No. 127 for not clearly disclosing the market value feature in some of its advertisements for products that have this feature. A similar violation appeared in the prior report on examination. (See item 6A of this report)

The Company violated Sections 2112(a) and 2114(a)(1) of the New York Insurance Law for paying commissions to unappointed agents. (See item 6A of this report)

2. SCOPE OF EXAMINATION

The prior examinations of the Company and JANY were both conducted as of December 31, 1995. This examination covers the period from January 1, 1996 through December 31, 1999. As necessary, the examiner reviewed transactions occurring subsequent to December 31, 1999 but prior to the date of this report (i.e., the completion date of the examination).

The examination comprised a verification of assets and liabilities as of December 31, 1999 to determine whether the Company's filed 1999 annual statement fairly presents its financial condition. The examiner reviewed the Company's income and disbursements necessary to accomplish such verification and utilized the National Association of Insurance Commissioners' Examiners Handbook or such other examination procedures, as deemed appropriate, in such review and in the review or audit of the following matters:

- Company history
- Management and control
- Corporate records
- Fidelity bond and other insurance
- Territory and plan of operation
- Market conduct activities
- Growth of Company
- Business in force by states
- Mortality and loss experience
- Reinsurance
- Accounts and records
- Financial statements

The examiner reviewed the corrective actions taken by the Company with respect to violations and recommendations contained in the prior report on examination. The results of the examiner's review are contained in item 9 of this report.

This report on examination is confined to financial statements and comments on those matters which involve departure from laws, regulations, or rules or which require explanation or description.

3. DESCRIPTION OF COMPANY

A. History

The Company was incorporated as a stock life insurance company under the laws of New York on December 5, 1978 under the name Capitol Life Insurance Company of New York. The Company was licensed and commenced business on September 30, 1980. The Company's present name was adopted on March 20, 1989. Initial resources of \$9,000,000, consisting of capital paid up of \$3,000,000 and contributed surplus of \$6,000,000, were provided through the sale of 300 shares of common stock (with a par value of \$10,000 each) for \$30,000 per share.

The Company received a capital contribution of \$5,000,000 from its parent SunAmerica Life Insurance Company ("SALIC") in 1997. An increase in surplus of \$29,863,578 resulted from the merger with JANY (see below). Capital and paid in and contributed surplus were \$3,000,000 and \$40,863,578, respectively, as of December 31, 1999.

Pursuant to an agreement dated November 29, 1996, SALIC entered into an agreement to purchase John Alden Life Insurance Company ("Alden"). As part of the purchase of Alden, on March 31, 1997, SALIC purchased all of the outstanding stock of JANY. On October 31, 1997, JANY was merged with and into the Company. On November 30, 1997, the Company entered into an asset purchase and sale agreement, an indemnity reinsurance agreement, an assumption reinsurance agreement, a trust agreement, and an administration agreement with Bankers Life Insurance Company of New York ("Bankers") to sell the non-annuity business acquired through the acquisition of JANY. The assumption reinsurance agreement provides for Bankers to assume 100% of the contractual liabilities of JANY's life, long-term care, health and disability insurance policies until the direct assumption of all liabilities under the policies by novation basis is completed. Bankers administers all policies covered under the assumption reinsurance agreement in the name of and on behalf of the Company.

Effective January 1, 1999 SunAmerica was acquired by AIG in a stock for stock transaction.

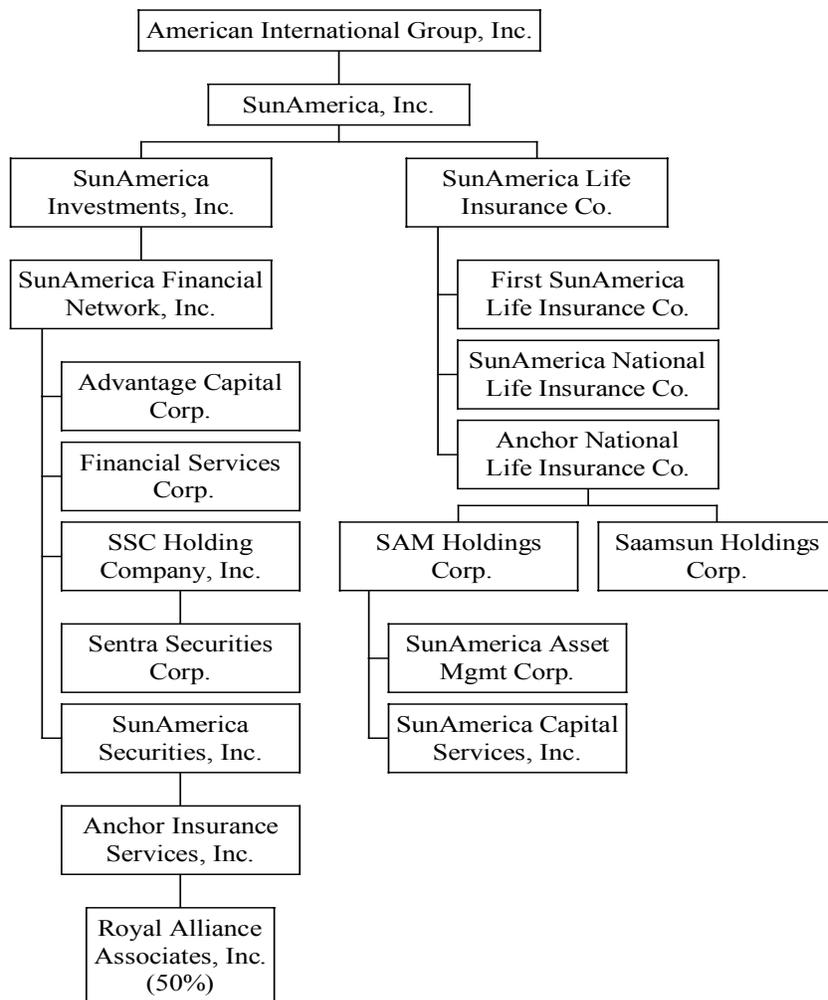
Effective July 1, 1999, the Company acquired, through an assumption reinsurance agreement, MBL's New York business. As part of the rehabilitation of MBL, the New Jersey Superior Court mandated the sale of all individual life and annuity and group annuity business.

Included in the block of business was approximately \$250,000,000 of individual life business and \$590,000,000 of group annuity business whose contract owners are residents of New York State. The remainder of the business (non New York business) was acquired by Anchor National Life Insurance Company (“ANLIC”) through an assumption reinsurance agreement from MBL.

B. Holding Company

The Company is a wholly owned subsidiary of SALIC, an Arizona domiciled life insurer. SALIC is in turn a wholly owned subsidiary of SunAmerica, Inc., a Delaware financial services company. The ultimate parent of the Company is AIG, a Delaware holding company.

An organization chart reflecting the relationship between the Company and significant entities in its holding company system as of December 31, 1999 follows:



The Company had 14 service agreements in effect as of December 31, 1999.

The Company has an agreement with SunAmerica Financial ("SUF"), a division of SALIC, whereby SUF provides certain services to the Company including equipment, space, actuarial, tax preparation, marketing services and the preparation of annual reports. The agreement was modified to include personnel and benefit administration, legal counsel, and internal audit, on December 31, 1997.

The Company has two agreements with SunAmerica Capital Services ("SACS"), whereby SACS arranges for the marketing and distribution of variable annuity contracts issued by the Company through its Separate Accounts. SACS provides information and marketing assistance to licensed broker-dealers and insurance agents on a continuing basis.

The Company has three agreements with various trusts to arrange for the funding of variable annuity contracts issued through the Separate Accounts. Under the agreements, the trusts make shares of certain of their portfolios available to serve as the underlying investments for certain variable annuity contracts.

The Company has an agreement with Royal Alliance Associates, Inc., dated January 1, 1993. The agreement states that Royal Alliance will provide the use of facilities, space, and equipment. These services are now provided for under the service agreement with SUF. Management is currently reviewing the relevancy and applicability of the agreement. The Company made no payments in 1997, 1998, and 1999 under this agreement.

The Company has agreements with five affiliated broker-dealers to sell their fixed and variable annuity products. The agreements cover the payment of commissions to the affiliated broker-dealers. The affiliates are; Advantage Capital Corporation, SunAmerica Securities, Inc., Royal Alliance Associates, Inc., Sentra Securities Corporation, and Financial Services Corporation.

The Company has a tax sharing agreement with SALIC.

The Company also has an investment advisory agreement with SunAmerica Investments, Inc., where SunAmerica Investments, Inc. advises the Company in the management of its investment portfolio. Periodically the Company participates in the same investments as its affiliates. The examiner recommends that the Company amend the investment advisory agreement to provide for such participation.

Section 1505(d) of the New York Insurance Law states, in part:

“The following transactions between a domestic controlled insurer and any person in its holding company system may not be entered into unless the insurer has notified the superintendent in writing of its intention to enter into any such transaction at least thirty days prior thereto, or such shorter period as he may permit, and he has not disapproved it within such period . . .

(3) rendering of services on a regular or systematic basis . . .”

The Company made commission payments to five affiliates without notifying the Superintendent (i.e., the aforementioned broker-dealer agreements were not submitted to the Superintendent.

The Company violated Section 1505(d)(3) of the New York Insurance Law for making commission payments to five affiliates, without notifying the Superintendent.

C. Management

The Company’s by-laws provide that the board of directors shall be comprised of not less than 13 and not more than 19 directors. Directors are elected for a period of one year at the annual meeting of the stockholders held in June of each year. As of December 31, 1999, the board of directors consisted of 14 members. Most actions taken by the board are resolutions by unanimous written consent of the board of directors. The Company held one board meeting in 1997, one in 1998 and none in 1999.

The 14 board members and their principal business affiliation, as of December 31, 1999, were as follows:

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>	<u>Year First Elected</u>
Thomas W. Baxter* Pasadena, CA	Partner O’Melveny & Myers LLP	1999
James R. Belardi Los Angeles, CA	Senior Vice President First SunAmerica Life Insurance Company	1992
Eli Broad Los Angeles, CA	Chairman, Chief Executive Officer, and President First SunAmerica Life Insurance Company	1987

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>	<u>Year First Elected</u>
Marc H. Gamsin Pacific Palisades, CA	Senior Vice President First SunAmerica Life Insurance Company	1999
Jana W. Greer Encino, CA	Senior Vice President First SunAmerica Life Insurance Company	1987
Susan L. Harris Los Angeles, CA	Senior Vice President and Secretary First SunAmerica Life Insurance Company	1987
Vicki E. Marmorstein* Los Angeles, CA	Partner Latham & Watkins	1999
Peter McMillan Pacific Palisades, CA	Executive Vice President SunAmerica Investments Inc.	1994
Margery K. Neale* Sands Pointe, NY	Partner Swindler, Berlin, Shereff & Friedman, LLP	1996
Lester Pollack* New York, NY	Chief Executive Officer Centre Partners, L.P.	1987
Debbie Potash-Turner New York, NY	Senior Vice President and Chief Financial Officer SunAmerica Asset Management Corporation	1999
Scott L. Robinson North Hills, CA	Senior Vice President First SunAmerica Life Insurance Company	1987
Richard D. Rohr* Gross Pointe, MI	Partner Bodman, Longley & Dahling	1987
Jay S. Wintrob Los Angeles, CA	Executive Vice President First SunAmerica Life Insurance Company	1989

* Not affiliated with the Company or any other company in the holding company system

In January 2000, Scott L. Robinson resigned from the board and was replaced by N. Scott Gillis. In March 2000, Peter McMillan resigned from the board. In May 2000, Susan Harris resigned from the board and Christine Nixon and Lawrence Goldman were elected as directors.

Section 1202(b)(2) of the New York Insurance Law states, in part:

“The board of directors of a domestic life insurance company shall establish one or more committees comprised solely of directors who are not officers or employees of the company or of any entity controlling, controlled by, or under common control with the company and who are not beneficial owners of a controlling interest in the voting stock of the company or any such entity. Such committee or committees shall have responsibility for . . . nominating candidates for director for election by shareholders or policyholders, evaluating the performance of officers deemed by such committee or committees to be principal officers of the company and recommending to the board of directors the selection and compensation of such principal officers . . .”

The Company established a committee comprised of outside directors having the responsibilities stated in Section 1202(b)(2) of the New York Insurance Law, however the committee did not nominate candidates for director, nor recommend to the board of directors the selection and compensation of the principal officers.

The Company violated Section 1202(b)(2) of the New York Insurance Law for failing to have a committee comprised of outside directors fulfill all of its responsibilities as specified in the Law. A similar violation appeared in the prior report on examination.

The following is a listing of the principal officers of the Company, as of December 31, 1999:

<u>Name</u>	<u>Title</u>
Eli Broad	Chairman, Chief Executive Officer and President
Jay S. Wintrob	Executive Vice President
David R. Bechtel	Vice President and Treasurer
James R. Belardi	Senior Vice President
Marc H. Gamsin	Senior Vice President
N. Scott Gillis	Vice President and Controller
Jana W. Greer	Senior Vice President
Susan L. Harris	Senior Vice President and Secretary
Edwin R. Raquel	Senior Vice President and Chief Actuary
Scott L. Robinson	Senior Vice President

Scott H. Richland, Vice President, is the designated consumer services officer per Section 216.4(c) of Department Regulation No. 64.

Jay S. Wintrob replaced Eli Broad as President, on July 20, 2000 and as Chief Executive Officer, on January 1, 2001.

D. Territory and Plan of Operation

The Company is authorized to write life insurance, annuities and accident and health insurance as defined in paragraphs 1, 2 and 3 of Section 1113(a) of the New York Insurance Law.

The Company is licensed to transact business in three states, namely Nebraska, New Mexico, and New York. In 1999, 99.97% of all premiums (life, accident and health, annuity considerations, and deposit type funds) were received from New York. The majority of the Company's premium, 65.9%, is for deposit type funds.

The Company currently writes only fixed-rate annuities and flexible premium variable annuities. The Company's existing life insurance business was acquired from JANY in 1997 as a result of the merger, and from MBL in 1999 as a result of assumption reinsurance. A third party administrator, Liberty Services, Inc, services the life insurance business that was acquired from MBL. The Company also acquired group annuities from MBL. The Company's existing accident and health business was also acquired from JANY as a result of the merger in 1997. The life and accident and health business acquired from JANY is coinsured and administered by Bankers. The Company also acquired a large block of fixed annuities from JANY as a result of the merger in 1997.

The Company's agency operations are conducted on a general agency basis only.

E. Reinsurance

As of December 31, 1999, the Company had reinsurance treaties in effect with 14 companies, of which 13 were authorized or accredited. The Company's life policies are ceded on a coinsurance and yearly renewable term basis. The single premium deferred annuities acquired during the merger with JANY are ceded on a coinsurance basis. Reinsurance is provided on an automatic and facultative basis.

The total face amount of life insurance ceded as of December 31, 1999, was \$985,821,272, which represents 62% of the total face amount of life insurance in force.

4. SIGNIFICANT OPERATING RESULTS

Indicated below is significant information concerning the operations of the Company during the period under examination as extracted from its filed annual statements. Failure of items to add to the totals shown in any table in this report is due to rounding.

The following table indicates the Company's financial growth during the period under review:

	<u>December 31,</u> <u>1995</u>	<u>December 31,</u> <u>1999</u>	<u>Increase</u>
Admitted assets	<u>\$162,636,315</u>	<u>\$2,457,160,972</u>	<u>\$2,294,524,657</u>
Liabilities	<u>\$148,774,084</u>	<u>\$2,345,822,844</u>	<u>\$2,197,048,760</u>
Common capital stock	\$ 3,000,000	\$ 3,000,000	\$ 0
Gross paid in and contributed surplus	6,000,000	40,863,578	34,863,578
Separate account mortality fluctuation fund	3,161	5,280	2,119
Unassigned funds (surplus)	<u>4,859,070</u>	<u>67,469,270</u>	<u>62,610,200</u>
Total capital and surplus	<u>\$ 13,862,231</u>	<u>\$ 111,338,128</u>	<u>\$ 97,475,897</u>
Total liabilities, capital and surplus	<u>\$162,636,315</u>	<u>\$2,457,160,972</u>	<u>\$2,294,524,657</u>

The increase in assets, liabilities and surplus is due to the merger with JANY in 1997 and the acquisition of MBL's New York business in 1999.

The Company's invested assets as of December 31, 1999, exclusive of Separate Accounts, were mainly comprised of bonds (85%) and mortgage loans (11%). The majority (90.9%) of the Company's bond portfolio, as of December 31, 1999, was comprised of investment grade obligations.

The following has been extracted from the Exhibits of Annuities in the filed annual statements for each of the years under review:

	<u>Ordinary Annuities</u>			
	<u>1996*</u>	<u>1997</u>	<u>1998</u>	<u>1999</u>
Outstanding, end of previous year	51,558	53,682	52,827	49,102
Issued during the year	6,137	4,675	3,636	4,115
Other net changes during the year	<u>(4,013)</u>	<u>(5,530)</u>	<u>(7,361)</u>	<u>(1,833)</u>
Outstanding, end of current year	<u>53,682</u>	<u>52,827</u>	<u>49,102</u>	<u>51,384</u>
	<u>Group Annuities</u>			
	<u>1996*</u>	<u>1997</u>	<u>1998</u>	<u>1999</u>
Outstanding, end of previous year	0	526	828	1,060
Issued during the year	628	463	382	206
Other net changes during the year	<u>102</u>	<u>(161)</u>	<u>(150)</u>	<u>3,469</u>
Outstanding, end of current year	<u>526</u>	<u>828</u>	<u>1,060</u>	<u>4,735</u>

*The 1996 numbers have been restated to include JANY business.

The increase in group annuities from 1998 to 1999 is due to the acquisition of MBL's New York business.

The following is the net gain (loss) from operations by line of business after federal income taxes but before realized capital gains (losses) reported for each of the years under examination in the Company's filed annual statements:

	<u>1996*</u>	<u>1997</u>	<u>1998</u>	<u>1999</u>
Ordinary:				
Life insurance	\$ 454,535	\$ 5,438,514	\$ 375,126	\$ 4,980,458
Individual annuities	10,205,934	14,340,111	17,391,092	21,999,841
Supplementary contracts	<u>723,434</u>	<u>259,402</u>	<u>(760,052)</u>	<u>(732,151)</u>
Total ordinary	<u>\$11,383,903</u>	<u>\$20,038,027</u>	<u>\$17,006,166</u>	<u>\$26,248,148</u>
Group annuities	<u>\$ (673,926)</u>	<u>\$ 66,845</u>	<u>\$ 101,361</u>	<u>\$(7,936,392)</u>
Accident and health:				
Group	\$ 179,811	\$ (205,506)	\$ 0	\$ 0
Credit	54,476	0	0	0
Other	<u>(148,806)</u>	<u>209,459</u>	<u>45,798</u>	<u>4,014</u>
Total accident and health	<u>\$ 85,481</u>	<u>\$ 3,953</u>	<u>\$ 45,798</u>	<u>\$ 4,014</u>
Total	<u>\$10,795,458</u>	<u>\$20,108,825</u>	<u>\$17,153,325</u>	<u>\$18,315,770</u>

*The 1996 amounts have been restated to include JANY.

The fluctuations in the ordinary life gains in 1997 and 1998 are due to the acquisition of JANY's life business and subsequent sale to Bankers. The increase in the gain in the ordinary life line in 1999 is due to the assumption of MBL's New York business.

The group annuity loss in 1999 is due to the high number of surrenders of MBL contracts.

The loss reported in 1997 for group accident and health is due to the business acquired from JANY. The fluctuations in accident and health-other are due to the acquisition of policies from JANY and the subsequent sale to Bankers.

5. FINANCIAL STATEMENTS

The following statements show the assets, liabilities, capital, surplus and other funds as of December 31, 1999, as contained in the Company's filed 1999 annual statement, a condensed summary of operations and a reconciliation of the capital and surplus account for each of the years under review. The examiner's review of a sample of transactions did not reveal any differences which materially affected the Company's financial condition as presented in its financial statements contained in the December 31, 1999 filed statement.

A. ASSETS, LIABILITIES, CAPITAL, SURPLUS AND OTHER FUNDS AS OF DECEMBER 31, 1999

Admitted Assets

Bonds	\$1,584,869,299
Common stocks	2
Mortgage loans	
First liens	212,782,429
Real estate	
Properties acquired in satisfaction of debt	400,251
Policy loans	42,204,711
Cash and short term investments	29,737,557
Other invested assets	487,416
Receivable for securities	9,496
Reinsurance ceded:	
Amounts recoverable from reinsurers	1,676,710
Other amounts receivable under reinsurance contracts	641,773
Life insurance premiums and annuity considerations	
deferred and uncollected on in force business	181,195
Investment income due and accrued	25,565,186
From Separate Accounts Statement	<u>558,604,947</u>
 Total admitted assets	 <u>\$2,457,160,972</u>

Liabilities, Capital, Surplus and Other Funds

Aggregate reserve for life policies and contracts	\$1,728,611,490
Supplementary contracts without life contingencies	29,408,246
Policy and contract claims	
Life	1,017,756
Policyholders' dividend and coupon accumulations	238,577
Policy and contract liabilities:	
Other amounts payable on reinsurance assumed	1,760,218
Interest maintenance reserve	8,826,973
Commissions to agents due or accrued	87,527
General expenses due or accrued	109,610
Transfers to Separate Accounts due or accrued	(19,990,474)
Taxes, licenses and fees due or accrued	1,916,421
Federal income taxes due or accrued	(6,441,426)
Amounts withheld or retained by company as agent or trustee	506,995
Remittances and items not allocated	4,559,831
Miscellaneous liabilities:	
Asset valuation reserve	15,000,898
Payable to parent, subsidiaries and affiliates	1,232,088
Drafts outstanding	19,497,160
Payable for securities	62,983
Separate account contingency reserve	750,000
Acquisition-related expense reserve	63,024
From Separate Accounts Statement	<u>558,604,947</u>
Total liabilities	<u>\$2,345,822,844</u>
Common capital stock	\$ 3,000,000
Gross paid in and contributed surplus	40,863,578
Separate account mortality fluctuation fund	5,280
Unassigned funds (surplus)	<u>67,469,270</u>
Total capital, surplus and other funds	<u>\$ 111,338,128</u>
Total liabilities, capital, surplus and other funds	<u>\$2,457,160,972</u>

B. CONDENSED SUMMARY OF OPERATIONS

	<u>1996*</u>	<u>1997</u>	<u>1998</u>	<u>1999</u>
Premiums and considerations	\$277,943,611	\$247,728,742	\$208,074,127	\$157,449,646
Investment income	110,513,742	119,401,115	116,588,368	128,171,259
Commissions and reserve adjustments on reinsurance ceded	1,111,342	5,766,507	437,342	121,169
Miscellaneous income	<u>15,243,080</u>	<u>13,064,371</u>	<u>3,969,584</u>	<u>6,700,518</u>
 Total income	 <u>\$404,811,775</u>	 <u>\$385,960,735</u>	 <u>\$329,069,421</u>	 <u>\$292,442,592</u>
 Benefit payments	 \$139,974,122	 \$222,528,733	 \$273,794,890	 \$434,218,241
Increase in reserves	175,013,815	28,193,610	(92,008,657)	(321,497,728)
Commissions	18,611,732	15,671,213	11,687,645	19,296,668
General expenses and taxes	9,541,590	7,511,501	10,109,133	10,984,280
Increase in loading and cost of collection	(20,821)	(14,167)	0	0
Net transfers to Separate Accounts	37,927,541	80,119,889	105,599,085	115,934,840
Miscellaneous deductions	<u>9,601,152</u>	<u>7,599,631</u>	<u>0</u>	<u>784,520</u>
 Total deductions	 <u>\$390,649,131</u>	 <u>\$361,610,410</u>	 <u>\$309,182,096</u>	 <u>\$259,720,821</u>
 Net gain (loss)	 \$ 14,162,644	 \$ 24,350,325	 \$ 19,887,325	 \$ 32,721,771
Dividends	417,711	369,717	0	0
Federal income taxes	<u>2,949,476</u>	<u>3,871,783</u>	<u>2,734,000</u>	<u>14,406,000</u>
 Net gain (loss) from operations before net realized capital gains	 \$ 10,795,457	 \$ 20,108,825	 \$ 17,153,325	 \$ 18,315,771
Net realized capital gains (losses)	<u>(806,515)</u>	<u>(1,718,641)</u>	<u>(890,167)</u>	<u>(4,105,437)</u>
 Net income	 <u>\$ 9,988,942</u>	 <u>\$ 18,390,184</u>	 <u>\$ 16,263,158</u>	 <u>\$ 14,210,334</u>

*The 1996 amounts have been restated to include JANY.

C. CAPITAL AND SURPLUS ACCOUNT

	<u>1996*</u>	<u>1997</u>	<u>1998</u>	<u>1999</u>
Capital and surplus, December 31, prior year	\$ <u>69,727,636</u>	\$ <u>77,929,012</u>	\$ <u>83,860,940</u>	\$ <u>96,474,046</u>
Net income	\$ 9,988,942	\$18,390,184	\$16,263,158	\$14,210,334
Change in net unrealized capital gains (losses)	149,444	58,750	(1,358,750)	843,501
Change in non-admitted assets and related items	(106,479)	475,017	(73,464)	54,428
Change in reserve valuation basis	0	(6,526,514)	0	0
Change in asset valuation reserve	(1,830,531)	(2,835,491)	(1,217,838)	(244,181)
Surplus adjustments				
Paid in	0	5,000,000	0	0
Surplus impact of acquisition related expense	<u>0</u>	<u>(8,630,018)</u>	<u>(1,000,000)</u>	<u>0</u>
Net change in capital and surplus	\$ <u>8,201,376</u>	\$ <u>5,931,928</u>	\$ <u>12,613,106</u>	\$ <u>14,864,082</u>
Capital and surplus, December 31, current year	\$ <u>77,929,012</u>	\$ <u>83,860,940</u>	\$ <u>96,474,046</u>	\$ <u>111,338,128</u>

*The 1996 amounts have been restated to include JANY.

6. MARKET CONDUCT ACTIVITIES

The examiner reviewed various elements of the Company's market conduct activities affecting policyholders, claimants, and beneficiaries to determine compliance with applicable statutes and regulations and the operating rules of the Company.

A. Advertising and Sales Activities

The examiner reviewed a sample of the Company's advertising files and the sales activities of the agency force including trade practices, solicitation and the replacement of insurance policies.

1. Section 219.5(a) of Department Regulation No. 34-A states, in part:

“Each insurer shall maintain at its home office a complete file containing a specimen copy of every printed, published or prepared advertisement . . . disseminated in this State, with a notation indicating the manner and extent of distribution . . .”

The Company does not maintain its advertising file in the home office. The advertising file is maintained at SALIC's offices in Los Angeles, California. In addition, the advertising file maintained in Los Angeles did not contain information as to the manner and extent of distribution of any advertisement.

The Company violated Section 219.5(a) of Department Regulation No. 34-A for not maintaining the advertising file at the Company's home office and for not indicating the manner and extent of distribution of any advertisement in the advertising file.

2. Section 219.4(p) of Department Regulation No. 34-A states, in part:

“In all advertisements made by an insurer, or on its behalf, the name of the insurer shall be clearly identified, together with the name of the city, town or village in which it has its home office in the United States. . . .”

The Company did not include the city, town or village of the home office in seven of the 41 advertisements reviewed.

The Company violated Section 219.4(p) of Department Regulation No. 34-A for not indicating in its advertisements the name of the city, town or village in which the Company has its home office in the United States.

3. Section 2122(a)(2) of the New York Insurance Law states:

“No insurance agent, insurance broker or other person, shall, by any advertisement or public announcement in this state, call attention to any unauthorized insurer or insurers.”

A review of 41 advertisements revealed 16 instances that identified both the Company and Anchor National Life Insurance Company, an affiliated unauthorized insurer, as issuers of the contracts advertised.

In corresponding with the beneficiaries on 17 death claims, the Company used the stationery and/or claim forms of Anchor National Life Insurance Company. In addition, for two death claims, the Company used stationery that listed several unauthorized insurers.

The Company violated Section 2122(a)(2) of the New York Insurance Law for calling attention to unauthorized insurers in its advertisements and correspondence.

4. Section 44.8(c) of Department Regulation No. 127 states, in part:

“All advertisements should clearly disclose . . . that any market-value adjustment formula may result in an increase or decrease in cash surrender value in accordance with the terms of the contract.”

Four advertisements did not clearly disclose that the market-value adjustment feature may result in an increase or decrease in the cash surrender value in accordance with the terms of the contract.

The Company violated Section 44.8(c) of Department Regulation No. 127 for not clearly disclosing the market value feature in some of its advertisements for products that have this feature. A similar violation appeared in the prior report on examination.

5. Section 2112(a) of the New York Insurance Law states, in part:

“Every insurer . . . doing business in this state shall file a certificate of appointment in such form as the superintendent may prescribe in order to appoint insurance agents to represent such insurer . . .”

Section 2114(a)(1) of the New York Insurance Law states, in part:

“No insurer . . . doing business in this state shall pay any commission or other compensation to any person, firm or corporation, for any services in obtaining in this state any new contract of life insurance or any new annuity contract, except to a licensed life insurance agent of such insurer . . .”

The Company paid commissions to 46 agents who were not appointed by the Company.

The Company violated Sections 2112(a) and 2114(a)(1) of the New York Insurance Law for not appointing agents to represent the Company and for paying commissions to agents who were not appointed with the Company.

6. Section 51.6(b)(2) of Department Regulation No. 60 states, in part:

“Where a replacement has occurred or is likely to occur, the insurer replacing the life insurance policy or annuity contract shall . . .
Require with or as part of each application . . . the completed ‘Disclosure Statement’ . . .”

A review of 16 applications involving replacements revealed that four did not have a completed Disclosure Statement. One application did not contain a Disclosure Statement and the other three were incomplete.

The Company violated Section 51.6(b)(2) of Department Regulation No. 60 for failing to require a completed Disclosure Statement for applications involving replacement.

B. Underwriting and Policy Forms

The examiner reviewed a sample of new underwriting files, both issued and declined, and the applicable policy forms.

Section 3201(b)(1) of the New York Insurance Law states, in part:

“No policy form shall be delivered or issued for delivery in this state unless it has been filed with and approved by the superintendent”

The review of a sample of 48 annuity application files revealed seven instances where unapproved policy forms were used. The Company used unapproved application forms in three instances. In addition, the Company used SALIC’s policy forms, which were never approved for use in New York, in four instances.

The Company violated Section 3201(b)(1) of the New York Insurance Law for using unapproved policy forms.

C. Treatment of Policyholders

The examiner reviewed a sample of various types of claims, surrenders, changes and lapses. The examiner also reviewed the various controls involved, checked the accuracy of the computations and traced the accounting data to the books of account.

Section 3214(c) of the New York Insurance Law states, in part:

“If no action has been commenced, interest upon the principal sum paid to the beneficiary or policyholder shall be computed daily at the rate of interest currently paid by the insurer on proceeds left under the interest settlement option, from the date of the death of an insured or annuitant in connection with a death claim on such a policy of life insurance or contract of annuity . . . to the date of payment and shall be added to and be a part of the total sum paid.”

The Company did not pay any interest on three of the 36 annuity death claims reviewed. The examiner notified the Company and the interest owed was paid. In addition, the Company’s procedures for payment of interest on life claims provide that interest is paid only until the date a check is requisitioned. The death claim check may not be mailed for up to three days.

The Company violated Section 3214(c) of the New York Insurance Law for not paying interest on three annuity death claims and not paying interest until the date of payment on life claims.

Section 216.11 of Department Regulation No. 64 states, in part:

“To verify compliance with this Part and related statutes, Insurance Department examiners will investigate the market performance of insurers. To enable department personnel to reconstruct an insurers activities, all insurers . . . must maintain within each claim file all communications, transactions, notes and workpapers relating to the claim. All communications and transactions, whether written or oral, emanating from or received by the insurer shall be dated by the insurer. Claim files must be so maintained that all events relating to a claim can be reconstructed by the Insurance Department examiners. . . .”

The adjustable life policies that were assumed from MBL have three possible death benefit options. The greatest of the three options should be used in the payment of the death benefit proceeds. The first death benefit proceeds option is the specified amount plus or minus any increases or decreases in the specified amount. The second death benefit proceeds option is the specified amount, plus or minus any increases or decreases in the specified amount, plus the cash value on the date of death. The third death benefit proceeds option is the cash value on the date of death divided by the net single premium based on the sex, age, and rating class of the insured. There was no documentation in any of the death claim files that showed the calculation of the three possible death benefit options or that any comparisons were performed in determining the greater of the three amounts. The examiner was unable to verify that the correct death benefit was paid.

The Company violated Section 216.11 of Department Regulation No. 64 by not maintaining death claim files so that the examiner could reconstruct all events relating to claims.

7. ALLOCATION OF EXPENSES

The Company has a service agreement with SUF, effective January 1, 1993, which provides that SUF perform various administrative, accounting and investment management services.

A review of the allocation methods employed by the Company revealed that the general expenses consisted primarily of a management fee to SUF for services performed pursuant to the service agreement. The management fee expenses were determined by using the cost studies performed by 23 responsibility centers of SUF. A review of these cost studies revealed that in 11 responsibility centers, SUF relied upon discussions with managers and staff regarding their “specific recollection” of time spent performing tasks for the Company. The documentation provided to the examiner did not show how the amount of time allocated to the Company was derived from the total amount of time charged for the responsibility center. The information furnished from SUF to the Company only showed a total charge to the Company, making it impossible to determine if the Company was being allocated a fair and equitable amount of expenses.

The examiner recommends the Company maintain records with sufficient detail to show the system actually used for the allocation of expenses and the basis of allocation.

8. CORPORATE RECORDS

The examiner was unable to confirm two private placements, reported in Schedule D, Part 1 (i.e., long term bonds) of the annual statement totaling \$5,399,990, with the custodian or the issuer. The custodian was only able to confirm the amount for each security in the parent's name, SunAmerica. The Company indicated that it has an ownership interest in the securities in question and provided some internal worksheets showing the Company's share of such securities. However, the Company was unable to provide any legal evidence of ownership for the securities in question.

The examiner recommends that the Company acquire and maintain legal evidence of ownership for all its assets in order to maintain the Company's separate, legal and operating identity.

9. PRIOR REPORT SUMMARY AND CONCLUSIONS

Following are the violations contained in the prior reports on examination of the Company and JANY and the subsequent actions taken by the Company in response to each citation:

<u>Item</u>	<u>Description</u>
A	<p>The Company violated Section 1505(d)(3) of the New York Insurance Law by entering into a transaction with an affiliate without giving prior notice to the Superintendent.</p> <p>A review indicated that the Company filed the service agreement in question with the Superintendent. However, the Company has entered into various agreements with affiliates without notifying the Superintendent and is again in violation of Section 1505(d) of the New York Insurance Law. (See item 3B of this report)</p>
B	<p>The Company violated Section 1202(b)(2) of the New York Insurance Law by failing to establish a committee of the board, comprised solely of outside directors, to have the responsibilities as stated in the section of the law.</p> <p>A review indicated that the Company established a committee of the board, comprised solely of outside directors on January 1, 1996. However, the committee did not perform the responsibilities as stated in Section 1202(b)(2) of the New York Insurance Law. (See item 3C of this report)</p>
C	<p>The Company violated Section 4211(a) of the New York Insurance Law by failing to file notices of election of its directors with the Superintendent.</p> <p>A review indicated that the Company made the required filings.</p>
D	<p>The Company violated Section 325(a) of the New York Insurance Law by failing to maintain the board and committee minutes at its principal office.</p> <p>A review indicated that the Company maintains all board and committee minutes at its principal office.</p>

<u>Item</u>	<u>Description</u>
E	<p>The Company violated Section 4228(d)(5) of the New York Insurance Law by using a plan of compensation other than commissions without obtaining an approval from the Superintendent.</p> <p>A review indicated that the Company's plan of compensation was approved by the Superintendent.</p>
F	<p>The Company violated Section 91.4(a)(1) of Department Regulation No. 33 by failing to use an allocation method which produced a suitable and equitable distribution of income and expenses.</p> <p>A review indicated that the Company could not provide documentation on how its share of expenses was derived for several responsibility centers, and a recommendation was made that the Company maintain records with sufficient detail to show the system of allocation actually used and the basis of allocation. (See section 8 of this report)</p>
G	<p>The Company violated Section 90.7(a) of Department Regulation No. 33 by failing to itemize general expense items to specific lines of Exhibit 5 in sufficient detail to indicate their precise nature.</p> <p>A review indicated that the Company revised its methodology used to prepare Exhibit 5 and is in compliance with Section 90.7(a) of Department Regulation No. 33.</p>
H	<p>The Company violated Section 219.4(p) of Department Regulation No. 34-A by using the name of the parent company and its logo in a larger print which has a tendency to create the impression that the parent company would have the financial obligation for the annuity products being advertised.</p> <p>A review indicated that the Company either corrected or discontinued the use of the advertisements in question.</p>
I	<p>The Company violated Section 44.8(c) of Department Regulation No. 127 by failing to disclose the market value adjustment feature in some of its marketing materials for the variable annuity products which have this feature.</p> <p>A review indicated that the Company discontinued use of the marketing materials that were in violation. However, the review of other advertisements revealed additional advertisements that did not contain the required disclosure information. The Company is again in violation of Section 44.8(c) of Department Regulation No. 127. (See item 7A of this report)</p>

<u>Item</u>	<u>Description</u>
J	<p>The Company violated Section 3201(b)(1) of the New York Insurance Law by using policy forms that were not filed with and approved by the Department during the examination period.</p> <p>A review indicated that the Company filed these forms with the Department for approval, but subsequently withdrew the filings and terminated the use of the forms. However, a review of policy forms revealed the Company used other unapproved policy forms. The Company is again in violation of Section 3201(b)(1) of the New York Insurance Law. (See item 7B of this report)</p>
K	<p>JANY's report on examination contained violations of Sections 1505(b) and (d), 3214(c), and 4232 of the New York Insurance Law, and Department Regulations No. 34, No. 34-A and No. 49. In addition, recommendations were made concerning income allocation, annual statement reporting, and underwriting procedures.</p> <p>JANY was merged into the Company on October 31, 1997. A review was not made of the specific violations and recommendations contained in JANY's report on examination. The Company responded that due to the merger of JANY and the Company the procedures of the Company supersede the procedures formerly employed by JANY.</p>

10. SUMMARY AND CONCLUSIONS

Following are the violations and recommendations contained in this report:

<u>Item</u>	<u>Description</u>	<u>Page No(s).</u>
A	The examiner recommends that the Company amend the investment advisory agreement to provide for participation in investments with its affiliates.	6
B	The Company violated Section 1505(d)(3) of the New York Insurance Law for receiving services under selling agreements without notifying the Superintendent.	7
C	The Company violated Section 1202(b)(2) of the New York Insurance Law for failing to have the committee comprised of outside directors fulfill its responsibilities.	9
D	The Company violated Section 219.5(a) of Department Regulation No. 34-A for not maintaining the advertising file at the Company's home office and for not indicating the manner and extent of distribution in the advertising file.	18
E	The Company violated Section 219.4(p) of Department Regulation No. 34-A for not indicating the name of the city, town or village in which the Company has its home office in the United States.	18 – 19
F	The Company violated Section 2122(a)(2) of the New York Insurance Law for calling attention to an unauthorized insurer in its advertisements and correspondence.	19
G	The Company violated Section 44.8(c) Department Regulation No. 127 for not clearly disclosing the market value feature in some of its advertisements for products that have this feature.	19
H	The Company violated Sections 2112(a) and 2114(a)(1) of the New York Insurance Law for not appointing agents to represent the Company and for paying commissions to agents who were not appointed with the Company.	20
I	The Company violated Section 51.6(b)(2) of Department Regulation No. 60 for failing to require a completed Disclosure Statement for applications involving replacements.	20

<u>Item</u>	<u>Description</u>	<u>Page No(s).</u>
J	The Company violated Section 3201(b)(1) of the New York Insurance Law for using unapproved policy forms.	21
K	The Company violated Section 3214(c) of the New York Insurance Law for not paying interest on three annuity death claims and not paying interest until the date of payment on life claims.	21
L	The Company violated Section 216.11 of Department Regulation No. 64 by not maintaining certain death claim files so that the examiner could reconstruct all events relating to the claims.	22
M	The examiner recommends that the Company maintain records with sufficient detail to show the system actually used for the allocation of expenses and the basis of allocation.	23
N	The examiner recommends that the Company acquire and maintain legal evidence of ownership for all its assets in order to maintain the Company's separate, legal and operating identity.	24

APPOINTMENT NO. 21562

STATE OF NEW YORK
INSURANCE DEPARTMENT

I, NEIL D. LEVIN, Superintendent of Insurance of the State of New York,
pursuant to the provisions of the Insurance Law, do hereby appoint:

PATRICIA O'ROURKE

as a proper person to examine into the affairs of the

FIRST SUNAMERICA LIFE INSURANCE COMPANY

and to make a report to me in writing of the condition of the said

COMPANY

with such other information as she shall deem requisite.

In Witness Whereof, I have hereunto subscribed by name
and affixed the official Seal of the Department
at the City of New York

this 21th day of July, 2000



NEIL D. LEVIN

Superintendent of Insurance

A handwritten signature in black ink, appearing to read "Gregory V. Serio".

by **GREGORY V. SERIO**
First Deputy Superintendent