

STATE OF NEW YORK INSURANCE DEPARTMENT

REPORT ON EXAMINATION

OF THE

BAPTIST LIFE ASSOCIATION

AS OF

DECEMBER 31, 2000

DATE OF REPORT:

JULY 24, 2001

EXAMINER:

JOSHUA WEISS

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

July 24, 2001

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

Sir:

In accordance with instructions contained in Appointment No. 21666, dated January 10, 2001 and annexed hereto, an examination has been made into the condition and affairs of the Baptist Life Association, hereinafter referred to as "the Association" or "BLA," at its home office located at 8555 Main Street, Buffalo, New York 14221.

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

The examiner's review of a sample of transactions did not reveal any differences which materially affected the Association's financial condition as presented in its financial statements contained in the December 31, 2000 filed annual statement. (See item 5 of this report)

The Association's investment securities are held on deposit with two brokerage houses, Salomon Smith Barney and Paine Webber. The Association has previously been advised by the Department that brokerage houses are not acceptable custodians for securities. The examiner recommends that the Association enter into a custodial agreement with an authorized bank or trust company for the holding of its securities. (See item 7 of this report)

2. SCOPE OF EXAMINATION

The prior examination was conducted as of December 31, 1997. This examination covers the period from January 1, 1998 through December 31, 2000. As necessary, the examiner reviewed transactions occurring subsequent to December 31, 2000 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, 2000 to determine whether the Association's 2000 filed annual statement fairly presents its financial condition. The examiner reviewed the Association'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:

- Association history
- Management and control
- Corporate records
- Fidelity bond and other insurance
- Officers' and employees' welfare and pension plans
- Territory and plan of operation
- Market conduct activities
- Growth of Association
- Business in force by states
- Mortality and loss experience
- Reinsurance
- Accounts and records
- Financial statements

The examiner reviewed the corrective actions taken by the Association with respect to violations, recommendations and/or comments 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 ASSOCIATION

A. History

The Association was established in Buffalo, New York in 1883 and was incorporated on June 23, 1899 under the name of the Mutual Benefit Association of the German Baptists of North America. The Association received its final certificate of authority to transact business as a fraternal benefit society on August 22, 1899. The name was changed to the German Baptist Life Association in 1911, and to its present name, Baptist Life Association, in 1934.

The by-laws set forth the purposes of the Association, which are as follows:

“The corporate purpose of the Association shall be to provide protection to its Baptist Life constituency against financial loss upon disability or death and retirement security through annuities, in any form authorized by the Insurance Law of the State of New York relating to fraternal benefit societies. Fraternal and Benevolent activities shall promote the spiritual, physical, and cultural welfare of its members, Baptist congregations and institutions, or any Christian cause as the Board of Directors may determine.”

B. Management

The Quadrennial Convention is the supreme governing body that has exclusive legislative authority and it meets every four years. The Quadrennial Convention consists of elected delegates and directors of the Association. Each local branch society is entitled to one delegate. The board of directors is elected by a plurality of delegates at the Quadrennial Convention. The board of directors (“board”) may fill any vacancies occurring between regular meetings of the Quadrennial Convention for the unexpired term.

Special conventions may be called by the Chairman of the Board, the President of the Association, or upon the authorization of a majority of the board.

The Association’s by-laws had previously stated that the board should be comprised of not less than 15 directors. On August 19, 2000, the Association amended its by-laws to reduce the number of required directors from 15 to 12. As of December 31, 2000, the board consisted of 12 members. The board meets at least twice a year.

The 12 board members and their principal affiliation, as of December 31, 2000, were as follows:

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>	<u>Year First Elected</u>
John M. Andrews* Erie, PA	Accountant Baldwin General Contractors	1980
Dr. David Draewell* East Dundee, IL	Retired Financial Administrator Judson College	1984
John C. Garas* Clarence, NY	Attorney Renaldo, Myers & Palumbo, P.C.	2000
Kenneth L. Griffiths* Tonawanda, NY	Retired Disability Claims Adjuster Sellers Agency	1984
Dr. Richard E. Ice* Alameda, CA	President Emeritus American Baptist Homes of the West	1988
R. Gordon Mooney* New Castle, PA	District Account Executive Canon U.S.A.	1992
Richard H. Murphy East Amherst, NY	Vice Chairman of the Board Baptist Life Association	1984
Stephen L. Pelton, M.D.* Victor, NY	Dermatologist Barrington – Park Dermatological	1998
Marilyn R. Schaer* Wheaton, IL	Associate Director of Development North American Baptist Conference	1995
Calvin A. Suess Lancaster, NY	Chairman of the Board Baptist Life Association	1980
William A. Wells Jr.* Pendleton, NY	Vice President Beechwood Continuing Care	1998
Steven J. Woodard* Lancaster, NY	Vice President Alden State Bank	1998

*Not affiliated with the Association

As of December 31, 2000, the Association had six sub-committees of the board of directors as follows:

1. Executive Committee
2. Finance Committee
3. Business Policy and Strategy
4. Examining Committee
5. Compliance Committee
6. Fraternal Service Committee

The examiner's review of the minutes of the meetings of the board of directors and its committees indicated that meetings were well attended and that each director attended a majority of meetings.

The following is a listing of the principal officers of the Association as of December 31, 2000:

<u>Name</u>	<u>Title</u>
Kenneth C. Kirsch	President
John Q. Curtin, Jr.*	Secretary/Treasurer

* Designated consumer services officer per Section 216.4 (c) of Department Regulation No. 64

C. Territory and Plan of Operation

The Association 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 Association stopped writing accident and health insurance in 1993.

The Association is licensed to do business in 26 states. In 2000, 70.7% of life premiums were received from Texas (23.3%), New York (23.2%), Michigan (9.4%), North Carolina (7.6%) and Pennsylvania (7.2%). Policies are written on a participating basis. Life insurance products sold by the Association during the period under examination included whole life, interest sensitive whole life, annual renewable term, term to age 25, and 10-year term. Annuity products sold during the same period included flexible annuities and single premium deferred annuities. During the examination period, 80% of first year premium income was derived from the sale of annuity contracts and 20% was derived from the sale of life insurance certificates.

The Association's agency operations are conducted on a general agency basis. The Association's agency force decreased substantially during the period under examination. As of December 1997, the Association had 264 independent agents throughout the country. By December 2000, the agency force had decreased to 115, mostly due to agents being terminated because of lack of production. The decrease in the agency force occurred primarily in Texas, New York and Pennsylvania.

D. Reinsurance

As of December 31, 2000, the Association had reinsurance treaties in effect with four reinsurance companies, all of which were authorized or accredited. Reinsurance of the Association's life and accident and health policies is ceded on a coinsurance, modified coinsurance, and yearly renewable term basis. Reinsurance is provided on an automatic and facultative basis.

The maximum retention limit for individual life contracts is \$50,000. The total face amount of life insurance ceded, as of December 31, 2000, was \$82,905,107, which represents 40% of the total face amount of life insurance in force.

The Association reported surplus relief of \$259,870 as of December 31, 2000.

4. SIGNIFICANT OPERATING RESULTS

Indicated below is significant information concerning the operations of the Association 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 Association's financial growth during the period under review:

	December 31, <u>1997</u>	December 31, <u>2000</u>	<u>Increase</u>
Admitted assets	\$ <u>18,443,161</u>	\$ <u>19,346,466</u>	\$ <u>903,305</u>
Liabilities	\$ <u>17,653,156</u>	\$ <u>18,539,384</u>	\$ <u>886,228</u>
Aggregate write-ins for special surplus funds	\$ 20,000	\$ 20,000	\$ 0
Unassigned funds (surplus)	<u>770,005</u>	<u>787,082</u>	<u>17,077</u>
Total surplus	\$ <u>790,005</u>	\$ <u>807,082</u>	\$ <u>17,077</u>
Total liabilities and surplus	\$ <u>18,443,161</u>	\$ <u>19,346,466</u>	\$ <u>903,305</u>

The Association's invested assets as of December 31, 2000, were mainly comprised of bonds (91.3%). The majority (98.6%) of the bond portfolio, as of December 31, 2000, was comprised of investment grade obligations.

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 Association's filed annual statements:

	<u>1998</u>	<u>1999</u>	<u>2000</u>
Ordinary:			
Life insurance	\$(106,076)	\$ 108,014	\$ 104,775
Individual annuities	70,906	96,427	70,264
Supplementary contracts	<u>(2,011)</u>	<u>(16,157)</u>	<u>18,451</u>
Total ordinary	\$ <u>(37,181)</u>	\$ <u>188,284</u>	\$ <u>193,490</u>
Accident and health	\$ <u>(9,374)</u>	\$ <u>(255)</u>	\$ <u>(139)</u>
Fraternal expenses	\$(113,879)	\$(112,138)	\$(106,648)
Total	\$ <u>(160,434)</u>	\$ <u>75,891</u>	\$ <u>86,703</u>

The Association's net loss for 1998 was due to an unusual increase in death claims which was partially offset by additional surplus relief reinsurance obtained in the amount of \$212,000.

The fraternal line will always reflect a loss, as that line of business has no income. The Association does not charge its members dues or fees.

5. FINANCIAL STATEMENTS

The following statements show the assets, liabilities, surplus and other funds as of December 31, 2000, as contained in the Association's 2000 filed annual statement, a condensed summary of operations and a reconciliation of the 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 Association's financial condition as presented in its financial statements contained in the December 31, 2000 filed annual statement.

A. ASSETS, LIABILITIES, SURPLUS AND OTHER FUNDS AS OF DECEMBER 31, 2000

Admitted Assets

Bonds	\$17,139,150
Mortgage loans on real estate other than first liens	17,713
Real estate property occupied by the Association	363,945
Certificate loans and liens	610,864
Cash and short-term investments	649,699
Amounts recoverable from reinsurers	400
Electronic data processing equipment	29,042
Life insurance premiums and annuity considerations deferred and uncollected on in force business	163,295
Investment income due and accrued	<u>372,358</u>
Total admitted assets	<u>\$19,346,466</u>

Liabilities, Surplus and Other Funds

Aggregate reserve for life certificates and contracts	\$18,123,586
Supplementary contracts without life contingencies	108,359
Certificate and contract claims: life	38,972
Refund accumulations	53,803
Premiums and annuity considerations received in advance	26,192
Commissions to fieldworkers due or accrued	8,586
General expenses due or accrued	23,190
Taxes, licenses and fees due or accrued	20,094
Amounts withheld or retained by Association as agent or trustee	4,432
Remittances and items not allocated	1,521
Asset valuation reserve	112,945
Unclaimed benefits	14,587
Benevolent fund	<u>3,117</u>
Total liabilities	<u>\$18,539,384</u>
Contingent reserve for orphan benefits	\$ 20,000
Unassigned funds (surplus)	<u>787,082</u>
Total surplus and other funds	\$ <u>807,082</u>
Total liabilities, surplus and other funds	<u>\$19,346,466</u>

B. CONDENSED SUMMARY OF OPERATIONS

	<u>1998</u>	<u>1999</u>	<u>2000</u>
Premiums and considerations	\$2,092,805	\$1,861,305	\$1,723,972
Investment income	1,310,800	1,318,353	1,328,415
Commissions and reserve adjustments on reinsurance ceded	720	684	684
Miscellaneous income	<u>1,133</u>	<u>1,221</u>	<u>1,365</u>
Total income	<u>\$3,405,458</u>	<u>\$3,181,563</u>	<u>\$3,054,436</u>
Benefit payments	\$2,172,834	\$1,866,467	\$1,811,045
Increase in reserves	433,026	301,590	270,753
Commissions	160,501	123,586	119,997
General expenses and taxes	804,816	809,481	756,861
Increase in loading and cost of collection in excess of loading on deferred and uncollected premiums	<u>(5,285)</u>	<u>4,548</u>	<u>9,077</u>
Total deductions	<u>\$3,565,892</u>	<u>\$3,105,672</u>	<u>\$2,967,733</u>
Net gain (loss) from operations before net realized capital gains	\$ (160,434)	\$ 75,891	\$ 86,703
Net realized capital gains (losses)	<u>(99)</u>	<u>(97)</u>	<u>(94)</u>
Net income	<u>\$ (160,533)</u>	<u>\$ 75,794</u>	<u>\$ 86,609</u>

C. SURPLUS ACCOUNT

	<u>1998</u>	<u>1999</u>	<u>2000</u>
Surplus, December 31, prior year	\$ <u>790,005</u>	\$ <u>798,143</u>	\$ <u>803,008</u>
Net income	\$(160,533)	\$ 75,794	\$ 86,609
Change in net unrealized capital gains (losses)	0	(4,657)	(385)
Change in non-admitted assets and related items	978	4,028	(8,121)
Change in asset valuation reserve	(5,166)	2,614	(6,813)
Change in surplus as a result of reinsurance	<u>172,859</u>	<u>(72,914)</u>	<u>(67,216)</u>
Net change in surplus	\$ <u>8,138</u>	\$ <u>4,865</u>	\$ <u>4,074</u>
Surplus, December 31, current year	\$ <u>798,143</u>	\$ <u>803,008</u>	\$ <u>807,082</u>

6. MARKET CONDUCT ACTIVITIES

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

A. Advertising and Sales Activities

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

Based upon the sample reviewed, no significant findings were noted.

B. Underwriting and Policy Forms

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

Section 2611 of the New York Insurance Law states, in part:

“(a) No insurer or its designee shall request or require an individual proposed for insurance coverage to be the subject of an HIV related test without receiving the written informed consent of such individual prior to such testing and without providing general information about AIDS and the transmission of HIV infection.
(b) Written informed consent to an HIV related test shall consist of a written authorization that is dated and includes at least the following . . .
(3) a statement that a positive test result is an indication that the individual may develop AIDS and may wish to consider further independent testing . . .
(5) the department of health's statewide toll-free telephone number that may be called for further information about AIDS, the meaning of HIV related test results, and the availability and location of HIV related counseling services . . .”

Five certificates were reviewed for receipt of the proper HIV consent forms. Three of the five certificates did not have a consent form that contained: general information about AIDS and the transmission of HIV infection; a statement that a positive test result is an indication that the individual may develop AIDS and may wish to consider further independent testing; and, the department of health's statewide toll-free telephone number that may be called for further

information about AIDS, the meaning of HIV related test results, and the availability and location of HIV related counseling services.

The Association violated Section 2611(a), (b)(3) and (b)(5) of the New York Insurance Law by not using consent forms that contained the information required by Law.

C. Treatment of Certificateholders

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.

Based upon the sample reviewed, no significant findings were noted.

D. Response to Supplement No. 1 to Department Circular Letter No. 19 (2000)

Supplement No. 1 to Circular Letter No. 19 (2000) (the "Supplement"), issued by the Department on June 22, 2000, notified all licensed fraternal benefit societies that the Department was investigating allegations of race-based underwriting of life insurance by its licensees. The Supplement directed, pursuant to Section 308 of the New York Insurance Law, each domestic and foreign fraternal benefit society to review its past and present underwriting practices regarding race-based underwriting and to report its findings to the Department, no later than August 15, 2000.

Pursuant to Section 308 of the New York Insurance Law, the Company submitted in a timely manner a report of the findings of its review of past and present underwriting practices regarding race-based underwriting made in accordance with the requirements of the Supplement.

The Company reported that ". . . we have reviewed all relevant documents, including but not limited to, rate charts, mortality tables, agent and broker contracts, compensation schedules, underwriting and agent manuals, applications and policy form filings, Board of Director and committee minutes, internal memoranda, all current documents and all available past documents particularly those relating to the operating policies of the Association."

In summary, the Company's findings were that it does not currently employ race-based underwriting practices and it has found no evidence that any such practice ever existed.

An analysis of the Company's response to the Supplement and other factors indicated that the Company's review of its past and present underwriting practices complied with the requirements of the Supplement.

7. CUSTODIAN AGREEMENTS

Department Circular Letter No. 2 (1977) sets forth affidavits to be used to confirm insurers' securities held by custodian banks. Based upon the guidance provided by this Circular Letter, brokerage firms are not acceptable custodians for securities. The Association has held securities on deposit at Smith Barney since May 14, 1985 and at Paine Webber since April 1, 1987. The Association continues to maintain its securities at the two brokerage houses despite the Department's recommendations to transfer the assets to an authorized bank or trust company. The Association does not have a custodial agreement with either of the brokerage houses.

The examiner recommends that the Association enter into a custodial agreement with an appropriate bank or trust company for the safekeeping of its securities.

This recommendation is repeated from the prior report on examination.

8. AGENCY OPERATIONS

Section 2112 of the New York Insurance Law states, in part:

“(a) Every . . . fraternal benefit society . . . 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 . . . fraternal benefit society . . .

(c) Certificates of appointment shall be valid until . . . (iii) the license expires and is not renewed.”

Section 2114 of the New York Insurance Law states, in part:

“(a)(1) No . . . fraternal benefit society doing business in this state shall pay any commission or other compensation to any person . . . 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 . . . society . . .”

The Association pays 30% for first year commissions on five year renewable term policies and a lower percentage for renewal commissions. When the five year term expires and the insured chooses to renew the policy, the agent is again paid first year commissions of 30%. Although the policy retains the same policy number it is still a new contract and the agent is required to be licensed and appointed by the Association in order to receive compensation on a new contract.

The Association violated Sections 2112 and 2114 of the New York Insurance Law when it compensated two agents that were neither licensed nor appointed with the Association.

9. PRIOR REPORT SUMMARY AND CONCLUSIONS

Following are the violation and recommendations contained in the prior report on examination and the subsequent actions taken by the Association in response to each citation:

<u>Item</u>	<u>Description</u>
A	<p>As of December 31, 1997, the board of directors had 13 members. A fourteenth member was elected effective April 1, 1998. The examiner recommends that the Association take the necessary steps to comply with its by-laws with respect to the number of directors.</p> <p>The Association amended its by-laws to reduce the minimum number of directors to 12.</p>
B	<p>The Association violated Section 3214(c) of the New York Insurance Law by not paying interest on the proceeds of matured endowments rolled over into new certificates.</p> <p>A review of a sample of matured endowments revealed that the Association is now paying interest on the proceeds of matured endowments rolled over into new certificates.</p>
C	<p>The examiner recommends that the Association enter into a custodial agreement for the holding of its securities with an appropriate institution.</p> <p>The Association continues to hold its securities with two unauthorized brokers. This recommendation is repeated in the current report on examination. (See item 7 of this report)</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 Association violated Section 2611(a), (b)(3) and (b)(5) of the New York Insurance Law by not using consent forms that contained the information required by Law.	14 - 15
B	The examiner recommends that the Association enter into a custodial agreement for the holding of its securities with an appropriate institution.	16
C	The Association violated Sections 2112 and 2114 of the New York Insurance Law when it compensated two agents that were neither licensed nor appointed with the Association.	17

APPOINTMENT NO. 21666

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:

JOSHUA WEISS

as a proper person to examine into the affairs of the

BAPTIST LIFE ASSOCIATION

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

SOCIETY

with such other information as he 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 10th day of January, 2001



NEIL D. LEVIN

Superintendent of Insurance

A handwritten signature in black ink, appearing to read "Gregory V. Serio", is written over a horizontal line.

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