NEW YORK STATE DEPARTMENT OF FINANCIAL SERVICES

REPORT ON MARKET CONDUCT EXAMINATION

OF THE

VARIABLE ANNUITY LIFE INSURANCE COMPANY

CONDITION: DECEMBER 31, 2007

DATE OF REPORT: JANUARY 30, 2009

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EXAMINER: MARC A. TSE, CFE, CLU

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Honorable Benjamin M. Lawsky
Superintendent of Financial Services
New York, New York 10004

Sir:

In accordance with instructions contained in Appointment No. 22740, dated January 15, 2008, and annexed hereto, an examination has been made into the condition and affairs of The Variable Annuity Life Insurance Company, hereinafter referred to as "the Company" or "VALIC," at its home office located at 3600 Route 66, Neptune, NJ 07753.

On October 3, 2011, the Insurance Department merged with the Banking Department to create the New York State Department of Financial Services. Wherever "Department" appears in this report, it refers to the New York State Department of Financial Services.

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

1. EXECUTIVE SUMMARY

The material violations contained in this report are summarized below:

- The Company violated Section 51.6(b)(2) of Department Regulation No. 60, by failing to require with or as part of each application the Important Notice, the sales material used and the completed Disclosure Statement.

- The Company violated Section 51.6(b)(3) of Department Regulation No. 60, by failing to examine the "Disclosure Statement," and ascertain that it is accurate and meet the requirements of the Insurance Law and this Part.

- The Company violated Section 51.6(b)(4) of Department Regulation No. 60 by failing to furnish to the insurer whose coverage is being replaced a copy of any proposal, including the sales material used in the sale of the proposed annuity contract, and the completed "Disclosure Statement" within ten days of receipt of the application.

- The Company violated Section 243.2(b) of Department Regulation No. 152 by failing to maintain a copy of the authorization letter signed by the applicant.

- The Company violated Section 3201 of the New York Insurance Law by utilizing policy forms that were not approved by the Department and by using forms for which the approval had been withdrawn by the Department.

2. SCOPE OF EXAMINATION

This examination covers the period from January 1, 2003 through December 31, 2007. As necessary, the examiner reviewed transactions occurring subsequent to December 31, 2007 but prior to the date of this report (i.e., the completion date of the examination).

The examination was limited to a review of policy forms, replacements and surrenders. The examiner utilized the National Association of Insurance Commissioners' Market Regulation Handbook or such other examination procedures, as deemed appropriate, in such review.

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

3. DESCRIPTION OF COMPANY

A. History

VALIC was originally organized as a stock life insurance company under the laws of the District of Columbia, on December 21, 1955 as The Variable Annuity Life Insurance Company of America Incorporated, located in Washington, D.C.. American General Corporation ("AGC") acquired a majority interest in the Company in 1967 and subsequently VALIC was re-organized in the State of Texas on August 20, 1968, as Variable Annuity Life Insurance Company of Texas. The name was changed to The Variable Annuity Life Insurance Company on November 5, 1968. VALIC became a wholly-owned subsidiary of AGC in 1977.

On August 29, 2001, AGC, was acquired by American International Group, Inc. (“AIG”), a Delaware corporation. As a result, VALIC is an indirect, wholly owned subsidiary of AIG. AIG is a holding company which, through its subsidiaries, is engaged in a broad range of insurance and insurance-related activities, financial services, retirement savings and asset management.

As of December 31, 2007 the Company had three affiliates, The United States Life Insurance Company in the City of New York (“USL”), American International Life Insurance Company of New York (“AIL”) and First Sunamerica Life Insurance Company (“FSA”), which are domiciled in New York.

B. 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 all states, and the District of Columbia. The Company’s main product line is individual deferred annuities. In 2007, 1.84% of annuity considerations were received from New York. Policies are written on a non-participating basis.

The Company’s agency operations are conducted on a general agency and brokerage basis.

4. 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. Sales Activities

The examiner reviewed the replacement of insurance policies.

Section 51.6 of Department Regulation No. 60 states, in part:

"(a) Each insurer shall . . .
(2) Require with or as part of each application, a completed "Definition of Replacement" signed by the applicant and agent or broker . . .

(b) Where a replacement has occurred or is likely to occur, the insurer replacing the life insurance policy or annuity contract shall . . .
(2) Require with or as part of each application a copy of any proposal, including the sales material used in the sale of the proposed life insurance policy or annuity contract, and proof of receipt by the applicant of the "IMPORTANT Notice Regarding Replacement or Change of Life Insurance Policies or Annuity Contracts" and the completed "Disclosure Statement;"
(3) Examine any proposal used, including the sales material used in the sale of the proposed life insurance policy or annuity contract, and the "Disclosure Statement," and ascertain that they are accurate and meet the requirements of the Insurance Law and this Part;
(4) Within ten days of receipt of the application furnish to the insurer whose coverage is being replaced a copy of any proposal, including the sales material used in the sale of the proposed life insurance policy or annuity contract, and the completed "Disclosure Statement" . . .
(6) Where the required forms are received with the application and found to be in compliance with this Part, maintain copies of: any proposal, including the sales material used in the sale of the proposed life insurance policy or annuity contract; proof of receipt by the applicant of the "IMPORTANT Notice Regarding Replacement or Change of Life Insurance Policies or Annuity Contracts;" the signed and completed "Disclosure Statement;" and the notification of replacement to the insurer whose life insurance policy or annuity contract is to be replaced indexed by agent, for six calendar years or until after the filing of the report on examination in which the transaction was subject to review by the appropriate insurance official of its state of domicile, whichever is later . . ."

Section 243.2(b) of Department Regulation No. 152 states, in part:

> "Except as otherwise required by law or regulation, an insurer shall maintain:
> (1) A policy record for each insurance contract or policy for six calendar years after the date the policy is no longer in force or until after the filing of the report on examination in which the record was subject to review, whichever is longer . . .
> (8) Any other record for six calendar years from its creation or until after the filing of a report on examination or the conclusion of an investigation in which the record was subject to review."

In performing the review, the examiner requested that the Company furnish a list of annuities that were issued in New York State from January 1, 2003 to December 31 2007. The Examiner requested that the list include an indicator identifying whether each annuity was a replacement or a non-replacement. The list provided by the Company revealed that the Company issued 14,038 annuities in New York State; 12,650 non-replacements, 790 replacements and 598 issues which were not identified by the Company.

The examiner selected three samples from the list as follows: 50 files identified as replacements; 20 files identified as non replacements; and 10 files where no indicator was provided. In each of the three samples selected the examiner found 1. There were files that were misidentified (replacements identified as non replacements and non replacements identified as replacements); 2. A substantial number of files for which the Company claimed were exempt from Regulation 60. Of the 80 policies that were sampled, 24 were reviewed for Regulation 60 compliance.

The Examiner recommends that the Company maintain its replacement documentation so that those files subject to Department Regulation No. 60 are clearly identified.

The examiner's review of the 24 application files deemed to be subject to Department Regulation 60 revealed:

1. a) 17 of the 24 (70.8%) replacement files reviewed were missing either: the Disclosure Statement, Important Notice Regarding Replacement or

Change of Life Insurance Policies or Annuity Contracts ("Important Notice") or; both of the these required forms.

b) In three of the 12 (25%) replacement files reviewed that contained a Disclosure Statement, the agent indicated that sales material was used in the sale of the new policy. However, the sales material was not included in any of the three files.

The Company violated Section 51.6(b)(2) of Department Regulation No. 60, by failing to require with or as part of each application the Important Notice, the sales material used and the completed Disclosure Statement.

2. In five of 12 (41.6%) replacements that contained a Disclosure Statement, the agent indicated "none" where the Disclosure Statement requires the advantages of retaining the existing coverage, despite the fact that the existing coverage had no surrender charge, while the proposed coverage contained a surrender charge.

The Company violated Section 51.6(b)(3) of Department Regulation No. 60, by failing to examine the "Disclosure Statement," and ascertain that it is accurate and meets the requirements of the Insurance Law and this Part.

The 24 replacements reviewed consisted of 20 external replacements and four internal replacements. Based on the examiner's review of the external replacements the examiner found:

1. In 15 of the 20 (75%) external replacement files reviewed there was no evidence in the files that the Disclosure Statement and sales material were sent to the existing insurer. However, in 10 cases, the Company provided a cover letter sent along with a rollover form to the existing insurer requesting that funds be transferred to the Company. The only attachments referenced in the letters were signed rollover forms, not the Disclosure Statement or the sales material.

The Company violated Section 51.6(b)(4) of Department Regulation No. 60 by failing to furnish to the insurer whose coverage is being replaced a copy of any proposal, including the sales material used in the sale of the proposed annuity contract, and the completed "Disclosure Statement" within ten days of receipt of the application.

2. In 10 of the 20 (50%) external replacement files reviewed, the file did not contain an authorization letter. The authorization letter is a form signed by the client, giving the existing insurer permission to release information to the Company in order to complete the Disclosure Statement. Without the authorization letter, the examiner can not confirm the date that information needed to complete the Disclosure Statement was requested from the other insurer. This date is necessary for the examiner to ascertain whether the other insurer is complying with the 20 day requirement and whether the Company waited 20 days prior to utilizing estimates to complete the Disclosure Statement.

The Company violated Section 243.2(b) of Department Regulation No. 152 by failing to maintain a copy of the authorization letter signed by the applicant.

B. Underwriting and Policy Forms

The examiner reviewed a sample of newly issued annuity application files and the applicable policy forms.

Section 3201 of the New York Insurance Law states, in part:

> "(a) In this article, "policy form" means any policy, contract, certificate, or evidence of insurance and any application therefor, or rider or endorsement thereto. . .
> (b)(1) No policy form shall be delivered or issued for delivery in this state unless it has been filed with and approved by the superintendent as conforming to the requirements of this chapter and not inconsistent with law. . . ."

The examiner reviewed the full population of 80 application files previously described to ensure that the forms utilized in the sales process met the provisions of Article 32 of the New York Insurance Law. The examiner's review revealed:

- The Department withdrew the approved form VL 13010-NY VER 12/01 on January 17, 2002, (to be effective in 90 days). The Company continued to use form VL 13010-NY VER 12/01 after the Department withdrew the approval for this form.
- The Company utilized policy form VL 13084-NY 12/01 – Portfolio Director Fixed and Variable Annuity Enrollment which was not approved by the Department.
- The Company utilized policy form VL18869 VER 8/2006 – Agreement to Use Electronic Application for Portfolio Director Fixed and Variable Annuity which was not approved by the Department.

The Company violated Section 3201 of the New York Insurance Law by utilizing policy forms that were not approved by the Department and by using forms for which the approval had been withdrawn by the Department.

C. Treatment of Policyholders

The examiner reviewed a sample of surrenders. The examiner also reviewed the various controls involved, checked the accuracy of the computations.

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

5. SUMMARY AND CONCLUSIONS

Following are the violations and recommendation contained in this report:

Item	Description	Page No(s).
A	The Examiner recommends that the Company maintain its replacement documentation so that those files subject to Department Regulation No. 60 are clearly identified.	6
B	The Company violated Section 51.6(b)(2) of Department Regulation No. 60, by failing to require with or as part of each application the Important Notice, the sales material used and the completed Disclosure Statement.	7
C	The Company violated Section 51.6(b)(3) of Department Regulation No. 60, by failing to examine the "Disclosure Statement," and ascertain that it is accurate and meet the requirements of the Insurance Law and this Part.	7
D	The Company violated Section 51.6(b)(4) of Department Regulation No. 60 by failing to furnish to the insurer whose coverage is being replaced a copy of any proposal, including the sales material used in the sale of the proposed annuity contract, and the completed "Disclosure Statement" within ten days of receipt of the application.	8
E	The Company violated Section 243.2(b) of Department Regulation No. 152 by failing to maintain a copy of the authorization letter signed by the applicant.	8
F	The Company violated Section 3201 of the New York Insurance Law by utilizing policy forms that were not approved by the Department and by using forms for which the approval had been withdrawn by the Department.	9

Respectfully submitted,

/s/
Marc A. Tse, CFE, CLU
Associate Insurance Examiner

STATE OF NEW YORK)
)SS:
COUNTY OF NEW YORK)

Marc A. Tse, being duly sworn, deposes and says that the foregoing report, subscribed by him, is true to the best of his knowledge and belief.

/s/
Marc A. Tse

Subscribed and sworn to before me

this_____ day of _____

APPOINTMENT NO. 22740

STATE OF NEW YORK

INSURANCE DEPARTMENT

*I, **ERIC R. DINALLO**, Superintendent of Insurance of the State of New York, pursuant to the provisions of the Insurance Law, do hereby appoint:*

MARC TSE

as a proper person to examine into the affairs of the

VARIABLE ANNUITY LIFE INSURANCE COMPANY

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

COMPANY

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 15th day of January, 2008

ERIC R. DINALLO
Superintendent of Insurance

Superintendent