

STATE OF NEW YORK INSURANCE DEPARTMENT
REPORT ON EXAMINATION
OF THE
FIRST SAFECO NATIONAL LIFE INSURANCE COMPANY OF NEW YORK
AS OF
DECEMBER 31, 2001

DATE OF REPORT:

JANUARY 10, 2003

EXAMINER:

VINCENT TARGIA

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

George E. Pataki
Governor

Gregory V. Serio
Superintendent

January 10, 2003

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

Sir:

In accordance with instructions contained in Appointment No. 21930, dated August 27, 2002 and annexed hereto, an examination has been made into the condition and affairs of the First SAFECO National Life Insurance Company of New York, hereinafter referred to as "the Company," at its home office located at 375 Woodcliff Drive, Fairport, New York 14450.

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 that materially affected the Company's financial condition as presented in its financial statements contained in the December 31, 2001 filed annual statement. (See item 5 of this report)

The Company violated Section 243.2(b)(4) of Department Regulation No. 152 by failing to maintain claim files for six calendar years or until the filing of the report on examination in which the claim file was subject to review, whichever is longer. (See item 6C1 of this report)

The Company violated Section 216.11 of Department Regulation No. 64 by failing to maintain claim files so that events relating to a claim can be reconstructed by the Department examiners. (See item 6C2 of this report)

2. SCOPE OF EXAMINATION

The prior examination was conducted as of December 31, 1998. This examination covers the period from January 1, 1999 through December 31, 2001. As necessary, the examiner reviewed transactions occurring subsequent to December 31, 2001 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, 2001 to determine whether the Company's 2001 filed 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
- Officers' and employees' welfare and pension plans
- 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 contained in the prior report on examination. The results of the examiner's review are contained in item 7 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

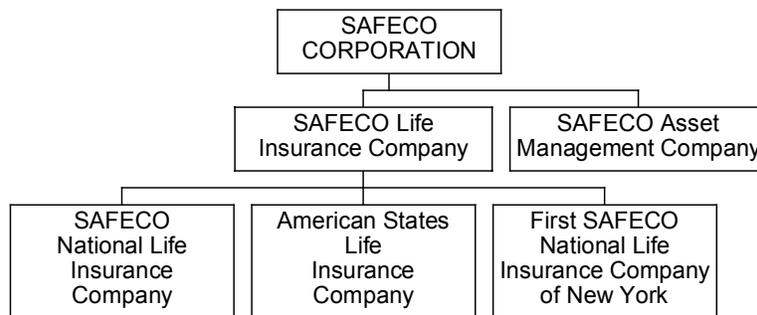
A. History

The Company was incorporated as a stock life insurance company under the laws of New York on April 23, 1987 and was licensed and commenced business on January 2, 1990. Initial resources of \$8,500,000, consisting of common capital stock of \$2,000,000 and paid in and contributed surplus of \$6,500,000, were provided through the sale of 20,000 shares of common stock for \$425 per share.

B. Holding Company

The Company is a wholly owned subsidiary of SAFECO Life Insurance Company (“SAFECO”), a Washington domiciled life insurer. SAFECO is in turn a wholly owned subsidiary of the Company’s ultimate parent, SAFECO Corporation, a Washington corporation.

An organization chart reflecting the relationship between the Company and significant entities in its holding company system as of December 31, 2001 follows:



The Company has no employees and essentially relies upon affiliates for all services. The Company had two service agreements in effect as of December 31, 2001, one with its parent SAFECO, and one with an affiliate, SAFECO Asset Management Company (“SAMC”). The agreement with SAFECO dated November 1, 1998 states that SAFECO will provide the Company with accounting, underwriting, claims, advertising, policyholder and functional support services. The agreement with SAMC dated June 1, 1990 provides for the rendering by SAMC to

the Company of advice and services necessary for the purchase, sale and other disposition of securities in accordance with the Company's investment policies.

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 21 directors. Directors are elected at each annual meeting of the shareholders held in August of each year. Directors are elected to hold office until the next annual meeting of the shareholders and until their successors have been elected and qualified. As of December 31, 2001, the board of directors consisted of 12 members. The annual meeting of the board of directors is held each year directly after the adjournment of the annual shareholders' meeting. Regular meetings of the board are held at such time as may from time to time be fixed by the board.

The 12 board members and their principal business affiliation, as of December 31, 2001, were as follows:

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>	<u>Year First Elected</u>
Scott L. Bartholomaus Mukilteo, WA	Vice President First SAFECO National Life Insurance Company of New York SAFECO Life Insurance Company	2000
Kenneth N. Berk Monroe, NY	Regional Commercial Manager SAFECO Insurance Company of America	1987
Barbara J. Dingfield* Seattle, WA	Independent Consultant	1990
Roger F. Harbin Redmond, WA	Vice President First SAFECO National Life Insurance Company of New York Executive Vice President SAFECO Life Insurance Company	2001
Peter K. Ledwith* Lynbrook, NY	Partner Law Offices of Peter Ledwith	1989

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>	<u>Year First Elected</u>
Richard E. Lundgren* Federal Way, WA	Retired	1987
Rodney A. Pierson Redmond, WA	Vice President and Secretary First SAFECO National Life Insurance Company of New York Senior Vice President, Chief Financial Officer and Secretary SAFECO Corporation	1991
Larry L. Pinnt* Redmond, WA	Independent Consultant	1987
Terence M. Quinlan* Belle Harbor, NY	Partner White, Quinlin & Staley, L.L.P.	1989
John W. Schneider* Seattle, WA	President Wallingford Group, Inc.	1987
Ronald L. Spaulding Mill Creek, WA	Vice President and Treasurer First SAFECO National Life Insurance Company of New York Treasurer and Chief Investment Officer SAFECO Corporation	1996
Randall H. Talbot Medina, WA	President First SAFECO National Life Insurance Company of New York SAFECO Life Insurance Company	1998

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

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

“(1) . . . the number of directors shall be fixed by the by-laws . . .
 (2) If not otherwise fixed under this article, the number shall be thirteen but it may be increased or . . . decreased by amendment of the by-laws, or by action of the board . . .”

Section 2, Article II of the Company’s by-laws state, in part:

“Number of Directors. The number of directors constituting the entire Board of Directors shall not be less than thirteen nor more than twenty-one. Within such limits, the number of directors may be fixed from time to time by vote of a majority of the Board of Directors at any regular or special meeting . . .”

The Company violated Section 1202(a)(2) of the New York Insurance Law and its by-laws by failing to maintain the minimum number of directors (13).

In December 2001, Rodney A. Pierson retired from the board and was replaced by Christine Mead.

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 Company as of December 31, 2001:

<u>Name</u>	<u>Title</u>
Randall H. Talbot	President
Rodney A. Pierson	Vice President and Secretary
Ronald L. Spaulding	Vice President and Treasurer
Michael J. Kinzer	Vice President and Actuary
Scott L. Bartholomaus	Vice President
Stephen D. Collier	Vice President
Roger F. Harbin	Vice President
Michele M. Kemper*	Vice President
James D. Pirak	Vice President
Leslie L. Rice	Vice President and Controller
Paul A. Stevenson	Vice President
Malcolm S. Taylor	Vice President

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

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 in New York only. The Company's operations are conducted on a general agency basis. The Company's business is comprised entirely of individual and group annuities. The Company began writing fixed deferred annuities in 1990 but, due to a low interest rate environment and the lack of profitability, it ceased actively marketing these annuities in 1998. In December 2001, the Company received approval from the Department for a new fixed deferred annuity contract that will be distributed primarily through financial institutions and banks. The Company began issuing variable annuities in 1997 but also ceased selling this business in 1998.

E. Reinsurance

As of December 31, 2001, the Company had reinsurance treaties in effect with two companies, both of which were authorized or accredited. The Company's variable annuities with life or disability contingencies are reinsured on an automatic yearly renewable term basis. Less than 1% of the Company's business is reinsured.

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>1998</u>	<u>December 31,</u> <u>2001</u>	<u>Increase</u> <u>(Decrease)</u>
Admitted assets	<u>\$34,092,597</u>	<u>\$28,618,819</u>	<u>\$(5,473,778)</u>
Liabilities	<u>\$22,906,185</u>	<u>\$15,464,361</u>	<u>\$(7,441,824)</u>
Common capital stock	\$ 2,000,000	\$ 2,000,000	\$ 0
Gross paid in and contributed surplus	6,500,000	6,500,000	0
Unassigned funds (surplus)	<u>2,686,412</u>	<u>4,654,458</u>	<u>1,968,046</u>
Total capital and surplus	<u>\$11,186,412</u>	<u>\$13,154,458</u>	<u>\$ 1,968,046</u>
Total liabilities, capital and surplus	<u>\$34,092,597</u>	<u>\$28,618,819</u>	<u>\$(5,473,778)</u>

The Company's invested assets as of December 31, 2001, exclusive of Separate Accounts, were mainly comprised of bonds (94.3%) and cash and short-term investments (5.5%). The majority (99%) of the Company's bond portfolio, as of December 31, 2001, was comprised of investment grade obligations.

The Company's reduction in admitted assets and liabilities was a result of the Company's 1998 decision to discontinue marketing its insurance products. With no new business, the Company sold assets or used bonds that matured to cover benefit payments. Similarly, policyholder withdrawals and surrenders caused the Company's reserves to decrease.

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>Group Annuities</u>		
	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>1999</u>	<u>2000</u>	<u>2001</u>
Outstanding, end of previous year	202	187	171	43	37	28
Issued during the year	3	2	0	1	0	0
Other net changes during the year	<u>(18)</u>	<u>(18)</u>	<u>(10)</u>	<u>(7)</u>	<u>(9)</u>	<u>(4)</u>
Outstanding, end of current year	<u>187</u>	<u>171</u>	<u>161</u>	<u>37</u>	<u>28</u>	<u>24</u>

The Company ceased the active marketing of its annuities in 1998 due to the lack of profitability, which it attributes to the low interest rate environment.

The following is the net gain 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>1999</u>	<u>2000</u>	<u>2001</u>
Individual annuities	\$438,908	\$442,036	\$384,332
Group annuities	<u>311,926</u>	<u>315,164</u>	<u>227,390</u>
Total	<u>\$750,834</u>	<u>\$757,200</u>	<u>\$611,722</u>

5. FINANCIAL STATEMENTS

The following statements show the assets, liabilities, capital, surplus and other funds as of December 31, 2001, as contained in the Company's 2001 filed 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 that materially affected the Company's financial condition as presented in its financial statements contained in the December 31, 2001 filed annual statement.

A. ASSETS, LIABILITIES, CAPITAL, SURPLUS AND OTHER FUNDS AS OF DECEMBER 31, 2001

Admitted Assets

Bonds	\$26,037,063
Policy loans	34,812
Cash and short term investments	1,526,848
Life insurance premiums and annuity considerations deferred and uncollected on in force business	(18)
Investment income due and accrued	453,898
From Separate Accounts statement	<u>566,216</u>
 Total admitted assets	 <u>\$28,618,819</u>

Liabilities, Capital, Surplus and Other Funds

Aggregate reserve for life policies and contracts	\$14,339,935
Policy and contract liabilities: Interest maintenance reserve	234,292
Commissions to agents due or accrued	186
General expenses due or accrued	14,402
Transfers to Separate Accounts due or accrued	(13,640)
Taxes, licenses and fees due or accrued	24
Federal and foreign income taxes	72,960
Amounts withheld or retained by company as agent or trustee	39,031
Remittances and items not allocated	17,371
Miscellaneous liabilities:	
Asset valuation reserve	98,857
Payable to parent, subsidiaries and affiliates	94,727
From Separate Accounts statement	<u>566,216</u>
 Total liabilities	 <u>\$15,464,361</u>
 Common capital stock	 \$ 2,000,000
Gross paid in and contributed surplus	6,500,000
Unassigned funds (surplus)	<u>4,654,458</u>
 Total capital, surplus and other funds	 <u>\$13,154,458</u>
 Total liabilities, capital, surplus and other funds	 <u>\$28,618,819</u>

B. CONDENSED SUMMARY OF OPERATIONS

	<u>1999</u>	<u>2000</u>	<u>2001</u>
Premiums and considerations	\$ 80,031	\$ 53,489	\$ 40,944
Investment income	2,347,538	2,167,824	1,835,750
Miscellaneous income	<u>54,751</u>	<u>50,872</u>	<u>20,079</u>
 Total income	 <u>\$2,482,320</u>	 <u>\$2,272,185</u>	 <u>\$1,896,773</u>
Benefit payments	\$3,275,726	\$4,987,661	\$2,529,514
Increase in reserves	(1,971,852)	(3,902,369)	(1,622,136)
Commissions	2,429	1,777	1,238
General expenses and taxes	100,520	78,139	132,712
Net transfers to (from) Separate Accounts	<u>(64,806)</u>	<u>(36,223)</u>	<u>(24,833)</u>
 Total deductions	 <u>\$1,342,017</u>	 <u>\$1,128,985</u>	 <u>\$1,016,495</u>
Net gain	\$1,140,303	\$1,143,200	\$ 880,278
Federal and foreign income taxes incurred	<u>389,469</u>	<u>385,999</u>	<u>268,554</u>
Net gain (loss) from operations before net realized capital gains	\$ 750,834	\$ 757,201	\$ 611,724
Net realized capital gains (losses)	<u>0</u>	<u>(263,924)</u>	<u>67,662</u>
 Net income	 <u>\$ 750,834</u>	 <u>\$ 493,277</u>	 <u>\$ 679,386</u>

The Company's net income decreased significantly in 2000 as compared to 1999 primarily as a result of a decrease in net investment income and an increase in benefit payments. The decrease in net investment income was the result of a decrease in invested assets due to the Company's decision to discontinue sales in 1998. The substantial increase in benefit payments (withdrawals) during 2000 was due to the expiration of the surrender charge period for a large number of policies.

C. CAPITAL AND SURPLUS ACCOUNT

	<u>1999</u>	<u>2000</u>	<u>2001</u>
Capital and surplus, December 31, prior year	<u>\$11,186,412</u>	<u>\$11,947,028</u>	<u>\$12,569,156</u>
Net income	\$ 750,834	\$ 493,277	\$ 679,386
Change in non-admitted assets and related items	21,820	(17,630)	4,773
Change in asset valuation reserve	(12,038)	146,480	(98,857)
Other changes in surplus in Separate Accounts statement	<u>0</u>	<u>1</u>	<u>0</u>
Net change in capital and surplus	<u>\$ 760,616</u>	<u>\$ 622,128</u>	<u>\$ 585,302</u>
Capital and surplus, December 31, current year	<u>\$11,947,028</u>	<u>\$12,569,156</u>	<u>\$13,154,458</u>

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.

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

B. Underwriting and Policy Forms

The examiner reviewed new underwriting files and the applicable policy forms.

Based upon the review, no significant findings were noted.

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.

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

“Except as otherwise required by law or regulation, an insurer shall maintain . . .
 (4) A claim file for six calendar years after all elements of the claim are resolved and the file is closed or until after the filing of the report on examination in which the claim file was subject to review, whichever is longer. A claim file shall show clearly the inception, handling and disposition of the claim, including the dates that forms and other documents were received. . . .”

As part of the review of the Company's treatment of policyholders 11 surrendered policy files and seven death claim files were requested. The Company could not provide two (18.2%) of the surrendered policy files and three (42.8%) of the death claims files requested.

The Company violated Section 243.2(b)(4) of Department Regulation No. 152 for failing to maintain claim files for six calendar years or until after the filing of the report on examination in which the claim file was subject to review, whichever is longer.

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

“ . . . To enable department personnel to reconstruct an insurer’s activities, all insurers subject to the provisions of this Part must maintain within each claim file all communications, transactions, notes and work papers 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. Insurers shall either make a notation in the file or retain a copy of all forms mailed to claimants.”

A review of nine surrendered policy files and four death claim files indicated that the files were not complete. The examiner could not determine the effective date of the surrender, the surrender notification date, and whether any surrender charges were applicable. Similarly, the examiner was unable to determine the death claim proceeds amount, the claim notification date, or the date that all necessary information to process the claim was received by the Company.

The Company violated Section 216.11 of Department Regulation No. 64 for failing to maintain claim files so that events relating to a claim can be reconstructed by the Department examiners.

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 life insurers 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 life insurer 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 it was incorporated on April 23, 1987 and solely writes annuity products and has never sold nor assumed from another company any life insurance policies in the State of New York. In addition, the Company reviewed product applications, new business processing, underwriting, benefit application and benefit payment practices and procedures.

In summary, the Company's findings confirmed that it does not now nor has it ever engaged in race-based underwriting or other business processing using race as a criterion.

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. PRIOR REPORT SUMMARY AND CONCLUSIONS

Following are the violations contained in the prior report on examination 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) of the New York Insurance Law by receiving premium collection services from its parent without giving the superintendent notice of its intention to enter into such services.</p> <p>A review indicated that the Company submitted and received Department approval to receive premium collection services from its parent.</p>
B	<p>The Company violated Section 325(a) of the New York Insurance Law by not maintaining all of its books of account at its principal office in this state.</p> <p>A review indicated that the Company instituted procedures to ensure that it maintains its books of account at its principal office in this state. The examination revealed that the Company's books of account were maintained in this state.</p>
C	<p>The Company violated Section 219.5(a) of Department Regulation No. 34-A by not maintaining its advertising files at its home office.</p> <p>A review indicated that the Company instituted procedures to ensure that their advertising files are maintained at its home office. The examination revealed that the Company's advertisements were maintained at its home office.</p>
D	<p>The Company violated Section 2122(a)(2) of the New York Insurance Law by distributing advertisements calling attention to an unauthorized insurer.</p> <p>A review indicated that the Company instituted procedures to ensure that its advertisements do not call attention to an unauthorized insurer. The examination did not reveal any instances where the Company's advertisements called attention to an unauthorized insurer.</p>

8. SUMMARY AND CONCLUSIONS

Following are the violations contained in this report:

<u>Item</u>	<u>Description</u>	<u>Page No(s).</u>
A	The Company violated Section 1202 of the New York Insurance Law and its by-laws by failing to maintain the minimum number of directors.	7
B	The Company violated Section 243.2(b)(4) of Department Regulation No. 152 by failing to maintain claim files for six calendar years or until the filing of the report on examination in which the claim file was subject to review, whichever is longer.	15 – 16
C	The Company violated Section 216.11 of Department Regulation No. 64 by failing to maintain claim files so that events relating to a claim can be reconstructed by the Department examiners.	16

APPOINTMENT NO. 21930

STATE OF NEW YORK
INSURANCE DEPARTMENT

I, GREGORY V. SERIO, Superintendent of Insurance of the State of New York, pursuant to the provisions of the Insurance Law, do hereby appoint:

VINCENT TARGIA

as a proper person to examine into the affairs of the

FIRST SAFECO NATIONAL LIFE INSURANCE COMPANY OF NEW YORK

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 27th day of August, 2002



GREGORY V. SERIO
Superintendent of Insurance


Superintendent