

STATE OF NEW YORK INSURANCE DEPARTMENT

REPORT ON EXAMINATION

OF THE

UNITY MUTUAL LIFE INSURANCE COMPANY

AS OF

DECEMBER 31, 2002

DATE OF REPORT:

OCTOBER 10, 2003

EXAMINER:

EDEN M. SUNDERMAN

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

October 10, 2003

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

Sir:

In accordance with instructions contained in Appointment No. 22000, dated January 21, 2003 and annexed hereto, an examination has been made into the condition and affairs of Unity Mutual Life Insurance Company, hereinafter referred to as "the Company," at its home office located at 507 Plum Street, Syracuse, New York 13204.

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 Company's financial condition as presented in its financial statements contained in the December 31, 2002 filed annual statement. (See item 5 of this report)

The Company violated Section 1712 of the New York Insurance Law by providing an interest free loan to its subsidiary in the amount of \$175,000. A similar violation appeared in the prior report on examination. (See item 3B of this report)

The Company violated Section 2108(a)(3) of the New York Insurance Law by contracting with a third party, who is not a licensed adjuster, to provide claims adjudication services with regard to its accident and health policies. (See item 3B of this report)

The Company violated Section 91.4(a)(2) of Department Regulation No. 33 by failing to maintain records with sufficient detail to show fully: (i) the system actually used for allocation of income and expenses; (ii) the actual bases of allocation of income and expenses; and (iii) the actual monetary distribution of income and salaries to lines of business and companies. (See item 4 of this report)

The Company violated Section 420.5(a)(1) of Department Regulation No. 169 by failing to provide privacy notices to a number of customers at least once in any period of 12 consecutive months since July 1, 2001. (See item 7D of this report)

The examiner recommends that the Company maintain minutes for its Investment Review Committee meetings that clearly document the final decision of the Committee regarding whether or not an other than temporary write down of an impaired asset is required and the evidentiary material used as a basis for that decision. (See item 8 of this report)

The Company violated Section 4228(f)(1)(B) of the New York Insurance Law by failing to file a compensation arrangement with the Department. A similar violation appeared in the prior report on examination. (See item 9 of this report)

## 2. SCOPE OF EXAMINATION

The prior examination was conducted as of December 31, 1999. This examination covers the period from January 1, 2000 through December 31, 2002. As necessary, the examiner reviewed transactions occurring subsequent to December 31, 2002 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, 2002 to determine whether the Company's 2002 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, recommendations and comments contained in the prior report on examination. The results of the examiner's review are contained in item 10 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 organized as a fraternal benefit society in 1903 under the name of the Imperial Order Tycoons and commenced business in 1905. The name of the Society was changed in 1908 to the Unity Insurance Society, in 1918 to The Unity Protective Insurance Association and in 1928 to The Unity Life and Accident Insurance Association.

Effective January 1, 1957, the Society was converted to a mutual life insurance company, pursuant to the provisions of Section 487 (now Section 7304) of the New York Insurance Law. At the time of conversion, the name of the Company was changed to The Unity Mutual Life Insurance Company of New York. The present name, Unity Mutual Life Insurance Company was adopted in September 1972.

Effective December 1983, Guarantee Mutual Life Insurance Company was merged with and into the Company.

Effective December 31, 1985, Empire State Mutual Life Insurance Company was merged with and into the Company.

Effective September 30, 1987, Volunteer Firemen's Mutual Life Insurance Company was merged with and into the Company.

Effective November 30, 1989, Progressive Life Insurance Company was merged with and into the Company.

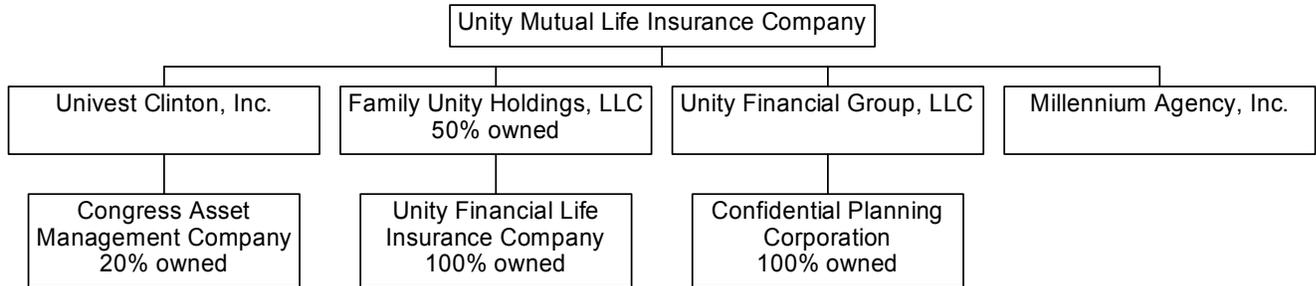
Effective May 31, 1993, Eastern Mutual Life Insurance Company of New Jersey was merged with and into the Company.

Effective December 30, 1993, Empire State Life Insurance Company, a subsidiary of the Company, was merged with and into the Company.

On May 15, 2001, the Company issued a 15-year surplus note, dated May 15, 2001, with a face amount of \$5,000,000 and bearing interest at 11% payable to Scottish Annuity & Life Insurance Company (Cayman) Limited. The surplus note is scheduled to mature on May 16, 2016. Each accrual and payment of interest on the note may be made only with the prior approval of the Superintendent under the provisions of Section 1307 of the New York Insurance Law.

## B. Subsidiaries

An organization chart reflecting the relationship between the Company and significant entities in its holding company system as of December 31, 2002 follows:



Following are descriptions of the significant subsidiaries of the Company.

1. Univest Clinton, Inc. (“UNIVEST”) is a wholly owned subsidiary of the Company. UNIVEST was formed as a subsidiary to purchase an interest (20%) in Congress Asset Management Company (“CAM”), a Boston based investment advisory firm. CAM performs investment-related activities for the Company. As of December 31, 2002 UNIVEST had assets of \$3,804,898 and stockholder’s equity of \$3,508,127.
2. Family Unity Holdings, LLC (“FUH”) was formed in December 2001 by the Company and a partner, each with a 50% ownership interest and an initial investment of \$5,000. Subsequent to the establishment of FUH, the Company sold a 50% interest in its wholly owned Pennsylvania domiciled stock life insurance subsidiary, Unity Financial Life Insurance Company (“UFLIC”), to its partner in FUH. Immediately following the sale, each of the partners in FUH contributed their 50% interest in UFLIC to FUH. UFLIC is a life insurer authorized to write life insurance, annuities and accident and health insurance in 38 states, but not New York. As of December 31, 2002, UFLIC had assets of \$19,230,857 and capital and surplus of \$5,463,806. As of December 31, 2002 Unity’s investment in the stockholder equity of FUH was valued at \$2,736,904.
3. Unity Financial Group, LLC (“UFGLLC”) was formed on October 28, 1998 as a limited liability company for the purpose of purchases and acquisitions. UFGLLC purchased Confidential Planning Corporation (“CPC”), a financial services company, on October 31, 1998. As of December 31, 2002, UFGLLC had assets of \$2,323,832 and stockholder equity of \$1,858,601.

4. Millennium Agency, Inc. (“Millennium”) was formed on February 5, 1998 as a subsidiary to house the debit insurance business purchased from the R.O. Lan Insurance Agency, Inc. The Company purchased 100% of the outstanding shares of R.O. Lan Agency, Inc., for \$600,000. As of December 31, 2002, Millennium had assets of \$422,122 (of which \$361,767 was related to goodwill/intangible assets) and stockholder’s equity of \$382,667.

The Company had 6 service agreements in effect as of December 31, 2002.

Type of Agreement	Effective Date	Provider(s) of Service(s)	Recipient(s) of Service(s)	Specific Service(s) Covered
Service and Expense Allocation Agreement	December 18, 2001	the Company	UFLIC	Policy administration services for pre-need and final expense production in addition to the use of facilities, equipment, and services of personnel, including but not limited to: agency reporting; management reporting; actuarial services; accounting services.; claims; agent licensing and administration; records maintenance; regulatory compliance; legal; printing; and marketing.
Service and Expense Allocation Agreement	January 1, 2002	the Company	FUH	Use of facilities, equipment and services of personnel including, but not limited to: accounting; regulatory compliance; and legal.
Service and Expense Allocation Agreement	December 14, 1988 amended December 14, 1988 and January 27, 1995	the Company	UNIVEST	Use of facilities, equipment and services of personnel including, but not limited to: agency reporting; management reporting; accounting; actuarial; underwriting; claims; agent licensing and administration; mailroom; records maintenance; regulatory compliance; printing; legal; and marketing.

Type of Agreement	Effective Date	Provider(s) of Service(s)	Recipient(s) of Service(s)	Specific Service(s) Covered
Service and Expense Allocation Agreement	October 30, 1998	the Company	CPC	Use of facilities, equipment and services of personnel including, but not limited to: agency reporting; management reporting; accounting; actuarial; agent licensing and administration; mailroom; records maintenance; regulatory compliance; printing; legal; and marketing.
Service and Expense Allocation Agreement	January 28, 1998	the Company	Millennium	Use of facilities, equipment and services of personnel including, but not limited to: agency reporting; management reporting; accounting; actuarial; agent licensing and administration; mailroom; records maintenance; regulatory compliance; printing; legal; and marketing.
Service and Expense Allocation Agreement	December 27, 2002	the Company	UFGLLC	Use of facilities, equipment and services of personnel including, but not limited to: agency reporting; management reporting; accounting; actuarial; agent licensing and administration; mailroom; records maintenance; regulatory compliance; printing; legal; and marketing.

Section 1712 of the New York Insurance Law states, in part:

“ . . . All transactions between the parent corporation and its subsidiaries shall be fair and equitable . . . ”

A review of inter-company transactions and billing statements during the current examination period revealed that the Company had not received any reimbursement from its subsidiary, UFGLLC, for debt service paid on its behalf in connection with a loan from Chase Manhattan Bank and for other amounts paid on behalf of the subsidiary.

The Company violated Section 1712 of the New York Insurance Law by providing an interest free loan to its subsidiary in the amount of \$175,000. A similar violation appeared in the previous report on examination.

### 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 divided into three classes and one class is elected for a period of three years at each annual meeting of the policyholders held in April of each year. As of December 31, 2002, the board of directors consisted of 16 members. Meetings of the board are held in February, May, September, and November.

The 16 board members and their principal business affiliation, as of December 31, 2002, were as follows:

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>	<u>Year First Elected</u>
Patricia T. Civil* Marcellus, NY	Retired	2002
Frank T. Crohn* Rhinebeck, NY	Retired	1983
Arnold G. Gough, Jr.* Hindsdale, IL	Partner Winston & Strawn	1998
Eugene T. Herbert* Great Falls, VA	Attorney	1987
George T. Hornig* New York, NY	Managing Director and Chief Operating Officer Credit Suisse First Boston	1995

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>	<u>Year First Elected</u>
John F.X. Mannion Lafayette, NY	Chairman of the Board Unity Mutual Life Insurance Company	1974
Patrick A. Mannion Fayetteville, NY	President and Chief Executive Officer Unity Mutual Life Insurance Company	1991
Terence A. J. Mannion* Syracuse, NY	Partner Mannion & Copani	1998
Joseph Masella Syracuse, NY	Executive Vice President Unity Mutual Life Insurance Company	1987
William L. O'Halloran, S.J.* Worcester, MA	Vice President College of the Holy Cross	1983
Robert D. Pietrafesa* Vero Beach, FL	Retired	1977
Elaine M. Ryan* Washington, DC	Government Affairs Director American Public Human Service Association	1998
Kenneth A. Shaw* Syracuse, NY	Chancellor and President Syracuse University	1992
Edward J. Slaby Manlius, NY	Senior Vice President, Investments and Actuarial Unity Mutual Life Insurance Company	1987
Phillip A. Turberg* Newtown Square, PA	Independent Consulting Actuary	1988
Joseph N. Walsh, Jr.* Bedford, NY	Independent Consultant	1983

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

In September 2003, Joseph N. Walsh, Jr. passed away and has not been replaced as of the date of this report.

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, 2002:

<u>Name</u>	<u>Title</u>
Patrick A. Mannion*	President and Chief Executive Officer
Joseph Masella	Executive Vice President
Joyce H. Kopicik	Senior Vice President and Chief Financial Officer
Jeffrey S. Shaw	Senior Vice President and Chief Marketing Officer
Edward J. Slaby	Senior Vice President, Investments and Actuarial
Jay W. Wason, Jr.	Senior Vice President, General Counsel and Secretary

\* 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 to transact business in 50 states, the District of Columbia, Puerto Rico, and the U.S. Virgin Islands.

The following tables show the percentage of direct premiums received, by state, and by major lines of business for the year 2002:

<u>Life Insurance Premiums</u>		<u>Annuity Considerations</u>	
New York	49.4%	New York	89.6%
New Jersey	<u>29.3</u>	All others	<u>10.4</u>
Subtotal	78.7%	Total	<u>100.0%</u>
All others	<u>21.3</u>		
Total	<u>100.0%</u>		

During the examination period, the Company primarily sold life insurance and annuity products. The life insurance line included whole life, final expense, pre-need, and monthly debit ordinary. Monthly debit ordinary (“MDO”) life insurance is generally small face whole life insurance (maximum issue amount of \$10,000) where the premium is collected and remitted to the Company by the servicing/writing agent on a monthly basis. The Company’s final expense business is sold on a simplified issue basis and is currently available up to a maximum face amount of \$25,000. Final expense insurance is designed to meet the final expenses that occur at the end of life and are payable directly to an insured’s family. Pre-need insurance is also designed to meet one’s final expenses and is typically sold by funeral home employees that are licensed life insurance agents. Pre-need benefits are paid directly to the funeral home for the services that the institution provides. Until 2001, the Company wrote pre-need insurance in states other than New York. New sales of pre-need products were transitioned to its subsidiary, UFLIC, by year-end 2000. In addition to the shift of new pre-need insurance to its subsidiary, the Company embarked on the latest phase of its re-structuring plan by limiting the acceptance of applications for its monthly debit ordinary policies. After September 2003, the Company will only accept new additions to existing family groups with regard to its MDO product. It is the Company’s long-term marketing strategy to transition from MDO products to final expense products.

The annuity line includes single and flexible premium fixed annuity contracts. In 2002, due to the current interest rate environment and narrowing spreads, the Company decided to control or de-emphasize sales of its fixed annuity products.

The Company’s agency operations are conducted on a general agency basis. In December 2000, the board approved a multi-phase restructuring plan to improve the Company’s profitability that included closing agency branch offices (in the Atlantic Region) in 2001 and converting its captive agents to independent agents.

Section 2108(a)(3) of the New York Insurance Law states:

“No adjuster shall act on behalf of an insurer unless licensed as an independent adjuster, and no adjuster shall act on behalf of an insured unless licensed as a public adjuster.”

A review of the Company’s third party administrative service agreement with Maurice W. Pomfrey & Associates, Ltd. (“POMCO”) revealed that POMCO provides administrative and claims processing services to the Company on its accident and health policies. POMCO is not a licensed adjuster.

The Company violated Section 2108(a)(3) of the New York Insurance Law by contracting with a third party, who is not a licensed adjuster, to provide claims adjudication services with regard to its accident and health policies.

#### E. Reinsurance

##### Ceded

As of December 31, 2002, the Company had individual life and accident and health reinsurance cession agreements with 22 companies, of which 14 were authorized or accredited. The Company’s life and accident and health policies are reinsured 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 \$150,000. The total face amount of life insurance ceded as of December 31, 2002, was \$498,239,741, which represents 46.9% of the total face amount of life insurance in force. Reserve credit taken for reinsurance ceded to unauthorized companies, totaling \$237,452,518, was supported by letters of credit and trust agreements.

##### Assumed

As of December 31, 2002, the Company assumed individual life business from one affiliated insurer, UFLIC. The total amount of life insurance assumed as of December 31, 2002, was \$22,391,000 or 2.1% 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:

	December 31, <u>1999</u>	December 31, <u>2002</u>	Increase (Decrease)
Admitted assets	\$ <u>483,359,273</u>	\$ <u>412,952,312</u>	\$( <u>70,406,961</u> )
Liabilities	\$ <u>457,900,034</u>	\$ <u>391,696,914</u>	\$( <u>66,203,120</u> )
Guaranty fund – State of Colorado	\$ 400,000	\$ 0	\$ (400,000)
Group contingency life reserve	259,302	0	(259,302)
Surplus notes	0	5,000,000	5,000,000
Unassigned funds (surplus)	<u>24,799,937</u>	<u>16,255,398</u>	<u>(8,544,539)</u>
Total surplus	\$ <u>25,459,239</u>	\$ <u>21,255,398</u>	\$ ( <u>4,203,841</u> )
Total liabilities and surplus	\$ <u>483,359,273</u>	\$ <u>412,952,312</u>	\$( <u>70,406,961</u> )

The decrease in admitted assets and liabilities is primarily attributable to increased reinsurance.

The Company's invested assets as of December 31, 2002 were mainly comprised of bonds (86.0%), cash and short-term investments (5.5%), and policy loans (5.2%).

The majority (94.3%) of the Company's bond portfolio, as of December 31, 2002, 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 Company's filed annual statements:

	<u>2000</u>	<u>2001</u>	<u>2002</u>
Industrial life	\$ <u>(425,244)</u>	\$ <u>805,562</u>	\$ <u>355,950</u>
Ordinary:			
Life insurance	\$ (926,887)	\$(1,052,636)	\$(1,243,099)
Individual annuities	585,567	(213,179)	1,777,701
Supplementary contracts	<u>158,536</u>	<u>194,738</u>	<u>170,350</u>
Total ordinary	\$ <u>(182,784)</u>	\$ <u>(1,071,077)</u>	\$ <u>704,952</u>
Credit life	\$ <u>(10,603)</u>	\$ <u>0</u>	\$ <u>12,577</u>
Group:			
Life	\$(1,034,885)	\$ (189,614)	\$ (150,802)
Annuities	<u>(12,780)</u>	<u>216,572</u>	<u>311,922</u>
Total group	\$ <u>(1,047,665)</u>	\$ <u>26,958</u>	\$ <u>161,120</u>
Accident and health:			
Group	\$ (246,213)	\$ (289,133)	\$ (137,244)
Credit	41	0	0
Other	<u>(255,380)</u>	<u>(84,062)</u>	<u>22,657</u>
Total accident and health	\$ <u>(501,552)</u>	\$ <u>(373,195)</u>	\$ <u>(114,587)</u>
Total	\$ <u>(2,167,848)</u>	\$ <u>(611,752)</u>	\$ <u>1,120,012</u>

The loss in the industrial line of business in 2000 is attributable to an increase in expenses relating to the review of possible race-based underwriting in that line of business.

The increasing losses on the ordinary life insurance line of business are directly related to initial start-up and marketing expenses associated with the Company's new final expense business. In addition, the Company experienced continued and increased losses as compared to prior years on its monthly debit ordinary product line due to a combination of an increase in claims and a larger allocation of expenses to this secondary line of business. The Company's current marketing plan includes the discontinuation of monthly debit ordinary business and an emphasis on the sale of the Company's final expense business.

In the late 1990's and through 2001, the Company continued to emphasize and build its annuity block of business. Between 1999 and 2001, the earnings on the individual annuity line of business were impacted by lower annuity spreads and higher acquisition costs incurred from an increase in production. To mitigate the impact on earnings, the Company entered into a coinsurance agreement during 1999 reinsuring 49% of certain annuities that was increased retroactively to 90% in 2000. Cessions under the coinsurance agreement were discontinued effective March 1, 2002. In 2002, because of the decreasing interest rate environment and the Company's relatively high minimum guaranteed interest rate on its annuity products, the Company drastically reduced new Single Premium Deferred Annuity production by de-emphasizing its annuity product portfolio. Consequently, the amount of expenses allocated to this line of business in 2002 was also decreased to reflect the reduction in time and expense associated with marketing/acquisition costs.

In 2000, group pre-need life claims experience was higher than expected. In addition, the Company incurred some extraordinary expenses related to amounts owed to the Internal Revenue Service and to the New Jersey Insurance Department in connection with certain group life pre-need business.

The group annuity line has shown marked improvement since 1999 which is directly attributable to the commission and expense allowances received under a 100% coinsurance treaty with an unaffiliated insurer.

The Company's accident and health business is a closed block and is in run off.

Section 91.4(a) of Department Regulation No. 33 states, in part:

“ . . . (2) Each life insurer shall maintain records with sufficient detail to show fully:

(i) the system actually used for allocation of income and expenses;  
(ii) the actual bases of allocation;  
(iii) the actual monetary distribution of the respective items of income, salaries, wages, expenses, and taxes to . . .

(c) annual statement lines of business,

(d) companies, and

(e) a recapitulation and reconciliation of items . . . (c) and (d) with the insurer's books of account and annual statement.

(3) Such records shall be classified and indexed in such form as to permit ready identification between the item allocated and the basis upon which it was

allocated, and shall be maintained in such a manner as to be readily accessible for examination . . . ”

In 2002, the Company implemented a new method for allocating expenses between lines of business. The documentation provided to support the Company’s new method of allocating expenses to annual statement lines of business does not clearly demonstrate or show fully the actual basis of allocation for each type of expense.

The Company violated Section 91.4(a)(2) of Department Regulation No. 33 by failing to maintain records with sufficient detail to show fully: (i) the system actually used for allocation of income and expenses; (ii) the actual bases of allocation; and (iii) the actual monetary distribution of the respective items of income and salaries to annual statement lines of business and companies.

## 5. FINANCIAL STATEMENTS

The following statements show the assets, liabilities and surplus and other funds as of December 31, 2002, as contained in the Company's 2002 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 Company's financial condition as presented in its financial statements contained in the December 31, 2002 filed annual statement.

### A. ASSETS, LIABILITIES, SURPLUS AND OTHER FUNDS AS OF DECEMBER 31, 2002

#### Admitted Assets

Bonds	\$339,643,825
Stocks:	
Preferred stocks	3,030,000
Common stocks	8,927,751
Mortgage loans	
First liens	4,468
Real estate	
Investment real estate	331,897
Policy loans	20,399,672
Cash and short term investments	21,815,517
Other invested assets	597,323
Collateral loans	10,071
Reinsurance ceded:	
Amounts recoverable from reinsurers	177,356
Commissions and expense allowances due	60
Other amounts receivable under reinsurance contracts	1,780,383
Electronic data processing equipment and software	215,335
Federal and foreign income tax recoverable and interest thereon	1,174,681
Life insurance premiums and annuity considerations	
deferred and uncollected on in force business	3,124,889
Accident and health premiums due and unpaid	2,529
Investment income due and accrued	11,772,974
Receivable from parent, subsidiaries and affiliates	416,320
Reserve adjustments due reinsurers	<u>(472,739)</u>
 Total admitted assets	 <u>\$412,952,312</u>

Liabilities, Surplus and Other Funds

Aggregate reserve for life policies and contracts	\$362,071,653
Aggregate reserve for accident and health policies	667,423
Liability for deposit-type contracts	17,090,589
Policy and contract claims:	
Life	2,299,416
Accident and health	79,750
Policyholders' dividends and coupons due and unpaid	11,161
Provision for policyholders' dividends and coupons payable in following calendar year - estimated amounts:	
Dividends apportioned for payment	500,142
Premiums and annuity considerations for life and accident and health policies and contracts received in advance	82,750
Policy and contract liabilities:	
Other amounts payable on reinsurance ceded	10,663
Interest maintenance reserve	656,356
Commissions to agents due or accrued	41,051
General expenses due or accrued	1,080,881
Taxes, licenses and fees due or accrued	220,776
Unearned investment income	45,239
Amounts withheld or retained by company as agent or trustee	28,318
Amounts held for agents' account	35,427
Remittances and items not allocated	816,982
Miscellaneous liabilities:	
Asset valuation reserve	611,110
Reinsurance in unauthorized companies	30,790
Drafts outstanding	1,504,906
Deferred compensation fund	1,901,604
Accrued interest on policy funds and other liabilities	85,936
Severance and other contingent liabilities	<u>1,823,991</u>
 Total liabilities	 <u>\$391,696,914</u>
Surplus notes	\$ 5,000,000
Unassigned funds (surplus)	<u>16,255,398</u>
 Total surplus and other funds	 <u>\$ 21,255,398</u>
 Total liabilities, surplus and other funds	 <u>\$412,952,312</u>

B. CONDENSED SUMMARY OF OPERATIONS

	<u>2000</u>	<u>2001</u>	<u>2002</u>
Premiums and considerations	\$ 34,171,646	\$ 24,686,976	\$ 31,219,163
Investment income	30,537,214	27,388,561	24,609,499
Commissions and reserve adjustments on reinsurance ceded	5,405,801	2,943,148	1,685,312
Miscellaneous income	<u>1,170,778</u>	<u>479,014</u>	<u>129,700</u>
Total income	<u>\$ 71,285,439</u>	<u>\$ 55,497,699</u>	<u>\$ 57,643,674</u>
Benefit payments	\$ 58,212,043	\$ 44,897,091	\$ 47,070,405
Increase in reserves	(34,841,377)	(15,739,664)	(10,011,595)
Commissions	7,827,473	5,673,820	5,039,041
General expenses and taxes	18,918,164	15,002,827	12,726,388
Increase in loading on deferred and uncollected premium	49,588	(415,175)	164,092
Miscellaneous deductions	<u>22,001,287</u>	<u>5,409,531</u>	<u>1,407,961</u>
Total deductions	<u>\$ 72,167,178</u>	<u>\$ 54,828,430</u>	<u>\$ 56,396,292</u>
Net gain (loss)	\$ (881,739)	\$ 669,269	\$ 1,247,382
Dividends	1,620,650	1,504,201	542,057
Federal and foreign income taxes incurred	<u>(334,541)</u>	<u>(223,181)</u>	<u>(414,688)</u>
Net gain (loss) from operations before net realized capital gains	\$ (2,167,848)	\$ (611,751)	\$ 1,120,013
Net realized capital gains (losses)	<u>(227,800)</u>	<u>(3,301,329)</u>	<u>(2,802,532)</u>
Net income	<u>\$ (2,395,648)</u>	<u>\$ (3,913,080)</u>	<u>\$ (1,682,519)</u>

C. SURPLUS ACCOUNT

	<u>2000</u>	<u>2001</u>	<u>2002</u>
Surplus, December 31, prior year	\$ <u>25,459,239</u>	\$ <u>23,022,454</u>	\$ <u>24,490,764</u>
Net income	\$ (2,395,648)	\$ (3,913,080)	\$ (1,682,519)
Change in net unrealized capital gains (losses)	(302,411)	395,175	(2,663,860)
Change in net deferred income	0	0	(3,680)
Change in non-admitted assets and related items	336,495	(302,279)	(659,372)
Change in liability for reinsurance in unauthorized companies	(39,322)	(261,325)	278,493
Change in reserve valuation basis	(196,670)	(146,216)	0
Change in asset valuation reserve	138,234	1,749,909	1,130,827
Change in surplus notes	0	5,000,000	0
Cumulative effect of changes in accounting principles	0	(683,423)	1,064,051
Surplus adjustments:			
Change in surplus as a result of reinsurance	22,537	(370,451)	(641,871)
Minimum pension liability	<u>0</u>	<u>0</u>	<u>(57,435)</u>
Net change in capital and surplus	\$ <u>(2,436,785)</u>	\$ <u>1,468,310</u>	\$ <u>(3,235,366)</u>
Capital and surplus, December 31, current year	\$ <u>23,022,454</u>	\$ <u>24,490,764</u>	\$ <u>21,255,398</u>

## 6. SUBSIDIARY REPORTING

The Company failed to report the value of three of its subsidiaries to the Securities Valuation Office as called for in the Purposes and Procedures Manual of the NAIC Securities Valuation Office in a timely manner. The subsidiaries and their values in the filed annual statement are: Unity Financial Group, LLC with a value of \$1,858,601; Millennium Agency, Inc. with a value of \$382,667; and Univest Clinton, Inc. with a value of \$3,508,127.

The examiner recommends that the Company report the value of all of its subsidiaries to the Securities Valuation Office as called for in the Purposes and Procedures Manual of the NAIC Securities Valuation Office in a timely manner. This is a repeat recommendation. (See item 9C of this report)

## 7. 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 a sample of new underwriting files, both issued and declined, and the applicable policy forms.

Based upon the sample reviewed, 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.

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

### D. Privacy and Safeguarding

The examiner reviewed various elements of the Company's privacy and safeguarding activities affecting customers and consumers to determine compliance with applicable statutes and regulations, the operating rules of the Company, and internal control standards deemed adequate by the Department. The review included an evaluation of: the Company's documented privacy and safeguarding policies and procedures (including information previously submitted to the Department); internal, external and compliance audit workpapers;

and management and internal control reports. The examination included a review of the following:

- privacy notices;
- opt out and opt in notices, if applicable;
- disclosure of non-public personal information (financial and health);
- re-disclosure and re-use of non-public personal information (financial and health) received and disclosed; and
- the written information security program for the protection of customer information.

The examiner also conducted limited tests and other procedures, as deemed appropriate, in the review of privacy and safeguarding activities.

Section 420.5(a)(1) of Department Regulation No. 169 states:

“General rule. A licensee shall provide a clear and conspicuous notice to customers that accurately reflects its privacy policies and practices not less than annually during the continuation of the customer relationship. Annually means at least once in any period of 12 consecutive months during which that relationship exists. A licensee may define the 12-consecutive-month period, but the licensee must apply it to the customer on a consistent basis.”

The Company implemented various methods of sending annual privacy notices through existing mailings (e.g., premium billing notices, annual dividend statements) to its policyholders to avoid incurring costs associated with a separate mailing. During the development of the privacy policies and procedures, the Company failed to take into account certain categories of policyholders that do not receive mailings from the Company on an annual basis. The Company identified approximately 14,000 policyholders that did not receive a privacy notice during 2002.

The Company violated Section 420.5(a)(1) of Department Regulation No. 169 by failing to provide privacy notices to a number of customers at least once in any period of 12 consecutive months since July 1, 2001.

Section 421.2 of Department Regulation No. 173 states:

“Each licensee shall implement a comprehensive written information security program that includes administrative, technical and physical safeguards for the protection of customer information. The administrative, technical, and physical safeguards included in the information security program shall be appropriate to the size and complexity of the licensee and the nature and scope of its activities.”

Section 421.3 of Department Regulation No. 173 states:

“A licensee’s information security program shall be designed to:

- (a) Ensure the security and confidentiality of customer information;
- (b) Protect against any anticipated threats or hazards to the security or integrity of such information; and
- (c) Protect against unauthorized access to or use of such information that could result in substantial harm or inconvenience to any customer.”

Section 421.6 of Department Regulation No. 173 states, in part:

“The licensee: (a) Designs its information security program to control the identified risks, commensurate with the sensitivity of the information as well as the complexity and scope of the licensee's activities; (b) Trains staff, as appropriate, to implement the licensee's information security program . . . ”

In response to the examination privacy questionnaire, the Company stated that it does not have a formal training program to train its employees and sales force to protect the security and confidentiality of customer nonpublic information obtained during the processing and servicing of a policy.

The Company violated Section 421.2 and Section 421.3 of Department Regulation No. 173 by not developing a formal training program to adequately train its employees and sales force to protect and safeguard its customers’ nonpublic financial and personal information against unauthorized uses.

## 8. PROCESS FOR MONITORING AND DETERMINING IMPAIRED SECURITIES

A review of the Company's process for monitoring and determining impaired securities revealed the following:

1. The Company did not have formal written procedures related to the monitoring and determination of impaired assets prior to the Department's request for such procedures during the examination planning process;
2. The Company's monitoring process, prior to year-end 2002, consisted primarily of monitoring the credit or default risk (credit watch list) of the Company's holdings, and did not consider the accounting treatment of assets that had suffered an other than temporary loss. In addition, the Company was unable to provide documentation to support the monitoring process described above;
3. After year-end 2002, the Company developed written guidelines and procedures for determining whether declines in the fair values of individual securities are other than temporary, described below:
  - Assets with a market value of less than 80% of the original cost will be evaluated to determine if it is impaired;
  - Assets will be reviewed on a quarterly basis;
  - The Chief Investment Officer will prepare a report that will be presented to the Company's Investment Review Committee ("IRC");
  - The IRC will make a final determination as to whether or not an asset should be written down; and
  - The Company's Chief Financial Officer will be responsible for determining how the write down should be reflected (accounted for) with respect to financial statement reporting;
4. No minutes are maintained for the weekly IRC meetings;
5. The Company was unable to provide documentation regarding whether or not the IRC either accepted or rejected the Chief Investment Officer's recommendations with respect to impaired asset determinations; and
6. No formal documented process was in place during the examination period.

In general, declines in the value of investments in marketable securities caused by general market conditions or by specific information pertaining to an industry or an individual company require further investigation by senior management. Senior management should consider all available evidence to evaluate the realizable value of the investment, including other than temporary declines resulting in a write down of a security. In addition, it is the responsibility of senior management to establish written guidelines and procedures for evaluating and determining whether an impairment exists. Such written guidelines should ensure that all available evidence concerning declines in market values below cost are identified, evaluated, and documented in a disciplined manner.

The examiner recommends that the Company maintain minutes for its IRC meetings that clearly document the final decision of the Committee regarding whether or not an other than temporary write down of an impaired asset is required and the evidentiary material used as a basis for that decision.

## 9. AGENT COMPENSATION

Section 4228(e)(10)(A) of the New York Insurance Law states, in part:

“ . . . if a general agent performs services for a company other than those related to the sale or servicing of a policy or contract, or the recruiting, training or supervision of agents, the company may compensate the broker or agent for the performance of such services. . . . ”

Section 4228(f)(1) of the New York Insurance Law, states in part:

“Filing requirements for agent and broker compensation plans are as follows:  
(B) Filings are required on or before the effective date of any changes to compensation arrangements . . . A company may implement such compensation arrangements immediately upon filing same. If the superintendent notifies the company within ninety days of the receipt of the filing, that in his opinion the compensation arrangement described in such filing is not permitted under the law, and if the company within sixty days of the superintendent’s notice, is not able to satisfy the superintendent’s concern, with or without modifying the plan, the superintendent may order the company to cease using the plan. The company may request a formal hearing, but the plan that is the subject of the hearing may not be used unless and until permitted as a result of the hearing.”

The Company provided the examiner with a copy of a “Letter of Agreement” between the Company and John A. Tardera dated August 9, 1999. The “Letter of Agreement” describes the compensation Mr. Tardera will receive for consulting work “to assist in increasing sales of Unity products through the recruitment of independent General Agents and Agents to represent Unity.”

Section 4228(e)(10)(A) of the New York Insurance Law states that compensation paid to a general agent for the recruiting of other agents is agent compensation. In addition, because the plan of compensation is neither premium-based nor fund-based, Section 4228(f)(1)(B) of the New York Insurance Law requires that it be filed with the Department before it becomes effective.

The Company violated Section 4228(f)(1)(B) of the New York Insurance Law by failing to file the aforementioned compensation arrangement with the Department. A similar violation appeared in the prior report on examination. (See item 10I of this report)

## 10. PRIOR REPORT SUMMARY AND CONCLUSIONS

Following are the violations, recommendations and comments 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 1712 of the New York Insurance Law by providing an interest free loan to one of its subsidiaries.</p> <p>Effective March 31, 2001 (the transaction was posted December 31, 2001), the board authorized an additional capital contribution to UFG LLC in the amount of \$1,250,000 in order to forgive outstanding debt balances. However, a review of inter-company transactions and billing statements during the current examination period revealed that the Company had not received any reimbursement from its subsidiary, UFG LLC, for debt service paid on its behalf in connection with the aforementioned Chase Manhattan Bank loan during 2001 and other amounts paid to creditors. A violation of Section 1712 of the New York Insurance Law appears in this report on examination.</p>
B	<p>The Department has not certified, as to accuracy or adequacy, the Company's reserves for the year ending December 31, 1999. The Department has concerns with respect to completeness of supporting formula reserve details, and justification of certain assumptions with respect to the Company's asset adequacy analysis.</p> <p>The December 31, 1999 reserves were certified by the Department on September 19, 2001.</p>
C	<p>It is recommended that the Company report the value of all of its subsidiaries to the Securities Valuation Office as called for in the Purposes and Procedures Manual of the NAIC Securities Valuation Office.</p> <p>The Company has not reported the value of all of its subsidiaries to the Securities Valuation Office as called for in the Purposes and Procedures Manual of the NAIC Securities Valuation Office. This recommendation is repeated in this report on examination.</p>
D	<p>It is recommended that the Company exercise due care in properly completing Schedule D Part 6 of the annual statement, including the required disclosure of the intangible assets of its subsidiaries.</p> <p>A review indicated that Schedule D, Part 6 of the annual statement was properly completed for December 31, 2002.</p>

<u>Item</u>	<u>Description</u>
E	<p>The Company violated Section 51.7(b) of Department Regulation No. 60 by failing to closely monitor its agents annuity replacement business thereby preventing the orderly working of the Regulation.</p> <p>A review of annuity replacement business conducted during the examination period did not reveal any similar instances of circumvention of the requirements of Department Regulation No. 60. In addition, the Company implemented additional control procedures in order to identify and prevent future occurrences after the last report on examination was filed.</p>
F	<p>The Company violated Section 51.6(b)(6) of Department Regulation No. 60 by failing to maintain copies of the notification of replacement to the insurer whose life insurance policy is being replaced.</p> <p>The examiner's review of replacements indicated that the Company maintains copies of the notification of replacement to the insurer whose life insurance policy is being replaced.</p>
G	<p>The Company violated Section 3207(c) of the New York Insurance Law by issuing policies to juveniles for amounts of life insurance in excess of the limits of such section. This is a repeat violation.</p> <p>The examiner's review of a sample of policies issued on the lives of juveniles indicated that the amounts issued were within the limits of Section 3207(c) of the New York Insurance Law.</p>
H	<p>The Company violated Section 2611 of the New York Insurance Law by failing to obtain signed and/or dated written consent forms prior to performing HIV related tests.</p> <p>The examiner's review of cases for which Company underwriting requirements dictate that a blood test, which includes an HIV screen, be given to the applicant did not reveal any instances where the Company failed to obtain signed and/or dated written consent forms prior to performing HIV related tests.</p>

<u>Item</u>	<u>Description</u>
I	<p>The Company violated Section 4228(f)(1)(A) of the New York Insurance Law by failing to file all agent compensation plans by February 28, 1999.</p> <p>The Company filed its existing compensation plans with the Department on October 2, 2000. The Company failed to file a new compensation arrangement with the Department.</p>
J	<p>The Company has been named as a defendant in a complaint filed by a policyholder in the U.S. District Court for the Southern District of New York alleging, among other things, that the Company sold policies which were underwritten on the basis of the race of the insured. The policyholder is seeking class action status on behalf of the affected policyholders, and the Company is currently evaluating the merits of the claim and its defenses. The claim seeks unspecified damages.</p> <p>The Company has settled this complaint.</p>

## 11. 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 Company violated Section 1712 of the New York Insurance Law by providing an interest free loan to its subsidiary in the amount of \$175,000.	8
B	The Company violated Section 2108(a)(3) of the New York Insurance Law by contracting with a third party, who is not a licensed adjuster, to provide claims adjudication services with regard to accident and health policies.	12
C	The Company violated Section 91.4(a)(2) of Department Regulation No. 33 by failing to maintain records with sufficient detail to show fully: (i) the system actually used for allocation of income and expenses; (ii) the actual bases of allocation; and (iii) the actual monetary distribution of the respective items of income and salaries to lines of business and companies.	15 – 16
D	The examiner recommends that the Company report the value of all of its subsidiaries to the Securities Valuation Office as called for in the Purposes and Procedures Manual of the NAIC Securities Valuation Office in a timely manner.	21
E	The Company violated Section 420.5(a)(1) of Department Regulation No. 169 by failing to provide privacy notices to a number of customers at least once in any period of 12 consecutive months since July 1, 2001.	23
F	The Company violated Section 421.2 and Section 421.3 of Department Regulation No. 173 by not developing a formal training program to adequately train its employees and sales force to protect and safeguard its customers' nonpublic financial and personal information against unauthorized uses.	24
G	The examiner recommends that the Company maintain minutes for its IRC meetings that clearly document the final decision of the Committee regarding whether or not an other than temporary write down of an impaired security is required and the evidentiary material used as a basis for that decision.	25 – 26

<u>Item</u>	<u>Description</u>	<u>Page No(s).</u>
H	The Company violated Section 4228(f)(1)(B) of the New York Insurance Law by failing to file an agent compensation arrangement with the Department.	27

Respectfully submitted,

\_\_\_\_\_  
/s/  
Eden M. Sunderman  
Associate Insurance Examiner

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

Eden M. Sunderman, being duly sworn, deposes and says that the foregoing report, subscribed by her, is true to the best of her knowledge and belief.

\_\_\_\_\_  
/s/  
Eden M. Sunderman

Subscribed and sworn to before me  
this \_\_\_\_\_ day of \_\_\_\_\_

**APPOINTMENT NO. 22000**

**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:*

**EDEN SUNDERMAN**

*as a proper person to examine into the affairs of the*

**UNITY MUTUAL 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 21<sup>st</sup> day of January, 2003*



**GREGORY V. SERIO**  
*Superintendent of Insurance*

*[Handwritten Signature]*  
*Superintendent*