NEW YORK STATE DEPARTMENT OF FINANCIAL SERVICES

REPORT ON EXAMINATION

OF THE

BAPTIST LIFE ASSOCIATION

CONDITION: DECEMBER 31, 2012

DATE OF REPORT: FEBRUARY 28, 2014

<u>NEW YORK STATE DEPARTMENT OF FINANCIAL SERVICES</u>

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<u>AS OF</u>

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<u>EXAMINER</u>:	<u>STANLEY CHAN</u>

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NEW YORK STATE
DEPARTMENT *of*
FINANCIAL SERVICES

Andrew M. Cuomo
Governor

Benjamin M. Lawsky
Superintendent

April 9, 2014

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

Sir:

In accordance with instructions contained in Appointment No. 30968, dated September 3, 2013 and annexed hereto, an examination has been made into the condition and affairs of Baptist Life Association, hereinafter referred to as "the Association," at its home office located at 8555 Main Street, Buffalo, New York, 14221.

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 violation and comments contained in this report are summarized below.

- The Association has voluntarily stopped the sale of its annuity and single premium universal life products. These actions were implemented as of September 1, 2010. Subsequently, in June 2012, the Association informed the Department that it has suspended sales of all insurance and annuity products and that the only certificates being issued, are those required to meet the obligations of certificates already in force, such as term conversion and guaranteed insurability rider options. The Association indicated that it will consult with the Department before re-establishing sales activities. (See item 4B of this Report)
- The Association violated Section 1302(b) of the New York Insurance Law by including a doubtful receivable in the amount of $157,030 as an admitted asset. The examiner recommends that the Association write-off the entire receivable due from its affiliate KQF and refrain from accruing receivables from any affiliate when the affiliate cannot generate income to cover its expenses. (See Section 6B of this Report)
- The Department conducted a review of reserves as of December 31, 2012. During this reserve review, the Department found that greater conservatism is needed in the assumptions and methodology used for asset adequacy analysis. The greater conservatism is needed to be consistent with the Department's industry guidance relating to Regulation No. 126. In light of these ongoing adequacy concerns, certificates of reserve valuation for December 31, 2012 and prior years will continue to be held in abeyance until the Department is able to find sufficient conservatism has been incorporated into asset adequacy analysis. The Department will continue to monitor the Association’s reserves and work with the Association to help ensure that its reserves will be sufficient to meet anticipated policyholder obligations and related expenses. A similar comment appeared in the prior report on examination. (See Section 6F of this Report)

2. SCOPE OF EXAMINATION

The examination of the Association was a full scope examination as defined in the *NAIC Financial Condition Examiners Handbook, 2013 Edition* (the "Handbook"). The examination covers the three-year period from January 1, 2010 through December 31, 2012. The examination was conducted observing the guidelines and procedures in the Handbook and, where deemed appropriate by the examiner, transactions occurring subsequent to December 31, 2012 but prior to the date of this report (i.e., the completion date of the examination) were also reviewed.

In the course of the examination, a review was also made of the manner in which the Association conducts its business and fulfills its contractual obligations to policyholders and claimants. The results of this review are contained in item 7 of this report.

The examination was conducted on a risk focused basis in accordance with the provisions of the Handbook published by the National Association of Insurance Commissioners ("NAIC"). The Handbook guidance provides for the establishment of an examination plan based on the examiner's assessment of risk in the insurer's operations and utilizing that evaluation in formulating the nature and extent of the examination. The examiner planned and performed the examination to evaluate the current financial condition as well as identify prospective risks that may threaten the future solvency of the insurer. The examiner identified key processes, assessed the risks within those processes and evaluated the internal control systems and procedures used to mitigate those risks. The examination also included assessing the principles used and significant estimates made by management, evaluating the overall financial statement presentation, and determining management's compliance with New York statutes and Department guidelines, Statutory Accounting Principles as adopted by the Department, and annual statement instructions.

Information about the Association's organizational structure, business approach and control environment were utilized to develop the examination approach. The Association's risks and management activities were evaluated incorporating the NAIC's nine branded risk categories. These categories are as follows:

- Pricing/Underwriting
- Reserving
- Operational
- Strategic
- Credit
- Market

- Liquidity
- Legal
- Reputational

The Association was audited annually, for the years 2010 through 2012, by the accounting firm of Amato, Fox and Association, PC. The Association received an unqualified opinion in all years under examination. Certain audit workpapers of the accounting firm were reviewed and relied upon in conjunction with this examination.

The examiner reviewed the corrective actions taken by the Association with respect to the violation, recommendation and comments contained in the prior report on examination. The results of the examiner's review are contained in item 8 of this report.

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

3. DESCRIPTION OF ASSOCIATION

A. History

The Association was incorporated under the laws of New York on June 21, 1899, under the name Mutual Benefit Association of the German Baptists of North America. The Association received its final certificate of authority to transact business as a fraternal benefit association on August 22, 1899. The name was changed to German Baptist Life Association in 1911, and to its present name, Baptist Life Association in 1934.

B. Subsidiaries

The Association formed a wholly-owned subsidiary on January 4, 2008, Kingdom Quest Financial, Inc. ("KQF"), a life insurance agency licensed by the state of New York. The Association owns 100% of the common stock, a total of 200 shares.

C. Service Agreements

The Association did not have any service agreements with affiliates.

D. Management

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

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

On August 15, 2008 the Association amended Article IV, Section 1 of its by-laws reducing the number of directors from 12 to at least nine.

As of December 31, 2009, the board of directors consisted of nine members. Meetings of the board are held at least twice a year.

The nine board members and their principal business affiliation, as of December 31, 2012, were as follows:

Name and Residence	Principal Business Affiliation	Year First Elected
Kelly J. Bullis* Carson City, NV	Owner Bullis and Co. CPAs LLC	2012
Deborah R Hart* Oakland, FL	Vice President Investor Relations The Timothy Plan	2008
John D. Hunter* East Amherst, NY	Six Sigma Financial Champion Praxair, Inc	2004
Jesse J. Jerge* Tonawanda, NY	Loan Operations Manager Alden State Bank	2012
Nurline A. Lawrence* Williamsville, NY	Head of School Christian Central Academy	2012
R. Gordon Mooney* New Castle, PA	Management Consultant Mooney, Ayres & Associates	1992
Richard H. Murphy* East Amherst, NY	Attorney Sheffer, Murphy and White	1984
Donald D. Troyer* Williamsville, NY	Owner Print King	2012
Steven J. Woodard* Lancaster, NY	Vice President and Chief Executive Officer Alden State Bank	1998

* Not affiliated with the Association.

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

The following is a listing of the principal officers of the Association as of December 31, 2012:

Name	Title
Jeffery A. Armstrong	President
John Q. Curtin, Jr.*	Secretary and Treasurer

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

4. TERRITORY AND PLAN OF OPERATIONS

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

The Association is licensed to transact business in 25 states. In 2012, life premiums were received from New York (27.1%), Texas (13.6%), and North Carolina (11.4%) and annuity considerations were received from Pennsylvania (29%) and New York (24.9). Policies are written on a participating basis.

A. Statutory and Special Deposits

As of December 31, 2012, the Association had no deposits with the State of New York. Deposits, which were reported in Schedule E of the 2012 filed annual statement, were held by the States of North Carolina and South Carolina in the amounts of $42,885 and $14,338, respectively.

B. Direct Operations

The Association's insurance products include; whole life, single premium whole life, interest sensitive single premium universal life, term life, term for children and flexible premium fixed annuities. However, the Association advised the Department that it has voluntarily stopped the sale of its annuity and single premium universal life products. These actions were implemented as of September 1, 2010.

Subsequently, in June 2012, the Association informed the Department that it has suspended sales of all insurance and annuity products and that the only certificates being issued, are those required to meet the obligations of certificates already in force, such as term conversion and guaranteed insurability rider options. The Association indicated that it will consult with the Department before re-establishing sales activities.

The Association had minimal life insurance sales during the examination period as it issued 129, 83 and 25 life policies in 2010, 2011 and 2012, respectively.

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

C. Reinsurance

As of December 31, 2012, the Association had reinsurance treaties in effect with three companies, of which two were authorized. The Association's life and accident and health policies are reinsured on a coinsurance and yearly renewable term basis. Reinsurance is provided on an automatic and facultative basis.

The maximum retention limit for individual life contracts is $50,000. The total face amount of life insurance ceded as of December 31, 2012 was $78,233,308, which represents 43.8% of the total face amount of life insurance in force.

The Association ceded premiums for its accident and health insurance business to one authorized reinsurer. As of December 31, 2012, the Association ceded $2,216 of premiums under this reinsurance contract, representing 100% of the Association's accident and health insurance premiums.

Reserve credit taken for reinsurance ceded to unauthorized companies totaling $137,225, was supported by letters of credit.

5. SIGNIFICANT OPERATING RESULTS

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

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

	December 31, 2009	December 31, 2012	Increase (Decrease)
Admitted assets	$26,393,173	$31,324,780	$4,931,607
Liabilities	$25,611,887	$30,528,440	$4,916,553
Contingent reserve for orphan Benefits	20,000	20,000	0
Unassigned funds (surplus)	761,286	776,340	15,054
Total capital and surplus	$ 781,286	$ 796,340	$ 15,054
Total liabilities, capital and surplus	$26,393,173	$31,324,780	$4,931,607

The Association's invested assets as of December 31, 2012, were mainly comprised of bonds (95.8%).

The majority (99.1%) of the Association's bond portfolio, as of December 31, 2012, was comprised of investment grade obligations.

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

	2010	2011	2012
Ordinary:			
Life insurance	$(108,654)	$ 94,250	$ 153,398
Individual annuities	131,149	154,436	265,029
Supplementary contracts	(44,086)	(48,959)	806
Total ordinary	$ (21,591)	$ 199,727	$ 419,233
Accident and health:			
Other	$ (61)	$ (126)	$ (213)
Total accident and health	$ (61)	$ (126)	$ (213)
Fraternal	$(137,827)	$(126,031)	$(138,525)
Total	$(159,479)	$ 73,570	$ 280,495

The net loss in ordinary life insurance in 2010 was mainly due to higher than normal net death benefits paid, as well as the change in accounting treatment of "deferred and uncollected premiums" to meet Department requirements regarding reinsurance credits.

The increases in net gain for both ordinary life insurance and ordinary individual annuities in 2012 was a direct result of an increase in investment income from the previous year coupled with lower operating expenses.

6. FINANCIAL STATEMENTS

The following statements show the assets, liabilities, capital and surplus as of December 31, 2012, as contained in the Association's 2012 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 which materially affected the Association's financial condition as presented in its financial statements contained in the December 31, 2012 filed annual statement.

A. Independent Accountants

The firm of Amato, Fox and Company, PC was retained by the Association to audit the Association's combined statutory basis statements of financial position as of December 31st of each year in the examination period, and the related statutory-basis statements of operations, capital and surplus, and cash flows for the year then ended.

Amato, Fox and Company, PC concluded that the statutory financial statements presented fairly, in all material respects, the financial position of the Association at the respective audit dates. Balances reported in these audited financial statements were reconciled to the corresponding years' annual statements with no discrepancies noted.

B. Net Admitted Assets

Bonds	$29,275,823
Stocks:	
Common stocks	63,463
Cash, cash equivalents and short term investments	452,399
Contract loans	778,354
Investment income due and accrued	453,030
Premiums and considerations:	
Deferred premiums, agents' balances and installments booked but deferred and not yet due	124,901
Reinsurance:	
Amounts recoverable from reinsurers	500
Electronic data processing equipment and software	14,280
Receivables from parent, subsidiaries and affiliates	157,030
Security deposit	5,000
Total admitted assets	$31,324,780

Section 1301(a)(13)(A) of the New York Insurance Law states, in part:

> "Electronic data processing apparatus and related equipment constituting a data processing, record keeping, or accounting system and operating system software, provided that such assets shall be deemed admitted . . . provided that electronic data processing apparatus and related equipment and operating system software shall be amortized over the lesser of its useful life or three years. Nonoperating system software shall be nonadmitted and depreciated over the lesser of its useful life or five years."

The Association reported an admitted asset in the amount of $14,280 for its electronic data processing ("EDP") equipment on its December 31, 2012 annual statement. The Association used a 10 year straight-line depreciation method to amortize their EDP equipment.

The Association violated Section 1301(a)(13)(A) of the New York Insurance Law by failing to amortize EDP equipment over the lesser of its useful life or three years.

The examiner recommends that the Association immediately write-off the amount of admitted asset for EDP equipment which is beyond the depreciation period. In the future, the Association is required to follow the depreciation methods cited in Section 1301(a)(13)(A) of the New York Insurance Law for any purchase of EDP equipment.

Section 1302(b) of the New York Insurance Law states the following:

> "All non-admitted assets and all other assets of doubtful value or character included as ledger or non-ledger assets in any statement by an insurer to the superintendent, or in any examiner's report to him, shall also be reported, to the extent of the value disallowed, as deductions from the gross assets of such insurer except where the superintendent permits a reserve to be carried among the liabilities of such insurer in lieu of any such deduction."

A review of the asset "Receivable from Subsidiary" revealed that the Association listed a receivable due from its subsidiary KQF in the amount of $157,030. The Association paid expenses that were incurred by KQF and recorded these paid expenses as a receivable from subsidiary in the years 2008 through 2012. Discussions held with the Association determined that the receivable would not be collectible.

The Association violated Section 1302(b) of the New York Insurance Law by including a doubtful receivable in the amount of $157,030 as an admitted asset.

The examiner recommends that the Association write-off the entire receivable due from its affiliate KQF and refrain from accruing receivables from any affiliate when the affiliate cannot generate income to cover its expenses.

C. Liabilities and Surplus

Aggregate reserve for life policies and contracts	$29,764,094
Liability for deposit-type contracts	306,142
Contract claims:	
Life	131,303
Premiums and annuity considerations for life and accident and health contracts received in advance	15,617
Contract liabilities not included elsewhere:	
Interest maintenance reserve	142,050
Commissions to fieldworkers due or accrued	311
General expenses due or accrued	25,868
Taxes, licenses and fees due or accrued, excluding federal income taxes	20,602
Remittances and items not allocated	5
Miscellaneous liabilities:	
Asset valuation reserve	86,017
Unclaimed benefits	31,728
Benevolent fund	4,703
Total liabilities	$30,528,440
Contingent reserve for orphan benefits	$20,000
Unassigned funds (surplus)	776,340
Total surplus and other funds	$ 796,340
Total liabilities and surplus	$31,324,780

D. Condensed Summary of Operations

	2010	2011	2012
Premiums and considerations	$7,084,992	$1,292,853	$1,164,582
Investment income	1,616,923	1,694,772	1,842,171
Commissions and reserve adjustments On reinsurance ceded	414	342	288
Miscellaneous income	836	15,881	392
Total income	$8,703,165	$3,003,848	$3,007,433
Benefit payments	$2,175,674	$2,226,002	$2,714,314
Increase in reserves	5,490,538	(118,777)	(730,183)
Commissions	361,625	36,268	19,376
General expenses and taxes	841,865	793,391	731,557
Increase in loading on deferred and uncollected premium	(7,058)	(6,606)	(8,152)
Total deductions	$8,862,644	$2,930,278	$2,726,938
Net gain (loss) from operations before net realized capital gains	$ (159,479)	$ 73,750	$ 280,495
Net realized capital gains (losses)	(10,115)	(78,752)	486
Net income	$ (169,594)	$ (5,182)	$ 280,981

E. Surplus Account

	2010	2011	2012
Surplus, December 31, prior year	$ 781,286	$507,552	$509,575
Net income	$(169,594)	$(5,182)	$280,981
Change in net unrealized capital gains (losses)	20,146	(43,551)	14,801
Change in non-admitted assets and related items	(2,210)	1,146	330
Change in asset valuation reserve	(61,139)	49,610	(9,347)
Valuation correction	(60,937)	0	0
Net change in surplus for the year	$(273,734)	$ 2,023	$286,765
Surplus, December 31, current year	$ 507,552	$509,575	$796,340

F. Reserves

The Department conducted a review of reserves as of December 31, 2012. During this reserve review, the Department found that greater conservatism is needed in the assumptions and methodology used for asset adequacy analysis. The greater conservatism is needed to be consistent with the Department's industry guidance relating to Regulation No. 126. In light of these ongoing adequacy concerns, certificates of reserve valuation for December 31, 2012 and prior years will continue to be held in abeyance until the Department is able to find sufficient conservatism has been incorporated into asset adequacy analysis. The Department will continue to monitor the Association’s reserves and work with the Association to help ensure that its reserves will be sufficient to meet anticipated policyholder obligations and related expenses. A similar comment appeared in the prior report on examination.

7. MARKET CONDUCT ACTIVITIES

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

A. Advertising and Sales Activities

The examiner reviewed a sample of the Association’s advertising files and the sales activities of the agency force including trade practices and solicitation 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.

8. PRIOR REPORT SUMMARY AND CONCLUSIONS

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

Item	Description
A	The examiner recommends that the Association maintain the minutes of the Examining Committee as stated in the Charter. The examination revealed that the Association now maintains the minutes of the Examining Committee as stated in their Charter.
B	The Association has voluntarily stopped the sale of its annuity and single premium universal life products. These actions were implemented as of September 1, 2010 and will remain in effect until further notice. The examination revealed that the Association has not issued annuity and single premium universal life products since September 1, 2010.
C	The Department conducted a review of reserves as of December 31, 2009. During the review, the Department found that greater conservatism may be needed in the assumptions and methodology used for asset adequacy analysis pursuant to Department Regulation No. 126. To ensure reserves are adequate on a current basis, the Department is conducting a further review of the asset adequacy analysis supporting December 31, 2010 reserves. This review may lead to revised assumptions and methodology. Accordingly, the certificates of reserve valuation for December 31, 2010 and prior years are being held in abeyance until the Department completes this further review and analysis and is able to determine that the necessary conservatism has been incorporated into the asset adequacy analysis. This follow-up reserve review will be completed subsequent to the examination. The examination revealed that greater conservatism continues to be needed in the assumptions and methodology used for asset adequacy analysis pursuant to Department Regulation No. 126. (See item 6F of this report)
D	The Association violated Section 86.4 of Department Regulation No. 95 by using claim forms that were not in the form and placement as required by Section 86.4 of Department Regulation No. 95 and, by not submitting the Fraud Warning Statement to the Insurance Frauds Bureau for prior approval as required. The examination revealed that the Association is using claim forms that comply with Section 86.4 of Department Regulation No. 95.

9. SUMMARY AND CONCLUSIONS

Following are the violations, recommendation and comments contained in this report:

Item	Description	Page No(s).
A	The Association has voluntarily stopped the sale of its annuity and single premium universal life products. These actions were implemented as of September 1, 2010. Subsequently, in June 2012, the Association informed the Department that it has suspended sales of all insurance and annuity products and that the only certificates being issued, are those required to meet the obligations of certificates already in force, such as term conversion and guaranteed insurability rider options. The Association indicated that it will consult with the Department before re-establishing sales activities.	7
B	The Association violated Section 1301(a)(13)(A) of the New York Insurance Law by failing to amortize EDP equipment over the lesser of its useful life or three years.	12
C	The examiner recommends that the Association immediately write-off the amount of admitted asset for EDP equipment which is beyond the lesser of its useful life or three years. In the future, the Association is required to follow the depreciation methods cited in Section 1301(a)(13)(A) of the New York Insurance Law for any purchase of EDP equipment.	12
D	The Association violated Section 1302(b) of the New York Insurance Law by including a doubtful receivable in the amount of $157,030 as an admitted asset.	12
E	The examiner recommends that the Association write-off the entire receivable due from its affiliate KQF and refrain from accruing receivables from any affiliate when the affiliate cannot generate income to cover its expenses.	13

Item	Description	Page No(s).
F	The Department conducted a review of reserves as of December 31, 2012. During this reserve review, the Department found that greater conservatism is needed in the assumptions and methodology used for asset adequacy analysis. The greater conservatism is needed to be consistent with the Department's industry guidance relating to Regulation No. 126. In light of these ongoing adequacy concerns, certificates of reserve valuation for December 31, 2012 and prior years will continue to be held in abeyance until the Department is able to find sufficient conservatism has been incorporated into asset adequacy analysis. The Department will continue to monitor the Association’s reserves and work with the Association to help ensure that its reserves will be sufficient to meet anticipated policyholder obligations and related expenses. A similar comment appeared in the prior report on examination.	15

Respectfully submitted,

_____________/s/___________
Stanley Chan
Senior Insurance Examiner

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

Stanley Chan, being duly sworn, deposes and says that the foregoing report, subscribed by him, is true to the best of him knowledge and belief.

_____________/s/___________
Stanley Chan

Subscribed and sworn to before me

this__________ day of ___________________