

STATE OF NEW YORK INSURANCE DEPARTMENT

REPORT ON EXAMINATION

OF THE

NATIONAL INCOME LIFE INSURANCE COMPANY

AS OF

DECEMBER 31, 2002

DATE OF REPORT:

VINCENT TARGIA

EXAMINER:

SEPTEMBER 19, 2003

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

September 19, 2003

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

Sir:

In accordance with instructions contained in Appointment No. 21995, dated January 21, 2003 and annexed hereto, an examination has been made into the condition and affairs of National Income Life Insurance Company, hereinafter referred to as "the Company," at its home office located at 1020 Seventh North Street, Liverpool, New York 13088.

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 1505(d)(3) of the New York Insurance Law by failing to notify the Superintendent of its intention to sublease office space from an affiliate at least 30 days prior thereto. (See item 3B of this report)

The Company violated Section 308(a) of the New York Insurance Law by failing to file a copy of its tax allocation agreement with the Department in accordance with Department Circular Letter No. 33 (1979). (See item 3B of this report)

2. SCOPE OF EXAMINATION

This examination covers the period from October 16, 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

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

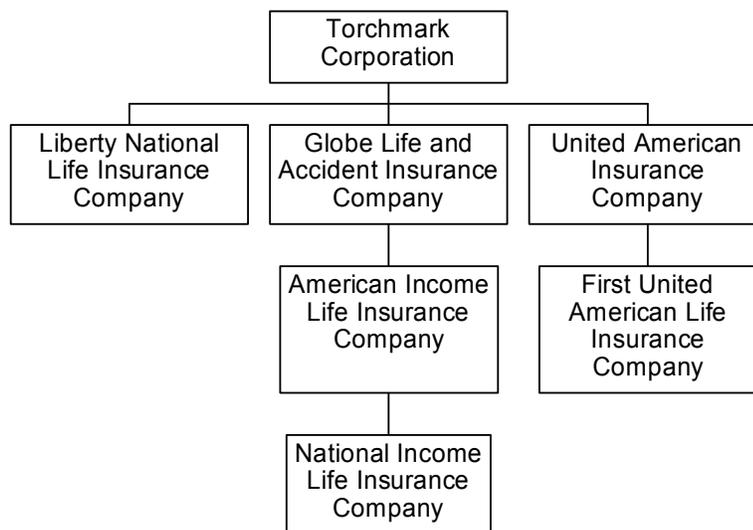
A. History

The Company was incorporated as a stock life insurance company under the laws of New York on May 14, 1996, was licensed on October 16, 2000 and commenced business on November 16, 2000. Initial resources of \$8,000,000, consisting of common capital stock of \$2,000,000 and paid in and contributed surplus of \$6,000,000, were provided through the sale of 100 shares of common stock (with a par value of \$20,000 each) for \$80,000 per share. On April 5, 2002, an additional capital contribution was made in the amount of \$5,000,000 bringing its paid in and contributed surplus to \$11,000,000 as of December 31, 2002.

B. Holding Company

The Company is a wholly owned subsidiary of American Income Life Insurance Company (“AILIC”), a Texas insurance company. AILIC is in turn a wholly owned subsidiary of Globe Life and Accident Insurance Company (“GLAIC”), a Texas insurance company. The ultimate parent of the Company is Torchmark Corporation (“TMK”) a Delaware investment advisory company.

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



The Company had the following three 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
Administrative	5/17/2000	AILIC	the Company	Distribution/producer management, marketing, reinsurance and underwriting, claims processing and payment, actuarial and financial, information technology and human resources
Administrative	5/17/2000	First United American Life Insurance Company ("FUALIC")	the Company	Administrative general support services in connection with the Company's business and operations, supervisory, oversight, support and managerial services by making a senior officer available with expertise and experience in managing the operations of a life insurance company
Investment	5/17/2000	Torchmark Corporation ("TMK")	the Company	Investment advisory services

Section 1505(d) of the New York Insurance Law states, in part:

"The following transactions between a domestic controlled insurer and any person in its holding company system may not be entered into unless the insurer has notified the superintendent in writing of its intention to enter into any such transaction at least thirty days prior thereto, or such shorter period as he may permit, and he has not disapproved it within such period . . .
 (3) rendering of services on a regular or systematic basis . . ."

A review of services provided to the Company by affiliates indicated that the Company entered into a Sublease Agreement with First United American Life Insurance Company ("FUALIC"), a New York domiciled licensed life insurer. The Sublease Agreement called for the Company to sublease approximately 140 square feet of FUALIC's home office for a term of five years commencing on May 1, 2002. The Sublease Agreement was submitted to the Department on April 24, 2003.

The Company violated Section 1505(d)(3) of the New York Insurance Law by failing to notify the Superintendent in writing of its intention to sublease office space from an affiliate at least 30 days prior thereto.

Section 308(a) of the New York Insurance Law states, in part:

“The superintendent may also address to any . . . authorized insurer or its officers any inquiry in relation to its transactions or condition or any matter connected therewith. Every corporation or person so addressed shall reply in writing to such inquiry promptly . . .”

Department Circular Letter No. 33 (1979) advises, in part:

“ . . . Any domestic insurer which currently does not participate in a consolidated tax return shall file a copy of its tax allocation agreement with this Department within 30 days of electing to do so. . . .”

The Company has a consolidated federal tax allocation agreement in effect with its ultimate parent, TMK. The Company never submitted the consolidated federal tax allocation agreement to the Department.

The Company violated Section 308(a) of the New York Insurance Law by failing to file a copy of its tax allocation agreement with the Department in accordance with Department Circular Letter No. 33 (1979).

C. Management

The Company’s by-laws provide that the board of directors shall be comprised of not less than nine and not more than 21 directors. The number of directors, however, shall be increased to not less than 13 within one year following the end of the calendar year in which the Company exceeds \$500 million in admitted assets. Directors are elected for a period of one year at the annual meeting of the shareholders held in April of each year. As of December 31, 2002, the board of directors consisted of ten members. Meetings of the board are held immediately following the annual meeting of the shareholders and at such intervals and on such dates as the board designates. All meetings of the board of directors were held by means of unanimous written consent.

The ten 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>
Tony G. Brill Plano, TX	Executive Vice President and Chief Administrative Officer Torchmark Corporation United American Insurance Company National Income Life Insurance Company	1999
Edward Cleary* Fort Myers, FL	Retired	2000
Gary L. Coleman McKinney, TX	Executive Vice President and Chief Financial Officer Torchmark Corporation United American Insurance Company National Income Life Insurance Company	1999
Terence P. Cummings* Montclair, NJ	Attorney at Law Ohrenstein & Brown, LLP	2002
Charles B. Hudson Plano, TX	Chairman of the Board and Chief Executive Officer Torchmark Corporation	1999
Larry M. Hutchison Duncanville, TX	Executive Vice President and General Counsel Torchmark Corporation American Life Insurance Company Vice President, General Counsel, and Secretary National Income Life Insurance Company	1999
Mark S. McAndrew McKinney, TX	President and Chief Executive Officer United American Insurance Company National Income Life Insurance Company	1999
Bernard Rapoport* Waco, TX	Marketing Consultant Bernard Rapoport Investments	1999
Reed Rubin* New York, NY	Officer Wachovia Securities	1999
James A. Savo Liverpool, NY	Vice President, Operations and General Manager First United American Life Insurance Company	2002

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

The following is a listing of the principal officers of the Company as of December 31, 2002:

<u>Name</u>	<u>Title</u>
Mark S. McAndrew	President and Chief Executive Officer
Danny H. Almond	Treasurer
Larry M. Hutchison	Vice President, General Counsel and Secretary
Tony G. Brill	Executive Vice President and Chief Administrative Officer
Diana Crosby*	Senior Vice President, Administration

* 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 only licensed to write business in New York. In 2002, all life premiums and accident and health premiums were received from New York. Policies are written on a non-participating basis.

During the examination period, the Company primarily sold life insurance and accident and health products. The life insurance line included ordinary and term life insurance. The accident and health line included individual and group accident policies. The Company's emphasis is on selling basic individual life coverage and fixed-benefit accident and health insurance to moderate income wage earners, through the cooperation of labor unions, credit unions, and other associations in the state of New York.

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

E. Reinsurance

As of December 31, 2002, the Company had no reinsurance treaties in effect for new business.

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>October 16,</u> <u>2000*</u>	<u>December 31,</u> <u>2002</u>	<u>Increase</u> <u>(Decrease)</u>
Admitted assets	<u>\$8,168,556</u>	<u>\$11,650,512</u>	<u>\$ 3,481,956</u>
Liabilities	<u>\$ 61,732</u>	<u>\$ 1,651,934</u>	<u>\$ 1,590,202</u>
Common capital stock	\$2,000,000	\$ 2,000,000	\$ 0
Gross paid in and contributed surplus	6,000,000	11,000,000	5,000,000
Unassigned funds (surplus)	<u>106,824</u>	<u>(3,001,422)</u>	<u>(3,108,246)</u>
Total capital and surplus	<u>\$8,106,824</u>	<u>\$ 9,998,578</u>	<u>\$ 1,891,754</u>
Total liabilities, capital and surplus	<u>\$8,168,556</u>	<u>\$11,650,512</u>	<u>\$ 3,481,956</u>

* Date the Company was licensed

The Company's invested assets as of December 31, 2002, were mainly comprised of bonds (86.1%) and cash and short-term investments (13.9%). The Company's entire bond portfolio, as of December 31, 2002, was comprised of investment grade obligations.

The large decrease in unassigned funds was primarily due to commissions advanced to agents on first year premiums. These advanced commissions are repayable from future commissions earned by the agent.

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>
Ordinary:			
Life insurance	\$109,562	\$55,013	\$ (7,843)
Supplementary contracts	<u> 0</u>	<u> 0</u>	<u> 122</u>
Total ordinary	<u>\$109,562</u>	<u>\$55,013</u>	<u>\$ (7,721)</u>
Accident and health:			
Group	\$ 0	\$10,059	\$ (429)
Other	<u> 0</u>	<u> 22,880</u>	<u> (5,154)</u>
Total accident and health	<u>\$ 0</u>	<u>\$32,939</u>	<u>\$ (5,583)</u>
Total	<u>\$109,562</u>	<u>\$87,952</u>	<u>\$(13,304)</u>

The decreases in net gain from operations for the years 2001 and 2002 were primarily a result of first year acquisition costs (i.e., commissions) as the Company began to write life insurance. In addition, a large accidental death claim in the amount of \$50,000 impacted net gain from operations for the accident & health - other line of business in 2002.

5. FINANCIAL STATEMENTS

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

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

Admitted Assets

Bonds	\$ 9,012,752
Cash and short term investments	1,452,166
Federal and foreign income tax recoverable and interest thereon	246,000
Life insurance premiums and annuity considerations deferred and uncollected on in force business	770,091
Accident and health premiums due and unpaid	28,864
Investment income due and accrued	<u>140,639</u>
 Total admitted assets	 <u>\$11,650,512</u>

Liabilities, Capital, Surplus and Other Funds

Aggregate reserve for life policies and contracts	\$ 898,851
Aggregate reserve for accident and health policies	85,734
Liability for deposit-type contracts	17,402
Policy and contract claims:	
Life	63,164
Accident and health	24,819
Premiums and annuity considerations for life and accident and health policies and contracts received in advance	1,319
Policy and contract liabilities:	
Interest maintenance reserve	27,644
Commissions to agents due or accrued	10,184
Taxes, licenses and fees due or accrued	(10,321)
Amounts withheld or retained by company as agent or trustee	9,784
Amounts held for agents' account	31,368
Remittances and items not allocated	68,652
Miscellaneous liabilities:	
Asset valuation reserve	12,470
Payable to parent, subsidiaries and affiliates	408,864
Uncashed drafts and checks pending escheatment	<u>2,000</u>
 Total liabilities	 \$ <u>1,651,934</u>
 Common capital stock	 \$ 2,000,000
Gross paid in and contributed surplus	11,000,000
Unassigned funds (surplus)	<u>(3,001,422)</u>
 Total capital, surplus and other funds	 \$ <u>9,998,578</u>
 Total liabilities, capital, surplus and other funds	 \$ <u>11,650,512</u>

B. CONDENSED SUMMARY OF OPERATIONS

	<u>2000</u>	<u>2001</u>	<u>2002</u>
Premiums and considerations	\$ 0	\$1,361,990	\$5,218,877
Investment income	168,556	489,058	437,652
Miscellaneous income	<u>0</u>	<u>318</u>	<u>531</u>
 Total income	 <u>\$168,556</u>	 <u>\$1,851,366</u>	 <u>\$5,657,060</u>
Benefit payments	\$ 0	\$ 61,944	\$ 673,069
Increase in reserves	0	170,593	813,992
Commissions	0	600,669	2,713,688
General expenses and taxes	0	319,483	1,058,503
Increase in loading on deferred and uncollected premium	0	563,253	996,520
Miscellaneous deductions	<u>0</u>	<u>0</u>	<u>5,071</u>
 Total deductions	 <u>\$ 0</u>	 <u>\$1,715,942</u>	 <u>\$6,260,843</u>
Net gain (loss)	\$168,556	\$ 135,424	\$ (603,783)
Federal and foreign income taxes incurred	<u>58,994</u>	<u>47,472</u>	<u>(590,479)</u>
Net gain (loss) from operations before net realized capital gains	\$109,562	\$ 87,952	\$ (13,304)
Net realized capital gains (losses)	<u>0</u>	<u>(2,555)</u>	<u>0</u>
 Net income	 <u>\$109,562</u>	 <u>\$ 85,397</u>	 <u>\$ (13,304)</u>

C. CAPITAL AND SURPLUS ACCOUNT

	<u>2000</u>	<u>2001</u>	<u>2002</u>
Capital and surplus, December 31, prior year	\$ <u>0</u>	\$ <u>8,106,824</u>	\$ <u>6,793,747</u>
Net income	\$ 109,562	\$ 85,397	\$ (13,304)
Change in net deferred income tax	0	102	123,481
Change in non-admitted assets and related items	0	(1,395,426)	(1,898,181)
Change in asset valuation reserve	(2,738)	(2,567)	(7,165)
Cumulative effect of changes in accounting principles	0	(583)	0
Capital changes: Paid in	2,000,000	0	5,000,000
Surplus adjustments: Paid in	<u>6,000,000</u>	<u>0</u>	<u>0</u>
Net change in capital and surplus	<u>\$8,106,824</u>	<u>\$(1,313,077)</u>	<u>\$3,204,831</u>
Capital and surplus, December 31, current year	<u>\$8,106,824</u>	<u>\$ 6,793,747</u>	<u>\$9,998,578</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.

Section 4228(e)(6) of the New York Insurance Law states, in part:

“A company, including any person, firm or corporation on its behalf or under any agreement with it, may pay or award, or permit to be paid or awarded, prizes and awards to agents or brokers pursuant to a plan of agent or broker compensation, provided that no single prize or award may exceed a value of two hundred fifty dollars, and that the total value of such prizes and awards paid or awarded to any agent or broker within a calendar year may not exceed one thousand dollars. . . .”

A review of the Company's agency operations revealed that the Company awarded a ring with an approximate cost of \$500 to five agents that qualified to attend its 2002 agent conference.

The Company violated Section 4228(e)(6) of the New York Insurance Law by awarding to five agents a ring that exceeded the \$250 limit imposed therein.

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.

7. 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 1505(d)(3) of the New York Insurance Law by failing to notify the Superintendent in writing of its intention to sublease office space from an affiliate at least 30 days prior thereto.	5
B	The Company violated Section 308(a) of the New York Insurance Law by failing to file a copy of its tax allocation agreement with the Department in accordance with Department Circular Letter No. 33 (1979).	6
C	The Company violated Section 4228(e)(6) of the New York Insurance Law by awarding to five agents a ring that exceeded the \$250 limit imposed therein.	15

APPOINTMENT NO. 21995

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

NATIONAL INCOME LIFE INSURANCE COMPANY

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

COMPANY

with such other information as he shall deem requisite.

*In Witness Whereof, I have hereunto subscribed by name
and affixed the official Seal of the Department
at the City of New York*

this 21st day of January, 2003



GREGORY V. SERIO

Superintendent of Insurance

[Handwritten Signature]
Superintendent