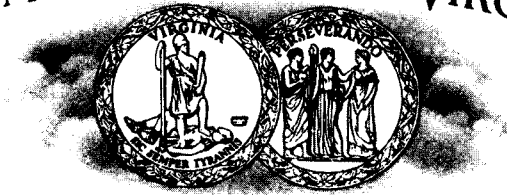


**ASSOCIATION EXAMINATION REPORT**  
**on**  
**COMMONWEALTH DEALERS LIFE INSURANCE COMPANY**  
**RICHMOND, VIRGINIA**  
**as of**  
**DECEMBER 31, 2007**

# COMMONWEALTH OF VIRGINIA

ALFRED W. GROSS  
COMMISSIONER OF INSURANCE  
STATE CORPORATION COMMISSION  
BUREAU OF INSURANCE



P.O. BOX 1157  
RICHMOND, VIRGINIA 23218  
TELEPHONE: (804) 371-9741  
TDD/VOICE: (804) 371-9206  
<http://www.scc.virginia.gov/division/boi>

I, Alfred W. Gross, Commissioner of Insurance of the Commonwealth of Virginia, do hereby certify that the annexed copy of the Examination Report of Commonwealth Dealers Life Insurance Company as of December 31, 2007, is a true copy of the original report on file with this Bureau.

**IN WITNESS WHEREOF**, I have hereunto set my hand  
and affixed to the original the seal of the Bureau at the City  
of Richmond, Virginia this 29<sup>th</sup> day of May, 2009

---

Alfred W. Gross  
Commissioner of Insurance

(SEAL)

**TABLE OF CONTENTS**

DESCRIPTION.....1

HISTORY .....2

MANAGEMENT AND CONTROL .....2

DIVIDEND PAYMENTS TO STOCKHOLDERS.....3

FIDELITY BOND AND OTHER INSURANCE .....4

OFFICERS AND EMPLOYEES BENEFIT PLANS.....4

TERRITORY AND PLAN OF OPERATION .....4

REINSURANCE.....5

GROWTH OF THE COMPANY .....7

LITIGATION AND CONTINGENT LIABILITIES .....8

SCOPE .....9

FINANCIAL STATEMENTS .....10

RECOMMENDATIONS FOR CORRECTIVE ACTION.....17

SUBSEQUENT EVENTS .....20

CONCLUSION.....22

Richmond, Virginia  
February 24, 2009

Honorable Alfred W. Gross  
Chairman of the NAIC Financial  
Condition (E) Committee  
Commissioner of Insurance  
Virginia Bureau of Insurance  
Richmond, Virginia

Honorable Scott H. Richardson  
Secretary, NAIC Southeastern Zone  
South Carolina Department of Insurance  
Columbia, South Carolina

Dear Sirs:

Pursuant to your instructions and by authority of § 38.2-1317 of the Code of Virginia, a National Association of Insurance Commissioners (NAIC) Association examination of the financial condition, records and affairs of the

**COMMONWEALTH DEALERS LIFE INSURANCE COMPANY**  
Richmond, Virginia

hereinafter referred to as the Company, has been completed. The report thereon is submitted for your consideration.

**DESCRIPTION**

The Company is a stock life insurance company and is licensed under and subject to the general insurance laws contained in Title 38.2 of the Code of Virginia. An examination was last performed as of December 31, 2004. This examination covers the period from January 1, 2005 through December 31, 2007, and was conducted by Examiners from the Virginia State Corporation Commission's (Commission) Bureau of Insurance (Bureau) who represented the NAIC's Southeastern Zone. Notice of the current examination was provided to all applicable NAIC zones.

## HISTORY

On December 16, 1987, Commonwealth Dealers Life Insurance Company, an Arizona reinsurance Company (CDLIC-A), caused Rebel Insurance Company (Rebel) to be incorporated as a Virginia corporation. CDLIC-A was issued 1,000 shares of common stock, which constituted all of the issued stock of Rebel, for \$100.00. On February 14, 1989, CDLIC-A contributed an additional \$2,500,000 in capital and surplus to Rebel.

Rebel was formed for the purpose of making formal application to the Commission for a license to write credit life insurance and credit accident and health insurance. On February 28, 1989, the Commission granted such a license to Rebel.

On March 24, 1989, the Commission approved the merger of CDLIC-A into Rebel and on April 17, 1989, the Arizona Department of Insurance approved the merger. Pursuant to the terms of the merger agreement, Rebel's name was changed to Commonwealth Dealers Life Insurance Company, a Virginia corporation. Effective January 1, 1993, North Carolina Life Insurance Company, an Arizona corporation, merged into the Company.

## MANAGEMENT AND CONTROL

The Company's bylaws provide that its business and affairs are to be vested in a board of directors of which there shall be not less than five nor more than fifteen, a majority of which shall constitute a quorum. The board of directors are elected at the annual meeting of the stockholders.

The bylaws provide that the officers of the company shall be a chairman of the board, a president, one or more vice presidents, a secretary and a treasurer, who shall be elected by the board of directors. Two or more officers may be combined in one person except for the offices of the president and secretary. At December 31, 2007, the board of directors and elected officers of the Company were as follows:

### Directors

### Principal Business Affiliation

Richard G. Barkhouser

President and Owner  
Barkhouser Motors  
Danville, Virginia

Homer E. Derrick, Jr.

President  
Derrick Enterprises  
Lexington, Virginia

|                     |   |
|---------------------|---|
| Richard D. Kern     | President and Co-owner<br>Kern Motor Company, Inc.<br>Winchester, Virginia                  |
| Donald R. Lacefield | President<br>Larry King Chevrolet, Inc.<br>Hillsborough, North Carolina                     |
| Joseph H. Nelson    | President<br>Davenport Motor Company of<br>Rocky Mount, Inc.<br>Rocky Mount, North Carolina |
| Hubert B. Parks     | President<br>Parks Chevrolet, Inc.<br>Kernersville, North Carolina                          |

**Officers****Title**

|                       |                       |
|-----------------------|-----------------------|
| Richard G. Barkhouser | Chairman of the Board |
| Mark E. Albert        | President             |
| Richard D. Kern       | Treasurer, Secretary  |

The authorized amount of capital stock of the Company as of December 31, 2007 was 23,500,000 shares and is divided into the following classes:

- 3,500,000 shares with a par value of \$2.00 per share, designated as Voting Common Stock.
- 20,000,000 shares with a par value of \$2.00 per share, designated as B Participating Common Stock (non-voting).

As of December 31, 2007, 423,009 of Voting Common Stock and 230,962 shares of the B Participating Common Stock were issued and outstanding. All of the Company's outstanding stock was held by automobile dealers and certain officers and board members of the Company.

**DIVIDEND PAYMENTS TO STOCKHOLDERS**

The Company paid dividends to stockholders totaling \$16,644 during 2007, \$3,048,423 during 2006 and \$719,569 during 2005.

### **FIDELITY BOND AND OTHER INSURANCE**

The Company maintained fidelity insurance in force at year-end in the amount of \$400,000, as well as property, business liability, workers compensation and officers and directors liability coverages.

### **OFFICERS AND EMPLOYEES BENEFIT PLANS**

The Company sponsors a defined contribution pension benefit plan (Plan) which is administered through the National Association of Automobile Dealers & Associates Retirement Trust. The Plan is available to all employees age 21 and older who have accumulated at least 1,000 hours of service during the 12-month period January through December. The Company is obligated to contribute 3% of an employee's compensation into the Plan. In addition, the Company may contribute each year a discretionary amount if authorized by the Board of Directors. The employee may elect to make pre-tax contributions subject to a maximum limit and may also make a supplemental voluntary contribution (non-tax deductible) to the Plan in an amount not to exceed the annual limit provided by IRS regulation. An employee is not 100% vested until completing 6 years of credited service.

In addition to the above, the Company offers employees life and health benefits through a group insurance contract issued by Anthem Inc. The Company is currently paying 75% of the premium associated with the cost of providing the coverage to the employees.

### **TERRITORY AND PLAN OF OPERATION**

The Company is licensed in Virginia to transact the business of life, accident and health, credit life and credit accident and health insurance. In addition, the Company is licensed in Delaware, Georgia, Indiana, Maryland, North Carolina, Ohio, Pennsylvania, South Carolina and Tennessee.

During the period under review through November 1, 2007, the Company engaged in the business of direct writing credit life and credit accident and health insurance written through various automobile dealerships, the majority of whom are stockholders of the Company. The Company also wrote credit life and accident and health insurance on American Republic certificates. Billings, collections and claims payments were processed and controlled at the home office. During a September 2007 board meeting, the board authorized and approved the proposal for the Company to cease writing insurance policies, enter into run-off and, upon completion of such run-off, dissolve and terminate the Company. Since that time, the Company has ceased all ongoing business operations and is limiting its activities to those necessary to complete the run-off process.

After the board elected to begin the run-off process, the Company engaged Life of the South to manage the run-off process with respect to the credit life and credit accident and health insurance business. As a result, in January 2008, all of the Company's files and records were moved to the Life of the South's headquarters in Jacksonville, Florida. The board has authorized the Company to sell its Richmond, Virginia corporate office.

The Company also sells third-party warranty and guaranteed auto protection products, for which it is paid a fee for each product sold. The Company is not liable for any claims from such products. For 2007, the Company reported \$300,641 in fees from the sales of these products.

### REINSURANCE

#### Assumed:

The Company had two indemnity reinsurance agreements in effect as of December 31, 2007 for assumed business. Under an agreement with American Republic Insurance Company (American Republic), the Company assumed credit life and credit accident and health (A&H) policies that were originally written by American Republic, but which were produced by automobile dealers through the marketing efforts of the Company. All of the life policies, and the A&H policies issued in the two states where the Company was not licensed, were assumed by the Company. The Company assumes 100% quota share of the mortality and morbidity risks from American Republic on an automatic basis. As of December 31, 2007, the life policies comprised 68% of the Company's total life reserves, while the A&H policies were an immaterial portion of the Company's total A&H reserves.

Similarly, under an agreement with LOTS Reassurance Company (LOTS), the Company, through a retrocession, assumed credit A&H policies that were originally written by American Republic, but produced by automobile dealers through the marketing efforts of the Company. All of the credit A&H policies that were not reinsured via the aforementioned American Republic agreement were ceded to LOTS, and then retroceded to the Company. The Company assumes 100% quota share of the risks from LOTS on an automatic basis. LOTS holds the claim reserves and pays premiums on an earned basis, while the Company pays claims as incurred and any increases to the claim reserves. Thus, no reserves are held by the Company for this reinsurance.

#### Ceded:

The Company had two indemnity reinsurance agreements in effect as of December 31, 2007 for ceded business. These two treaties were both with Rafiki Reinsurance Limited (Rafiki), an unauthorized alien reinsurer. The two treaties were both effective at



the same time, one for credit life and the other for credit A&H business. Under the agreements, the Company reinsures 100% quota share of the mortality and morbidity (on an earned premium basis) risks for a few non-stockholder dealerships on an automatic basis. Approximately 84% of the credit life reserves ceded to Rafiki was originally assumed by the Company from American Republic. Approximately 48% of the credit A&H reserves ceded to Rafiki was originally assumed by the Company from LOTS.

The total reserve credit taken by the Company at December 31, 2007 was \$601,789, or approximately 7.5% of the Company's total aggregate life and A&H reserves. However, since Rafiki is an unauthorized reinsurer, the reinsurance reserve credit was appropriately reported as an offsetting liability in the Company's 2007 Annual Statement (Line #24.2-Reinsurance in Unauthorized Companies).

Two indemnity reinsurance agreements with Munich American Reassurance Company were recaptured during 2007. Thus, Schedule S in the Company's 2007 Annual Statement appropriately shows the wind-up premiums, but no reserve credits, for the reinsurance formerly ceded to Munich American Reassurance Company.

The Examiners reviewed all reinsurance reserves ceded and assumed for accuracy and no material errors were noted during this review.

## GROWTH OF THE COMPANY

The following data, taken from copies of annual statements filed with the Commission and the financial statements contained in examination reports, reflects the growth of the Company for the ten-year period ending December 31, 2007.

| <u>Year</u> | <u>Admitted<br/>Assets</u> | <u>Liabilities</u> | <u>Common<br/>Capital<br/>Stock</u> | <u>Gross Paid-in<br/>&amp; Unassigned<br/>Funds (Surplus)</u> |
|-------------|----------------------------|--------------------|-------------------------------------|---|
| 1998        | \$30,789,919               | \$22,501,726       | \$1,249,402                         | \$7,038,791   |
| 1999        | 31,354,389                 | 21,675,430         | 1,200,982                           | 8,477,977   |
| 2000        | 31,547,919                 | 22,310,411         | 1,723,662                           | 7,513,846   |
| 2001        | 32,262,169                 | 24,698,095         | 1,635,338                           | 5,928,736   |
| 2002        | 31,945,537                 | 24,724,122         | 1,619,578                           | 5,601,837   |
| 2003        | 33,044,474                 | 23,498,917         | 1,629,578                           | 7,915,979   |
| 2004        | 29,750,755                 | 23,763,907         | 1,343,542                           | 4,643,306   |
| 2005        | 25,013,776                 | 18,297,629         | 1,321,942                           | 5,394,205   |
| 2006        | 21,140,225                 | 15,900,626         | 1,307,942                           | 3,931,657   |
| 2007        | 16,375,704                 | 10,907,127         | 1,307,942                           | 4,160,635   |

### Life Insurance in Force

| <u>Year</u> | <u>Credit Life</u> |
|-------------|--------------------|
| 1998        | \$384,394,000      |
| 1999        | 405,811,000        |
| 2000        | 416,234,000        |
| 2001        | 425,141,000        |
| 2002        | 422,701,000        |
| 2003        | 418,395,000        |
| 2004        | 398,243,000        |
| 2005        | 358,252,000        |
| 2006        | 290,250,000        |
| 2007        | 228,628,000        |

**LITIGATION AND CONTINGENT LIABILITIES**

The Company is involved in several legal suits occurring in the normal course of business. In the opinion of the Company management, the outcome of these suits is not expected to have a material adverse effect on the financial condition of the Company.

## SCOPE

This is a full scope financial condition examination initiated and conducted under the provisions of Article 4, Chapter 13 of Title 38.2 of the Code of Virginia. The examination covers the period from January 1, 2005 through December 31, 2007. Assets were verified and liabilities were established at December 31, 2007. A review of income and disbursements for the period was made to the extent deemed necessary.

The items comprising the Balance Sheet for which Specific Risk Analyses (SRA) were required had a medium or low risk assessment as determined from the NAIC *Examiners Handbook*. Analytical review procedures were applied for non-SRA items.

In addition, the following items were reviewed, several of which are discussed separately under their respective captions in this report.

History  
Management and control  
Corporate records  
Fidelity bonds and other insurance  
Pension plans  
Territory and plan of operation  
Growth of the Company  
Reinsurance  
Litigation  
Accounts and records  
Financial statements

**FINANCIAL STATEMENTS**

There follows a statement of financial condition as of December 31, 2007; a summary of operations for the year ended December 31, 2007; a reconciliation of capital and surplus for the period under review; a statement of cash flow for the year ended December 31, 2007; and a statement of Examiners' changes in capital and surplus at December 31, 2007. The financial statements are presented in accordance with Statutory Accounting Principles.

**ASSETS**

|   | <u>Assets</u>              | Nonadmitted<br><u>Assets</u> | Net Admitted<br><u>Assets</u> |
|---|----------------------------|------------------------------|-------------------------------|
| Bonds   | \$13,256,175               |                              | \$13,256,175                  |
| Stocks:   |                            |                              |                               |
| Preferred stocks  | 402,842                    |                              | 402,842                       |
| Common stocks   | 135,015                    |                              | 135,015                       |
| Properties occupied by the company                      | 365,484                    |                              | 365,484                       |
| Cash and short-term investments                         | 2,039,756                  |                              | 2,039,756                     |
| Subtotals, cash and invested assets                     | <u>\$16,199,272</u>        | <u>\$0</u>                   | <u>\$16,199,272</u>           |
| Investment income due and accrued                       | 104,201                    |                              | 104,201                       |
| Net deferred tax asset                                  | 92,029                     | 60,658                       | 31,371                        |
| Electronic data processing equipment                    | 91                         |                              | 91                            |
| Furniture and equipment                                 | 259                        | 259                          | 0                             |
| Receivables from parent, subsidiaries<br>and affiliates | 267,525                    | 267,525                      | 0                             |
| Aggregate write-ins for other than<br>invested assets   | <u>148,292</u>             | <u>107,523</u>               | <u>40,769</u>                 |
| Total assets  | <u><u>\$16,811,669</u></u> | <u><u>\$435,965</u></u>      | <u><u>\$16,375,704</u></u>    |

**LIABILITIES, SURPLUS AND OTHER FUNDS**

|   |                            |
|---|----------------------------|
| Aggregate reserve for life contracts                | \$5,279,122                |
| Aggregate reserve for accident and health contracts | 2,763,590                  |
| Contract claims:                                    |                            |
| Life  | 268,696                    |
| Accident and health                                 | 246,624                    |
| Interest maintenance reserve                        | 1,229,143                  |
| General expenses due or accrued                     | 20,038                     |
| Taxes, licenses and fees due or accrued             | 596                        |
| Current federal income taxes                        | 242,139                    |
| Remittances and items not allocated                 | 92,571                     |
| Miscellaneous liabilities:                          |                            |
| Asset valuation reserve                             | 115,941                    |
| Reinsurance in unauthorized companies               | 648,667                    |
|   | <hr/>                      |
| Total liabilities                                   | <u>\$10,907,127</u>        |
| Common capital stock                                | \$1,307,942                |
| Gross paid in and contributed surplus               | 492,599                    |
| Unassigned funds (surplus)                          | 3,668,036                  |
|   | <hr/>                      |
| Total surplus                                       | <u>\$5,468,577</u>         |
|   | <hr/>                      |
| Total liabilities, capital and surplus              | <u><u>\$16,375,704</u></u> |

**SUMMARY OF OPERATIONS**

|   |                         |
|---|-------------------------|
| Premiums and annuity considerations for life and accident<br>and health contracts         | \$2,966,026             |
| Net investment income   | 567,980                 |
| Amortization of Interest Maintenance Reserve  | 109,927                 |
| Commissions and expense allowances on reinsurance ceded                                   | (169,471)               |
| Aggregate write-ins for miscellaneous income  | 300,641                 |
| Total   | <u>\$3,775,103</u>      |
| Death benefits  | \$559,026               |
| Disability benefits and benefits under accident and<br>health contracts                   | 1,163,828               |
| Increase in aggregate reserves for life and accident<br>and health contracts              | <u>(2,283,561)</u>      |
| Total   | (\$560,707)             |
| Commissions on premiums, annuity considerations<br>and deposit-type funds                 | \$43,744                |
| Commissions and expense allowances on reinsurance assumed                                 | 1,522,803               |
| General insurance expenses  | 2,111,980               |
| Insurance taxes, licenses and fees  | 107,194                 |
| Total   | <u>\$3,225,014</u>      |
| Net gain from operations before federal income taxes                                      | \$550,089               |
| Federal and foreign income taxes incurred   | <u>135,955</u>          |
| Net gain from operations after federal income taxes and before<br>realized capital losses | \$414,134               |
| Net realized capital losses   | <u>(73,654)</u>         |
| Net income  | <u><u>\$340,480</u></u> |



**RECONCILIATION OF CAPITAL AND SURPLUS**  
**FOR PERIOD UNDER REVIEW**

|  | <u>2005</u>               | <u>2006</u>               | <u>2007</u>               |
|--|---------------------------|---------------------------|---------------------------|
| Capital and surplus, December 31,<br>prior year                  | <u>\$5,986,848</u>        | <u>\$6,716,147</u>        | <u>\$5,239,599</u>        |
| Net income   | \$2,077,142               | \$2,236,932               | \$340,480                 |
| Change in net unrealized capital gains                           | 47,200                    |                           |                           |
| Change in net deferred income tax                                | (58,701)                  | (69,887)                  | (41,638)                  |
| Change in nonadmitted assets                                     | 232,227                   | 1,851                     | (32,957)                  |
| Change in liability for reinsurance in<br>unauthorized companies | 1,557                     | 46,770                    | (63,677)                  |
| Change in asset valuation reserve                                | 49,343                    | (38,373)                  | 40,662                    |
| Capital changes:   |                           |                           |                           |
| Paid in  | (168,712)                 | (14,000)                  |                           |
| Surplus adjustments:   |                           |                           |                           |
| Paid in:   | (3,351)                   | (1,585)                   |                           |
| Dividends to stockholders  | (719,569)                 | (3,048,423)               | (16,644)                  |
| Aggregate write-ins for gains and losses<br>in surplus           | <u>(727,837)</u>          | <u>(589,833)</u>          | <u>2,752</u>              |
| Net change in capital and surplus for the year                   | <u>\$729,299</u>          | <u>(\$1,476,548)</u>      | <u>\$228,978</u>          |
| Capital and surplus, December 31,<br>current year                | <u><u>\$6,716,147</u></u> | <u><u>\$5,239,599</u></u> | <u><u>\$5,468,577</u></u> |

**CASH FLOW****Cash from Operations**

|  |                      |
|--|----------------------|
| Premiums collected net of reinsurance                                | \$3,042,118          |
| Net investment income  | 671,473              |
| Miscellaneous Income   | 131,170              |
| Total  | <u>\$3,844,761</u>   |
| Benefit and loss related payments                                    | \$1,765,644          |
| Commissions, expenses paid and aggregate write-ins<br>for deductions | 3,776,167            |
| Federal income taxes paid  | (209,899)            |
| Total  | <u>\$5,331,912</u>   |
| Net cash from operations   | <u>(\$1,487,151)</u> |

**Cash from Investments**

|  |                    |
|--|--------------------|
| Proceeds from investments sold, matured or repaid: |                    |
| Bonds  | \$7,702,764        |
| Stocks   | 584,349            |
| Net gains on cash and short-term investments       | 9,435              |
| Total investment proceeds                          | <u>\$8,296,548</u> |
| Costs of investments acquired (long-term only):    |                    |
| Bonds  | \$3,650,245        |
| Stocks   | 311,163            |
| Total investments acquired                         | <u>\$3,961,408</u> |
| Net cash from investments                          | <u>\$4,335,140</u> |

**Cash from Financing and Miscellaneous Sources**

|   |                      |
|---|----------------------|
| Cash provided (applied):                          |                      |
| Dividends to stockholders                         | (\$2,633,139)        |
| Other cash applied                                | (110,099)            |
| Net cash from financing and miscellaneous sources | <u>(\$2,743,238)</u> |

**RECONCILIATION OF CASH AND SHORT-TERM INVESTMENTS**

|   |                    |
|---|--------------------|
| Net change in cash and short-term investments | \$104,751          |
| Cash and short-term investments:              |                    |
| Beginning of the year                         | <u>1,935,005</u>   |
| End of the year                               | <u>\$2,039,756</u> |

**EXAMINERS' CHANGES IN CAPITAL AND SURPLUS**

|  | <u>Company</u> | <u>Examiners</u> | Increase<br>(Decrease) |
|--|----------------|------------------|------------------------|
| <u>Assets:</u>   |                |                  |                        |
| Aggregate write-ins for other than invested<br>assets (Due from reinsurer) | \$116,861      | \$40,769         | <u>(\$76,092)</u>      |
| Examiners' change in capital and surplus                                   |                |                  | <u>(\$76,092)</u>      |
| Capital and surplus per the Company  |                |                  | \$5,544,669            |
| Capital and surplus per the Examiners                                      |                |                  | <u>5,468,577</u>       |
| Net decrease in capital and surplus  |                |                  | <u>(\$76,092)</u>      |

## RECOMMENDATIONS FOR CORRECTIVE ACTION

### Management and Control

1. Code of Virginia (Code) § 38.2-1408 states, in part, "No domestic insurer shall make any loan, investment, or any sale or exchange of a loan or investment... unless authorized or approved. Authorization or approval shall be made by (i) its board of directors, or other governing body, or (ii) a committee authorized by the governing body or bylaws, to make investments, loans, sales or exchanges. The minutes of the committee shall be recorded, and reports of the investments, loans, sales or exchanges authorized or approved shall be submitted to the board or other governing body at its next meeting." During the review of the Company's board minutes, it was noted that the board, or a committee delegated by the board, failed to ratify all the Company's investments during the period under review. Additionally, there were a number of loans to Company employees and dealerships during the examination period that were not approved by the board. Furthermore, the Company could not provide the attachments to the 2006 and 2007 minutes to verify that detailed reports of such investments were submitted to the board.

This is the third consecutive examination report in which a recommendation regarding the board's failure to review and approve all investments, loans to dealers and loans to employees has appeared. The Examiners recommend that the Company immediately initiate those changes in procedure that are necessary to bring the Company into compliance with § 38.2-1408 of the Code.

2. The Company's bylaws require the board of directors to elect several officers, including one or more vice presidents. A review of the board minutes for the three-year period under examination indicated that an election of the vice president(s) did not occur in 2006 and 2007.

In addition, the following exceptions were noted during the review of the Company's Annual Statement jurat page for the period under examination: a) the 2006 and 2007 jurat page identified an individual as treasurer; however, a review of the board minutes indicated that another individual was actually elected to that position; b) the chairman of the board was elected as an officer of the Company for each year under examination, but he was not identified on the respective jurat page; and c) seven directors were elected by the stockholders during the May 2005 stockholders meeting, but only six were reported on the 2005 jurat page.

It is recommended that the Company correctly identify the elected officers and directors in future Annual Statement filings and comply with its bylaws regarding the

election of its officers. This is the second consecutive examination report in which a similar recommendation has appeared.

3. During a review of the Company's 2007 Supplemental Compensation Exhibit (Exhibit), the Examiners noted discrepancies in the salary and bonus amounts that were reported for the President in 2005, 2006 and 2007. The amounts reported in the Exhibit did not reconcile to the amounts reported on the President's W-2. In addition, the payroll detail which supported the President's 2007 W-2 did not reconcile to the Company's general ledger and the President's payroll file.

In addition, according to the Company's payroll detail, the President's salary increased during the August 31, 2007 to September 15, 2007 pay period. However, there was no approval or ratification of the increase by the board of directors, which is required by the Company's bylaws. Furthermore, the Company was unable to provide detailed support, as requested by the Examiners, to verify a bonus and a compensation payment to the President.

The Examiners recommend that the Company ensure compliance with the bylaws by requiring the board of directors to approve an increase in the President's salary and maintain accurate accounting records to support all salaries, bonuses and commissions.

4. Code § 38.2-1318 B states, in part, "...in conducting the examination, the examiner shall observe, to the extent practicable, those guidelines and procedures set forth in the Examiners' Handbook...". To verify the existence of securities, the Examiners' Handbook requires that the securities be (i) maintained in a manner that will allow the Examiner to perform an actual inspection or count or (ii) held pursuant to a custodial or safekeeping agreement with a bank, trust company, or securities depository. The Company had an executed custodial agreement; however, it did not contain all of the required safeguards and controls.

The Examiners recommend that the Company make the necessary changes to the existing custodial agreement to be consistent with the requirements of the Handbook or move its securities to a custodian who will comply with the NAIC guidelines.

5. When initially requested, the Company was unable to provide conflict of interest statements for any of its officers and directors for each of the years under review. Subsequently, conflict of interest statements were provided for several officers and directors. However, conflict of interest statements could not be provided for one of the officers for 2005 and 2006 and one of the directors for 2005.

In order to demonstrate compliance with §§ 38.2-210 and 38.2-211 of the Code, it is recommended that each director and officer complete conflict of interest disclosure statements on an annual basis.

6. According to § 55-210.12 of the Code, every person holding funds or property presumed abandoned shall report and remit such funds or property to the State Treasurer. Under Article 2 of Title 55, sums payable on a check or draft that have been outstanding for more than five years are presumed abandoned. During the period under examination, the Company failed to remit approximately 300 checks (totaling approximately \$36,000) that were outstanding for more than five years to the State Treasurer.

The Examiners recommend that the Company implement procedures to ensure compliance with provisions of Title 55 of the Code. This is the second consecutive examination report in which a similar recommendation has appeared.

7. During the review of dividends paid to stockholders, the Examiners noted the following errors and discrepancies:
  - a) The Company could not provide attachments to the 2006 and 2007 board minutes to document that each cash and liquidating dividend payments to stockholders was approved by the board.
  - b) On several occasions, the board approved a number of stockholders' dividend requests; however, some of these dividend requests were not paid. A review of subsequent board minutes indicated that the board did not rescind the approval of such dividends.
  - c) The Examiner's review of a Company-provided document indicated \$16,644 of cash dividends were declared and paid in 2007. However, these cash dividends were not submitted to the board or to the Commission for approval.
  - d) During the Examiner's review of dividends approved by the board during the May 2005 board meeting, it was noted that dividends of \$819,052 were approved by the board, \$896,563 was submitted and approved by the Commission and only \$719,569 was paid per the Company's general ledger and Summary of Operations.

The Examiners recommend a) the Company ensure attachments to the board's minutes are maintained and are available for review, b) the board take action to rescind any unpaid dividends made during the period under review, c) the Company submit all dividend requests to its board and to the Commission for approval and d) the Company ensure the detailed listing of dividend requests submitted to the board and to the Commission are accurate.

### Accounts and Records

8. In conjunction with the audit of the Company's statutory financial statements as of and for the year ended December 31, 2007, the Company's independent auditors identified a deficiency in internal controls that they considered to be a significant deficiency: the Company did not have sufficient controls in place (including an independent review) to ensure that all balance sheet accounts were properly reconciled prior to the filing of the Annual Statement. The independent auditors noted certain transactions that had not been properly recorded in the Company's general ledger, resulting in a required reconciliation between the audited statutory financial statements and the filed Annual Statement.

The Examiners recommend that the Company monitor and evaluate its internal control over financial reporting on a continuous basis to ensure that adequate internal controls are in place and functioning effectively. Specifically, the Examiners also recommend that the Company implement procedures to ensure that all transactions are properly included in the Company's general ledger and that all balance sheet reconciliations are performed in a timely and accurate manner. In addition, the input of such transactions and the performance of such reconciliations should be subject to an independent management review.

9. Due from Reinsurer \$40,769

The above asset is \$76,092 less than the amount reported by the Company in its 2007 Annual Statement. The decrease is a result of the Company erroneously including an amount relating to the November 2006 balance which had previously been received by the Company. It is recommended that the Company review its processing of receipts to ensure that amounts are properly applied to the respective accounts and that balances are accurately reported in future statements filed with the Bureau.

### SUBSEQUENT EVENTS

1. On August 6, 2007, the Company filed a claim with The Hartford Insurance Company (Hartford) related to an alleged theft by the secretary of the Company. The amount of the claim was approximately \$450,000 and the limit under the Company's fidelity bond policy was \$400,000. At December 31, 2007, there was not a recoverable recorded in the Company's financial statement with respect to this claim. On April 18, 2008, Hartford paid the \$400,000 claim as full and final settlement. On July 10, 2008, the Henrico County Circuit Court granted a motion for nolle prosequi, which means that the case was dismissed, but it could be reopened if new information becomes available.

2. On June 23, 2008, Mark E. Albert, President of the Company, and his brother, Thomas W. Albert, pled guilty to a tax fraud conspiracy to divert \$2.1 million of corporate income to themselves and to evade \$575,000 of their personal income taxes on the diverted income. According to the U.S. Attorney's press release, Mark Albert diverted the money from the Company to his brother's company, Next Millennium Marketing, a Texas corporation through which the income was sent offshore. The defendants used multiple steps to conceal the transactions from the IRS. According to a statement of facts presented to the U.S. District Court and signed by Mark Albert, the unreported income was used to support Mark Albert's lavish lifestyle, such as rental of expensive beach houses, beach vacations, trips to Pittsburgh Steelers football games, dining at fine restaurants and the purchase of fine wines. On November 10, 2008, Mark Albert was sentenced to 33 months in prison and was ordered to pay \$348,186 in restitution for tax deficiencies. The Company continues to investigate Mr. Albert's activities as they relate to the Company. Preliminary findings of the Company indicate that it is unlikely that any funds due with respect to its credit life or credit accident and health business were diverted. The Company is now focusing on Mr. Albert's activities with respect to fees and commissions due for third party warranty products and guaranteed auto protection (GAP) products. Final resolution of Mr. Albert's case and the impact the entire incident had on the day-to-day operations of the Company caused the issuance of this examination report to be delayed.

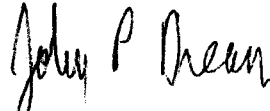


**CONCLUSION**

The courteous cooperation extended by the officers and employees of the Company during the course of the examination was sincerely appreciated.

In addition to the undersigned, Bryan Almond; John Bunce, CFE; Christopher Collins; David Fiden; William Knight, AFE; David Lin; Hai Nguyen and Michael Peterson participated in the work of the examination.

Respectfully submitted,



John P. Drear, CFE  
Senior Insurance Examiner  
Commonwealth of Virginia  
Representing the Southeastern Zone, NAIC

# **CDLIC**

**Commonwealth Dealers Life**

**Insurance Company**

226-5 Solano Road, Suite 102, Ponte Vedra, Florida 32082

May 20, 2009

David H. Smith, CFE, CPA, CPCU  
Chief Examiner  
State Corporation Commission  
Bureau of Insurance  
1300 East Main Street  
Richmond, Virginia 23219

**Re: Commonwealth Dealers Life Insurance Company  
Examination Report as of December 31, 2007**

Dear Mr. Smith:

On behalf on Commonwealth Dealers Life Insurance Company (the "Company"), I am writing this letter to respond to the Bureau's draft Examination Report of the Company as of December 31, 2007 ("2007 Exam Report").

The Company and its advisors have reviewed the 2007 Exam Report and do not take issue with any matter contained therein. As such, the Company does not wish to request a hearing before the Commission.

I have set forth below the Company's written responses to the Bureau's recommendations for corrective actions:

#### **Management and Control.**

1. Going forward the Company's Board of Directors will take such actions as are necessary to comply with Section 38.2-1408 of the Code of Virginia. In November of 2008 the Board met with Marco Bravo of AAM Investment Management. Mr. Bravo reviewed the Company's investment holdings and discussed then current market conditions. The Board did not officially ratify all of the investments in its account at that time but was well informed. At the next meeting of the Company's Board of Directors the Board will review all of the Company's investments and ratify all of such investments. Since the Company is in the run-off process the Board does not intend to permit the Company to make any further loans to dealers or employees. In any event no loans will be made by the Company without the Board's prior approval.

2. The Company will comply with its Bylaws with respect to the election of officers and directors. At the next meeting of the Board of Directors the Board will elect a new slate of officers, including a Vice President. Following such meeting the Company will correct its annual report filings with the State Corporation Commission by filing a corrected annual report. The corrected annual report will list all of the directors then in office as well as the correct officers.

3. As the Bureau is aware, the Company's President during the examination period is no longer affiliated with the Company. The Company has not paid such individual any compensation for almost two (2) years. In fact, since the Company is in the run-off process there are currently no employees. As a result the Company is not currently paying any compensation to any individual other than to Kaye Biby (the Bureau has previously seen a copy of her agreement). However before any compensation is paid to any employee or other contractor the Board will approve such arrangement in advance.

4. The Company has contacted T D Bank North and requested that its custodial agreement be revised to be consistent with the requirements set forth in the Examiners Handbook. T D Bank North has indicated that it will make the necessary revisions and is working with Kaye Biby to that end. If T D Bank North fails to make such revisions the Company will move the securities to a custodian who will comply with the NAIC guidelines.

5. The Company has circulated new conflict of interest disclosure statements to all of its officers and directors and is in the process of gathering such statements now. Once those statements are signed the Company will provide copies to the Bureau.

6. The Company is working with its administrator, Life of the South, to identify all checks that have been outstanding for more than five years and will comply with the provisions of Title 55 of the Code of Virginia with respect to any checks identified.

7. Going forward, the Company will ensure that all Board minutes incorporate all attachments and will make those minutes and attachments available for review by the Bureau. Furthermore, at the next Board Meeting the Board will rescind any unpaid dividends referenced in the 2007 Exam Report. Since the Company is in the run-off process, the Company will not declare or pay any further dividends until such time as the Board of Directors, as well as the Bureau of Insurance, approves such declaration and payment. In the future all dividend requests submitted to the Board, as well as the Bureau, will be accurate.

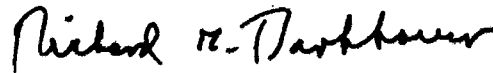
8. The Company believes that its current arrangement ensures that adequate internal controls are in place and functioning effectively. During the examination period the Company's general ledger was maintained internally. As you are aware, the Company engaged Life of the South ("LOTS") to administer the Company's financial affairs during the run-off process. As such, LOTS is responsible for maintaining the Company's general ledger and other financial statements. On a monthly basis LOTS sends the general ledger and other financial statements to the Company's independent actuary, J. Huell Bristoe & Associates, who review the ledger and accompanying financial statements and perform any necessary reconciliation.

9. The Company has reviewed the manner in which it processes receipts and believes that all controls are in place to ensure that such amounts are properly applied to the respective accounts and properly reported to the Bureau. Since the Company is currently in run-off there are very few receipts to apply. However all receipts are received by LOTS and applied to the appropriate account. As noted above, J. Huell Bristoe & Associates reviews all transactions on a monthly basis.

It is the Company's desire to work with the Bureau to ensure that it is complying with all of the corrective actions stated in the 2007 Exam Report. if any of the foregoing is not acceptable or does not address the issues raised in the 2007 Exam Report please let me know.

Thank you for your assistance.

Sincerely yours,

A handwritten signature in black ink that reads "Richard G. Barkhouser". The signature is written in a cursive, slightly slanted style.

Richard G. Barkhouser

cc: Board of Directors