New Jersey State Legislature
Office of Legislative Services
Office of the State Auditor

Department of Banking and Insurance
Division of Insurance
Unclaimed Life Insurance Benefits

July 1, 2014 to September 28, 2016

Stephen M. Eells
State Auditor

New Jersey State Legislature

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The Honorable Stephen M. Sweeney
President of the Senate

The Honorable Vincent Prieto
Speaker of the General Assembly

Ms. Peri A. Horowitz
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Enclosed is our report on the audit of the Department of Banking and Insurance, Division of Insurance, Unclaimed Life Insurance Benefits for the period of July 1, 2014 to September 28, 2016. If you would like a personal briefing, please call me at (609) 847-3470.

S. Eells

Stephen M. Eells
State Auditor
January 19, 2017

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Scope

We have completed an audit of the Department of Banking and Insurance, Division of Insurance, Unclaimed Life Insurance Benefits for the period July 1, 2014 to September 28, 2016. Our audit was limited to the insurance industry's use of the Social Security Administration's Death Master File or similar databases and whether adequate state laws and regulations exist to ensure that New Jersey consumers' interests are fully protected with regards to life insurance benefits. The ongoing Department of Banking and Insurance, Administration audit will be reported under separate cover at a later date.

The life insurance industry in New Jersey collected an annual average of $4.8 billion in individual life insurance premiums from residents over the last three years. The Division of Insurance's (division) prime responsibility is to regulate the insurance industry in a professional and timely manner that protects and educates consumers and promotes the growth, financial stability, and efficiency of the industry. The division's goals and objectives are to ensure solvency of insurance companies, protect the public from unlawful or unfair practices by insurers, their agents or other licensees, promptly investigate complaints and aggressively prosecute violators, issue licenses to qualified individuals and companies to provide insurance services to New Jersey citizens, review and approve insurance rates and policy forms, enforce the New Jersey Insurance Fraud Prevention Act, and apply technology to more effectively interact with the public and regulated industry.

Objectives

The objectives of our audit were to obtain an understanding of the insurance industry's use of the Social Security Administration's Death Master File or similar databases to identify deceased policyholders and to determine if state laws and regulations require insurance companies to identify unclaimed death benefits, locate beneficiaries, and make prompt payments to ensure New Jersey consumers' interests are fully protected.

This audit was conducted pursuant to the State Auditor's responsibilities as set forth in Article VII, Section I, Paragraph 6 of the State Constitution and Title 52 of the New Jersey Statutes.

Methodology

Our audit was conducted in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our conclusions based on our audit objectives.

In preparation for our testing, we studied legislation, the administrative code, and policies of the agency. Provisions we considered significant were documented and compliance with those requirements was verified by interview, observation, and research. We also read the budget messages, researched the insurance industry's use of Death Master File data and other states' life insurance laws and regulations, and interviewed agency personnel to obtain an understanding of New Jersey's insurance laws and regulations and claim payment process.

Conclusions

We found that twenty-three states have adopted legislation expanding the insurance companies' responsibilities regarding the use of the Social Security Administration's Death Master File or similar databases to identify deceased policyholders. We observed that New Jersey's current laws and regulations do not require insurance companies to routinely identify unclaimed death benefits and, absent notification of a claim by a claimant, locate beneficiaries and make prompt payments to ensure that New Jersey consumers' interests are fully protected.

Observation

Insurance companies are currently being examined by several states for their use of the Social Security Administration's Death Master File (DMF) or other similar databases to identify deceased policyholders to stop annuity payments but not expand its use to include identifying unclaimed life insurance benefits. It is also a practice of insurance companies to terminate life insurance policies for non-payment once they stop receiving premiums from the deceased policyholders or once the accumulated cash value of the policy has been depleted, without attempting to contact the beneficiary.

Under current New Jersey Statutes and regulations, insurance companies are only obligated to pay life insurance death benefits after a claim has been submitted by a designated beneficiary along with the policyholder's proof of death. Individuals may be unaware that they are a beneficiary to an existing insurance policy. In the absence of a claim, the life insurance benefits are retained by the insurance companies until the policy matures, which occurs when the policyholder achieves the omega/limiting age currently set at 121 years. If neither the policyholder nor the beneficiary can be located, the insurance proceeds will then be classified as abandoned and typically in three to five years escheat to the respective states' Unclaimed Property Administrator (UPA).

State insurance regulators and multiple other government organizations across the country have launched joint examinations into the insurance industry's business practices. Based on these examinations many of the major insurance companies, although admitting no wrongdoing, have entered into settlement agreements. Companies that have signed settlement agreements are required to run comparisons between the DMF and all of their life insurance policies that were in-force at any time from January 1, 1992 to the present day. Insurance policies that had been terminated for non-payment after the policyholder's date of death have been restored, as well as any accumulated cash value associated with the policy. The companies covered under these agreements are working on providing the insurance proceeds to the beneficiary or if they cannot be located, the proceeds may be escheated to the appropriate state's UPA.

The National Conference of Insurance Legislators and the National Association of Insurance Commissioners have each developed and released model legislation to address these issues. In addition, as of July 2016, twenty-three states have enacted legislation and another six states have introduced bills requiring insurance companies to perform DMF comparisons on a routine basis for their annuity, life insurance, and retained asset accounts. After validating the DMF information, insurance companies are now required to search for beneficiaries to provide them with claim forms and instructions. New Jersey is among the six states that currently have legislation pending regarding this matter.

Data obtained from the division provided the following information. In the past three years, the 364 life insurance companies operating in the state have collected an average of $4.8 billion annually from our residents in individual life insurance premiums. New Jersey has participated in the multi-state examinations and has signed Regulatory Settlement Agreements (RSAs) with

77 companies, resulting in $183 million in previously unclaimed life insurance benefits being disbursed to New Jersey beneficiaries. Agreements are currently pending with another 62 companies. These RSAs cover 70 percent of the average premiums collected in the state's market for individual life insurance.

While these RSAs address a significant portion of the individual life insurance market, these agreements can only be used to require a company to perform DMF comparisons on a routine basis and to subsequently search for beneficiaries if it sells annuities and is found to engage in the uneven use of the DMF. Absent defining laws and regulations, the remaining insurance companies may unfairly and knowingly retain unclaimed life insurance benefits due to beneficiaries.

The Department of Banking and Insurance should consider promulgating regulations under their current statutory authority or consider supporting necessary legislation which would require insurance companies to routinely identify unclaimed death benefits and absent notification of a claim by a claimant, locate beneficiaries, and make prompt payment. This would ensure that all insurance companies will provide life insurance benefits timely or identify these proceeds as unclaimed property.

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January 12, 2017

Mr. John J. Termyna
Assistant State Auditor
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Dear Mr. Termyna:

Thank you for the opportunity to comment on the audit of the New Jersey Department of Banking and Insurance, Division of Insurance, Unclaimed Life Insurance Benefits. Our comments are below.

The report indicates that the Department entered into Regulatory Settlement Agreements ("RSAs") with 77 companies, resulting in $183 million in previously unclaimed life insurance benefits being disbursed to New Jersey beneficiaries. Audit Report at 4. Please be advised that the Department has entered into four additional RSAs during the time period of the audit (from July 1, 2014 to September 28, 2016) and these RSAs represent an additional nine companies that are not included in the 77 figure shown in the report. All of the companies that entered into RSAs are required to institute retroactive and forward-looking corrective action to address those companies' uneven use of the Death Master File ("DMF") to halt annuity payments without checking to determine if there was a life claim for that policyholder that was eligible for claim payment.

The RSAs define "policy" as any individual life policy or endowment policy or group life insurance policy or certificate of life insurance for which the insurance company performs recordkeeping services and that provides a death benefit payable by the insurance company. The audit report fails to recognize the inclusion of group life insurance in the definition of "policy," based on an anecdotal statement by an unidentified Department employee suggesting that most groups perform their own recordkeeping. In light of the definition, the Department suggests that it would have been more accurate to calculate the percentage of life insurance premium subject to RSAs in two ways: (1) with individual life insurance premium only, and (2) with individual and group life insurance premium combined. The actual percentage of the market that would be subject to the RSAs' corrective action would fall within the range between the two percentages because there is no data on the amount of group life premium for which insurance companies provide and do not provide recordkeeping services. The presentation of both percentages and a statement that the actual market share falls between those figures would present a more accurate picture.

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Finally, and more significantly, there is nothing in the RSAs that concludes or finds that an insurance company's use of the Death Master File for the singular purpose of terminating annuity payments and not to search for life insurance policies on deceased persons violates current insurance law. The recitals section of the RSAs refers to "concerns" only, and the RSAs intentionally contain no citation to the Unfair Trade Practices Act or any other insurance laws. The RSAs explicitly state that the insurance company denies any wrongdoing or activities that violate any insurance or other applicable laws. The recommendation that the Department promulgate regulations under its current statutory authority to regulate use of the DMF is ill-advised because the current insurance statutes do not prohibit the one-sided or asymmetrical use of the DMF described in the RSAs. This lack of authority under current statutes explains why 23 states adopted specific statutes, rather than departmental regulations, to address DMF use. Moreover, the recommendations in the audit report go much farther than is necessary to address the uneven use of the DMF that was the subject of nationwide regulator concern. Many of the newly enacted legislation in other states mandate the affirmative use of the DMF even when a company has never used the database before. This is a policy call for the Legislature, not the Department, and it is one that could be costly for smaller companies. Absent the enactment of such legislation in New Jersey, the Department is without statutory authority to adopt regulations to limit uneven use of, or mandate all companies' proactive use of the DMF.

Please contact me if you have any questions regarding these comments.

Very truly yours,

Richard J. Badolato
Commissioner

Auditor's Follow-up Response

The inclusion of group life insurance premiums would provide an upper range limit of 72 percent of market share coverage as compared to the lower range limit of 70 percent noted in the report.