

STATE OF ARIZONA
FILED

AUG 26 2002

DEPT. OF INSURANCE

REPORT OF EXAMINATION
OF THE
MARKET CONDUCT AFFAIRS
OF

ALLMERICA FINANCIAL LIFE INSURANCE AND ANNUITY COMPANY

NAIC #84824

JUNE 26, 2001

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**Consumer Affairs Division
Market Conduct Examinations Section**

DEPARTMENT OF INSURANCE

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Governor

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CHARLES R. COHEN
Director Of Insurance

Honorable Charles R. Cohen
Director of Insurance
State of Arizona
2910 North 44th Street, Suite 210
Phoenix, Arizona 85018-7256

Dear Director Cohen:

In conformity with the provisions of the Insurance Laws and Rules of the State of Arizona, an examination has been made of the market conduct affairs of the:

**Allmerica Financial Life Insurance and Annuity Company
NAIC # 84824**

Market Conduct Examiner-In-Charge Earl Brown and Senior Examiner Jay Hodges conducted the examination.

As a result of that examination, the following Report of Examination is respectfully submitted.

The courtesy and cooperation extended by the officers and employees of the Company are sincerely appreciated.

Sincerely yours,

A handwritten signature in cursive script that reads "Paul J. Hogan" followed by a stylized flourish.

Paul J. Hogan, FLMI, ALHC, AIE
Chief Market Conduct Examiner

AFFIDAVIT OF MARKET CONDUCT EXAMINER-IN-CHARGE

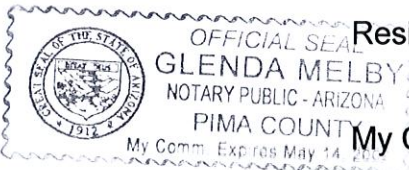
State of Arizona)
) ss
County of Pima)

Earl C. Brown, AIE, being first duly sworn, states that I am a duly appointed Market Conduct Examiner-in-Charge for the Arizona Department of Insurance. Under my direction and with my participation and the participation of Jay E Hodges, CIE, a Market Conduct examination of the insurance operations of Allmerica Financial Life Insurance and Annuity Company was performed at the Company's home office in Worcester, MA. No copy or synopsis of this Report has been furnished to the Company because the Examination has not yet been finalized at the Arizona Department of Insurance. The information contained in this Report, consisting of the following pages, is true and correct to the best of my knowledge and belief. Any conclusions and recommendations contained in and made a part of this Report submitted herewith are such as may be reasonably warranted from the facts disclosed in the Examination Report.

Earl C. Brown
Earl C. Brown, AIE
Market Conduct Examiner-in-Charge

Subscribed and sworn to before me this 13 day of July 2001, by Earl C. Brown

Glenda Melby
Notary Public

Residing at Tucson AZ
 OFFICIAL SEAL
GLENDA MELBY
NOTARY PUBLIC - ARIZONA
PIMA COUNTY
My Commission expires 5-14-02

FOREWORD

This Market Conduct Examination is, in general, a report by exception. This means that references to Company practices, procedures or files subject to review may not appear in this Report if the Examiners found no improprieties.

The company examined in this Report is Allmerica Financial Life Insurance and Annuity Company, hereinafter referred to as "AFLIAC" or the "Company".

The Examiners conducted the Examination of the Company in accordance with Arizona Revised Statutes (A.R.S.) §§ 20-142, 20-156, 20-157, 20-158 and 20-159.

Company personnel or printed manuals provided the information used in the History, Adjudication of Fraudulent Activities, Marketing Distribution Channels section of this Report.

The EXHIBITS section of this Report contains the Report exhibits referenced in **bold**.

The APPENDIX section of this Report contains the text of Statutes and Administrative Rules cited in this report.

SCOPE OF EXAMINATION

The purpose of the examination was to determine the Company's compliance with Arizona Revised Statutes and Administrative Rules with regard to variable and non-variable annuities and life insurance. The examination period was January 1, 1999 through December 31, 2000.

The Examiners' charge included reviewing the Company's:

1. Contractual agreements with third party administrators and producers;
2. Producer agreements
3. Terminated agent files;
4. Producer licensing and commissions;
5. Agent training; guidelines for agent-produced advertising;
6. Complaints and complaint handling procedures;
7. Filings, forms, brochures and other advertising materials, including Internet and other electronic advertising for accuracy of representations and compliance with Arizona law;
8. Underwriting, rating and pricing;
9. Procedures relating to policy issuance/termination;
10. Individual and Group Annuities; compliance with applicable annuity laws;
11. Overall claims handling procedures;
12. Fraud and compliance with A.R.S. § 20-466;

The review of the Company's operations and marketing practices included the review of the list of agents filed with the Department.

The Examiners reviewed the Company's complaint handling procedures. The review of the Company's overall claims handling included claims procedures, hard-copy and electronic claims records, and cancelled checks representing claim payments.

EXAMINATION METHODOLOGY

The Examiners utilized both examination by test and examination by sample. Examination by test involves review of all records within the population

while examination by sample involves the review of a selected number of records from within the population.

Examination sampling methodology by section follows:

Complaints	Test
Advertising	Test
Agent Licensing	Systematic Sample
Agent Terminations	Test
Annuity Forms	Test
Annuity Issues	Systematic Sample
Annuity Free-Look Refunds	Test
Annuity Disbursements to Corporate Payees	Systematic Sample
Annuity Disbursements to Individual Payees	Systematic Sample
Annuity Disbursements / No Surrender Charge	Systematic Sample
Annuity Claims	Test
Life Forms	Test
Life Issues - Standard	Systematic Sample
Life Issues - Sub-standard	Test
Life Loans / Partial Surrenders	Systematic Sample
Life Total Surrenders	Systematic Sample
Life Claims	Test

STATUTES & RULES REFERENCED

The Examiners have alleged that AFLIAC violated the following Arizona statutes and administrative rules: Revised Statutes (A.R.S.) §§ 20-444(A), 20-446, 20-448(A), 20-448.01(B), 20-452, 20-461(A)(2), 20-462(A), 20-1233(A), 20-2110(A), 20-2604(D)(1)(f), 20-2607(A)(7), 20-2608(3) and Arizona Administrative Code (A.A.C.) R20-6-218(B)(1), R20-6-801(C), R20-6-801(E)(4) and R20-6-1203(C).

The text of the Statutes and Rules violated and other Statutes and Rules referenced in this Report are contained in the Appendix.

COMPANY HISTORY

Allmerica Financial Life Insurance and Annuity Company (AFLIAC) was originally incorporated as American Variable Life Assurance Company. The company name was changed to SMA Life Assurance Company in 1982. Demutualization and reorganization in 1995 resulted in adoption of the current company name as a wholly owned subsidiary of First American Financial Life Insurance Company, which was, in turn, wholly owned by a newly formed holding company named Allmerica Financial Corporation. The Allmerica Financial group offers a full range of financial products and services, and AFLIAC offers variable life and annuities as part of that group.

The sales focus of AFLIAC and its affiliates have been shifting in recent years from traditional insurance products to fee-based variable insurance products sold to small business owners and middle and upper income professionals. According to A. M. Best, AFLIAC's separate account assets now comprise over 80% of total admitted assets, compared to about one-third in 1993. Individual variable annuities now account for over 90% of new sales.

COMPLAINTS

The Examiners reviewed complaints filed with the Arizona Department of Insurance and complaints received directly by the Company. The primary purpose of this review is to provide the Examiners with information about Company problem areas and business practices related, but not limited to,

policyholder service, claim resolution, policy issuance and agent misconduct. The Examiners use this complaint review to better focus the examination and address questionable business practices or significant occurrences.

Department Of Insurance Complaints

During the examination period, there were no complaints filed with the Department of Insurance involving the examined lines of insurance.

Company Complaints

There were 24 complaints received by the Company during the examination period. The Examiners categorized the complaints as follows:

<u>Category</u>	<u>Number</u>	<u>Percentage</u>
Client Service Issues	8	33%
Surrender or Loan Charges	7	29%
Agent Misrepresentation	5	21%
Improper Sales	2	8%
Request for Information	<u>2</u>	<u>8%</u>
Total	24	100%

The Examiners criticized a complaint involving Policy Number V061914000. The policyholder wished to purchase term insurance and mutual funds. The agent sold him a variable life policy, which he admitted was not what the client desired. When the policyholder attempted to get a refund, the Company informed him that it would waive surrender charges if he purchased other products from the Company. This is an apparent violation of A.R.S. § 20-446 and § 20-452.

The Company disagreed with this criticism, stating in part: "We disagree with the above primarily on the basis that we do not believe either of the statutory sections referenced above applies [to] this matter. We also disagree on the

basis that the company refunded the client's money and did not require the purchase of another product manufactured by the company.”

The Examiners maintained that the Company's original position, as stated in its memorandum dated December 7, 1999, was an improper resolution of the situation in light of the Company's acknowledgement that the sale had been unsuitable. The Examiners recognize that the Company eventually refunded the client's money in full, less loan indebtedness, without requiring him to retain the funds in other Company products.

Class-Action Settlement

AFLIAC and its parent company Allmerica Financial Corporation settled a class-action lawsuit in December 1998. The plaintiffs charged Allmerica with deceptive sales practices in the sale of life insurance policies from 1978 through May 1998. The alleged practices included promises of vanishing premiums, twisting, and misrepresenting a life insurance policy as an investment.

The Examiners requested details as to the current status of the settlement.

Information furnished by the Company indicated that 8,079 Arizona policies were subject to and sent notification of the settlement. The settlement notification packet requested a response from the policyholder regarding which of two options they chose. The options were:

- General Policy Relief (GPR), which offered the opportunity to purchase an annuity enhanced with contributions by Allmerica or a new, discounted life insurance policy.

- Alternative Dispute Resolution (ADR), which offered a cash settlement to be determined by one or more independent adjudicators who scored each claim.

A total of 725 (9.0%) of the 8,079 eligible policyholders responded to the offer.

General Policy Relief was chosen by 414 (57.1%) of the 725 respondents, qualifying them to purchase an annuity enhanced with contributions by AFLIAC or a new discounted life insurance product.

Alternative Dispute Resolution was chosen by 311 (44.3%) of the 725 respondents, qualifying them for cash settlements subject to evaluation of their claim by independent adjudicators. Records indicate that 100 of the 311 ADR candidates submitted a claim, and 40 of those 100 claims resulted in a cash settlement. Arizona policyholders have, as of May 2001, received ADR settlements totaling \$31,304.00.

Adjudication Of Fraudulent Activities

During review of Company complaints, the Examiners noted references to fraudulent insurance and securities sales activities of one of AFLIAC's Arizona agents. The Examiners requested details to determine which of those activities involved insurance and occurred or became known during the examination period.

Information provided by the Company indicated that the Allmerica agent and registered representative engaged in fraudulent insurance and securities sales activities in the late 1980's and early 1990's. Certain of these fraudulent activities became known in 1993, at which time the agent was placed on

probation and required to move into agency offices. In 1995, additional fraudulent securities activities were discovered. The Company launched another investigation, resulting in the agent's termination in 1996. The continued investigation and settlement process has resulted in 120 settlements by AFLIAC and its affiliated broker-dealer, totaling \$1,780,386.70 as of May 2001. An additional 25 potential settlements, with offers totaling approximately \$84,000, are still outstanding.

Arizona Litigation

The Company reports that they were not involved in any litigation in Arizona during the examination period.

MARKETING

Distribution Channels

The Company distributes annuity and life insurance products through both a career agency system and through networks of broker-dealers who hold selling agreements with the Company. The broker-dealers who sell the Company's products can be further broken down into two general categories: Allmerica Select and Strategic Partners. Allmerica Select is a brand name owned by the Company that uses an extensive network of broker-dealers to distribute its products. The Company's Strategic Partners are generally, though not exclusively, mutual fund companies whose investment vehicles are used to fund annuity products issued by the Company.

A breakdown of the sales volume by distribution channel follows:

<u>Channel</u>	<u>Product</u>	<u>2000</u>	<u>1999</u>	<u>1998</u>
Allmerica Select	Annuity	\$6,216,215.20	\$15,417,447.16	\$8,428,962.53
	Life	834,580.19	663,409.17	762,124.13
Career Agents	Annuity	4,833,869.57	7,475,023.53	9,655,838.27
	Life	232,354.06	311,521.57	677,443.65
Partners	Annuity	50,054,865.73	47,736,630.67	51,953,302.99
	Life	0.00	0.00	0.00

ADVERTISING

The Company stated that all marketing materials (printed, electronic, seminar presentations, seminar invitations, telemarketing scripts, yellow page ads, stationery, and business cards) must be reviewed and approved by the Company's regulatory compliance office prior to use. Regional compliance offices handle ads submitted by agents while the home office regulatory compliance office staff handles those pieces submitted by the various marketing staffs. All electronic correspondence is reviewed by special software attached to AFLIAC's email system, which reviews both incoming and outgoing emails sent by agents to the public. Any items requiring further review are forwarded to the appropriate regional compliance office.

The Company maintains yearly Advertising and Sales Literature Review and Clearance Logs. The Examiners reviewed these logs for the years 1999 and 2000. There were approximately 1,000 submissions in each of the two years. The Company also maintains a web-based Marketing Library containing pre-approved sales and advertising materials and support materials available for downloading by the agent. This Marketing Library contains several hundred documents. The Examiners and Company personnel attempted to extract from

these logs, and Marketing Library's table of contents, those point-of-sale materials that were product or concept specific.

The Examiners reviewed 404 sales and advertising documents, and criticized three (0.7%) of the 404 documents.

The Examiners criticized advertising form AS-465 (1/00), because the sales training material (for broker-dealer use only) recommends that a variable universal life insurance policy be presented as a Life Insurance Retirement Plan (LIRP), rather than a life insurance policy. The training material specifically recommends that the agent handle the prospect's goals of protection and retirement income as follows:

YOU RESPOND...

"Let me show you one easy way to accomplish both of these goals. I can help you set up a LIRP --- a Life Insurance Retirement Plan which is an all in one tax-favored contract. This plan combines:

- significant tax advantages
- the security of life insurance
- growth potential of managed accounts
- assures continued deposits if disabled".

The Examiners' believe that this statement implies that the LIRP is a plan distinct from a life insurance policy.

On page two the training piece again distinguishes a LIRP by stating:

Plus, if you structure your clients' LIRP with an Allmerica Select Life Variable Universal Life Policy, you can offer them access to some of the world's leading money managers---on a tax-deferred basis.

A copy of advertising piece AS-465 (1/00) is attached as **EXHIBIT 1**. Causing a misleading statement to be made in the sale of insurance, by issuing misleading agent training material, is an apparent violation of A.R.S. § 20-444(A).

The Company disagreed with the criticism, stating in part:

“It is not misleading to state that the cash values of a life insurance policy can be used to supplement retirement benefits so long as it is clear that the product being sold is life insurance.”

A copy of the disagreement is attached as **EXHIBIT 2**.

The Examiners do not disagree with the Company’s comment, but note that the training material does not recommend that the agent state that these features are found in an Allmerica Select Life Variable Universal Life Policy. The material recommends that the agent present these features as belonging to a LIRP.

The training material furthers the idea that a LIRP is somehow separate from a life insurance policy on the second page, titled HOW TO PUT THIS IDEA INTO ACTION. The last paragraph states “...if you structure your clients’ LIRP with an Allmerica Select Life Variable Universal Life Policy,” This statement implies that a LIRP is a contract that is, or could be, something other than a life insurance policy. The Examiners maintain that the criticism was correct as written.

The Examiners criticized advertising form AS-744 (2/00), titled The Power of Tax-Deferred Investing, because it contains a graph that compares the pre-tax accumulated value of an annuity to the value of a “taxable investment”. The illustrated value of the taxable investment assumes that the investment is reduced by all taxes incidental to its growth as they occur. The comparison of accumulated values is misleading because accessing the annuity’s accumulated value will trigger taxation of gains and the illustrated annuity values have not been reduced by the effect of this taxation.

The after-tax value of the annuity is disclosed in the footnotes following the graph, but the graph does not reflect the annuity's value after taxes are paid as it does with the "taxable investment". In the Examiners' opinion, a comparison of accumulated values is valid if both alternatives are on an after-tax basis at the point of comparison. The difference in after-tax accumulation, which is substantial over time, can then be considered The Power of Tax-Deferred Investing.

A copy of advertising piece AS-744 (2/00) is attached as **EXHIBIT 3**. Dissemination of misleading advertising is an apparent violation of A.R.S. § 20-444(A).

The Company concurs with the Examiners position that tax-deferred investment value be reflected and published to the public as an after-tax amount on the graph, but disagrees that A.R.S. § 20-444 has been violated based on the fact that the material is disseminated only to broker-dealers. The advertising is footnoted in bold type "For Broker/dealer use only. Not to be distributed to the general public or used in conjunction with product solicitation."

The Examiners note that A.R.S. § 20-444 prohibits making, or causing, directly or indirectly, to be made any way any assertion, representation or statement with respect to the business of insurance that is deceptive or misleading. The Company concurs that the graphic representation is misleading. In the Examiners' opinion, the use of a misleading concept in materials intended as training materials for agents causes that misleading concept to be relayed to the public.

The Examiners criticized form ALSEA91BRO (5/96), an annuity sales brochure titled ExecAnnuity Plus Investing in your future. The brochure contains a chart on the page with the heading "Tax advantages help your investments grow at an accelerated rate". This chart is labeled in bold type "The value of tax-deferred growth", and compares the pre-tax accumulation of an annuity against a currently taxable alternative with the taxable alternative illustrated net of all tax incidental to its growth. As stated previously, comparison of a pre-tax amount to an after-tax amount as an example of tax-deferral is misleading. The comparison would be valid if it illustrated both amounts on an after-tax basis.

A copy of advertising form ALSEA91BRO (5/96) is attached as **EXHIBIT 4**. Dissemination of misleading advertising is an apparent violation of A.R.S. § 20-444(A).

The Company agreed that the chart was misleading, but disagreed with the criticism based on the fact that the advertising is no longer used because this annuity product is no longer being sold by the Company. The Company has reminded its Product Development and Marketing areas that tax-deferred investment values must be illustrated on an after-tax basis when compared against the after-tax values of other products.

The Examiners respond to the Company's comments by noting that this advertising piece was represented to the Examiners as currently available advertising. The ExecAnnuity Plus name appears in small print in the footnotes under the misleading chart, but the chart and accompanying explanation can be used with any of the Company's deferred annuities to compare accumulated values of competing investment vehicles in a misleading manner.

Life Illustration Software

The Company's Career Agent Agreement governs agent responsibilities and duties in its Career Agency distribution channel. Sales Agreements serve much the same function in the Allmerica Select and Strategic Partners distribution channels. Both agreements stipulate that the agent, registered representative or broker-dealer will not furnish any prospective insured or policy owner an illustration of the financial or other aspects of a policy or a proposal for a policy of the Company unless the same has been either furnished by the Company or prepared from computer software or other material furnished or approved by the Company.

The Examiners reviewed samples of sales illustrations generated by AFLIAC's life insurance illustration system. No exceptions were noted.

COMPANY OPERATIONS

Agent Licensing

The Examiners systematically sampled 51 (4.7%) of 1081 issued annuities to verify that the agent receiving sales commission was licensed on the application date. No exceptions were noted.

Agent Training

Product Training

The Examiners submitted a series of questions to the Company for the purpose of verifying adequate product training in each of the distribution channels. The Company's response to those questions indicated that product training by the Company is limited to their Career Agent distribution channel. The Company makes training available to their career agents through various

avenues but does not impose any baseline training standards. The Company notes that most of the Company's career agents hold insurance and securities industry designations, many achieved through widely accepted certification or examination processes, and the Company makes a practice of hiring, with very few exceptions, only experienced producers.

Training for producers in the Partner and Select channels is left to either the broker-dealer firms or the Partner. The Company, though no statutory imperative to do so, neither oversees nor audits product training, leaving that responsibility to the unaffiliated broker-dealers associated with the Select and Partners channels, who are required by the National Association of Securities Dealers (NASD) to appropriately train and supervise their representatives.

Agent Terminations

The Examiners requested a listing of terminated Arizona agents. The Company furnished information on 12 agents whose appointments with the Company were terminated during the examination period. All agents were voluntarily terminated. No exceptions were noted.

Contractual Agreements

The Examiners requested copies of any contracts between the Company and third-party administrators. The Company stated that it does not maintain any relationships with third-party administrators.

Policy Forms

Annuity Forms

The Examiners reviewed 32 variable annuity application forms furnished by Company as applying to policies eligible for issue in Arizona. These

application forms were reviewed for the purpose of verifying compliance with the disclosure requirements of A.R.S. § 20-1233. No exceptions were noted.

Life Forms

HIV Consent Forms

The Examiners reviewed the HIV-related testing consent forms used by the Company in Arizona. The Examiners noted four different forms in use during the examination period. The Examiners criticized four (100%) of the four forms.

The Examiners criticized two forms [27(3/95) and 07127 (3/95)] as follows:

<u>Violation</u>	<u>Applicable Regulation</u>
Failure to have consent form approved by the Director	A.A.C. R20-6-1203(C)
Failure to offer 10-day consideration period	A.A.C. R20-6-1203(C)(1)
Failure to disclose that refusal to be tested may be used to deny coverage	A.A.C. R20-6-1203(C)(1)
Failure to provide information on how the disease is spread	A.A.C. R20-6-1203(C)(2)
Failure to provide information concerning counseling	A.A.C. R20-6-1203(C)(3)
Failure to disclose type of test to be used	A.A.C. R20-6-1203(C)(5)
Failure to include required attestation	A.A.C. R20-6-1203(C)(6)
Failure to include optional release of information to personal physician	A.A.C. R20-6-1203(C)(7)
Failure to restrict release of information to 180 days	A.A.C. R20-6-1203(C)(8)

These forms were used in seven (22.6%) of the 31 issued life files that contained HIV-related test results and were reviewed by the Examiners.

The Examiners criticized two forms 07677AZ (3/95) and 07677AZ (6/93) as follows:

<u>Violation</u>	<u>Applicable Regulation</u>
Failure to have consent form approved by the Director	A.A.C. R20-6-1203(C)
Failure to restrict release of information to 180 days	A.A.C. R20-6-1203(C)(8)

These forms were used in seventeen (54.8%) of the 31 issued life files that were reviewed by the Examiners and contained HIV-related test results.

Identity Of Policy Owner

The Examiners reviewed six individual variable life insurance policy forms and 28 ancillary individual life rider and endorsement forms associated with those policies. The Examiners criticized three (50%) of the six individual life policy forms because the cover page or a page that corresponds to the cover page failed to identify the owner of the contract (1018-93, 1023-93, 1026-94). These are apparent violations of A.R.S. § 20-2604(D)(1)(f). A copy of the cover and declaration pages of policy form 1018-93 is attached as **EXHIBIT 5**.

The Company disagreed with the criticism, stating in part:

The first sentence on the cover of the policies identifies the owner as a party to the contract. The owner is defined within the body of the contract. (See page 9 of policy form 1018-93.) The owner is specifically identified in the application that is part of the contract.

We have not printed the name of the owner on the cover of the contract because the owner can, and often does, change over time. When an absolute assignment is recorded at the Home Office, a copy is returned to the new owner documenting the transfer of title.

The Examiners agree that referring to various clauses in and attachments to the contract can determine the policy owner. However, the Examiners believe that A.R.S. § 20-2604(D)(1)(f) very clearly states that the cover page or a page that corresponds to the cover page of a variable life insurance policy shall identify the owner of the contract.

Suitability Questions

The Examiners determined that nine different life application forms were included as part of the Life Issues Survey.

The Examiners criticized nine (100%) of the nine application forms because they had not been included in the Exempt Forms listing (**EXHIBIT 6**). This is an apparent violation of A.A.C. R20-6-218(B)(1).

These nine forms were reviewed to determine whether the Company's variable life applications contain questions that enable the insurer to determine the suitability of variable life insurance for the applicant.

The Examiners criticized three (33.3%) of the nine variable life application forms used because the forms did not contain sufficient questions to enable the insurer determine the suitability of variable life insurance for the applicant (AS-158-95, AS-401 8/98, AS-401 4/99). This is an apparent violation of A.R.S. § 20-2608(3)

One or another of these three applications appeared in 25 (44.6%) of the 56 application files included in the survey. The Examiners noted two other of the nine application forms, 1 JUV-95 and 05372 (9/95), that do not by themselves adequately address suitability. However, these forms were not criticized because application supplement SML 1287, which contains questions sufficient to adequately determine suitability, was included with, and as part of, the application.

The Company disagreed with the criticism, indicating that the applications did contain certain basic suitability questions and NASD member broker-dealers are governed by the rules of the NASD, including stringent requirements for registered representative licensing, supervision and training, such as the requirement that the representative "know their customer" and sell only products that are suitable for them. The Company also stated:

Each broker-dealer firm that sells these products enters into a selling agreement with Allmerica Investments, Inc., the distributor of the variable life products offered by Allmerica Select. The terms of the selling agreement indicate that the broker-dealer firm is responsible for the suitability of any product sold by its producers on behalf of the company. Each firm uses its own client questionnaire to collect suitability data related to its clients.

A copy of the Company's response is included as **EXHIBIT 7**.

The Examiners agree that the broker-dealer may have suitability responsibilities under NASD rules, but note that A.R.S. § 20-2608(3) appears to be unequivocal in its requirement that a variable life insurance policy application contain questions that enable the insurer to determine the suitability of variable life insurance for the applicant.

Product Suitability

In view of the Company's practice of including a clause in their Sales Agreements with nonaffiliated broker-dealers that appears to make the broker-dealer responsible for product suitability, the Examiners requested additional details as to what oversight or monitoring functions the Company had in place to assure product suitability and/or reveal potential suitability problems.

The Company stated that they have focused much attention on the issue of suitability. In March, 2001 they rolled out a suitability-training program, including CD-ROM, copies of recent NASD notices to member firms, and copies of pertinent company forms, for each registered representative in their career agency distribution channel. Additional changes are being made in house to review and assure adequate suitability.

The Company does not appear to accept responsibility for suitability in the sale of their products by registered representatives of non-affiliated broker-

dealers in the Allmerica Select and Strategic Partners. The Company responded in part:

Suitability for the sale of variable products, hybrid insurance/securities products, is the responsibility of the selling broker-dealer and the individual insurance agent/registered representative who made the sale. AFLIAC provides information relating to its products, which can assist these representatives in their determination as to whether an AFLIAC product is suitable for one of their clients.

In a separate memo, AFLIAC addressed efforts it does make toward assuring suitability of products sold through its Allmerica Select and Strategic Partners channels. This memo is attached as **EXHIBIT 8**.

Changes Pursuant To Gramm-Leach-Bliley Act

The Examiners requested details concerning any modifications to existing practices and/or notifications due to the Gramm-Leach-Bliley Act. The Company responded that a Privacy Task Force was established in May 2000, and an eight-step process was initiated. The audit determined that AFLIAC was not currently disclosing confidential information beyond the scope of the Act. The Task Force suggested that AFLIAC adopt a Privacy Policy that prohibited the disclosure of confidential information altogether, unless specifically permitted by law. The Company's model Privacy Policy originally followed a practice of preserving the possibility of sharing information with non-affiliated parties when a joint marketing agreement is in place, but a review of AFLIAC's selling agreements determined that the sharing of customer information with non-affiliated parties, other than agent/brokers or financial advisors, was prohibited contractually. Additionally, the Company's Privacy Policy also did not, and currently does not, contain an

opt-out mechanism for sharing information with entities other than financial institutions.

A formal Privacy Notice will be sent to all Company policyholders by July 1, 2001, and language in all third-party agreements will be amended to confirm that customer information shared with a third party will only be used for the purpose intended by the Company in disclosing the information.

VARIABLE LIFE

Life Issues

Standard Life Issues

The Company issued 86 variable life insurance policies during the examination period. The Examiners reviewed the underwriting files of 49 (56.9%) of the 86 issued life policies.

The Examiners criticized eight (16.2%) of the 49 files because the files contained HIV-related testing test results and, either did not contain a properly signed HIV-related testing consent form (VS10852000, VS10598400, VS10574700 and V063779900), or contained a consent form that was signed after the date of the HIV-related test (VS10646800, VS10639000, V063808775 and V063787700). Performing an HIV-related test without first receiving the specific written informed consent of the subject of the test in a form as prescribed by the Director is an apparent violation of A.R.S. § 20-448.01(B).

The Examiners criticized 19 (38.8%) of the 49 files, because the Company failed to provide the policyholder the required illustration of contractual benefits (**EXHIBIT 9**). This is an apparent violation of A.R.S. § 20-2607(A)(7).

The Company disagreed with this criticism, stating in part: "All clients receive a prospectus (that has been filed with the Securities and Exchange Commission) at the time of sale."

The Examiners maintained that while it was correct that clients received a prospectus at the time of sale, the prospectus provided was generic in nature, not specific to the client's situation and did not meet the standards for adequate disclosure as required by A.R.S. § 20-2607.

Substandard Life Issues

The Company underwrote nine life insurance applications during the examination period that resulted in the policies being issued on a substandard rated basis. The Examiners reviewed nine (100%) of these nine files.

The Examiners criticized three (33.3%) of the nine files because the Company failed to provide the applicant with the specific reason(s) for the adverse underwriting decision in writing (V064271900, V063944800 and V065094600). This is an apparent violation of A.R.S. § 20-2110(A).

The Examiners criticized six (66.7%) of the nine files because the files contained test results of HIV-related testing and, either did not contain a properly signed HIV-related testing consent form (V063794800, V062407200, VS10568000 and V063944800), or contained a form that had been signed after the date of the HIV-related test (VS10588100 and V064271900). Performing an HIV-related test without first receiving the specific written informed consent of the subject of the test in a form as prescribed by the Director is an apparent violation of A.R.S. § 20-448.01(B).

The Examiners criticized four (44.4%) of the nine files because the Company failed to provide the policyholder the required illustration of contractual benefits (VS10707600, VS10568000, V063944800 and V062407200). This is an apparent violation of A.R.S. § 20-2607(A)(7).

The Company disagreed with this criticism, stating in part: "All clients receive a prospectus (that has been filed with the Securities and Exchange Commission) at the time of sale."

The Examiners maintained that while it was correct that clients received a prospectus at the time of sale, the prospectus was generic in nature, not specific to the client's situation and did not meet the standards for adequate disclosure as required by A.R.S. § 20-2607. This was especially true when the contract was issued on a non-standard basis.

Declined Applications

The Company states that there were no declined life applications during the examination period.

Rescissions

The Company states that there were no life rescissions during the examination period.

Policy Servicing

Annual Policyholder Reports

The Examiners reviewed sample Annual Policyholder Reports generated from both life insurance administrative systems for the purpose of verifying compliance with the requirements of A.R.S. § 20-2609.

The Company informed the Examiners that it had discovered in late 2000 that the projection of values required by A.R.S. § 20-2609(1) was missing from the report, and a work order was initiated to institute a correction. The implementation date for the correction is July 19, 2001. The Examiners confirmed that the Company had taken self-corrective action and confirmed the revised format of the report. No criticisms were issued.

Annual Statements

The Examiners requested a copy of the annual statement furnished to the policy owner in accordance with A.R.S. § 20-2609(2). The Company furnished a copy of the statements, which are contained within the body of the product prospectus in which the client is invested. These prospectuses are distributed to each policyholder in May of each year.

Grace Period Correspondence

The Examiners requested copies of grace period letters that must be mailed to owners of flexible premium policies in accordance with A.R.S. § 20-2609(3). The Company furnished three letters that were produced automatically and mailed to flexible premium policy owners when policy values were less than needed to keep the policy in force. The first notice is mailed the day the grace period begins, the second is mailed 22 days after the grace period begins, and the third is mailed 42 days after the start of the grace period. The Examiners reviewed the content of the notices to verify compliance with the statute. No exceptions were noted.

Life Disbursements

Free Look Refunds

The Company stated that there were no free-look refunds during the examination period.

Total Surrenders

The Company processed 251 total surrenders of life insurance policies during the examination period. The Examiners reviewed 45 (17.9%) of the 251 policies. The Examiners reviewed the total surrenders to verify signature requirements, payees, amounts paid and procedures in general. No exceptions were noted.

Partial Surrenders And Loans

The Company processed 301 life insurance policy loans and 61 partial surrenders of life policies during the examination period. The Examiners reviewed 55 (15.2%) of these 362 policies. Forty-six policy loans and nine partial surrenders were selected and reviewed. The Examiners reviewed these policy files to verify signature requirements, payees, amounts paid and procedures in general. No exceptions were noted.

Life Claims

Paid Claims

The Company processed 11 life insurance claims during the examination period. The Examiners reviewed time service, signatures, payees and calculation for all 11 claims. The Examiners criticized two files. Both files received multiple criticisms for a total of four criticisms.

The Examiners criticized two (18.2%) of the 11 claims, for failure to provide claim forms, instructions and reasonable assistance to the claimant/beneficiary within 10 working days (L0324302 and V0579185). These are apparent violations of A.A.C. R20-6-801(E)(4).

The Company's failure to provide claim forms in a timely manner as cited above appeared to be indicative of a general business practice and an apparent violation of A.R.S. § 20-461(A)(2).

The Examiners criticized two (18.2%) of the 11 claims for failure to pay the correct amount of interest due in accordance with standard Company procedures (L0324302 and V0579185). Claim L0324302 was underpaid \$48.81 and Claim V0579185 was overpaid \$121.76. These are apparent violations of A.R.S. § 20-448(A).

Denied, Compromised Or Closed Claims

The Company stated that there were no life claims that were denied, compromised or closed without payment during the examination period.

VARIABLE ANNUITIES

Annuity Issues

The Company issued 1,772 annuity policies during the examination period. The Examiners reviewed 50 (2.8%) of the 1,772 policies. The Examiners criticized one (2.0%) of the 50 files because the application form neither contained notification of a ten day free look nor advised the applicant of his right to obtain other reasonable information regarding the annuity contract (VN00414066). This is an apparent violation of A.R.S. § 20-1233.

Free Look Refunds

The Company processed four requests for refunds under the free look provision on annuity policies during the examination period. The Examiners reviewed all four files with particular attention to compliance with A.R.S. § 20-1233(B). No exceptions were noted.

Declines And Rescissions

The Company stated that there were no variable annuity declines or rescissions during the examination period.

Policy Servicing

Annual Policy Statements

The Examiners reviewed a sample Annual Policyholder Report generated from both annuity administrative systems for the purpose of verifying compliance with the requirements of A.R.S. § 20-2637. No exceptions were noted.

Annuity Disbursements

The Company processed 2,032 annuity partial surrenders and withdrawals during the examination period. The Examiners ran a series of surveys to verify that all withdrawal and surrender requests had proper signatures and that the payee was as requested.

Disbursements To Corporate Payees

The Examiners surveyed 51 annuity disbursements to payees other than the annuitant. All payees were corporate entities. No exceptions were noted.

Disbursements To Individual Payees

The Examiners surveyed 50 annuity disbursements to individual payees. No exceptions were noted.

Disbursements With No Surrender Charge

The Examiners surveyed 44 annuity disbursements that did not involve a surrender charge. No exceptions were noted.

Annuity Claims

Paid Claims

The Company paid 96 annuity claims during the examination period. The Examiners reviewed the time service, signatures, payees and calculations for 51 (53.1%) of the 96 claim files.

The Examiners criticized two (3.9%) of the 51 claims for failure to provide claim forms, instructions and reasonable assistance to the claimant/beneficiary within 10 working days (MN00411951 and PQ00078002). This is an apparent violation of A.A.C. R20-6-801(E)(4).

The Examiners criticized one (1.9%) of the 51 claims for failure to pay interest on a delayed claim settlement (AN00423180). This claim was delayed in settlement and 99 days interest at the legal rate [10%] was due. Failure to pay interest at the legal rate on this claim was an apparent violation of A.R.S. § 20-462.

The Company disagreed with this criticism, stating in part: "It is our position that the claimants statement was signed 5/31 not 3/31. The death certificate was located on 6/2. However, the claimant's statement and other necessary paperwork to make the file in good order was not received until 6/15."

The Examiners maintained their position that the processing of this claim had been delayed unnecessarily, because all the documentation had been provided earlier to process a claim under another policy number, AN00417625.

The Examiners criticized 16 (31.4%) of the 51 claims, for failure to maintain adequate documentation within the claim files to allow chronological reconstruction of the pertinent events of the claim (**EXHIBIT 11**). These are apparent violations of A.A.C. R20-6-801(C).

The Company disagreed with this criticism and provided excerpts from its claim processing system as evidence of appropriate dates of receipt.

The Examiners maintain that claims system entry dates did not provide an acceptable alternative to the physical dating of the document upon receipt.

Denied, Compromised Or Closed Claims

The Company stated that there were no annuity claims denied, compromised or closed-without-payment during the examination period.

RECOMMENDATIONS

(Note: These recommendations are those of the Examiners based on the facts gathered during this examination. These recommendations do not necessarily represent the action that the Director of Insurance will ultimately require of the Company when the report is filed. Any action taken on these recommendations by the Company prior to the filed date of this Report will not alter the facts found by the Examiners during the examination and relayed herein and will not exempt the Company from any further action the Director deems appropriate.)

The Examiners recommend that Allmerica Financial Life Insurance and Annuity Company develop and implement written procedures to ensure that:

- a. All personnel who are responsible for complaint handling are familiar and comply with A.R.S. §§ 20-446 and 20-452.
- b. All personnel who are responsible for marketing and advertising are familiar and comply with A.R.S. § 20-444(A).
- c. All personnel who are responsible for policy form development are familiar and comply with A.A.C. R20-6-1203(C) and A.R.S. §§ 20-1233, 20-2604(D)(1)(f) and 20-2608(3).
- d. All personnel who are responsible for policy form filings are familiar and comply with A.A.C. R20-6-218(B)(1).
- e. All personnel who are responsible for underwriting are familiar and comply with A.R.S. §§ 20-448.01(B), 20-2110(A) and 20-2607.
- f. All personnel who are responsible for claims are familiar and comply with A.A.C. R20-6-801(C), and A.R.S. §§ 20-448(A), 20-461(A)(6) and 20-462.

We also recommend that the Director of Insurance, pursuant to A.R.S. §§ 20-161(A) and 20-220, determine if cause exists to take disciplinary action against the Company for violation of:

- a. A.R.S. §§ 20-446 and 20-452(4), because the Company offering to refund premiums following an admission of misrepresentation by the agent only if the policyholder used the refund to purchase another AFLIAC policy.
- b. A.R.S. § 20-444(A), because the Company:
 1. provided agent training material that recommends that the agent present a variable life insurance contract as something other than a life insurance policy, specifically a Life Insurance Retirement Plan (LIRP).
 2. used graphs in annuity sales material that compares the accumulation values of a “taxable investment” and an annuity in a misleading manner and thereby overstates the actual benefit of tax-deferral.
- a. A.A.C. R20-6-1203(C) because the Company used HIV-related testing consent forms that
 1. were not approved by the Director prior to use.
 2. failed to offer 10-day consideration period.
 3. failed to disclose that refusal to be tested may be used to deny coverage.
 4. failed to provide information on how the disease is spread.
 5. failed to provide information concerning counseling.
 6. failed to disclose the type of test to be used.
 7. failed to include the required attestation.
 8. failed to include the optional release of information to personal physician.
 9. failed to restrict release of information to 180 days.

- a. A.R.S. § 20-2604(D)(1)(f) because the Company had available for issue variable life insurance policies wherein the cover page failed to identify the owner of the contract.
- b. A.A.C. R20-6-218(B)(1) because variable life application forms used in Arizona had not been included in the Company's filed Exempt Forms Listing.
- c. A.R.S. § 20-2608(3) because variable life application forms used in Arizona did not contain questions sufficient to enable the insurer to determine the suitability of variable life insurance for the applicant.
- d. A.R.S. § 20-448.01(B) because the Company:
 - 1. required the performance of HIV-related tests without first receiving the specific written informed consent of the subject of the test.
 - 2. required the performance of HIV-related tests prior to receiving the specific written informed consent of the subject of the test in a form as prescribed by the Director.
 - a. A.R.S. § 20-2607 because the Company failed to provide the policyholder the required illustration of contractual benefits.
- b. A.R.S. § 20-2110(A) because the Company failed to provide the applicant with the specific reason(s) for an adverse underwriting decision in writing.
- c. A.R.S. § 20- 461(A)(2) because the Company failed with such frequency to provide claim forms, instructions and reasonable assistance within 10 working days as to indicate a general business practice.
- d. A.R.S. § 20-448(A) because the Company failed to pay the correct amount of interest due in accordance with standard Company procedures.
- e. A.R.S. § 20-1233 because the Company used an annuity application form that neither contained notification of a ten day free look nor

advised the applicant of his right to obtain other reasonable information regarding the annuity contract.

- f. A.R.S. § 20-462 because the Company failed to pay interest on a delayed claim settlement.
- g. A.A.C. R20-6-801(C) because the Company failed to maintain adequate documentation within the claim files to allow chronological reconstruction of the pertinent events of the claim.
- h. A.A.C. R20-6-801(E)(4) because the Company failed to provide claim forms, instructions and reasonable assistance within 10 working days.

EXHIBITS

SALES ACTION STEP

Double your sales opportunities with a life insurance retirement plan.

YOUR CLIENT SAYS...

"If something were to happen to me, I would like to know my family would be taken care of. But I'd also like to know that when I retire, I'll be taken care of as well."

YOU RESPOND...

"Let me show you one easy way to accomplish both of these goals. I can help you set up a LIRP—a Life Insurance Retirement Plan which is an all in one tax-favored contract. This plan combines:

- significant tax advantages
- the security of life insurance
- growth potential of managed accounts
- assures continued deposits if disabled"

HOW TO PUT THIS IDEA INTO ACTION

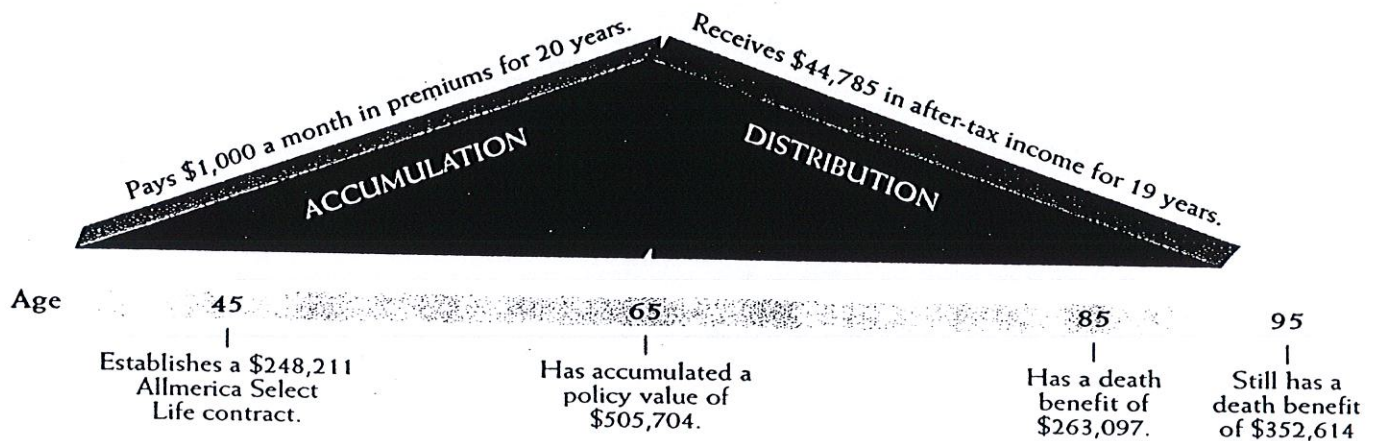
Today, your clients are faced with a disconcerting dilemma. They know they have to take *more* responsibility for their family's future financial security. Yet they have *less* time to manage this responsibility.

That makes this the perfect time to introduce them to the convenience of a Life Insurance Retirement Plan (LIRP). This one plan can help your clients address both short-term and long-term financial needs.

- In the early years of the contract, a LIRP will provide an estate tax-free life insurance benefit—if and when your clients' families need it most.
- In the later years of the contract, a LIRP can enhance your clients' own after-tax retirement income.

Plus, if you structure your clients' LIRP with an Allmerica Select Life Variable Universal Life Policy, you can offer them access to some of the world's leading money managers—on a tax-deferred basis.

HOW ALLMERICA SELECT LIFE CAN ADDRESS A LIFETIME OF NEEDS



This illustration is based on a 45-year-old male non-smoker and assumes a hypothetical 8.27% net rate of return. Please note that clients must be provided an illustration projecting a return of both 0.00% and 8.27% when using this type of sales approach.

Call today for more information on Allmerica Select
1-800-669-7353.

ALLMERICA SELECT
A Higher Standard

EXHIBIT 1
Page 2 of 2

For broker/dealer use only. Not to be distributed or communicated to the public. Allmerica Select Life (variable universal life insurance) and Allmerica Select Inheritance (variable universal survivorship insurance) are issued by Allmerica Financial Life Insurance and Annuity Company (First Allmerica Financial Life Insurance Company in NY) and distributed by Allmerica Investments, Inc., member NASD/SIPC. Allmerica Select is a division of the issuing companies. Allmerica Select Life may not be available in all states.



M E M O R A N D U M

TO: Earl Brown Arizona Insurance Examiner
FROM: Thomas A. Pierce, Jr. Office of the General Counsel N435
DATE: July 13, 2001
SUBJECT: Life/Disability Criticism – Advertising Form AS-465(1/00)

The Company disagrees with the finding that Advertising Form AS-465(1/00) is in violation of ARS Section 20-444. It is not misleading to state that the cash values of a life insurance policy can be used to supplement retirement benefits so long as it is clear that the product being sold is life insurance.

Marketing material must be designed to address the client's needs. The material in question identifies the need for a death benefit and the need for money at retirement. A variable universal life insurance policy can address these needs. The retirement need is addressed through the policy loan or partial withdrawal provisions of the policy. Policy loan provisions are required by ARS 20-2604E and partial withdrawals are recognized; for example, see ARS 20-2604D14.

The investment features of the cash value component of a variable life insurance policy are the principal attributes that differentiate variable universal life insurance from other insurance products. It is the Company's position that it is not misleading to discuss these mandatory features in the context of how those features may be applied to address a policyholder's needs.

It should also be noted that Advertising Form AS-465(1/00) is produced for broker-dealer use only and is not published or circulated before the public. The marketing materials used by our sales representatives, including sales illustrations, contain disclosures that alert the prospect that loans and withdrawals reduce the cash value and death benefit.

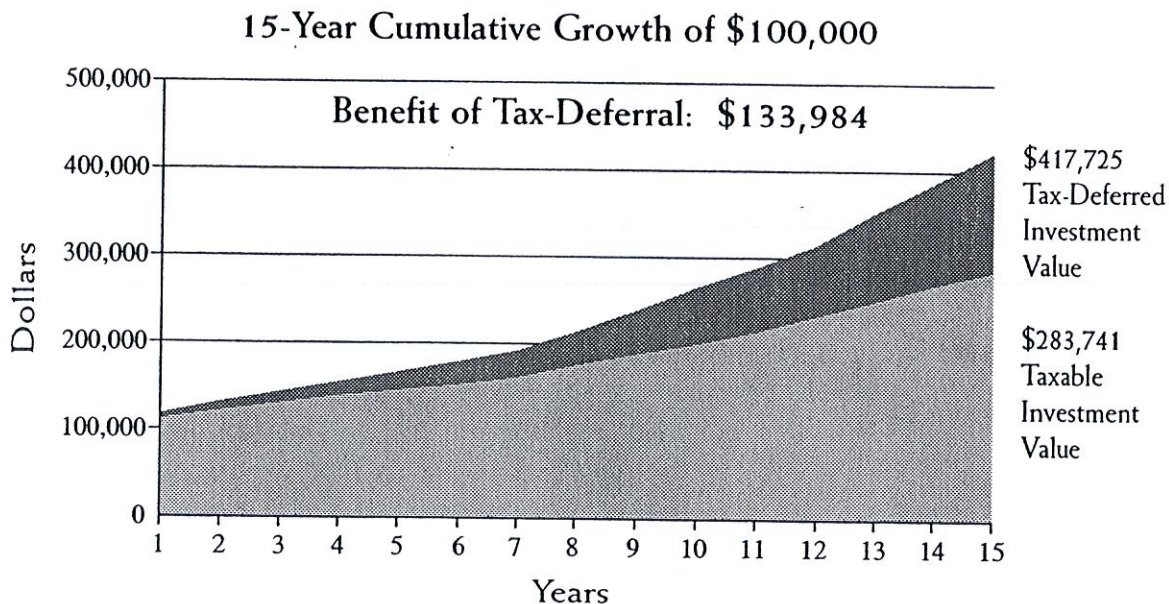
TAP/pak.297
cc: Abigail Armstrong, Esquire

Thomas A. Pierce

EXHIBIT 2

The Power of Tax-Deferred Investing

This hypothetical chart illustrates the value of two \$100,000 investments, each earning a 10% annual rate of return in the 28% tax bracket, for 15 years.* One investment is immediately taxable; its earnings are subject to income taxes each year. The other is tax deferred—no income taxes are paid on earnings until they are withdrawn.



1-800-669-7353

ALLMERICA SELECT
A Higher Standard

* The rate of return is hypothetical and should not be viewed as indicative of any specific investment results. As with all managed investment accounts and annuities, Allmerica Select Resource II carries fees and charges, including a 1.4% charge per year for mortality, expense and administrative charges and a \$30 annual contract fee. A contingent deferred sales charge may apply to withdrawals of amounts invested seven years or less on a declining scale as follows: 6.5%, 6%, 5%, 4%, 3%, 2%, 1%, depending on which year the withdrawal is made. These charges will reduce the tax-deferred value shown above. Withdrawals of tax-deferred accumulations are subject to ordinary income tax. For the example shown would be \$328,762. A 10% IRS penalty may be assessed on earnings withdrawn prior to age 59 1/2.

EXHIBIT 3

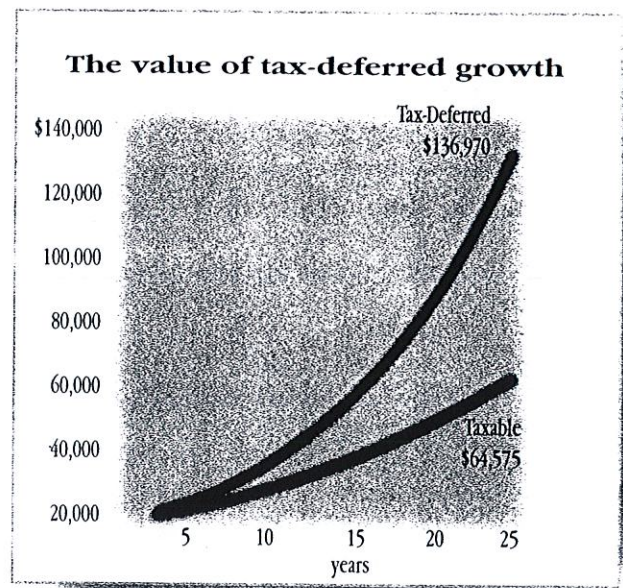
For broker/dealer use only. Not to be distributed to the general public or used in conjunction with product solicitation. Allmerica Select Resource II (variable annuity) is issued by Allmerica Financial Life Insurance and Annuity Company (First Allmerica Financial Life Insurance Company in New York and Hawaii) and distributed by Allmerica Investments Inc., member NASD/SIPC. Allmerica Select is a division of the issuing companies.

Tax advantages help your investments grow at an accelerated rate.

One way to get the most from the money you set aside for tomorrow is to postpone or defer taxes until that money is withdrawn. With ExecAnnuity Plus, 100% of any dividends, interest and capital gains earned inside your policy are protected against current taxes and compound tax deferred.* Because you can have significantly more money working for you each year, the impact is dramatic.

This chart shows two hypothetical \$20,000 investments, each earning an 8% average annual rate of return, with all earnings reinvested. One investment is taxable—its earnings are subject to income taxes each year. (Here, we assume a 40% tax bracket.) The other is tax deferred—no income taxes are paid on earnings until they are withdrawn.

Deferring taxes helps you keep more of what your investments earn. And this can mean thousands more over the long term.



A contingent deferred sales charge may apply to withdrawals of payments from ExecAnnuity Plus which have been credited under the policy for nine years or less as follows: 8%, 8%, 7%, 6%, 5%, 4%, 3%, 2%, 1%. An annual policy fee of \$30 or 3%, whichever is less, will be deducted from a policy account value unless the policy value exceeds \$50,000 or is a 401(k). The variable accounts of ExecAnnuity Plus are subject to a 1.25% mortality and expense risk charge and a 0.20% administrative charge, on an annual basis. These charges have not been deducted and would reduce the tax-deferred value shown above.

EXHIBIT 4

*Interest earnings will be taxed upon withdrawal. The IRS generally imposes a 10% penalty tax on earnings withdrawn before you reach age 59½.

PLEASE READ THIS POLICY CAREFULLY

This is a legal contract between the owner and Allmerica Financial Life Insurance and Annuity Company. Allmerica Financial Life Insurance and Annuity Company agrees, in accordance with the provisions of this policy, to pay the beneficiary the death proceeds upon receipt at the Principal Office of due proof of the insured's death.

This policy is a flexible premium variable life insurance policy. The face amount may be increased or decreased by the owner prior to the final premium payment date. Net premiums may be allocated to the General Account or to one or more sub-accounts of the Variable Account.

POLICY VALUES MAY INCREASE OR DECREASE IN ACCORDANCE WITH THE EXPERIENCE OF THE VARIABLE ACCOUNT SUBJECT TO ANY SPECIFIED MINIMUM GUARANTEES. SEE THE VARIABLE ACCOUNT POLICY VALUE PROVISION ON PAGE 16.

The policy value in the General Account will accumulate interest at a minimum guaranteed rate of 4% annually. Additional interest in excess of the guaranteed rate may be credited at the Company's sole discretion.

THE AMOUNT OF THE DEATH BENEFIT, THE DURATION OF THE DEATH BENEFIT, OR BOTH, MAY BE VARIABLE OR FIXED AS DESCRIBED IN THE BENEFIT AND POLICY VALUE PROVISIONS ON PAGES 13-17.

Allmerica Financial Life Insurance and Annuity Company

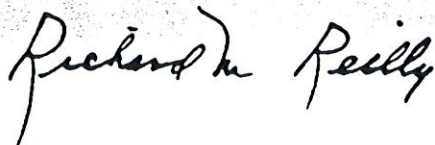
Home Office: DOVER, DELAWARE

Principal Office: 440 LINCOLN STREET, WORCESTER, MA 01653

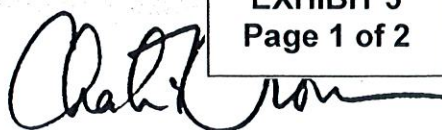
YOUR INSURANCE

Policy

Right to Examine Policy - You may return this policy by mailing or delivering it to the Principal Office or to an agent of the Company within ten days after receiving it, 45 days after you complete Part 1 of the application, or ten days after the Company mails you the Notice of Withdrawal Right. If returned, the policy will be considered void from the beginning and you will receive a refund equal to the sum of (1) the difference between any payments made, including any fees or other charges, and the amounts allocated to the Variable Account, (2) the value of the amounts allocated to the Variable Account on the date the returned policy is received at the Principal Office, and (3) any fees or other charges imposed on the amounts allocated to the Variable Account.



President



Secretary

EXHIBIT 5
Page 1 of 2

This Policy is in a Standard Premium Class

SCHEDULE OF BENEFITS AND PREMIUMS

FORM NO.	SCHEDULE OF BENEFITS	AMOUNT OF BENEFIT
----------	----------------------	----------------------

NOTE: Final premium payment date is shown below. It is possible that coverage will expire prior to the final premium payment date if premiums paid or the earnings credited are insufficient to continue coverage to such date.

Male Insured	John Doe	Age	55
Policy Number	V099995001	Monthly Payment Date	15th
Date of Issue	April 10, 2001	Initial Face Amount	\$50,000
Final Premium Payment Date	April 10, 2040		

EXHIBIT 5
Page 2 of 2

Flexible premium variable life insurance policy. Adjustable sum insured. Death proceeds payable at death of insured. Flexible premiums payable to the final premium payment date. Coverage to the final premium payment date and amount of policy value not guaranteed. Some benefits reflect investment results. Non-participating.

ALLMERICA FINANCIAL LIFE INSURANCE AND ANNUITY COMPANY

Violations of A.A.C. R20-6-218(B)(1) – failure to include forms on Exempt Forms

listing files each year with the Department.

Form Number

1A-97

10465

05372 (9/95)

AS-158 (4-99)

AS-401 8/98

AS-401 4/99

1 JUV-95

SML-1284

SML-1375 Rev. 10/96

EXHIBIT 6

LIFE / DISABILITY CRITICISM

COMPANY: Allmerica Financial Life Insurance and Annuity Company

LINE: Variable life insurance

APPLICATION FORMS: AS-158-95, AS-401 8/98, AS-401 4/99

STATUTE VIOLATED: A.R.S. § 20-2608

A variable life insurance policy application shall contain all of the following:

3) Questions that enable the insurer to determine the suitability of variable life insurance for the applicant.

COMMENTS: The listed application forms do not contain questions adequate to enable the insurer to determine the suitability of variable life insurance for the applicant.

EXAMINER: Earl Brown

DATE:

May 16, 2001

AGREE:

DISAGREE:

X

COMMENTS:

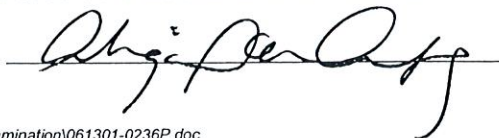
The three application forms noted above are used with Allmerica Select products. They request basic suitability data such as employer name, job responsibilities, annual earned income, annual unearned income, and net worth.

NASD member broker-dealers are governed by the rules of the NASD. These rules include stringent requirements for registered representative licensing, supervision and training. Representatives must "know their customer" and are required to sell clients only products which are suitable for them. NASD member firms must establish a plan of supervision and supervisors must review and approve representative sales. In addition, firms must hold annual compliance meetings with their representatives and must audit their offices on a regular basis. The NASD rules make no distinction between sales of variable life products and other securities in their rules.

Each broker-dealer firm that sells these products enters into a selling agreement with Allmerica Investments, Inc., the distributor of the variable life products offered by Allmerica Select. The terms of the selling agreement indicate that the broker-dealer firm is responsible for the suitability of any product sold by its producers on behalf of the company. Each firm uses its own client questionnaire to collect suitability data related to its clients.

Companies like Allmerica that sell insurance products through unaffiliated broker-dealers must rely on broker-dealer firms to review their representatives' sales practices. These unaffiliated broker-dealers are the only entities which truly know their representatives, their representatives' market practices and their clients. It would be impossible for adequate supervision to be done by an insurance company product manufacturer like Allmerica for Select distribution. The manufacturer is too far removed from the sale and the customer.

COMPANY OFFICIAL:



DAT

EXHIBIT 7



M E M O R A N D U M

To: Earl Brown
From: Abigail M. Armstrong *AWA*
CC: File
Date: 06/28/01
Re: Arizona Market Conduct Examination: Examiner Request EB-36

This memo is in response to your further inquiry of June 27, 2000 regarding suitability. Allmerica Financial closely monitors complaints regarding sales by outside broker-dealer representatives and communicates its concerns by forwarding information to broker-dealer compliance departments. In addition, when members of Allmerica Financial's Customer Relations Department observe what might be a pattern of inappropriate sales practices at a broker-dealer, the Company will communicate its concerns to the broker-dealer firm.

We have been asked by a number of broker-dealers to prepare specific reports to allow them to review their sales more closely. For example, one large broker-dealer asked for a customized replacement report and we are providing it on a monthly basis.

As we have discussed, suitability is currently an area of intense scrutiny by the SEC and NASD. Allmerica Financial is focussing attention and resources on this issue.

TMP/s
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EXHIBIT 8

ALLMERICA FINANCIAL LIFE INSURANCE AND ANNUITY COMPANY

*Violations of A.R.S. § 20-2607– failure to provide an illustration of benefits that
are payable under this policy*

Policy Number

201VS10707600
201VS10568000
201V063944800
201V062407200
201VS10891100
201VS10891000
201VS10852000
201VS10791600
201VS10729500
201VS10729400
201VS10710100
201VS10646800
201VS10639000
201VS10629800
201VS10598400
201VS10574700
201V065553523
201V064142600
201V064142500
201V064006700
201V063942400
201V063808775
201V063787700

EXHIBIT 9

ALLMERICA FINANCIAL LIFE INSURANCE AND ANNUITY COMPANY

*Violations of A.A.C. R20-6-801(C)– failure to record and maintain dates within
these claim files necessary to chronologically reconstruct the claim.*

Policy Number

AN00404763
AN00417625
AN00423180
AN00429459
GN00112246
GN00115299
MN00403813
PN00077029
PN00401219
PQ00078002
VN00404333
VN00405744
VN00407373
VN00410796
VN00414066
VN00415124

EXHIBIT 10

APPENDIX

APPENDIX

ARIZONA REVISED STATUTES

20-443. Misrepresentations and false advertising of policies

A person shall not make, issue or circulate, or cause to be made, issued or circulated, any estimate, illustration, circular, sales material or statement:

1. Misrepresenting the terms of any policy issued or to be issued or the benefits or advantages promised or the dividends or share of the surplus to be received.

20-444. False or deceptive advertising of insurance or status as insurer

A. No person shall make, publish, disseminate, circulate or place before the public, or cause, directly or indirectly, to be made, published, disseminated, circulated or placed before the public, in a newspaper, magazine or other publication, or in the form of a notice, circular, pamphlet, letter or poster, or over any radio or television station, or in any other way, any advertisement, announcement, sales material or statement containing any assertion, representation or statement with respect to the business of insurance or with respect to any person in the conduct of his insurance business, which is untrue, deceptive or misleading.

20-446. Acts tending to result in unreasonable restraint or monopoly of insurance business

No person shall enter into any agreement to commit, or by any concerted action commit, any act of boycott, coercion or intimidation resulting in or tending to result in unreasonable restraint of, or monopoly in, the business of insurance.

20-448.01. Required insurance procedures relating to HIV information; confidentiality; violations; penalties; definitions

A. In this section unless the context otherwise requires:

1. "Confidential HIV-related information" means information concerning whether a person has had an HIV-related test or has HIV infection, HIV-related illness or acquired immune deficiency syndrome and includes information which identifies or reasonably permits identification of that person or the person's contacts.

2. "HIV" means the human immunodeficiency virus.

3. "HIV-related test" means a laboratory test or series of tests for the virus, components of the virus or antibodies to the virus thought to indicate the presence of HIV infection.

4. "Protected person" means a person who takes an HIV-related test or who has been diagnosed as having HIV infection, acquired immune deficiency syndrome or HIV-related illness.

5. "Person" includes all entities subject to regulation under title 20, the employees, contractors and agents thereof, and anyone performing insurance related tasks for such entities, employees, contractors or agents.

B. Except as otherwise specifically authorized or required by this state or by federal law, no person may require the performance of, or perform an HIV-related test without first receiving the specific written informed consent of the subject of the test who has capacity to consent or, if the subject lacks capacity to consent, of a person authorized pursuant to law to consent for that person. Written consent shall be in a form as prescribed by the director.

20-452. Prohibited inducements

Except as permitted in sections 20-453 and 20-454, any insurer, agent, broker or other person, as an inducement to insurance or in connection with any insurance transaction, shall not provide in any policy for or offer, sell, buy or offer or promise to buy, sell, give, promise or allow to the insured or prospective insured or to any other person on behalf of the insured or prospective insured in any manner:

1. Any employment.
2. Any shares of stock or other securities issued or at any time to be issued or any interest therein or rights thereto.
3. Any advisory board contract, or any similar contract, agreement or understanding, offering, providing for or promising any special profits.
4. Any prizes, goods, wares, merchandise or tangible property of an aggregate value of more than ten dollars.

20-461. Unfair claim settlement practices

A person shall not commit or perform with such a frequency to indicate as a general business practice any of the following:

2. Failing to acknowledge and act reasonably and promptly upon communications with respect to claims arising under an insurance policy.

20-462. Timely payment of claims

A. From and after July 15, 1986 any first party claim not paid within thirty days after the receipt of an acceptable proof of loss by the insurer which contains all information necessary for claim adjudication shall be required to pay interest at the

legal rate from the date the claim is received by the insurer. The interest shall be calculated on the amount the insurer is legally obligated to pay according to the terms of the insurance contract under which the claim is being submitted.

20-1233. Free look; annuity contracts

A. Each annuity contract delivered or issued for delivery in this state and each annuity application shall contain a notice prominently printed on or attached to the first page stating that, on written request, an insurer is required to provide within a reasonable time reasonable factual information regarding the benefits and provisions of the annuity contract to the contract holder and that if for any reason the contract holder is not satisfied with the annuity contract the contract holder may return the annuity contract within ten days after the contract is delivered and receive a refund of all monies paid.

B. Notwithstanding subsection A, for variable annuity contracts, the refund under subsection A shall equal the sum of the difference between the premiums paid, including any policy or contract fees or other charges, and the amounts allocated to any separate accounts under the policy or contract, and the value of the amounts allocated to any separate accounts under the policy or contract on the date the returned policy is received by the insurer or its agent.

20-2110. Reasons for adverse underwriting decisions

A. In the event of an adverse underwriting decision the insurance institution or agent responsible for the decision shall either provide the applicant, policyholder or individual proposed for coverage with the specific reason for the adverse

underwriting decision in writing or advise the person that upon written request the person may receive the specific reason in writing and provide the applicant, policyholder or individual proposed for coverage with a summary of the rights established under subsection B of this section and sections 20-2108 and 20-2109.

20-2604. Variable life insurance policy and filing requirements

D. Each variable life insurance policy that is filed for approval in this state shall contain at least the following:

1. The cover page or a page that corresponds to the cover page of each policy that:

(f) Identifies the owner of the contract.

20-2607. Information to applicants

A. An insurer that delivers or issues for delivery in this state a variable life insurance policy shall deliver the following information to the applicant for the policy:

7. Illustrations of benefits that are payable under the variable life insurance contract. The insurer shall prepare the illustrations. The illustrations shall not include projections of past investment experience into the future or attempted predictions of future investment experience. This paragraph does not prohibit the use of hypothetical assumed rates of return to illustrate possible levels of benefits if the illustration makes it clear that the assumed rates are hypothetical only.

B. This section is satisfied if a disclosure that contains the information required by this section is delivered to the applicant. The disclosure shall either:

1. Be a prospectus that satisfies the requirements of the securities act of 1933 (15 United States Code sections 77a through 77aa) and that the securities and exchange commission declares effective.

20-2608. Variable life insurance policy application requirements

A variable life insurance policy application shall contain all of the following:

3. Questions that enable the insurer to determine the suitability of variable life insurance for the applicant.

20-2609. Policyholder reports

An insurer that delivers or issues for delivery in this state a variable life insurance policy shall mail the following reports to each variable life insurance policyholder at the policyholder's last known address:

1. Within thirty days after each anniversary of the policy, a statement or statements of the cash surrender value, the death benefit, any partial withdrawal or policy loan, any interest charge and any optional payments that are allowed under the policy and that are computed as of the policy anniversary date. The statement may be furnished within thirty days after a specified date in each policy year if the information contained in the statement is computed not more than sixty days before the notice is mailed. This statement shall state that the cash values and the variable death benefit may increase or decrease according to the investment experience of the separate account and shall prominently identify any value that the statement describes and that may be recomputed before the next statement required by this section. If the policy guarantees that the variable death benefit on the next policy

anniversary date will not be less than the variable death benefit specified in the statement, the statement shall be modified to indicate this policy guarantee. In addition, the report must show the projected cash value and cash surrender value, if different, as of one year from the end of the period covered by the report. In determining the projected value, the insurer shall assume that the planned periodic premiums, if any, are paid as scheduled, that the guaranteed costs of insurance are deducted and that the net return is equal to the guaranteed rate, or if there is no guaranteed rate, is not greater than zero. If the projected value is less than zero, the statement shall include a warning message that the policy may be in danger of terminating without value in the next twelve months unless additional premium is paid. For flexible premium policies, the report shall contain a reconciliation of the change since the previous report in cash value and cash surrender value, if different, because of payments made, less deductions for expense charges, withdrawals, investment experience, insurance charges and any other charges made against the cash value.

2. An annual statement or statements, including:

(a) A summary of the financial statement of the separate account that is based on the annual statement last filed with the director.

(b) The net investment return of the separate account for the last year and, for each year after the first, a comparison of the investment rate of the separate account during the last year with the investment rate during prior years, up to a total of not less than five years if available.

(c) A list of investments that are held by the separate account as of a date not earlier than the end of the last year for which an annual statement was filed with the director.

(d) Any charges that were levied against the separate account during the previous year.

(e) A statement of any change in the investment objective and orientation of the separate account, in any investment restriction or material quantitative or qualitative investment requirement that applies to the separate account or in the investment advisor of the separate account.

3. For flexible premium policies, if the amounts that are available under the policy on any policy processing day to pay the charges that are authorized by the policy are less than the amount necessary to keep the policy in force until the next following policy processing day, a report that indicates the minimum payment that is required under the terms of the policy to keep the policy in force and the length of the grace period for the payment of that amount.

20-2637. Reports

A. At least once in each contract year after the first contract year, a company that issues individual variable annuities shall mail to the contract holder at the contract holder's last known address a statement reporting the investments that are held in the separate account as of a date not more than four months before the date of mailing. The company shall submit annually to the director on a form prescribed by the national association of insurance commissioners a statement of the business of its separate account or accounts.

B. If payments under an annuity contract have not yet commenced the statement shall contain either:

1. The number of accumulation units that are credited to the contract and the dollar value of a unit.
2. The value of the contract holder's account.

ARIZONA ADMINISTRATIVE CODE (A.A.C.)

R20-6-218. Exemption Standards for Life and Disability Forms

A. Scope

1. Except as hereinafter exempted, this rule shall apply to all life and disability insurance forms that are delivered or issued for delivery in this state except any such forms previously approved by the Department of Insurance prior to the effective date of this rule.
2. This rule shall not apply to:
 - a. Credit life insurance.
 - b. Credit disability insurance.
 - c. Forms with indeterminate, adjustable or higher initial premiums, values or benefits based on other than guaranteed rates except as set forth in (C)(1)(d)(iii) of this rule.
 - d. Mass marketed insurance under A.R.S. § 20-1661.
 - e. Advertising forms.

B. Regulation of exempt forms

1. Each year, on or before June 30, insurers shall file with the Life and Disability Division of the Department of Insurance a verified list of all forms which are

available for issue in the State of Arizona as of June 1 for each year and which are exempt from the filing requirements of A.R.S. § 20-1110 by this rule.

R20-6-801. Unfair Claims Settlement Practices

A. Applicability. This rule applies to all persons and to all insurance policies, insurance contracts and subscription contracts except policies of Worker's Compensation and title insurance. This rule is not exclusive, and other acts not herein specified, may also be deemed to be a violation of A.R.S. § 20-461, The Unfair Claims Settlement Practices Act.

B. Definitions

1. "Agent" means any individual, corporation, association, partnership or other legal entity authorized to represent an insurer with respect to a claim.
2. "Claimant" means either a first party claimant, a third party claimant, or both and includes such claimant's designated legal representative and includes a member of the claimant's immediate family designated by the claimant.
3. "Director" means the Director of Insurance of the State of Arizona.
4. "First party claimant" means an individual, corporation, association, partnership or other legal entity asserting a right to payment under an insurance policy or insurance contract arising out of the occurrence of the contingency of loss covered by such policy or contract.
5. "Insurance policy or insurance contract" has the meaning of A.R.S. § 20-103.

6. "Insurer" has the meaning of A.R.S. § 20-106(C).

7. "Investigation" means all activities of an insurer directly or indirectly related to the determination of liabilities under coverages afforded by an insurance policy or insurance contract.

8. "Notification of claim" means any notification, whether in writing or other means, acceptable under the terms of any insurance policy or insurance contract, to an insurer or its agent, by a claimant, which reasonably apprises the insurer of the facts pertinent to a claim.

9. "Person" has the meaning of A.R.S. § 20-105.

10. "Third party claimant" means any individual, corporation, association, partnership or other legal entity asserting a claim against any individual, corporation, association, partnership or other legal entity insured under an insurance policy or insurance contract of an insurer.

11. "Worker's compensation" includes, but is not limited to, Longshoremen's and Harbor Worker's Compensation.

C. File and record documentation. The insurer's claim files shall be subject to examination by the Director or by his duly appointed designees. Such files shall contain all notes and work papers pertaining to the claim in such detail that pertinent events and the dates of such events can be reconstructed.

E. Failure to acknowledge pertinent communications

4. Every insurer, upon receiving notification of claim, shall promptly provide necessary claim forms, instructions, and reasonable assistance so that first party claimants can comply with the policy conditions and the insurer's reasonable requirements. Compliance with this paragraph within 10 working days of notification of a claim shall constitute compliance with paragraph (1) of this subsection.

R20-6-1203. Testing for HIV; Consent Form

C. The written consent form, which shall be approved by the Director in advance of its use, shall contain the following information:

1. Purpose of the consent form. The form shall contain a clear disclosure that the test to be performed is a test for the presence of HIV antibodies, antigens, or the virus, and that underwriting decisions will be based on the results of such test. The form shall further provide notice of a period of not less than 10 days during which the applicant may decide whether or not to sign the form, along with a disclosure that the applicant's refusal to be tested may be used as a reason to deny coverage.

2. Information on HIV. The form shall provide clear, concise, and accurate information on how the disease is spread and what behavior places persons at risk of contracting the virus.

3. Pretest counseling considerations. The written consent form shall contain information advising the applicant that counseling is recommended by many

public health organizations and that the applicant may obtain such counseling at the applicant's own expense. The form shall contain current information as provided by the Department regarding the availability in Arizona of free confidential or anonymous counseling through county health departments and through other governmental or government-funded agencies.

4. Disclosure of test results. The form shall advise the applicant that all test results shall be treated confidentially and that results shall be released only to the applicant and the named insurer or upon the applicant's written consent or as otherwise required or allowed by law, including but not limited to the release of information to the Department of Health Services as provided by law.

5. Meaning of positive test results. The form shall advise the applicant of the type of test (including but not limited to antibody, antigen, or viral culture) to be used, and that a positive test result indicates that the applicant has been infected with HIV but does not necessarily have AIDS. The form shall explain that a positive test result will adversely affect the application for insurance.

6. Consent. The consent form shall contain an attestation to be signed by the applicant or, if the applicant lacks legal capacity to consent, a person authorized pursuant to law to consent on behalf of the applicant, that he or she has read and understands the written consent form and voluntarily consents to the performance of a test for HIV and to the disclosure of the test results as described in the consent form. The applicant or the applicant's legal

representative shall have the right to request and receive a copy of the written consent form. A photocopy of the form shall be as valid as the original.

7. Optional release of information to personal physician. In addition to the release of information to the insurer provided in the consent form, the applicant may, at the applicant's option, consent to the release of information to the applicant's personal physician. The form shall provide for such release to be separately signed and dated by the applicant, or if the applicant lacks legal capacity to consent, by a person authorized pursuant to law to consent on behalf of the applicant.

8. Time period during which release of information is effective. The consent form shall specify the time period during which any and all release provisions of the consent form shall be effective, but in no case shall such time period exceed 180 days from the date the consent form is signed by the applicant or the applicant's legal representative. No HIV-related information shall be released to any person after the expiration of that time period unless the insurer obtains the express written consent, pursuant to R20-6-1204, of the applicant or, if the applicant lacks legal capacity to consent, by a person authorized by law to consent on behalf of the applicant.