

1 **CERTIFIED MAIL**  
2 **RETURN RECEIPT REQUESTED**  
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4

5 **STATE OF ALASKA**  
6 **DEPARTMENT OF COMMERCE, COMMUNITY, & ECONOMIC DEVELOPMENT**  
7 **DIVISION OF INSURANCE**  
8 **550 West Seventh Avenue, Suite 1560**  
9 **ANCHORAGE, ALASKA 99501-3567**  
10

11  
12 **ORDER # MCE P-10-03** ) Order under the Provisions of  
13 ) AS 21.06.150(b), approving  
14 In the matter of the Market ) the Report on Market Conduct  
15 Conduct Examination of ) Examination.  
16 **Leonard William Brown, Jr.** )  
17 \_\_\_\_\_ )  
18

19 The Director of Insurance for the State of Alaska, Linda S. Hall, issues this order  
20 adopting the Report of Targeted Market Conduct Examination of Leonard William Brown, Jr.  
21 (Mr. Brown), 9638 SW Bunker Trail, Vashon Island, Washington based upon the following  
22 findings:  
23

24 **FINDINGS OF FACT**

25 **Finding No. 1.**  
26

27 Mr. Brown is a licensed non-resident life and health insurance producer, located on  
28 Vashon Island, Washington, license number 22419. Mr. Brown is subject to examination under  
29 Alaska Statute (AS) 21.06.130.  
30

31 **Finding No. 2**  
32

33 The Notice of Examination was presented to the examinee on March 16, 2010, which  
34 outlined the scope of the examination.  
35

36 **Finding No. 3.**  
37

38 A Targeted Market Conduct Examination of Mr. Brown for the period August 1, 2009  
39 through March 16, 2010 was conducted between April 1, 2010 and December 1, 2010. During  
40 the examination, consideration was given to findings obtained in a 2009 examination of Mr.  
41 Brown. The 2009 examination covered the period from September 1, 2008 through March 5,  
42 2009. Mr. Brown's records were reviewed in the division's Juneau offices and work was  
43 completed on December 1, 2010.  
44

1 Finding No. 4.

2  
3 A Report of Targeted Market Conduct Examination of Mr. Brown on compliance with  
4 Alaska laws and matters enumerated in the Notice of Examination was presented to the examinee  
5 on January 14, 2011, and filed with the Division of Insurance in accordance with  
6 AS 21.06.150(b).  
7

8 Finding No. 5.

9  
10 Mr. Brown was afforded the opportunity to respond within 30 days to the Division of  
11 Insurance concerning matters contained in the Report of Targeted Market Conduct Examination  
12 pursuant to AS 21.06.150(b). Although Mr. Brown provided general comments regarding the  
13 report in an email to the division, dated February 11, 2011, he did not comment on the report  
14 findings within the 30 days allowed.  
15

16 After failing to receive a timely response from Mr. Brown, the division wrote on March  
17 18, 2011 to advise him of actions and proposed settlement options. Upon receiving the  
18 division's March 18, 2011 letter, Mr. Brown asked for more time to respond and requested a  
19 meeting in Juneau with the division's examination team (Katie Campbell, Life/Health Actuary,  
20 & Donald E. Hale, Insurance Specialist II). This request was granted and Mr. Brown met with  
21 the examination team on April 19, 2011. During the April 19, 2011 meeting, Mr. Brown did not  
22 offer any formal objection or rebuttal to the report findings. At the conclusion of the meeting,  
23 Ms. Campbell granted Mr. Brown additional time to respond in writing to the report findings.  
24

25 On May 13, 2011, the division received Mr. Brown's written response to the examination  
26 report (via email). This message was responsive to the report findings. However, the division  
27 notes that while Mr. Brown offered reasons for his actions (i.e. his national marketing firm's  
28 training) and disagreed with certain report findings/conclusions, he offered no formal evidence in  
29 support of his position and presented remedial actions he was taking to become compliant with  
30 Alaska insurance law.  
31

32 Finding No. 6.

33  
34 The Director of Insurance has fully considered and reviewed to the extent that she  
35 considered necessary the Report of Targeted Market Conduct Examination, the written (& oral)  
36 response from Mr. Brown, and any relevant portion of the examiner's work papers.  
37

38 Finding No. 7.

39  
40 The examination of Mr. Brown was conducted in accordance with applicable Alaska law.  
41 The report is a factual account of the findings of the examiners based on tests that determine  
42 compliance with Alaska laws and supported with appropriate documentation.  
43  
44

1 **CONCLUSIONS OF LAW**

2  
3 **Conclusion No. 1.**

4  
5 The examination report was filed with the division and transmitted to Mr. Brown in  
6 accordance with AS 21.06.150(b).

7  
8 **Conclusion No. 2.**

9  
10 After reviewing the report and considering Mr. Brown's responses, I conclude that the  
11 examination report cites sufficient evidence to proceed with administrative enforcement action  
12 for conduct described in the report that may violate Alaska insurance laws. These violations  
13 have been settled by Stipulated Agreement and Order No. D 11-14, dated September 19, 2011.

14  
15 **Conclusion No. 3.**

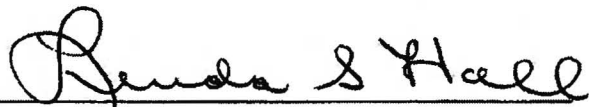
16  
17 An order should be issued in accordance with AS 21.060150(b) approving the  
18 examination report.

19  
20  
21 **ORDER**

22  
23 It is hereby ordered that under AS 21.06.150(b) the attached Report of Targeted Market  
24 Conduct Examination of Mr. Leonard William Brown, Jr. dated January 14, 2011, is approved,  
25 and directed that Mr. Brown's responses be noted, but not made a part of the examination report.

26  
27 This order is effective September 20, 2011,

28  
29 Dated this 20th day of September 2011, at Anchorage, Alaska.

30  
31  
32   
33 Linda S. Hall  
34 Director  
35  
36

**STATE OF ALASKA  
DEPARTMENT OF COMMERCE COMMUNITY  
AND ECONOMIC DEVELOPMENT**

**DIVISION OF INSURANCE**

**REPORT OF TARGETED MARKET CONDUCT EXAMINATION  
OF**

**Leonard W. Brown  
9638 SW Bunker Trail  
Vashon Island, WA 98070**

**MCE P-10-03**



**Submitted by  
Katie Campbell  
Life/Health Actuary  
January 14, 2011**



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DEPARTMENT OF  
**COMMERCE**  
COMMUNITY AND  
ECONOMIC DEVELOPMENT

Division of Insurance

January 14, 2011

Linda S. Hall  
Director, Division of Insurance  
Department of Commerce, Community and Economic Development  
550 West 7<sup>th</sup> Avenue, Suite 1560  
Anchorage, AK 99501-3567

Pursuant to Alaska Statute AS 21.06.130, the Alaska Division of Insurance performed a targeted market conduct examination (record review) of Insurance Producer Leonard W. Brown, Alaska License No. 22419, for insurance business he transacted in Alaska. In accordance with AS 21.27.350 (e), Mr. Brown copied requested records and forwarded them to the Alaska Division of Insurance (Division) for review in the Juneau Office. Katie Campbell, Life/Health Actuary, and Don Hale, Insurance Analyst, performed the examination. Along with the requested records, Mr. Brown provided a signed certification that stated that the information submitted, "is true and complete".

### **SCOPE OF TARGETED MARKET CONDUCT EXAMINATION**

This examination of Mr. Brown's files is the scheduled follow-up to a similar examination conducted by the Division in 2009. The Division conducted the 2009 examination in response to complaints received by the Division. Based on findings from the 2009 examination the Division determined that this follow-up examination was in needed in order to ascertain Mr. Brown's compliance with 3 AAC 26.750-769, (Annuity Disclosure), 3 AAC 26.770-789 (Annuity Suitability), 3 AAC 26.790-819 (Life and Annuity Replacement), 3 AAC 26.820-825 (Senior-Specific Certifications and Professional Designations), AS 21.79.160 (Life and Health Guaranty Association), AS 21.36.030 (Misrepresentation), and AS 21.36.100 (Rebates).

### **Subject Matters Reviewed**

The examination involved a review of Mr. Brown's insurance records, seminar announcements, Mr. Brown's statements made during one of his advertised seminars, Mr. Brown's responses to questions during a phone interview, and responses by Mr. Brown's clients to a questionnaire regarding their transaction with Mr. Brown.

### **Time Frame**

The examination covered insurance transacted by Mr. Brown during the period August 1, 2009 through March 16, 2010 with consideration given to records from the 2009 examination, which included transactions during the period from September 1, 2008 through March 5, 2009.

## **METHODOLOGY**

On March 16, 2010, Katie Campbell, wrote Mr. Brown advising him that pursuant to Director Linda Hall's July 21, 2009 letter to him, the Division was conducting a "follow-up investigation of his records" to determine his compliance with Title 21, the Alaska Insurance Code. The Division instructed Mr. Brown to provide the following items.

1. A copy of all documentation relating to each recommendation made to an Alaskan Consumer from August 1, 2009 to March 16, 2010, related to the purchase of an annuity, whether or not a sale occurred
2. All information provided to or received from an Alaskan consumer and all notes, work papers, and all other material in Mr. Brown's records relating to the consumer and his recommendations to the consumer
3. A copy of all information provided to Alaskans at Mr. Brown's seminars.
4. Any available seminar audio recordings
5. A signed copy of a certification that the information submitted "is true and complete"
6. A valid e-mail address

Mr. Brown responded timely with the requested information including 26 client files. Some of the files submitted contained multiple annuity sales. Mr. Brown provided four additional client files upon discovery by the Division that they were not provided.

### **The following are the procedure steps for the Targeted Examination:**

1. The Division reviewed each client file using a checklist created by the Division that outlines the applicable statutory and regulatory requirements.
2. The Division reviewed Mr. Brown's seminar announcements, seminar booklet, and an audio recording of his February 2010 seminar and the seminar materials.
3. The Division sent questionnaires to 20 of Mr. Brown's clients to obtain information directly from his clients about their transaction with Mr. Brown. The Division received only five responses to the questionnaires.
4. On September 20, 2010, the Division met with Mr. Brown by conference call to discuss the issues and questions raised during the Division's review of his client files, seminar materials and recordings, and responses from his clients to the Division's questionnaire.

## **FINDINGS AND REQUIRED ACTIONS**

<b>License requirements (Violations noted)</b>
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AS 21.27.010, AS 21.27.115, and AS 21.27.530 (3)
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### ***Requirement:***

A person may not sell, solicit, or negotiate insurance without the appropriate license and line of authority.

### ***Finding #1***

The Division found that Mr. Brown provided advice on variable annuities that constitutes the sale or negotiation of variable contracts without proper variable contract authority. This finding is based upon

1. Written statements documented in three client files in which clients exchanged or applied to exchange variable annuities for equity-indexed annuities recommended by Mr. Brown:
  - a. Mr. Brown wrote the following in the "appointment summary" document in client file #8, "(I) specifically asked her if she was OK giving up \$36K in death benefit. She said absolutely, she wanted to get out & (start) making \$ without all the fees attached to variable."
  - b. Mr. Brown wrote the following in the replacement form in client file #8, "(she) wants better growth, less cost, more safety of principal";
  - c. Mr. Brown wrote the following in the replacement form in client file #16, "Variable annuity is losing value & has risk" and "Variable annuity exposes applicant to risk".
  - d. In client file #4 Mr. Brown wrote the following in the replacement form "Poorly Performing and want security of fixed" and the following in the "Client Recommendation Documentation Summary" "take risk out of variable annuities & get nice bonus \$".
2. Mr. Brown's responses to questions during the interview:
  - a. In response to a question regarding the analysis Mr. Brown performs when making a recommendation to replace a variable annuity contract, Mr. Brown stated: "I ask them (clients) for a copy of the variable annuity, I read through it thoroughly, and I call the company of the variable annuity, I make sure I understand the fees, the cost, and I pretty well understand it inside and out."
  - b. In response to a question regarding the advice given to the client #8 referenced above regarding the variable annuity death benefit feature, Mr. Brown stated
    - i. "I was very, very clear with her, asking her if she wanted to give that up. Yes."
    - ii. "I asked her what was her goal, and the goal was to end the volatility of the product she currently had, (for) something that had much better opportunity to make more money in a volatile market, like it is right now, and in this product (Allianz MasterDex X) she made 12% in the first year."
    - iii. "Who knows how much that variable annuity would have been worth today, with the market like it is, if she wanted to take money out of it. It could have been way less, right?"
  - c. In response to a question regarding what he says about variable annuities during his seminar he stated "The mortality, exchange fees, and management fees. (Unintelligible) what an exchange fee is." When asked about what he says about fees he stated, "Just that they are high. So I explain that the mortality and exchange fees pay for a guarantee at death for the principal." When asked if this was discussed in his seminars he said, "Yes. I find most people don't understand their variable annuities at all. In fact most people don't know they are paying fees."

### ***Required Action***

Mr. Brown must obtain Alaska variable contract authority prior to giving any advice related to variable contracts including making a recommendation to exchange or surrender a variable contract.

**Misrepresentation  
(Violations noted)**

**AS 21.36.030(1)**

***Requirements***

Under AS 21.36.030 (1) "A person may not make, issue, circulate, or broadcast any form of communication that misrepresents the benefits, advantages, conditions, sponsorship, source, or terms of an insurance policy".

***Finding #2***

**Finding # 2A**

The Division found that Mr. Brown misrepresented the benefits of the equity-indexed annuities he sells. The equity-indexed annuities that Mr. Brown sells pay a bonus on premiums paid during the bonus period. For example, the Allianz annuity pays a 10% bonus on premiums received in the first three years, but none of the bonus is vested during the first year and only 1% is vested each year thereafter until the full 10% bonus is vested in the 11<sup>th</sup> year. In addition, withdrawals during the surrender period may result in loss of some or the entire bonus. Therefore, the 10% bonus interest is not earned in the first year. The Division found that Mr. Brown falsely told consumers that the annuities he sold paid interest at "12.25%", "12.5%-14.5%", "7%-9%" and "12%". This finding is based upon

1. Mr. Brown's seminar announcement and statements made during his February 2010 seminar
  - a. When an attendee asked him what are the ranges of interest rates being paid on fixed annuities, Mr. Brown responded, "I've got one that will pay 12.25% for the first year."
  - b. During the seminar Mr. Brown stated, "Nothing makes me feel better when I am calling up one of my clients after a year and telling them they have just made 12.5% or 14.5% interest in their first year on their annuity, when all their friends are crying in their soup about how much money they have lost. I sleep real good at night because of that."
  - c. A 2010 seminar announcement includes the statement "LEARN HOW TO:..How to secure a guaranteed cash flow of 7-9%". However, during the interview when asked to explain how bonus equity indexed annuity (EIA) returns compare overall with traditional annuities or EIAs without the bonus, Mr. Brown stated "I don't do that because that kind of suggests a performance. And, I really don't want to mislead people into thinking they're going to get a performance based on the projections I am showing them." When asked if he gave the clients any kind of expectation of what they can earn under different annuity types, he said, "I do not, we talk about the first year".
2. Mr. Brown's responses to interview questions:
  - a. When asked why, with the exception of two or three files, every client selected the fixed account; Mr. Brown said, "Especially, in last year's numbers, getting 12% interest in the first year is pretty good."
  - b. When asked about giving investment advice, Mr. Brown said, "I asked her what was her goal, and the goal was to end the volatility of the product she currently had, (for)



something that had much better opportunity to make more money in a volatile market, like it is right now, and in this product (new annuity) she made 12% in the first year, and it's got 100% death benefit." In response to a question regarding how he came up with 12%, Mr. Brown explained "There was a 10% bonus and 2% fixed, I think it was even better than that actually."

#### **Finding #2B**

The Division found that Mr. Brown indirectly through his wife, Ms. Leeann Brown, misrepresented how the commission he is paid by the insurers is funded. This finding is supported by a statement made by Ms. Leeann Brown during the seminar that, "We get paid by the insurance company; it does not come out of your money." This is incorrect because the surrender charge is designed to pay for commissions and related contract expenses.

#### ***Required Actions***

Mr. Brown must immediately refrain from misrepresenting how commissions are funded and the interest rate return on annuities he sells and must modify his seminar announcements and materials used during the seminar to correct or remove the references to the interest rate returns.

<b>False Information, advertising (Violations noted)</b>
--

<b>AS 21.36.040</b>
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#### ***Requirements***

Under AS 21.36.040 "A person may not make, publish, disseminate, circulate, or place before the public, or cause, directly or indirectly, to be made...and advertisement, announcement, or statement containing an assertion, representation, or statement with respect to the business of insurance or with respect to a person in the conduct of the person's insurance business, that is untrue, deceptive, or misleading"

#### **Finding #3**

##### **Finding #3A**

The Division found that Mr. Brown made false and misleading statements regarding the qualifications of the Brown Agency to give investment advice. This is supported by a statement made during the seminar in which Mr. Brown stated, "I watch all this stuff, but I am not in it, as I am not licensed to talk to you about it, LeeAnn is". However, although LeeAnn Brown has a Certified Financial Planner (CFP) designation, she is not a registered investment advisor, she has not been registered with the SEC since March 10, 2009 and has never been registered with the Alaska Division of Banking and Securities. Therefore, LeeAnn Brown is not licensed to give investment advice as stated by Mr. Brown.

##### **Finding #3B**

The Division found that Mr. Brown's seminar announcement and booklet titled "A CONFIDENT FINANCIAL FUTURE *Guiding you through the financial maze*" misrepresented the seminars to consumers as follows:

1. The title of the seminar announcement is "2010 Update of Income Taxes, Federal & Estate Taxes" and the announcement focuses primarily on federal tax laws. However, Mr. Brown is not a tax accountant or tax attorney and did not provide tax advice during his February 2009

seminar. In response to an interview question regarding how he explains the tax implications of annuities, he stated, "Well, I pretty much stay out of that because I tell people right up front that I am not a tax accountant, and if they want to receive information about taxes, they should go consult the person that does their taxes. I'm very upfront about that."

2. The announcement fails to disclose that the purpose of the seminar is to sell insurance and that he is licensed to sell insurance only.
3. The announcement fails to disclose that neither he nor his wife is licensed to sell or give advice on investments.
4. The booklet title is misleading in that it fails to accurately describe the purpose of the seminar, which is to sell insurance. In addition, the booklet is misleading as to Mr. Brown's qualifications and his business. In the BIOGRAPHY section Mr. Brown states "Bill has been extremely successful in his financial services career..." and no mention is made in this section that Mr. Brown is a licensed insurance producer and this section does not reference insurance, but rather states "assisted over a thousand individuals and families sleep better knowing that their retirement assets are protected and growing" and "discussing safe money strategies". However, Mr. Brown is only licensed to sell insurance and neither Mr. nor LeeAnn Brown is licensed to sell securities.

#### ***Required Actions***

Mr. Brown must immediately refrain from making misleading statements including those identified above.

Mr. Brown must modify his seminar announcements and materials used during the seminar and The Brown Agency website ([www.safesecuremoney.com](http://www.safesecuremoney.com)) to make clear the true purpose of the seminar and his and LeeAnn Brown's qualifications.

#### **Unfair financial planning practices (Violations noted)**

**AS 21.36.145**

#### ***Requirement***

AS 21.36.500 states, "A person may not represent, directly or indirectly, to be a financial planner, investment adviser, consultant, financial counselor, or similar specialist engaged in the business of giving financial planning or advice relating to investments, insurance, real estate, tax matters, or trust and estate matters when the person is in fact only engaging in the sale of insurance."

#### ***Finding#4***

Mr. Brown is licensed only to sell insurance and sells almost exclusively annuities and neither Mr. Brown nor Leeann Brown is registered with the SEC or with the Alaska Banking and Securities Division to provide investment advice or sell securities. Leeann Brown has a Certified Financial Planner (CFP) designation only. However, Mr. Brown indirectly represents himself to be financial planner, consultant, or counselor. This finding is based on:

1. Documents in the client files in which most of the 30 client files contained a document for clients to complete titled "Financial Planning Information" and Mr. Brown's form titled

"Response Sheet: Please contact me" that is provided to consumers to schedule a consultation includes the question "Name of mutual funds for review".

2. Mr. Brown's seminar announcement that states
  - a. "BANKS: Advantages and disadvantages", "HOW TO: Increase your spendable income", "IRA/401K Owners: Increase Your Income", "How to find safe alternatives to my low CD's and Money Market Accounts" and "How to avoid worrying about market volatility" and other statements. However, the seminar announcement does not mention annuities.
  - b. "TAXES: How to lower or eliminate taxes". However, neither Mr Brown not Leeann Brown are qualified to or provide tax advice.
3. Mr. Brown's booklet titled "A CONFIDENT FINANCIAL FUTURE *Guiding you through the financial maze*" which he provides to consumers that attend the seminar. This booklet contains numerous statements in which Mr. Brown represents himself directly or indirectly to be a financial planner, investment adviser, consultant, financial counselor, or similar specialist. Examples include
  - a. The title of the booklet itself
  - b. In the BIOGRAPHY section Mr. Brown states "Bill has been extremely successful in his financial services career..."
  - c. The discussions on "THE SEVEN COMMON FINANCIAL TOOLS", "FINANCIAL TOOLS", "SAVINGS TOOLS", "GOALS FOR RETIREMENT MONEY", "S&P MARKET TRENDS", "What are some things that can have a negative impact on the stock market?" and in the check list section of the booklet the list of items provided without charge during a consultation includes "TAX POINTERS FOR SENIORS You may be paying more in taxes than necessary" and "ADDITIONAL PORTFOLIO REVIEW Let us address and evaluate any additional aspects of your finances that you desire."
4. Mr. Brown's response to an interview question in which Mr. Brown stated, "They understand that this is a long range product and they are all totally OK with taking 4% or 5% out per year and they understand that is what most financial planners recommend anyway, using that in fact for income".

#### ***Required Actions***

Mr. Brown and The Brown Agency may not directly or indirectly represent or imply to the public in that Mr. Brown provides or is qualified to provide financial planning, investment, tax or estate planning advice and must

1. modify all seminar announcements and their website ([www.safesecuremoney.com](http://www.safesecuremoney.com)) accordingly and include a statement in large font, that Mr. Brown and The Brown Agency sells insurance, primarily annuities and that Mr. Brown is not licensed or qualified to provide financial planning, investment, tax or estate planning advice.
2. disclose at the beginning of each seminar that Mr. Brown is licensed to sell insurance products only and that the purpose of the seminar is to solicit or obtain appointments for insurance products, specifically annuities and clarify that although LeeAnn Brown is also licensed to sell insurance and is a certified financial planner, she is not qualified to provide investment advice or sell securities.



3. disclose to consumers that meet individually Mr. Brown that Mr. Brown is licensed to sell insurance products only and that insurance is what will be discussed with the consumer; and document such disclosure in the records.

Mr. Brown must not provide client-specific tax or legal advice to consumers unless he obtains the proper qualifications and must not state or imply that he or The Brown Agency will provide such advice in the seminar or during an individual consultation, unless a qualified advisor is made available and provides such advice.

**Compliance with record requirements in relation to suitability in annuity transactions, life insurance and annuity replacements, and annuity disclosures  
(Violations noted)**

**Bulletin B09-07**

**3 AAC 26.780; AS 21.09.320; AS 21.27.350**

***Requirements***

AS 21.27.350 states, "A licensee shall document each action taken in regard to an insurance transaction. The documentation must contain all notes, work papers, documents, and similar material, and be in sufficient detail that relevant events, the dates of those events, and all persons participating in those events can be identified."

3 AAC 26.780 states "An insurer shall comply with the requirements of AS 21.27.350 with respect to all information collected from a consumer and other information used in making a recommendation that was the basis for an insurance transaction".

Bulletin B09-07 clarifies that a licensee's records must contain "Detailed documentation of an insurer's and/or insurance producer's analysis and grounds for believing that a recommendation is suitable, and detailed documentation that the insurer and/or producer have made reasonable efforts to obtain the necessary information to make a suitable recommendation."

The 2009 examination-closing letter to Mr. Brown stated, "A recommendation made to a client is an action that must be documented. However, your records do not include documentation that supports the recommendation you made to each client, such as your analysis of: 1) each client's financial and investment status and objectives; 2) the various options available to meet each client's specific needs and objectives; and 3) why you believe the annuity that you ultimately recommended was suitable for the client."

***Finding#5***

Although Mr. Brown created and began using a "Client Recommendation Documentation Summary" in response to the Division's 2009 examination findings, the Division found that Mr. Brown failed to document each client's objectives consistently and completely; and/or failed to adequately document support for the recommended annuity. The following support this finding:

- a. In 9 client files Mr. Brown did not document client's objectives.
- b. In 4 client files Mr. Brown did not document any support for his recommendation.

- c. In 21 of 30 client files, Mr. Brown did not adequately explain how the recommended annuity met clients' objectives. In most of these 21 files, Mr. Brown gave features of the annuity, commonly, the 10% bonus or access to 10% per year, as support for his recommendation instead of his analysis of how the annuity met the objectives of the client in light of the client's financial and investment status.
- d. In the interview with Mr. Brown, Mr. Brown was asked about incomplete financial information in the client files, and whether he asks questions and does not document answers on the first appointment form and Mr. Brown stated, "I sometimes don't take the best notes and yes I am absolutely asking them questions, how they want their money to grow, how they are going to access it, how they are planning on spending it, or if they're not, cause as you know, a lot of people are planning to pass their money on. You know I ask them about what are their goals for using the money. Absolutely, I do that for everyone." Despite this response, none of the client files contains documentation that Mr. Brown asked, received, analyzed and considered this information in making a recommendation.

***Required Actions:***

Mr. Brown must keep complete and accurate records of all insurance transactions including any representations made before, during and after a sale, including in seminars, in individual solicitations, and in applications and supporting documents. Mr. Brown must review Bulletin B09-07 and referenced statutes and comply with the documentation requirements for records related to his insurance transactions including the suitability in annuity transactions, replacements of life insurance and annuity products, and annuity disclosures. In particular, Mr. Brown must consistently and fully document for each transaction

1. The client's financial status, tax status, investment objectives, and all other relevant information needed in order to make a suitable recommendation including the client's short and long term need for income
2. His analysis of the above information including how the information was considered in making his recommendation including such analysis as how the free withdrawal amount compares with the consumer's need for income
3. His recommendation and how he determined that the recommendation was suitable

Mr. Brown should develop procedures and controls to ensure compliance with the documentation requirements.

<p><b>Suitability: Duties of an insurance producer (Violations noted)</b></p>
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**3 AAC 26.775**

***Requirements:***

An insurance producer must have reasonable grounds for believing that his/her recommendations are suitable for the consumer, based on the facts disclosed by the consumer as to the consumer's financial situation, needs, investments, and other insurance products. An insurance producer must make an effort to obtain 1) the consumer's financial status; 2) the consumer's tax status; 3) the consumer's investment objectives; and 4) other information used or considered necessary for making a recommendation to the consumer.

Although not specifically stated in 3 AAC 26.775, "reasonable grounds" for believing the recommended product is suitable clearly requires that the insurance producer not only make an effort to obtain the information described above but must also:

1. make an effort to ensure that the information obtained from a consumer is accurate and complete
2. analyze and use that information in making a recommendation;
3. provide complete and accurate information to the consumer; and
4. make an effort to assure that the consumer understands all features of the product the producer sells, solicits or negotiates.

#### ***Finding #6***

##### **Finding #6A**

Mr. Brown created three different forms to collect and/or document his collection of the required information: "Financial Planning Information", "Client Documentation Summary" and "First Appointment Questionnaire". However, the Division found evidence that in the majority of client files Mr. Brown failed to review significant and relevant financial information and objectives for accuracy and completeness. This finding is based on the following:

1. 19 of the 30 client files from the follow-up examination show missing, inconsistent or inaccurate financial information. The following examples illustrate this:
  - a. In client file #10:
    - i. Income and expense data on "Allianz Product Suitability" form does not match the income and expense data on the "Financial Planning Information" form.
    - ii. In the "Allianz Product Suitability" form, net worth equals liquid assets with liquid assets incorrectly including real estate and non-liquid securities and retirement accounts.
    - iii. Although Mr. Brown documented the client's assets in the "Client Recommendation Documentation Summary" form, these assets do not match the assets reported in the "Allianz Product Suitability" form. Liquid assets documented by Mr. Brown were \$37,000 compared with \$1.78 million in the suitability form.
  - b. In client file #23:
    - i. In the "Allianz Product Suitability" form, net worth equals liquid assets with both net assets and liquid assets incorrectly including the full death benefits instead of the cash values of two life insurance policies. The life insurance death benefits represented \$400,000 of the total \$493,523 in assets. Therefore, both net worth and liquid assets were significantly overstated.
    - ii. In the "Financial Planning Information" form, Mr. Brown recorded two life insurance policies totaling \$400,000 in death benefit, but did not record the cash value of the policies.
    - iii. In the "Client Recommendation Documentation Summary" form, Mr. Brown documented \$500,000 in net worth, which incorrectly includes the \$400,000 in death benefit.
    - iv. Also in the "Allianz Product Suitability" form, liquid assets included the retirement account funds used to purchase the annuity. The form clearly states that these funds should not be included. This resulted in an additional overstatement of liquid assets.
    - v. In the "Client Recommendation Documentation Summary" form, Mr. Brown documented \$40,000 in liquid assets compared with \$493,523 included on the

company form submitted with the application and therefore the information provided to the insurer was inaccurate.

2. Mr. Brown's responses to questions during the interview:
  - a. When asked about apparent inaccuracies in client financial data, Mr. Brown stated, "I just go on what people tell me. At some point I've got to trust what they're telling me."
  - b. When asked about whether he questions clients about the data on the financial planning questionnaire, Mr. Brown stated, "Yes, I do, I'll question them sometimes" and "Some of my clients that are still working, the financial information they are giving me is still a work in progress." When asked if he meant he may not have all of the information for those still employed, Mr. Brown stated, "Sometimes that is true, they don't have the information with them, and they are not able to come up with it because you know, some of it is in their lake cabin at Big Lake, and another is down in Juneau, you know a lot of Alaskans, they're all over the place."
  - c. When asked about the selection by one of his clients of anticipating receiving distributions from the annuity in 1-5 years he stated, "they were just guessing on that. They had no idea. The way they're working, it could be 10 years. The question I ask is exactly what the form says, is when do you think you might possibly want some money out of this, and they answered 1-5 years, and I said OK, and marked it." He further explained "My rationale is that as long as they tell me that they don't think they would ever really want to take more than 3-5% out a year out of any of their annuities, I think that's a pretty good thing."
3. In 9 client files Mr. Brown did not document the client's objectives and the responses to the Division's questionnaire from two of Mr. Brown's clients was "no" to the question "Did Mr. Brown ask you about your financial goals?"

#### Finding #6B

Mr. Brown failed to analyze and use such information in making a recommendation. This finding is based on the fact that there is no evidence in the files that Mr. Brown analyzed and used relevant financial information prior to making the annuity recommendation and his response to questions during the interview. The following examples illustrate this:

1. In client file #10 Mr. Brown states on the "Client Recommendation Documentation Summary" that the client "need to have some safety & security plus earn a reasonable interest" and the reason for recommending the annuity as "receiving a 10% bonus at beginning is something he likes also the indexing option – likes Allianz Companies stability". The client had \$728,000 in tax sheltered retirement accounts and the funds for the recommended annuity came from one of those accounts. Mr. Brown did not document why transferring the funds from a tax-qualified retirement account to a tax-qualified equity indexed annuity with surrender charges met the client's goals.
2. In client file #23:
  - a. In the "Client Recommendation Documentation Summary", Mr. Brown included the death benefits in the client's net worth and liquid assets incorrectly and recommended an annuity that using corrected net worth and liquid asset amounts represented 57% of the client's net worth and 135% of liquid assets. Note that in the interview Mr. Brown stated, "I try to make sure that they are not using more



than 50% of their assets in an annuity. That's my general guideline." However, the file contains no documentation that he considered this "guideline" in recommending the annuity.

- b. The funds used to purchase the recommended annuity were the client's total deferred compensation account value and as of the application date, the client was old enough to draw on the account without restrictions or penalties, unlike the annuity, which assesses surrender charges in the first 10 years for amounts in excess of the 10% free withdrawal amount.
3. In client file #12, Mr. Brown recorded \$240,000 in net worth which incorrectly included the client's home. The net worth reported on the "Allianz Product Suitability" form was 63,585 and correctly excluded the home. However, Mr. Brown recommended two annuities of over \$46,000 even though this represented over 70% of the client's net worth and the clients' IRA accounts used to fund the annuities had earned 14% and 28% in 2009.
4. In a client file from the 2009 examination, Mr. Brown replaced a client's variable annuity that had no surrender charges with an equity-indexed annuity that had a market value adjustment and a 10-year surrender charge period with surrender charges starting at 17%. On the "Financial Needs Analysis" form, the client indicated that she does not "anticipate any material changes in her net worth, living expenses or liquid assets during the withdrawal penalty period of this annuity". However, the asset/liability inventory sheet showed that only the client only had \$8,000 in cash (checking and money market) and just two months after the annuity was issued the client requested withdrawal of \$3,000 to pay for repairs to her car. The client incurred a \$510 surrender charge and a market value adjustment of -\$180 and therefore received a net of only \$2,310. One fundamental consideration in determining the suitability of an annuity is whether the individual has sufficient cash reserves such that the need for withdrawal during the surrender charge period is unlikely. Based on the documentation in the file the client needed the \$3,000 in cash to pay for auto repair and Mr. Brown did not document any justification for his recommendation. Therefore, Mr. Brown either
  - i. failed to validate and analyze the financial information provided by the client and to consider the liquidity needs of the client before making the recommendation to exchange the variable annuity that was past the surrender charge period for an equity indexed annuity with extremely high surrender charges; or
  - ii. made an unsuitable recommendation for this client knowing that the client did not have sufficient cash (i.e. liquidity).
5. In the interview with Mr. Brown when asked how death benefit in the recommended annuity would compare with the death benefit that was guaranteed in the client's variable annuity Mr. Brown responded in part, "Well, let's take a look at that...". Clearly, Mr. Brown did not do this analysis prior to making the recommendation.

#### Finding #6C

The Division found that Mr. Brown failed to provide complete and accurate information to the consumer with one result being that he failed to make an effort to assure that the consumer understands all features of the product the producer sells, solicits or negotiates. This finding is based upon

1. The fact that in none of the files did Mr. Brown document his analysis or discussion with the client of whether another annuity such as an annuity without the premium bonus, with different interest/investment options, or a shorter surrender period would be more appropriate for the client. In addition, the files contain no documentation of his analysis or discussion with the client regarding the impact of key features such as market value adjustments and how early excess withdrawals may affect the amount of bonus earned.
2. Mr. Brown's responses to interview questions:
  - a. When asked to explain how bonus equity indexed annuity (EIA) returns compare overall with traditional annuities or EIAs without the bonus, Mr. Brown said "I don't do that because that kind of suggests a performance. And, I really don't want to mislead people into thinking they're going to get a performance based on the projections I am showing them."
  - b. When asked if he gave the clients any kind of expectation of what they can earn under different annuity types, he said, "I do not, we talk about the first year".
  - c. With respect to the market value adjustment" (MVA) feature in annuities, which can significantly impact the surrender value of the annuity during the surrender charge period, Mr. Brown stated that, "I honestly don't spend a lot of time explaining it (MVA), because most people can't understand it very well."
3. Mr. Brown's seminar announcement and statements made during his February 2010 seminar where:
  - a. Mr. Brown stated that in Alaska a 10 year fixed annuity is the longest duration available. In fact, 10 years is the maximum period that surrender charges may apply.
  - b. In regard to equity-indexed annuities Mr. Brown stated "you don't have risk". However, he does not qualify this statement by explaining the risks associated with early withdrawal which include surrender charges applicable during the surrender charge period for amounts over 10% of the annuity value in any year during the first ten years; or that the annuity bonuses may not be fully vested for several years.
4. Responses to the Division's questionnaire from Mr. Brown's clients regarding their transaction with Mr. Brown:
  - a. One of the five clients responded to the question "Did Mr. Brown emphasize any particular feature of the annuity?" with "Bonus at enrollment plus 2% interest 1<sup>st</sup> year, 8% return..."
  - b. Three of the five clients responded to the question "Did Mr. Brown explain in detail the pros and cons of the annuity or annuities he recommended?" with "No", "The pros", and "No cons, just pros".

### ***Required Actions***

In order to have reasonable grounds for believing that a recommendation is suitable Mr. Brown must not only make an effort to obtain the required information but must also:

1. make an effort to ensure that the information obtained from a consumer is accurate and complete
2. analyze and use that information in making a recommendation;

3. fully understand the insurance products he is transacting in Alaska and provide complete and accurate information to the consumer; and
4. make an effort to assure that the consumer understands all features of the products he sells and how those features affect annuity values the producer sells, solicits or negotiates including bonuses, surrender charges, and market value adjustments.

Mr. Brown should implement controls and procedures that will enable him to keep complete and accurate records of all insurance transactions.

**A licensee shall reply in writing within 10 working days to a records inquiry of the director.  
(Violations noted)**

**AS 21.27.350(e)**

***Requirement***

Under AS 21.27.350(e) "A licensee shall reply in writing within 10 working days to a records inquiry of the director".

***Finding #7***

Mr. Brown responded to the Division's record request within the required timeframe of 10 working days. Mr. Brown submitted a certification that the information submitted "is true and complete and that I am aware that submitting false information or omitting pertinent or material information to the Division of Insurance is grounds for license suspension or revocation and may subject me and my firm to civil or criminal penalties". However, the Division discovered that four client files were not submitted to the Division as required. Mr. Brown was made aware during the interview that these files were not provided to the Division and provided those files promptly after the interview.

***Required Actions***

Mr. Brown must organize his records and implement formal procedures and controls to assure timely and complete responses to requests for records by the Division.

**Registration requirements  
(WARNING)**

**AS 45.55.030**

***Requirement***

Under AS 45.55.030 "A person may not transact business in this state as a broker-dealer or agent unless the person is registered under this chapter". A non-registered person may not give investment advice on securities such as stocks, bonds, mutual funds, and variable contracts.

***Finding#8***

Mr. Brown is not registered to provide investment advice. However, the Division found that Mr. Brown may be giving investment advice by making statements about returns on investments and statements that discourage consumers from investing in mutual funds, stocks, bonds and variable annuities. This finding is based on

1. Mr. Brown's February 2010 seminar announcement and statements made during his February 2010 Seminar
  - a. Although Mr. Brown is not a registered investment advisor or a registered representative, he presented the investment information in his seminar for the "Financial Tools", S&P Market Trends, and "Negative Impact on the Stock Market" portions of his seminar.
  - b. Mr. Brown made the following statement in the seminar "I am able to get you out of that variable annuity, so that you are not harmed,"
2. Also, in Mr. Brown's contact sheet given to consumers titled "Response Sheet: Please contact me" one of the questions is "Name of mutual funds for review:" However, neither Mr. Brown nor Leeann Brown are registered with the SEC or with the Alaska Banking and Securities division to provide investment advice. Leeann Brown has a Certified Financial Planner (CFP) designation only.
3. Mr. Brown's "Client Recommendation Summary Document" in which Mr. Brown records his recommendation to the client includes "Various options available to meet each client's specific needs/objectives". In 12 client files, Mr. Brown recorded stocks, bonds, mutual funds, or variable annuities. For example, in client file #15, Mr. Brown wrote "more stocks & bonds-not safe enough for him, savings account-too low of interest, CD's still too low of interest"
4. Mr. Brown's responses to interview questions in which he stated that should a client want a specific review of their investments, he refers the client to Leeann Brown, compliance officer of the firm.
5. Responses to the Division's questionnaire from Mr. Brown's clients regarding their transaction with Mr. Brown: In response to the question "Did Mr. Brown discuss investing in money market, stocks, mutual funds, bonds, etc." one client stated "No, he ran those down as too risky" and one client stated "No-the above investing was discussed briefly, but yields were small as a whole".

#### ***Required Actions***

Mr. Brown must review the requirements of AS 45.55.030 in relation to the comments he has made/makes about investments to consumers, when marketing his insurance products and comply with the registration requirements.

Neither Mr. Brown nor LeeAnn Brown may directly or indirectly represent or imply to the public that either Mr. Brown or LeeAnn Brown is authorized to provide investment advice or is a registered investment advisor, without proper registration with the SEC and the State of Alaska.

**License required  
(WARNING)**

**AS 21.27.010**

#### ***Requirement***



A license is required for a person to act as an insurance producer.

***Finding #9***

Client files #7, #13, and #16 contained notes made by Morgan Ferrell in which she assisted in the sale/solicitation of an annuity. For example, in one of the files an e-mail from Ms. Ferrell to Mr. Brown regarding a call with the client states "I re-went over interest options and bonus". Ms. Ferrell is not licensed as a producer in Alaska and providing such assistance is a violation of AS 21.27.010.

***Required Actions***

Mr. Brown and Ms. Morgan Ferrell must review AS 21.27.010 and Mr. Morgan Ferrell must obtain a producer license in order to assist in the sale/solicitation of an insurance product.

The Brown Agency must implement controls and procedures to assure that staff of The Brown Agency does not perform unauthorized insurance activity.

<b>Recommendations</b>
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Mr. Brown should avoid encouraging clients to submit an application at the initial meeting and should encourage clients to take additional time in order to:

- a. consider whether the insurance product/annuity is suitable and seek potentially seek advice from family members or other qualified advisors.
- b. allow for more complete and accurate records of the transaction including accurate and complete responses to applications and related documents.

**CLOSING**

The above summarize the findings of the 2010 targeted market conduct examination of Leonard W. Brown (Alaska License No. 22419). The examination of Mr. Brown's insurance records, seminar advertising, Mr. Brown's statements made during one seminar, Mr. Brown's responses to questions during a phone interview, and responses by Mr. Brown's clients to a questionnaire regarding their transaction with Mr. Brown revealed significant violations of Alaska law and regulation as outlined above and require corrective action by Mr. Brown.

Submitted by:  
Katie Campbell  
Life/Health Actuary