

A

TARGETED MARKET CONDUCT EXAMINATION OF

PACIFIC LIFE INSURANCE COMPANY

NAIC #67466

As Of

December 31, 2009





Honorable Mary Taylor
Lt. Governor/Director
Ohio Department of Insurance
50 West Town Street Suite 300
Columbus, Ohio 43215

Lt. Governor:

Pursuant to your instructions and in accordance with the powers vested under Title 39 of the Ohio Revised Code, a targeted market conduct examination was conducted on the Ohio business of the following:

Pacific Life Insurance Company NAIC# 67466

The examination and risk assessment was conducted at the Ohio Department of Insurance:

50 West Town Street
Columbus, Ohio 43215

A report of the examination is enclosed.

Respectfully submitted,

Lynette Baker
Chief, Market Conduct Division

August 30, 2011

Date

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FOREWORD

This examination and risk assessment was conducted under authority provided under Ohio Revised Code (“R.C.”) 3901.011.

EXECUTIVE SUMMARY

This examination is a targeted market conduct examination of Pacific Life Insurance Company (“Company”) by the State of Ohio as it relates to the Company’s suitability compliance program for its fixed and variable, individual annuity products for the period of January 1, 2003, through December 31, 2009, (the file review was conducted on annuities issued, replaced, or surrendered, during the period of March 1, 2007, through December 31, 2009). The examination began May 2, 2011, and concluded May 13, 2011.

The most significant areas of concerns are:

- The major reasons for the examiner’s inability to determine suitability in the case of the four new business and replacement files were: (1) the Company’s allowance of different suitability forms used by the independent registered representatives and (2) The information provided by the Company to support the suitability determination made by the third-party broker/dealer firm(s) was deemed insufficient by the examiner.

SCOPE OF EXAMINATION

The basic business areas included as part of the examination included:

- A. Compliance
- B. New Business and Replacements
- C. Marketing and sales material
- D. Complaint Handling

Each business area has standards that were measured during the examination. Some of the standards have specific statutory guidance; others have specific company guidelines or contractual guidelines.

The focus of the examination was on the procedures and methods used by the Company to achieve compliance with applicable Ohio statutes and rules involving the issuance of fixed, individual annuity products. This included an analysis of how the Company communicates its instructions and philosophy with its employees and broker/dealers.

This examination report is a report by test, rather than a report by exception, and all standards and tests are described and the findings indicated.

METHODOLOGY

This examination is based on the standards and tests for a market conduct examination of a life and annuity insurer found in Chapters 16 and 19 of the NAIC Market Regulation Handbook and on applicable Ohio statutes and rules.

Some of the standards were measured using a single type of review, while others used a combination or all types of review. The types of review used in this examination fall into two general categories: Generic and Sample.

A “Generic” review indicates that a standard was tested through analysis of general data gathered by the examiners, or provided by the Company in response to interrogatories or personnel interviews conducted by the examiners.

A “Sample” review indicates that a standard was tested through direct review of a random sample of files selected using automated sampling software.

Each standard is accompanied by a comment describing the purpose or reason for the standard. Findings are indicated and any examiner comments or observations are noted.

COMPANY OPERATIONS

Pacific Life Insurance Company was established in 1868 and is organized under the laws of the state of Nebraska as a stock life insurance company, conducting business in the District of Columbia and every state except New York.

2009 Annuity Considerations

| Ohio Individual Ordinary | National Individual Ordinary |
|--------------------------|------------------------------|
| \$350,024,238 | \$6,470,468,960 |

FILE REVIEW METHODOLOGY

The findings are based on the standards for a market conduct examination of a life and annuity insurer according to applicable Ohio statutes and rules, including Ohio Administrative Code (“OAC”) 3901-6-13 and 3901-6-14.

NEW BUSINESS AND REPLACEMENTS REVIEW FINDINGS

Standard 5: Marketing and Sales

The insurer has suitability standards for its products as required by OAC 3901-6-13 (G)(5), (7), and (8).

Procedure Review

Methodology: The examiners reviewed compliance procedure manuals and interviewed Company personnel to determine how new business and replacements are reviewed and processed.

Examiner Observations:

Methodology:

Overall, the Company has demonstrated that effective annuity suitability oversight, reviews, compliance methods, and complaint handling procedures currently exist to assure compliance with Ohio required statutes and regulations.

The Company maintains a Corporate Compliance Department that reports directly to the Chief Compliance Officer (“CCO”). This department conducts compliance reviews of various areas throughout the year. These reviews are summarized in control matrices and distributed to Company management and the CCO. The CCO provides periodic reports on the Company’s compliance and ethics program to the Governance and Nominating Committee of the Board of Directors.

Each operating division maintains their own compliance functions, which have the primary responsibility for matters specific to their lines of business. Each division has a compliance officer who is responsible for ensuring that processes are in place to: 1) develop and maintain policies and procedures to comply with applicable statutes and rules, 2) assess compliance risks

of business activities, 3) monitor business activities to determine the effectiveness of the division's compliance program, and 4) periodically report to CCO these activities.

The Retirement Solutions Division ("RSD") of the Company offers variable and fixed annuities for sale through independent broker/dealers and contracts with the broker/dealers to establish and maintain a compliance system to supervise recommendations. The Company also contracts with these broker/dealers to perform suitability reviews. The Company obtains annual certifications from the senior management of the broker/dealers that this function is properly performed. Another check on suitability is a question on every variable product application that allows the annuitant to certify that he/she understands the purchase and has been asked about financial objectives and background.

The RSD reviews and monitors its annuity book of business as required by OAC 3901-1-13 (G)(5)(b). The reviews include replacements, suitability, complaints, market timing, and sales to seniors. All reviews are documented and reviewed by the department's management team. A recent random audit was completed on sixteen Ohio broker/dealers. Audits are conducted using the parameters set forth in the Company's "Broker Dealer Certifications and Suitability Review Procedures". Essentially, the main purpose of the reviews is to request client documentation from the broker/dealer regarding the suitability of the chosen contract. There appears to be no 'formal' report developed on the audit findings, but findings are communicated to RSD officers and senior managers.

Lastly, the Company has established annuity market conduct expectations and standards which are communicated to the broker/dealers through the Company website. These standards are included in a "Writing the Business" guideline manual which addresses suitability very thoroughly, along with many other sales-oriented areas/issues.

The Company does not apply a surrender charge at time of death. The surrender periods on the annuity products varies from zero to eight years. Most products fall into a six year surrender period.

One concern noted by the examiners during the file review involved the suitability forms used by the broker/dealers. Each broker/dealer is allowed to develop and use its own form to gather annuitant's financial information. These forms are inconsistent in the information provided. This inconsistency caused problems for examiners reviewing suitability due to missing information, especially with specific details on the annuitant's other investments that support the net worth figure that was provided. A few of the forms provide a breakdown of the annuitant's overall investment picture, e.g. how much the person has in cash, stocks, bonds, etc. Most others state only a total dollar figure with no supporting information on how that figure was developed, provide only the annuitant's investment experience in years, or do not provide any information at all. Some of the forms include home values in the determination of net worth, others do not. In addition to the missing information, the forms include broad ranges for net worth and annual income making it difficult to get an accurate financial picture. Some of the forms provide a detailed explanation of why the person is purchasing the annuity; others have brief statements such as 'Growth' or 'Income'. The inconsistency is also apparent in the percent of premium

used to fund the annuity compared to the net worth figure provided. Some of the broker/dealers allow premium to net worth ratios that range between 20% to over 80%.

File Review:

Methodology:

The examiners reviewed a sample of 50 Ohio new business and 50 replacement policies on individual fixed annuity contracts issued during the examination period. The major focus of the new business and replacements involved the issue of annuity suitability and the Company's oversight of its products.

New Business (non-replacement):

| Population | Sample | Yes | No | Standard | Compliance |
|------------|--------|-----|----|----------|------------|
| 4,240 | 50 | 48 | 2 | 90% | 96% |

The standard for compliance is 90%. The Company's handling practices were above this standard.

Two files provided by the Company were deemed to have insufficient information to support the suitability review conducted by the third-party broker/dealer:

A 67 year old female purchased a fixed annuity using 61% of her net worth (+\$91,000) of \$150,000. This file has a seven year surrender period. The person only has income of \$18,000 per year and savings of \$24,000. No other investment information was provided and there were no details of the possible inheritance the annuitant was to receive.

A 79 year old female purchased a fixed annuity with 81% of her net worth (\$50,000). This file has a six year surrender period. The person has a net worth of approximately \$65, 000, which includes cash of \$14,268 and \$51,700 in CD's. Her income is \$17,000 per year.

Replacements:

| Population | Sample | Yes | No | Standard | Compliance |
|------------|--------|-----|----|----------|------------|
| 903 | 50 | 48 | 2 | 90% | 96% |

The standard for compliance is 90%. The Company's handling practices were above this standard.

Two files provided by the Company were deemed to have insufficient information to support the suitability review conducted by the third-party broker/dealer:

A 52 year old female purchased a variable annuity with the fixed option for \$11,000. This amount is 50% of liquid net worth. There was no information on the annuitant's total net worth or occupation to support the sale. This person has other investments of \$14,000 and appears to have an annual income range of \$25,000-\$49,999.

An 87 year old retired female did a 1035 exchange with a premium of \$170,000 (28% of net worth) for a variable annuity. There were no specific details of investments provided that supported the net worth of \$600,000, nor the liquid net worth of \$500,000.

Examiner Recommendations:

- The exceptions noted were due to the examiner’s inability to determine suitability based on the information provided or the Company did not provide enough information to support the suitability review made by the third-party broker/dealer firm. This was discussed in more detail in the ‘Procedure Review’ section of this report. The Company should review all current versions of suitability forms being used to assure that all broker/dealers are using suitability forms that encompass all facets of financial information as required by the revised version of OAC 3901-6-13 (E)(9) and (F)(1)(2) effective July 1, 2011. This will eliminate the inconsistency of information gathered and should reduce the amount of missing information.
- The Company should consider whether the broad ranges used on third-party broker/dealers’ suitability forms for the net worth and income areas are appropriate in the recommendation of annuities. Additionally, certain broker/dealers’ procedures allow up to 40% of net worth to be acceptable (the industry average appears to be in the 16%-20% range).

Standard 11: Marketing and Sales
The insurer has procedures in place to educate and monitor insurance agents/producers and to provide full disclosure to consumers regarding all sales of products involving annuity products, and all sales are in compliance with OAC 3901-6-14 (E)(4)&(5) and R.C. 3901.21(A).

Procedure Review

Methodology: The examiners reviewed compliance procedure manuals and interviewed Company personnel to determine how agents/producers are educated and monitored on the use of sales brochures, disclosures and buyers guides.

Examiner Observations:

The examiners did not note any issues with the Company’s sales and marketing materials, policy contracts or disclosures. The disclosure is a two-page document that includes all information required by OAC 3901-1-14. The disclosure is given to the annuitant, along with the Buyer’s Guide, at the time of sale.

File Review:

Methodology:

The examiners reviewed a sample of 50 Ohio new business and 50 replacement policies on individual fixed annuity contracts issued during the examination period. Disclosures were reviewed to determine their compliance with OAC 3901-1-14 (E) (4) & (5).

New Business (non-replacement):

| Population | Sample | Yes | No | Standard | Compliance |
|------------|--------|-----|----|----------|------------|
| 4,240 | 50 | 50 | 0 | 90% | 100% |

The standard for compliance is 90%. The Company’s handling practices were above this standard.

Replacements:

| Population | Sample | Yes | No | Standard | Compliance |
|------------|--------|-----|----|----------|------------|
| 903 | 50 | 50 | 0 | 90% | 100% |

The standard for compliance is 90%. The Company's handling practices were above this standard.

COMPLAINT HANDLING

Standard: Complaint Handling

The regulated entity takes adequate steps to finalize and dispose of the complaint in accordance with statutes, rules, regulations, and contract language.

Examiner Observations:

The Company has in place procedures for handling complaints promptly and thoroughly. The complaints are also trended and analyzed to identify any specific problem areas, like specific agents with more than one complaint. The Company has a thirty-four page complaint handling manual that is very thorough and statute specific. The examiners review of Ohio Department of Insurance complaints showed that the Company had a minimal number of complaints on annuities in the past two years, including zero in 2010.

This concludes the report of the market conduct examination of the Pacific Life Insurance Company. The examiners, Don Layson, Ben Hauck, Laura Price, and Rob Stroup, would like to acknowledge the assistance and cooperation provided by the management and the employees of the Company.



August 30, 2011

Don Layson
Examiner in Charge

Date

ATTACHMENT



August 24, 2011

Daniel J. Atkisson, CPCU, CIDM, MCM
Insurance Compliance Supervisor
Ohio Department of Insurance
50 West Town Street
Third Floor, Suite 300
Columbus, OH 43215
(614) 728-1202

Re: Targeted Market Conduct Examination of Pacific Life Insurance Company, NAIC #67466, As
Of December 31, 2009

Dear Mr. Atkisson:

Pacific Life would like to thank the examiners and staff of the Ohio Department of Insurance for their professionalism and courtesy in conducting this examination. We found the examiners to be detailed and thoughtful with respect to their observations and the application of Ohio law. We appreciate the Department's fair and thorough consideration of our responses, processes and procedures.

With respect to the Department's findings and recommendations, we understand the Department's concern regarding observed inconsistencies in the suitability forms used by the independent third-party broker/dealer firms who sell Pacific Life annuities. In our experience, the various suitability forms and questionnaires in use by these broker/dealers have evolved over time as broker/dealers have responded to the dynamic federal and state suitability regulatory environment. Indeed, both the recent revision to OAC 3901-6-13 on July 1, 2011, and the adoption by the National Association of Insurance Commissioners (NAIC) in March, 2010, of its revised suitability model regulation, upon which the Ohio law is based, occurred after the application dates of the new business and replacement files reviewed by the Department during this examination.

PACIFIC LIFE INSURANCE COMPANY
RETIREMENT SOLUTIONS DIVISION

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In consideration of the Department's recommendations, we are in the process of issuing a reminder communication to the broker/dealers that sell our annuities. The purpose of our communication is to remind these broker/dealers to review their suitability forms and questionnaires to ensure they encompass all facets of the consumer's financial and suitability information, as required by the revised version of OAC 3901-6-13 (E)(9), (F)(1), and (F)(2). In addition, we shall advise the broker/dealers to evaluate the net worth and annual income measures they employ in their determination of whether an annuity is suitable for their individual clients to ensure these measures are consistent with industry standards and the expectations of federal and state regulators. In particular, we will ask them to consider their use of broad ranges for net worth or annual income on their suitability forms; the inclusion of specific details on such forms as to other investments that support net worth; and the firm's guidelines for acceptable percentage of net worth used to fund an annuity.

We would again like to thank the Department and the examination staff for its handling of this examination.

Sincerely,



Nancy A. Hill

Assistant Vice President, Compliance
Pacific Life Insurance Company
Retirement Solutions Division