THE COMPLIANCE & ETHICS FORUM
FOR LIFE INSURERS

PRICEWATERHOUSECOOPERS LLP

2013 CEFLI-PWC Compliance and Ethics Benchmarking Survey Report

Benchmarking Survey Report

Introduction

Compliance and ethics within the life insurance industry continues to evolve. As part of CEFLI's mission to serve the needs of the life insurance industry's compliance and ethics professionals, CEFLI has joined with CEFLI Affiliate Member organization PricewaterhouseCoopers LLP to develop and conduct its 2013 Compliance and Ethics Benchmarking Survey (the "Survey") to gauge the current state of compliance and ethics in the life insurance industry. Each year the Survey is designed to capture data associated with the current state of compliance and ethics functions within the life insurance industry. This year's Survey allows CEFLI to compare data derived through its 2012 Survey with a view toward identifying possible trends that may be of interest to the life insurance industry's compliance and ethics professionals and senior management. This report summarizes the key findings of the Survey.

Purpose

The purpose of this Survey was to determine the current state of the compliance and ethics functions within the life insurance industry. To gauge current practice, the Survey asked objective questions designed to identify overall staffing, organizational structure, budgeting, compensation, roles and responsibilities to allow respondents to comment upon practices that exist within their respective organizations.

The Survey sought to confirm distinctions between the important roles of compliance and ethics within organizations by gauging the extent to which organizations have established separate departments to address each of these functional areas as well as naming distinct executive officers (i.e., naming a Chief Ethics Officer in addition to a Chief Compliance Officer (CCO)). To achieve this objective, the Survey explored various organizational structures applicable to the compliance and ethics function within life insurance companies.

The Survey also collected data associated with staffing, budget and resources as a way to gauge differing levels of resource commitments across organizations of different sizes and different scope.

The Survey also sought to evaluate how various compliance matters may be handled within respective organizations. The Survey reviewed subject matters such as consumer protection, fraud prevention, privacy and confidentiality and anti-money laundering to determine whether these areas were the sole responsibility of the compliance function or whether other organizational departments were involved in their analysis.

Through evaluating this data, CEFLI will be able to establish a benchmark that can be used in later years to begin to evaluate trends in the design, staffing and budgets dedicated to supporting the compliance and ethics function within the life insurance industry.

Methodology

To complete its review, CEFLI solicited input from both CEFLI-member life insurance companies as well as non-CEFLI member companies. CEFLI received Survey responses from 50 life insurance companies across a range of company sizes (large, medium and small).

Survey respondents were asked to indicate the size of their organization based upon annual direct written premium for the organization.

For purposes of the Survey, large life insurance companies were characterized as organizations generating annual direct written premium in excess of $10 billion annually, medium companies were characterized as organizations generating annual direct written premium of between $1 billion-$10 billion annually and small companies were characterized as organizations generating annual direct written premium of $1 billion or less annually. Survey responses were received from a broad range of companies including large life insurance companies (20%), medium companies (36%) and small (44%) sized companies.

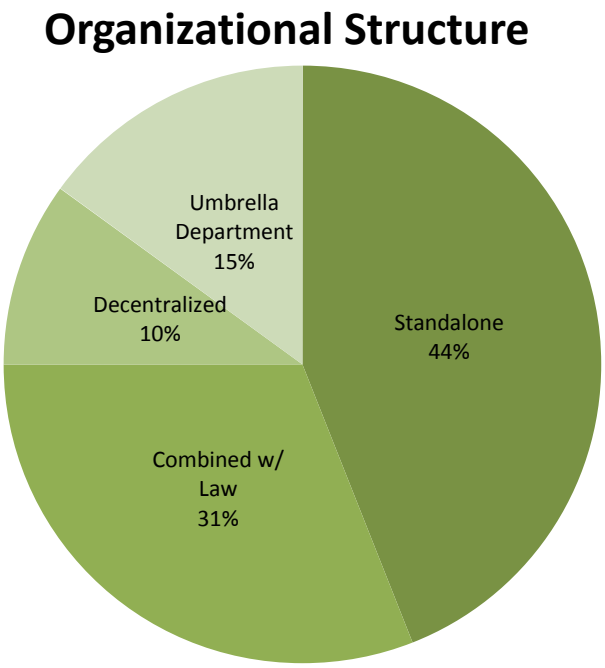
The overwhelming majority (96%) of organizations responding to the Survey indicated that their primary lines of business were represented by life insurance and annuity products. Most organizations (92%) responding to the Survey indicated that they operated primarily within the United States while a smaller number of organizations (8%) indicated that they operated in several other countries worldwide. For the most part, respondents to the Survey represented the compliance function within their respective organizations whereas a few Survey responses were submitted by an organization's General Counsel or Internal Auditor.

In sum, the Survey respondents constituted a representative cross-section of individuals with responsibility for the compliance and ethics function from organizations distributing life insurance and annuity products within the life insurance industry.

Organizational Structure

Compliance

Survey respondents were asked to indicate the organizational structure that best describes their company's compliance department. Responses were mixed to indicate the variety of organizational structures for compliance departments within the life insurance industry.



The largest number of Survey respondents (44%) indicated that their compliance department serves as a standalone department within their company. Another segment of Survey respondents (31%) indicated that compliance is combined with law and is considered part of the company's legal department. Other Survey respondents (15%) indicated that compliance serves as an "umbrella department" with representatives in each business unit and still others (10%) indicated that their compliance organizational structure has compliance representatives embedded within individual business units.

It came as no surprise that virtually all Survey respondents indicated that their organization has identified a Chief Compliance Officer. Many of these positions have been in existence for over 15 years. However, some Survey respondents indicated that their Chief Compliance Officer position has only been officially developed within the past decade.

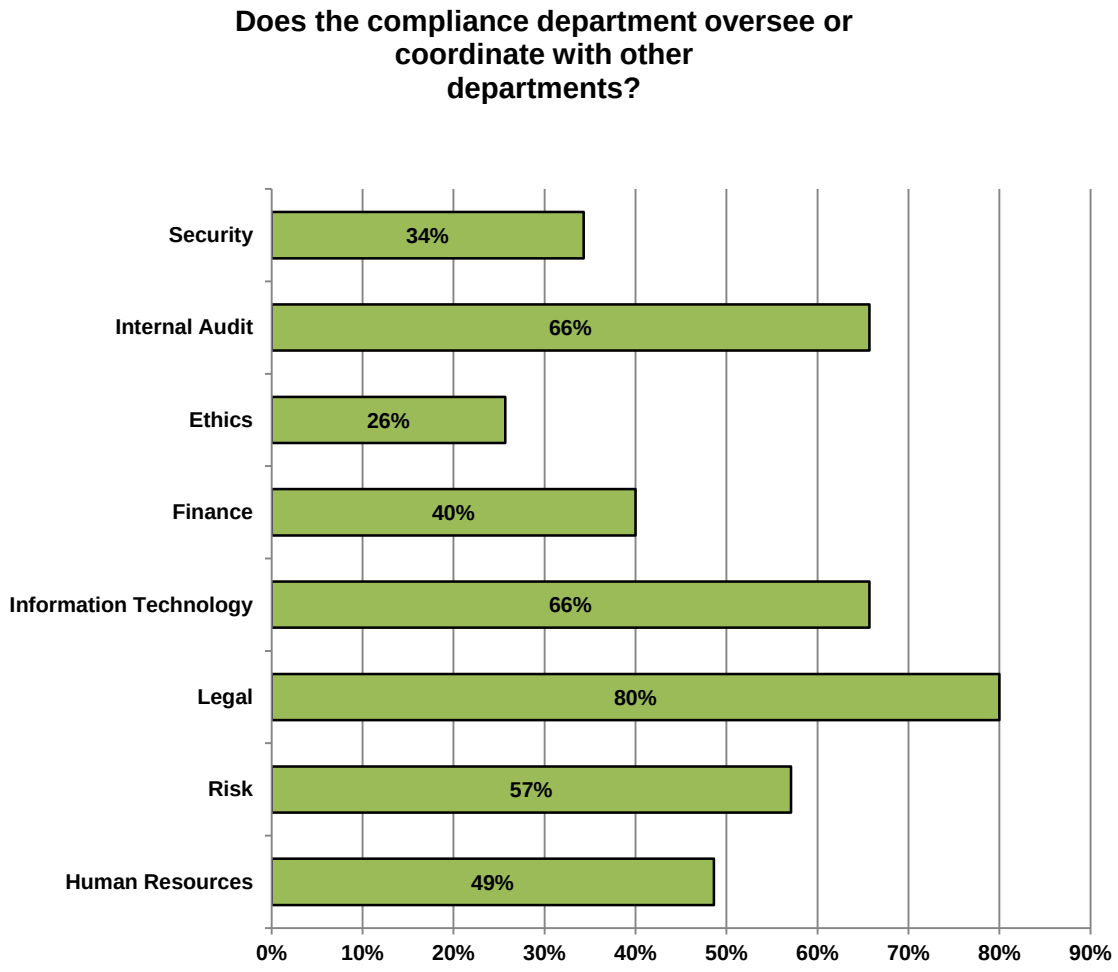
With respect to the reporting relationships for Chief Compliance Officers, the majority of Survey respondents (66%) indicated that their Chief Compliance Officer reports to the General Counsel, others (20%) report to the Chief Executive Officer, and still others (14%) report to their Board of Directors or a Committee of the Board.

Although the percentage of respondents within organizations where the Chief Compliance Officer reports directly to the Board of Directors is relatively low, most respondents indicated that their CCO often develops written reports to their company's Board of Directors (or an appropriate Committee of the Board), notwithstanding the existence of any formal reporting relationship to the Board or an appropriate Committee. To the extent such reports are required, they are provided at least annually and in, most instances, on a quarterly basis. The written report is offered to the Board or an appropriate Board Committee by the Chief Compliance Officer or by his/her senior report (i.e., the General Counsel or CEO).

With respect to the reporting relationships for Chief Compliance Officers, the majority of Survey respondents (66%) indicated that their Chief Compliance Officer reports to the General Counsel.

To the extent that Chief Compliance Officers may have a formal reporting relationship such as reporting to the General Counsel, many also indicated that they have informal (or "dotted line") reporting relationships to the Chief Executive Officer or other executive. These types of informal reporting relationships were reported most frequently with respect to Chief Compliance Officers within large companies.

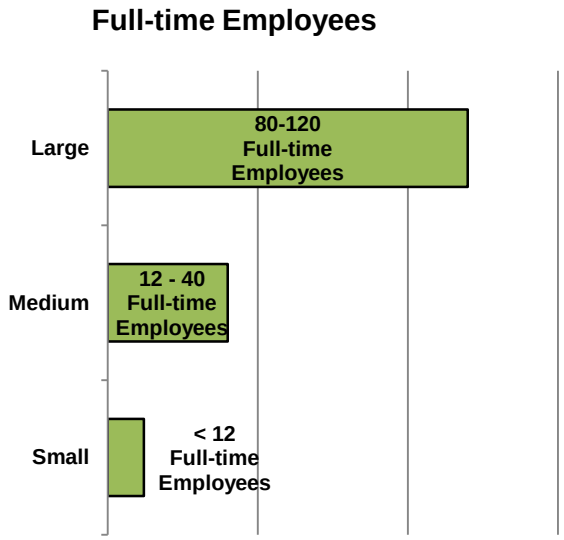
The Survey also gathered data concerning other corporate departments with which the compliance department coordinates its activities. According to the Survey respondents, compliance departments most often coordinate their activities with legal (80%), internal audit (66%), information technology (66%) and risk (57%).



Staffing and Budgeting

Compliance

The Survey attempted to gauge the number of individuals that devote the majority of their time to the compliance and ethics function within various life insurance companies.



Survey results were consistent with expectations to the extent that large, medium and small-sized companies reported differing levels of staff members dedicated to compliance and ethics within their respective organizations based upon company size. Respondents from large companies indicated that they devote a range of 80-120+ full time employees to compliance and ethics whereas respondents from medium-sized companies indicated that they devote a range of 12-40 full-time employees to compliance and ethics and respondents from small-sized companies indicated that they devote 12 or fewer full-time employees to the compliance and ethics function. It may be interesting to note that some Survey respondents representing small-sized companies indicated that 3 or fewer people are responsible for overall compliance within their organizations.

The Survey also sought to determine whether staffing devoted to compliance and ethics within life insurance companies changed over the past 18 months. The Survey results indicated a 50/50 mix with approximately half of the responding companies indicating no change and approximately half indicating some change in compliance staffing over the prior 18 months. Companies indicating a reduction in compliance staff reported that

these reductions were largely attributable to overall reductions in force within their organizations or a determination to not replace individuals who were retiring. However, the majority of companies that indicated that they had experienced a change in staffing over the past 18 months reported an increase in staffing. In some instances, these increases in staffing were subject matter specific (e.g., adding an annuity suitability specialist) or were related to increases in sales volume.

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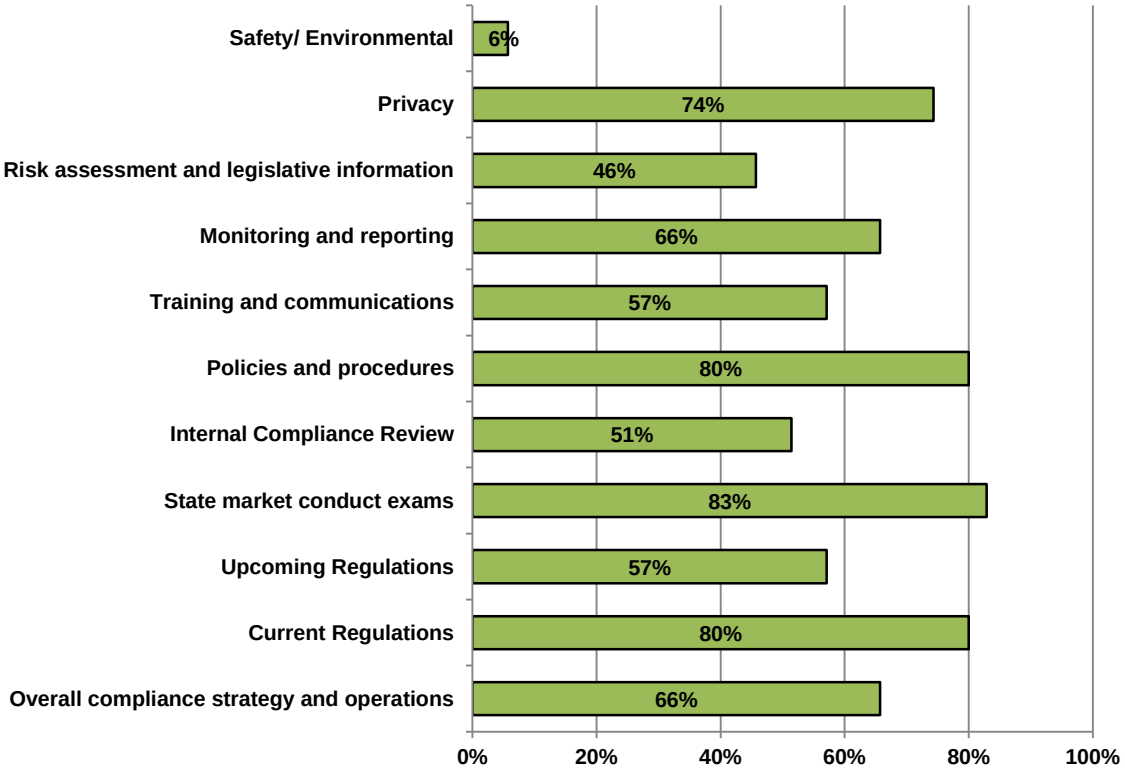
When asked whether staffing changes were anticipated within the next 18 months, most Survey respondents (75%) indicated that no change in staffing was anticipated with a smaller number of Survey respondents (25%) indicating a likely increase in compliance staffing over the next 18 months. To a large extent, any anticipated increases in staff were reportedly attributable to changes in current business models or increased regulatory requirements.

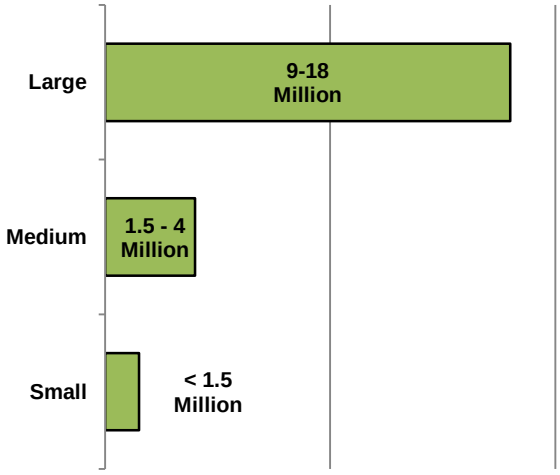
The Survey also sought to determine the extent to which companies have one full-time equivalent employee dedicated to specific subject matters. The top subject matters for which companies have dedicated a full-time employee include: state market conduct exams (83%), current regulations (80%), policies and procedures (80%), and privacy (74%).

Do you have at least one full time equivalent (FTE) in your compliance department that is focused on any of the following activities?



With respect to budgeting of resources for compliance and ethics, respondents from large companies indicated a budget range of $9 million-$18 million, respondents from medium sized companies indicated a budget range of $1.5 million-$4 million and respondents from small-sized companies indicated a budget range of $1.5 million or less.

Compliance Resources



The Survey also sought to identify the estimated total compensation of those individuals in the Chief Compliance Officer role. The Survey results indicated that Chief Compliance Officers within large companies are paid between $225,000-$450,000+ annually, Chief Compliance Officers within medium-sized companies are paid between $150,000-$225,000 and Chief Compliance Officers within small-sized companies are paid $150,000 or less.

In general terms, the Survey results indicated that most Chief Compliance Officers in the life insurance industry (70%) can expect to earn between $75,000-$225,000 based upon company size and level of organizational responsibility.

Ethics and Chief Ethics Officers

The Survey also collected data concerning life insurance company ethics programs. Specifically, Survey respondents were asked to indicate whether their respective organizations maintain a separate ethics (or business conduct) program. Only a small percentage (20%) of Survey respondents indicated that their organizations maintain a separate ethics (or business conduct) program. For most Survey respondent organizations (80%), ethics is part of a combined compliance and ethics program. It was noted however, that in some instances, individual business units are required to design ethics or business conduct programs specifically tailored to suit the business needs.

Organizations that maintain a separate ethics (or business conduct) program were represented primarily by large companies. Many large companies reportedly apply their ethics programs globally whereas others maintain an overall global program that may incorporate a separate ethics program for US business purposes.

Consistent with the results of last year's Survey, a small percentage of this year's Survey respondents (7%) indicated that their organizations maintain a separate position for a Chief Ethics Officer. To the extent that such positions exist, the Survey results indicated that the position has been in existence for more than 4 years and, in a few cases, in excess of 10 years. Though this year's Survey results confirm that only a few life insurance companies have taken the step of providing executive authority to the ethics function by naming a Chief Ethics Officer, it was clear from Survey respondents that ethics continues to play an important role as part of the overall compliance and ethics culture within the life insurance industry.

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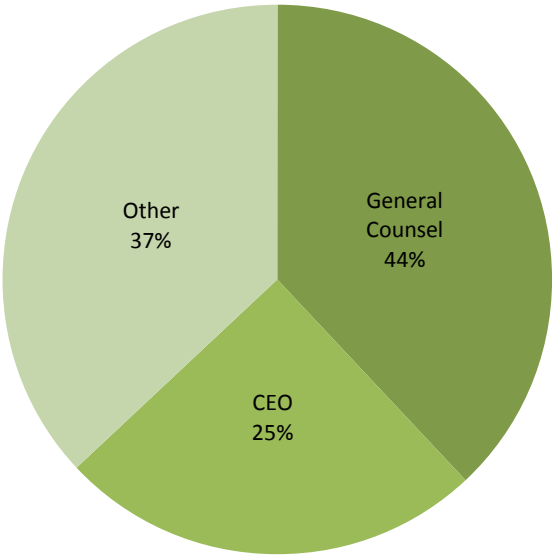
For those Survey respondents indicating that their organizations maintain a Chief Ethics Officer, the compensation range for the position was between $75,000-$150,000.

When asked about the nature of the reporting relationship for the Chief Ethics Officer, Survey results were mixed with some companies (38%) indicating that the Chief Ethics Officer reports to the General Counsel, others (25%) indicating that the Chief Ethics Officer reports directly to the CEO and still others (37%) indicating a variety of other reporting relationships for their Chief Ethics Officer including reporting directly to the company's Board of Directors or appropriate Board Committee.

Chief Ethics Officer reports to:



It may be important to note that many Survey respondents indicated that the Chief Compliance Officer role also assumes responsibility for ethics within their organization. Moreover, several companies have chosen to combine the compliance and ethics function into the single role of Chief Ethics and Compliance Officer. When asked to identify the rationale of combining the compliance and ethics function into the single role of Chief Ethics and Compliance Officer, Survey respondents provided several rationales including the fact that the title reinforces that ethics is embedded into their corporate compliance culture. Furthermore, it was indicated that the combined Chief Ethics and Compliance Officer role allows for consistency and control of these independent functions.

In reviewing Survey results over the past two years, we see several companies have taken the step to recognize that ethics as a functional business area has taken on a growing prominence within life insurance companies by naming individuals (either as Chief Ethics Officer or Chief Ethics and Compliance Officer) who have executive responsibility for ethics in their job title and job descriptions.

Compliance Department - Scope

This year's Survey also sought to determine the scope and effectiveness of the compliance function within life insurance companies. Given that there is a broad range of subject matters that may fall within the scope of the compliance function, the Survey queried respondents to gather data concerning several subject matters that, for many companies, fall within the scope of the compliance function.

Survey questions were posed concerning issues associated with consumer protection, conflicts of interest, fair competition and antitrust matters, anti-corruption and bribery issues, regulatory relationships, fraud prevention, privacy and confidentiality, anti-money laundering, intellectual property, insider trading and life insurance industry-specific regulations, in an effort to determine the extent to which the compliance function may be directly responsible for their oversight and resolution. Respondents were asked to indicate whether compliance is directly responsible, somewhat involved or not involved at all for each subject matter.

More than half of the Survey respondents indicated that compliance was directly responsible for the following subject matters: consumer protection, anti-money laundering, regulatory relationships, fraud prevention, privacy and confidentiality and life insurance industry-specific regulations. Issues pertaining to conflicts of interest, fair competition and antitrust matters, anti-corruption and bribery issues, intellectual property and insider trading were all identified as subjects that involve compliance but also involve input from other company functional areas including legal, internal audit and others.

More than half of the Survey respondents indicated that compliance was directly responsible for the following subject matters: consumer protection, anti-money laundering, regulatory relationships, fraud prevention, privacy and confidentiality and life insurance industry-specific regulations.

The Survey sought to specifically focus on whether social media activity is considered within scope for the compliance and ethics program. Only a small number of Survey respondents (28%) indicated that social media activity is considered within scope for the compliance and ethics program. In those instances, Survey respondents indicated that either all social media use is submitted for review and approval by the compliance department prior to use, or that the compliance department uses social media in their monitoring and supervision role. Several Survey respondents indicated that their companies do not permit social media use.

Compliance Department - Effectiveness

This year's Survey also gathered data concerning the extent to which compliance departments are reviewed and evaluated. The Survey sought to determine how the compliance department is evaluated, how the evaluations are performed and whether companies apply compliance metrics in the evaluation of the effectiveness of their compliance programs.

An overwhelming majority of Survey respondents (86%) indicated that the compliance department is reviewed and evaluated by their organization's internal audit division. In addition, a significant number of companies reported that they supplement this analysis through their own self-assessment process of the compliance function.

As to the frequency of the evaluations conducted by internal audit, several Survey respondents (34%) indicated that these reviews are conducted annually; other Survey respondents (28%) indicated that these reviews are conducted randomly and still other Survey respondents (25%) indicated that these reviews are conducted continuously. Other responses indicated that the reviews are conducted on either a quarterly or semiannual basis.

Some Survey respondents alluded to the fact that their evaluation of their compliance program is determined through state insurance department market conduct examination activities. Assumedly, if the state insurance department examination goes well, then compliance is determined to be effective whereas in the alternative, it is not. The Survey did not request additional information regarding the rationale underlying this strategy. However, it is clear that the majority of companies rely upon their internal audit process as the primary means to evaluate the effectiveness of their compliance programs.

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It was encouraging to note that the majority of Survey respondents (69%) conduct self-assessments of their compliance program. Of these respondents, over half indicated that they conduct self-assessments of their compliance programs on a continuous basis. This provides additional layers of control over the compliance function so that issues can be identified and addressed on a more immediate basis. While it is recognized that not all organizations have the resources necessary to conduct self-assessments of their compliance program on a continuous basis, the organizations that have implemented this type of strategy should be commended for their willingness to continually monitor and evaluate progress toward attaining desired compliance objectives.

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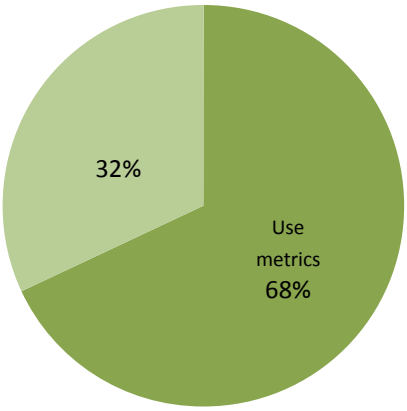
The majority of Survey respondents (68%) indicated that they use some type of metrics in their evaluation of the effectiveness of their compliance programs.



The use of metrics in the field of compliance is evolving rapidly. The majority of Survey respondents (68%) indicated that they now use some type of metrics in their evaluation of the effectiveness of their compliance programs. This movement toward compliance metrics is currently pervasive among large company Survey respondents whereas medium and small companies have not implemented compliance metrics to the same extent. Key areas identified by the majority of Survey respondents (in excess of 68%) for the use of compliance metrics included complaints, replacements, trend monitoring and regulatory fines and penalties.

Compliance Committees

Just over half (53%) of Survey respondents indicated that they use compliance committees to support their compliance efforts. These committees are comprised of representatives from other functional areas throughout the organization to provide input on current compliance issues. While the composition of the compliance committee varies from company to company, functional areas most commonly reported as serving on the compliance committee included: legal, operations, sales and marketing, internal audit and human resources.

Ethics

Survey respondents were asked to describe the elements of their company's ethics programs. The majority of Survey respondents (68%) indicated that their company uses a variety of different elements in implementing their overall ethics program. The most common elements cited included: code of ethics/conduct, training, communication, anonymous reporting, an ethics hotline, a whistleblower hotline and investigations.

Companies use a variety of techniques to reinforce the importance of ethics within their respective organizations. The Survey results indicated that companies use various strategies to promote ethics including: periodic publication of videos and articles reinforcing the importance of ethics, training through use of company intranets, quarterly compliance newsletters with articles focused on ethics, heightened promotion of ethics during Ethics Awareness Month or a Compliance & Ethics Week, and public statements from senior management endorsing the importance of ethics as part of the company's culture and core values.

The Survey also sought information concerning whether ethics (or adherence to a company's code of conduct) was a formally documented part of an employee's performance evaluation criteria. The Survey results indicated that a significant and growing percentage of companies responding to the Survey (40%) include ethics as part of an employee's performance evaluation criteria.

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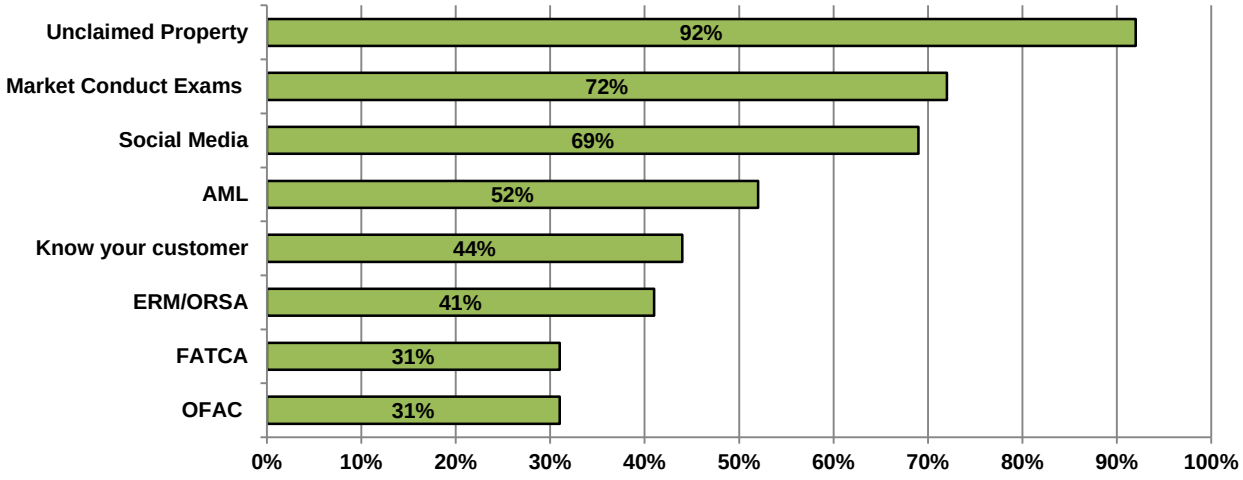
Technology

The Survey also gathered data regarding the use of technology within compliance departments. The majority of Survey respondents (68%) indicated that they use technology programs specifically tailored to their compliance needs. The most common instances of the use of technology programs cited by Survey respondents pertained to issues associated with data security and privacy, anti-money laundering practices, record retention technologies and legislative and regulatory monitoring.

"Hot Topics"

The Survey also sought to assess respondents' viewpoints with respect to potential "hot topics" facing compliance and ethics professionals in the life insurance industry in the months ahead. Topics were identified most frequently by Survey respondents in the following order of importance: Unclaimed Property (92%), Market Conduct Exams (72%), Social Media (69%), Anti-Money Laundering (52%), Know Your Customer (44%), ERM/ORSA (41%), Foreign Account Tax Compliance Act (FATCA) (31%), and Office of Foreign Assets Control (OFAC) (31%).

Hot Topics Identified Most Frequently by Survey Respondents



Summary

The overall Survey results indicate that there continues to be strong support for sound compliance and ethics practices in the life insurance industry. These findings are supported by Survey respondents who work in the compliance and ethics functions within their respective companies and, therefore, have unique insights into the compliance and ethics functions of their companies.

The Survey found that companies apply a variety of organizational structures with respect to their compliance departments. The largest percentage of Survey respondents indicated that their companies are organized in a way that allows the compliance department to serve as a standalone department. The results of the 2012 Survey indicated that this practice of separate departments was dominated primarily by large companies. In contrast, the results of this year's Survey indicate that more medium and small-sized companies are moving to an organizational model that allows compliance to be distinct from the legal department. However, this year's Survey results still indicated that many companies maintain an organizational structure that places the compliance function within the legal department. A smaller number of companies have chosen to pursue a decentralized compliance organizational model that embeds compliance employees within specific business units while still others choose what could be described as a "hybrid" model where compliance serves as an "umbrella department" with compliance representatives embedded within specific business units.

While virtually all Survey respondents indicated that their organizations maintain a position for a Chief Compliance Officer, the nature of the reporting relationships for Chief Compliance Officers differed. The most common reporting relationship for the Chief Compliance Officer is to report to the company's General Counsel with many Chief Compliance Officers also having a "dotted line" reporting relationship to the company's Chief Executive Officer or other executive (e.g., Chief Risk Officer).

One of the key functions for a Chief Compliance Officer is to provide written reports of compliance outcomes for the company's Board of Directors (or Board Committee). For many Survey respondent companies, these reports are required to be provided on a quarterly basis. In some instances, the reports are delivered to the Board by the Chief Compliance Officer whereas in other cases the reports are developed by the Chief Compliance Officer and are delivered by the company's General Counsel or CEO.

As anticipated, staffing levels and budgeting allocations within compliance and ethics departments were driven largely on the basis of company size (i.e., larger companies required more compliance and ethics staff). It is interesting to note that compliance and ethics professionals affiliated with small companies often have to cover a significant range of issues with relatively limited staff. We have heard anecdotal reports suggesting that compliance and ethics professionals affiliated with small companies place high value on networking opportunities with other compliance and ethics professionals as a way to gather additional insights into compliance challenges and leverage their compliance resources. Alternatively, large companies appeared to exhibit a greater degree of flexibility with respect to their assignment of staff to specific subject matters and the overall budget resources available to achieve their compliance and ethics objectives.

The Survey also sought to determine changes in compliance staffing over the past 18 months. While the recent economic downturn may have served as a rationale for overall corporate staffing reductions that may have impacted compliance departments as well, Survey respondents indicated that reductions in compliance staff were part of company-wide decisions to reduce staff which were applicable to all employees rather than a lack of dedication of resources to the

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compliance function. In fact, in many cases, companies added to compliance staff notwithstanding this recent challenging economic environment.

This year's Survey also sought to determine the extent to which companies maintain a separate ethics (or business conduct) program (as distinct from compliance). Consistent with the results of last year's Survey, this year's Survey continues to confirm that a small percentage of companies (primarily large companies) maintain a separate ethics (or business conduct) program. For most companies, the ethics program is embedded in the overall compliance and ethics program. In a few cases, some companies require business units to develop distinct ethics programs related to specific business functions.

This year's Survey results also confirmed last year's Survey results to note that a small percentage of companies maintain a separate position for a Chief Ethics Officer. Again, this practice is primarily associated with large companies who have had such positions in place for over 4 years. The Survey results indicated that most Chief Ethics Officers report to the General Counsel or to the CEO (and not to the Chief Compliance Officer). These results suggest that several companies have taken the step to formally recognize ethics as a functional business area distinct from compliance. For many Survey respondents, they indicated that responsibility for ethics within their respective organization lies within the role of the Chief Compliance Officer. This year's Survey also noted that several companies have moved to develop a single role of Chief Ethics and Compliance Officer as a way to acknowledge the independence though interrelatedness of these two important functions.

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The Survey also gathered data regarding the scope of subject matters falling within the compliance function. Specifically, Survey respondents were asked to identify those subject matters for which compliance is directly responsible. The Survey results indicated that, for most companies, consumer protection, anti-money laundering, regulatory relationships, fraud prevention, privacy and confidentiality in life insurance

industry-specific regulations were areas for which the compliance department assumes primary responsibility. It also was recognized, however, that compliance is engaged in a variety of subject matters through coordination with other company functions to arrive at a successful resolution. Issues such as conflicts of interest, fair competition and antitrust matters, anti-corruption and bribery, intellectual property of insider trading were examples of issues that Survey respondents identified as often requiring coordination with other company functional departments.

Measuring the effectiveness of compliance programs is a growing and challenging issue. The Survey results indicated that more companies are moving to various compliance metrics as a way to measure the effectiveness of their compliance programs. For most companies, the effectiveness of the compliance function is evaluated periodically by their internal audit department. We were encouraged to observe that the Survey results indicated that many companies supplement this internal audit analysis of the compliance department's effectiveness through their own self-assessment processes. Of those companies that reported that they conduct self assessments of their compliance function, over half indicated that they conduct these self assessments on a continuous basis. For companies that use compliance metrics to evaluate their compliance function, the most common metrics cited were complaints, replacements, trend monitoring and regulatory fines and penalties.

For most companies, the effectiveness of the compliance function is evaluated periodically by their internal audit department. We were encouraged to observe that the Survey results indicated that many companies supplement this internal audit analysis of the compliance department's effectiveness through their own self-assessment processes. Of those companies that reported that they conduct self-assessments of their compliance function, over half indicated that they conduct these self-assessments on a continuous basis.

Slightly over half of the Survey respondents indicated that they convene a Compliance Committee periodically which is comprised of representatives from other company functional areas to review and resolve various compliance issues. The

functional areas that most Survey respondents identified as serving on their Compliance Committee include: legal, operations, sales and marketing, internal audit in human resources.

When asked to describe their ethics program, the Survey results indicated that companies that maintain ethics programs utilize many elements to achieve their program objectives. These elements include: code of ethics/conduct, training, communication, anonymous reporting, and ethics hotline, whistleblower hotline and investigations. Companies also use a variety of techniques to reinforce the importance of ethics with their staff. These practices include use of company intranets and public statements by senior management to reinforce the importance of ethics in the company's culture of compliance. We also were encouraged to see that many companies have taken the step to include ethics and adherence to the company's values as part of an employee's performance evaluation criteria.

Most Survey respondents indicated that their organization utilizes technology specifically tailored to address their compliance needs. The issues that were cited most commonly as requiring specific technology needs included: data security and privacy, anti-money laundering practices, record retention technologies and legislative and regulatory monitoring.

We concluded this year's Survey by asking the respondents to identify what they considered to be the "hot topics" facing the life insurance industry compliance and ethics professionals over the months ahead. The topics they identified (listed in descending order) were: unclaimed property, market conduct exams, social media, anti-money laundering, know your customer, ERM/ORSA, FATCA and OFAC.

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CEFLI and PricewaterhouseCoopers LLP would like to thank all compliance and ethics professionals from CEFLI Member Companies as well as non-CEFLI Member Companies who responded to the 2013 CEFLI Compliance and Ethics Benchmarking Survey for offering their insights and perspectives. We hope that all Survey respondents find this information to be useful. CEFLI also would like to thank its Member Companies and Affiliate Members for their financial support of the 2013 CEFLI Compliance and Ethics Benchmarking Survey.

THE FORUM THAT CONNECTS.

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