



K a n s a s I n s u r a n c e D e p a r t m e n t

Sandy Praeger

COMMISSIONER OF INSURANCE

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For more information, contact:
Charlene Bailey
785-296-7807 (office)
785-221-4768 (cell)

Commissioner Sandy Praeger Announces \$11 Million Recovery

TOPEKA, KS -- Insurance Commissioner Sandy Praeger announced today that she, working with other states, has recovered \$11 million from the brokerage firm of Waddell & Reed, Inc. Consumers who were wronged will be awarded compensation from an \$11 million fund. In addition, the Insurance Department will receive \$145,291 in penalties as its share of the settlement. Other states will also be awarded penalties.

“Waddell & Reed violated the principles of good business by engaging in a deliberate campaign to switch customers from one variable annuity to another,” said Praeger. “These switches were recommended without regard to whether the transactions were in the customers' best interests.”

On January 14, 2004, the National Association of Securities Dealers (NASD) filed a complaint charging Waddell & Reed, Inc., for recommending 6,700 variable annuity exchanges to its customers without determining the suitability of the transactions. These exchanges, known as "switching," generated \$37 million in commissions and cost Waddell's customers nearly \$10 million in surrender fees. NASD also alleged that according to its analysis, at least 1,400 of the firm's customers were likely to lose money by making these switches.

Under the terms of the settlement, Waddell & Reed will repay customers one hundred percent of all surrender charges they incurred in the exchanges, and will compensate the purchasers of the more expensive annuity by repaying the cost difference between the two products. Waddell and Reed will also, at its own expense, retain an independent consultant to implement the repayment plan. Approximately 850 Kansans were affected by the variable annuity exchanges. Waddell & Reed will be sending letters to all customers that were the victim of this scheme.

Variable annuities are often described as mutual funds wrapped in an insurance policy. They are contracts between an investor and the company selling it in which the company agrees to make periodic payments to the investor, beginning immediately or at some future date. They are sold through brokerage firms and insurance agencies. Their periodic payouts change depending on the performance of underlying investments.

Waddell & Reed began its “switching campaign” after the brokerage firm failed to secure an agreement from United Investors to share fees it collected from customers. The firm then approached Nationwide, which agreed to split fees.

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Customers were told the Nationwide annuity would provide a better return than the United Investors product, despite the fact the mutual funds in which each of the products were invested were the same, according to the regulators. The switching is said to have delayed customers' access to the funds for eight years unless they paid substantial penalties.

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About the Kansas Insurance Commissioner

Sandy Praeger, Kansas Insurance Commissioner, oversees the activities of the Kansas Insurance Department (KID) which is headquartered in Topeka, Kansas. The overriding objective of Commissioner Praeger and KID is to protect consumers, and help maintain the financial stability of the insurance industry. KID regulates and monitors the activities of 23,000 resident agents, 42,000 non-resident agents and 1684 insurance companies licensed to do business in the state of Kansas. The Department offers financial, actuarial, legal, computer, research, market conduct and economic expertise. For more information, visit www.ksinsurance.org.