



COMPLIANCE & ETHICS FORUM FOR LIFE INSURERS

COI Litigation and Regulatory Developments: What You Need To Know

*CEFLI Educational Webinar
January 29, 2019*

2019 CEFLI Premier Partners



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Agenda

- CEFLI's Antitrust Policy.
- Presentation.
- Q & A.
- Post-meeting Survey.

Presenters

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Cost of Insurance (“COI”) Litigation and Regulatory Developments: What You Need To Know

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Agenda

- Brief history of COI rate litigation
- Current wave of COI rate litigation
- Regulatory issues and related actuarial considerations

COI Rate Litigation

History of COI Litigation

- Reported decisions dating back to 1990's
- Phoenix cases drew attention
- Typically lawsuits followed increases
- Focus typically was on breach of contract

Common COI Rate Provisions – “Based On”

1. The monthly COI rate is based on your attained age, sex, and rating classification.

[and/or]

2. The COI rates are based on our expectations as to future mortality experience [single consideration]; **or**

The COI rates are based on our expectations of future mortality, persistency, investment earnings, expense experience, capital and reserve requirements, and tax assumptions [multiple consideration]; **or**

The COI rates are based on our expectations as future experience.

[and/or]

3. However, the COI rates for your rating classification will not be greater than the guaranteed maximum shown in the policy schedule. The guaranteed maximum rates are based on the 1980 CSO Mortality Table, Male or Female, age nearest birthday. We may use lower monthly COI rates than those shown in the policy schedule at our option.

Competing Reported Decisions – “Based On”

	Norem v. Lincoln Ben. Life Co., 737 F.3d 1145 (7th Cir. 2013)	Fleisher v. Phoenix Life Ins. Co., 18 F. Supp. 3d 456 (S.D.N.Y. 2014)
Policy	“The cost of insurance rate is <i>based on</i> the insured’s sex, issue age, policy year, and payment class.”	“[S]uch rates will be <i>based on</i> our expectations of future mortality, persistency, investment earnings, expense experience, capital and reserve requirements, and tax assumptions.”
Holding	Language is <u>unambiguous</u> and the listed factors <u>are not the exclusive factors</u> to be considered by the insurer.	Language is <u>ambiguous</u> and construed against insurer to mean that the listed factors <u>are the exclusive factors</u> to be considered by the insurer.

The Current “Wave” of Putative COI Class Action Litigation

Class Actions Filed Re: COI Rate Increases	Class Actions Filed Re: Failure to Decrease COI Rates	Class Actions Filed Re: Determination of COI Rates
<i>In re AXA COI Litigation</i> , No. 1:16-cv-740 (S.D.N.Y.)*	<i>37 Besen Parkway, LLC v. John Hancock Life Ins. Co.</i> , No. 1:15-cv-9924 (S.D.N.Y.)	<i>Taylor v. Midland National Life Ins. Co.</i> , No. 4:16-cv-140 (S.D. Iowa)
<i>Feller v. Transamerica Life Ins. Co.</i> , No. 2:16-cv-1378 (C.D. Cal.)*	<i>Larson v. John Hancock Life Ins. Co.</i> , No. RG16813803 (Cal. Super.)	<i>Vogt v. State Farm Life Ins. Co.</i> , No. 2:16-cv-4170 (W.D. Mo.)
<i>Hanks v. Lincoln Life & Annuity Co. of N.Y.; Voya Ret. Ins. & Annuity Co.</i> , No. 1:16-cv-6399 (S.D.N.Y.)	<i>Glover v. Connecticut Gen. Life Ins. Co & Lincoln Nat. Life. Ins. Co.</i> , No. 3:16-cv-827 (D. Conn.)	<i>Smithson v. Jackson National Life Ins. Co.</i> , No. 2:17-cv-7485 (C.D. Cal.)
<i>Dickman v. Banner Life Ins. Co.</i> , No. 1:16-cv-192 (D. Md.)	<i>Iwanski v. First Penn-Pacific Life Ins. Co.</i> , No. 2:18-cv-1573 (E.D. Pa.)	<i>Sides v. State Farm Life Ins. Co.</i> , No. 2:18-cv-60 (M.D. Ala.)
<i>In re Lincoln COI Litigation</i> , No. 2:16-cv-6605 (E.D. Pa.)*	<i>Advance Trust & Life Escrow Services, LTA v. Security Life of Denver Ins. Co.</i> , No. 1:18-cv-1897 (D. Colo.)	<i>Maxon v. Sentry Life Life Ins. Co.</i> , No. 3:18-cv-254 (W.D. Wis.)
<i>Farris v. U.S. Financial Life Ins. Co. (AXA)</i> , No. 1:17-cv-417 (S.D. Ohio)	<i>Advance Trust & Life Escrow Services, LTA v. Reliastar Life Ins. Co.</i> , No. 18-cv-2863 (D. Minn.)	<i>Bally v. State Farm Life Ins. Co.</i> , No. 18-cv-4954 (N.D. Cal.)
<i>Spegele v. USAA Life Ins. Co.</i> , No. 5:17-cv-967 (W.D. Tex. Sept. 29, 2017)	<i>Advance Trust & Life Escrow Services, LTA v. Protective Life Ins. Co.</i> , No. 2:18-cv-1290 (N.D. Ala.)	<i>Davis v. State Farm Life Ins. Co.</i> , No. 2:17-cv-8773 (C.D. Cal.)
<i>Rich v. William Penn Life Ins. Co.</i> , No. 1:17-cv-2026 (D. Md.)	<i>TVPX ARS Inc. v. Lincoln National Life Ins. Co.</i> , No. 2:18-cv-2989 (E.D. Pa.)	
<i>Fan v. Phoenix Life Ins. Co.</i> , No. 1:18-cv-1288 (S.D.N.Y.)	<i>TVPX ARS Inc. v. Genworth Life and Annuity Ins. Co.</i> , No. 3:18-cv-637 (E.D. Va.)	
<i>Leonard v. John Hancock Life Ins. Co.</i> , No. 1:18-cv-4994 (S.D.N.Y.)		
<i>Fairlie v. Transamerica Life Ins. Co.</i> , No. 1:18-cv-32 (N.D. Iowa)		
<i>McMahon v. Transamerica Life Ins. Co.</i> , No. 1:17-cv-149 (N.D. Iowa)		
<i>Thompson, et al. v. Transamerica Life Ins. Co.</i> 2:18-cv-05422 CAS (C.D. Cal.)		

Some new plaintiffs' bar "theories" and emphases include:

- Allegations of recouping prior losses
- Reserves and dividends "theory"
- "Bait and switch" allegations
- Allegations of unfair discrimination
- Alleged breach of duty of good faith and fair dealing
- Other non-contract claims (e.g. conversion, fraud, unjust enrichment, elder abuse, and other statutory claims)
- Alleged obligation to lower rates
- General mortality rates allegedly improving

COI Increase: *Feller, et al. v. Transamerica Life Insurance Co.* (C.D. Cal.)

- Plaintiffs allege that Transamerica used COI to subsidize alleged losses due to (1) allegedly weakened financial condition through captive reinsurance transactions and dividend payments, and (2) declining interest rates
- December 11, 2017: Court granted plaintiffs' motion for class certification and certified a national class and two California subclasses that consist of owners of in-force policies
- Appealed to Ninth Circuit
- Potential class of 70,000 policyholders settled for \$195 million (representing 62% of alleged past overcharges), plus the first \$10 million awarded in costs and attorney's fees

COI Decrease

- Import of *Lincoln National v. Bezich*, 33 N.E.3d 1160 (Ind. Ct. App. June 2, 2015)

“We cannot help but comment on the absurdity of Lincoln’s own interpretation of the COI rate provision which is that the [policy] *allows Lincoln to unilaterally increase rates on customers to reflect a change in mortality factors but offers no parallel commitment to decrease rates despite an overwhelming improvement in mortality.* We have grave doubts that any policyholder of average intelligence would read the COI rate provision to confer on Lincoln that sort of ‘heads we win, tails you lose’ power.”

COI Decrease (Cont.)

- *37 Besen Parkway, LLC v. John Hancock Life Ins. Co.*, Case No. 15-cv-9924 (S.D.N.Y)
- Policy language at issue:

The Applied Monthly Rates are the actual rates used to calculate the Cost of Insurance Charge. We will determine the Applied Monthly Rates to be used for this policy. They will not exceed the applicable Maximum Monthly Rates shown in the applicable Table of Rates in Section 2. The Applied Monthly Rates will be based on our expectations of future mortality experience. They will be reviewed at least once every 5 Policy Years. Any change in Applied Monthly Rates will be made on a uniform basis for Insureds of the same sex, Issue Age, and Premium Class, including tobacco user status, and whose policies have been in force for the same length of time.

COI Decrease (Cont.)

- Two putative classes: (1) policyholders who have been forced to pay allegedly unlawful and excessive COI charges, and (2) policyholders who have been charged allegedly unlawful and excessive premiums under an “Age 100 Waiver of Charges Rider”
- Plaintiffs filed motion for class certification
- Case settled for \$91.25 million (represent 42% of the alleged overcharges to roughly 70,000 policyholders)

COI Rate Determinations – *Vogt v. State Farm*, No. 2:16-cv-4170 (W.D. Mo.)

- Policy language at issue

Monthly Cost of Insurance Rates. These rates for each policy year are based on the Insured's age on the policy anniversary, sex, and applicable rate class. A rate class will be determined for the Initial Basic Amount and for each increase. The rates shown on page 4 are the maximum monthly cost of insurance rates for the Initial Basic Amount. Maximum monthly cost of insurance rates will be provided for each increase in the Basic Amount. We can charge rates lower than those shown. Such rates can be adjusted for projected changes in mortality but cannot exceed the maximum monthly cost of insurance rates. Such adjustments cannot be made more than once a calendar year.

COI Rate Determinations (Cont.)

- Plaintiffs alleged State Farm breached contract by considering factors other than mortality, including age, sex, and rate class, when setting COI rates
- State Farm alleged policy allowed for consideration of other factors, such as expenses and persistency, when setting COI rates
- Summary Judgment: “no reasonable lay person would expect that State Farm was permitted to use any factor it wanted to calculate the cost of insurance”
- Jury awarded \$34.3 million in compensatory damages to a class of over 43,000 policyholders; punitive damages rejected
- Case on Appeal

Recent Decisions and Cases to Watch

- *Glover, et al. v. Connecticut General Life Ins. Co. and Lincoln National Life Ins. Co.* (D. Conn.)
- *Thompson, et al. v. Transamerica Life Ins. Co.* (C.D. Cal.)
- *Advance Trust & Life Escrow Services, LTA, et al. v. Protective Life Ins. Co.* (N.D. Ala.)

Recent Decision – *Glover*

- Plaintiff alleged defendants breached contract by considering factors other than future mortality expectations when setting COI rates, and failed to decrease COI rates in light of allegedly improving expectations as to future mortality experience
 - Policy: “monthly cost of insurance rates” are:
 - “based on the sex, attained age (nearest birthday) and Premium Class of the person Insured as described under the ‘Cost of Insurance Rates’ provision,” and
 - “based on [the company’s] expectations as to future mortality experience.”
- Defendants moved for judgment on the pleadings

Recent Decision – *Glover cont.*

- Lincoln National argued, *inter alia*, that the “based on” language was nonexclusive and that the complaint does not plausibly allege an improvement in expectations as to future mortality experience
- Connecticut General argued, *inter alia*, that the “based on” language was nonexclusive, that the statute of limitations barred plaintiff’s claims and that plaintiff ratified the COI charges, which were displayed on her annual statements
- January 11, 2019: Court granted defendants’ motions
 - “Based on” language was non-exclusive; “[w]ritten ruling will follow”
 - Plaintiff given until February 26 to file amended complaint

Recent Decision – *Thompson*

- December 26, 2018: Court rules on Transamerica’s motion to dismiss, stating:
 - “The provisions at issue here appear to be susceptible to plaintiff’s interpretation that Transamerica may not increase MDRs to recoup past losses, to avoid future losses, to make the Policies more profitable than assumed at issuances, or to avoid, subsidize, or defray the costs associated with its own no-lapse guarantees, and that Transamerica may not increase MDRs when there is no reasonable expectation of future adverse changes in legitimate cost factors. Plaintiff alleges that the MDR increases breached the Policies’ MDR provisions because they were not based on Transamerica’s actual expectations as to future cost factors but were rather based on a number of impermissible factors.”

Expected Decision – *Advance Trust*

- October 30, 2018: Protective moved for judgment on the pleadings on the grounds that plaintiff's claim was untimely
- November 7, 2018: Court ordered plaintiff to show cause why defendant's motion for judgment on the pleadings should not be granted
- Motion is fully briefed, but not yet decided

Regulatory Issues

Actuarial Considerations and Issues

- Actuarial standards of practice (ASOPs) and actuarial issues
 - Determination / Redetermination Policy (ASOP 2)
 - Cost Factors (ASOP 2)
 - Profitability (ASOP 2)
 - Past Losses (ASOP 2)
 - Class Issues (ASOP 2 and 12)

Actuarial Considerations and Issues

- Mortality Issues
 - Industry Mortality Tables
 - Older Aged Mortality
 - Mortality Improvement?
- Annual Statement Interrogatories
 - “Does the undersigned believe there is a substantial probability that illustrations authorized for new and existing business cannot be supported by current anticipated experience? If yes indicate which classes and explain”
 - Public statements on NGEs and Cost Factors

N.Y. Insurance Regulation 210 (“Reg. 210”) - Purpose

- Establish standards for the determination and readjustment of non-guaranteed elements
- Ensure policy forms do not mislead policy owners as to the crediting of non-guaranteed amounts or the deduction of non-guaranteed charges
- Ensure policy forms do not contain unjust, unfair, or inequitable provisions

Reg. 210 - Key Regulation Requirements

- Board Approved Criteria – Section 48.2(a)(1)
- Policy Owner Disclosure – Section 48.3(a)
- Adverse Change Disclosure – Section 48.3(b)
- Adverse Change Filing – Section 48.4(d)
- Adverse Change Annual Reporting – Section 48.4(e)

California AB 2634

- Passed on September 19, 2018
- Effective April 1, 2019
- Less onerous than Reg. 210
- Requires 90-day notification for any adverse change in scale of non-guaranteed elements
- Notice to policyholders must provide certain options

Takeaways

- Potential Future COI Rate Adjustments
- Policy Language Review
 - Single-factor policy language
 - Timing requirements
- Synergy with regulatory guidance and reporting
 - Annual Filing Requirements
 - Public Statements on Experience

Questions?

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We'd Love to Hear From You

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