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TOPIC: Class Action Claims Alleging Fraud Against Annuity Carrier Dismissed

CITE: *Harrington v. Equitrust Life Insurance Company*, No. 12-17267 (U.S.D.C. Dist AZ, Feb 24, 2015).

SUMMARY: This class action case was filed against EquiTrust Life Insurance Company ("EquiTrust") in federal district court in Arizona, alleging violations of federal and state law in the sale of annuities. The district court granted EquiTrust's motion for summary judgment. The federal appeals court affirmed the summary judgment of the District Court and sent the case back to the district court either to award EquiTrust the costs of litigation or explain its refusal to do so.

RELEVANCE: Sometimes, whether by ignorance or misunderstanding, policy owners have unrealistic expectations about how a permanent life policy or an annuity will perform. The best way for a financial professional to help avoid a client's misperceptions about product performance is by providing as complete a body of information as possible.

In this case, the court ruled that the insurance company provided ample information about the annuity product's pricing and expected performance. The buyer still sued; however, the court ultimately vindicated the conduct of the carrier.

FACTS: In 2007, Paul Harrington purchased an EquiTrust MarketPower Bonus Index Annuity from an insurance agency. The annuity used index accounts to generate index credits that increased the annuity's accumulation value. Index credits were calculated based on periodic changes in the closing value of the S & P 500.

Under the contract, EquiTrust has the express discretion to choose the amount of index credits awarded (the index cap), but the annuity guaranteed a minimum cap.

The annuity permits annual withdrawals of up to 10% of the accumulation value with no penalty. Larger withdrawals are subject to:

> (1) a surrender charge, a specified percentage of the accumulation value that decreases each year until it disappears in the fourteenth year; and

> (2) a market value adjustment ("MVA"), which increases or decreases the accumulation value based on interest rates in the market.

After his 105th birthday, the policy owner can opt to receive the accumulation value incrementally for a specified period without any surrender charges or market value adjustments. When the annuitant dies, the full accumulation value is available to beneficiaries.

Harrington's initial premium was $432,530.92. The annuity included a premium bonus, under which EquiTrust added to the accumulation value a sum equal to ten percent of the premiums paid during the first year.

Harrington's claimed that the insurer's promise of the ten percent premium bonus was fraudulent because EquiTrust failed to disclose that it did not invest any additional money in the market when crediting the bonus to a policy owner's account. EquiTrust would eventually recoup the bonus, he alleged, by crediting lower index credits to the annuity than it might have in an annuity contract without the bonus feature. Harrington argued that the bonus was *illusory*, because the ultimate increase over time in the accumulation value from the bonus might be less than increases that would occur for an annuity which provided higher returns. He filed a class action lawsuit, alleging that EquiTrust's marketing of the annuity violated the Racketeer Influenced and Corrupt Organizations ("RICO") Act and Arizona law. Harrington also argued EquiTrust failed to disclose all the factors that would affect the MVA, and that such failure constituted fraud.

Harrington later filed a motion for class certification, and EquiTrust filed a motion for summary judgment. The district court granted EquiTrust's motion, denied class certification, and entered judgment for Equitrust. The court, however, declined to award costs to the prevailing party. Harrington and EquiTrust both appealed.

In answering Harrington's allegation of fraudulent promises, EquiTrust pointed out that it explained in some detail in one of its brochures *exactly* how the annuity bonus worked. Harrington, in response, claimed that EquiTrust had a duty to disclose all elements of its annuity pricing.

The federal appeals court rejected Harrington's argument:

> We begin from the settled premise that a seller generally has no duty to disclose internal pricing policies or its method for valuing what it sells.

It then went further, saying that EquiTrust had done nothing wrong:

> But it is uncontested here that EquiTrust delivered precisely what it promised. The 10% bonus was accurately described in the Annuity materials and properly credited to Harrington's account. The bonus increased Harrington's accumulation value without requiring him to deposit additional funds, allowing him to withdraw more money without penalty than otherwise would have been possible. The promise of a "bonus" was thus not, as Harrington claims, illusory.

The court also found that EquiTrust had adequately disclosed how the MVA worked.

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