WRNewswire
An AALU Washington Report

The WRNewswire is created exclusively for AALU Members by insurance experts led by Steve Leimberg, Lawrence Brody and Linas Sudzius. WRNewswire 16.06.21 was written by Tom Commito of Lincoln Financial Distributors.

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Tuesday, 21 June 2016 WRN 16.06.21

TOPIC: Federal Class Action Suits Filed on COI Changes

CITES: Feller v. Transamerica Life Ins. Co., No. 2:16-cv-01378, (U.S.D.C., C.D. CA); Brach Family Foundation, Inc. v. AXA Equitable Life Ins. Co., No. 1:16-cv-00740-JMF, (U.S.D.C, S.D.N.Y.); 37 Besen Parkway, LLC v. John Hancock Life Ins. Co. (USA), No. 1:15-cv-09924-PGG, (U.S.D.C., S.D.N.Y.); Kriegman, Trustee v. Transamerica Life Ins. Co., No.1:16-cv-21074-KMW, (U.S.D.C., S.D. FL); Fleisher, Trustee v. Phoenix Life Insurance Company, No. 11-cv-8405 (CM)(JMF); CA Bus. & Prof Code Section 17200, et seq.; CA Wel. & Inst. Code Section 15657.5, et seq; "Phoenix settles suit for $134.8M," The Life Settlements Report, Volume IX, No. 18 (Sep 17, 2015).

SUMMMARY: A number of new federal class action lawsuits have been filed against insurers after they announced increases in the cost of insurance (COI) charges for various blocks of universal life business. Recently, at least four different federal class action lawsuits have been filed claiming damages as a result of these increases. All of the filed cases cite breach of contract and breach of fiduciary duty as the main claims for relief, while the case filed in California also pleads violations of California's "Unfair Competition Law" (UCL) and California's "Elder Abuse" statute.

It is important to note a number of issues with respect to these cases. First and foremost, these cases are only at the pleadings stage. There has not been a determination of the validity of these claims.

Second, these are all cases requesting class action status.

Finally, complaints about carriers raising policy charges are not new. Phoenix Life, for one, has been involved with suits involving policy cost increases going back to 1997. In the most recent decided case, a federal district court approved a mediated settlement that reportedly involved the creation of a $29 million fund for policyholders. The plaintiffs in that case apparently purchased the policies in STOLI transactions. Along with the cash, the settlement includes commitments by Phoenix not to raise its cost-of-insurance rates for five years and not to mount insurable-interest legal challenges against the validity of policies held by life settlement investors. Those guarantees are supposedly valued at $94.3 million under the settlement approved September 9, 2015 by Judge Colleen McMahon of the U.S. District Court in Manhattan. The legal fees accruing to the plaintiffs' law firm exceeded $13 million.

RELEVANCE: A number of life insurance companies have recently raised the COIs on various universal life policies. This development has been the subject of much discussion - both within and without the insurance community. For example, the Wall Street Journal on December 4, 2015 published an article entitled, "Surprise: Your Life Insurance Rates Are Going Up." Given current economic conditions, there may be even more increases on additional policies.

In WRNewswire 13.12.18, we discussed two court decisions where the validity of the carrier's decision to raise COI rates was challenged; the results in those cases depended upon the language of the policies regarding the breadth of the carrier's discretion to increase COIs. Those cases were brought by individual policy owners; the new federal class action cases have much higher financial stakes. It remains to be seen how the plaintiffs' legal arguments will play out.

If these cases go to trial, a number of important issues will have to be decided. Among these are:

- When can an insurer change charges in a policy? Does it depend on the language of the policy? Does it require a showing that the insurer's mortality experience has worsened?

- If the increased charges are below the maximum guarantees, is there a cause of action?

- Will insurers re-write policies so that they can freely change items such as COI without inviting lawsuits?

- In policies, what is meant by a "class" of policyholders? Is it all policyholders? Is it policyholders of the same age? Same sex? Same underwriting class?

- In defining the word “class” what expenses can be increased on one class that only affect that class - and does not affect other owners of the same policy?

- What are the money damages if a plaintiff is successful? How are they computed?

FACTS: The New York Cases

The New York cases have been filed by the same law firm which represented the plaintiffs in the above-mentioned Phoenix Life case. While the defendants are different insurance companies, the complaints are very similar. The policies were “minimum funded.” The complaint in Brach states this as follows:

> Flexible-premium policies are preferred by many policy owners because they allow the owners to pay the bare minimum required to keep the policy in force (that is, the policy owners can keep the policies' Policy Account Value as low as possible) while preserving capital for other investments that yield higher returns than the interest credited on the Policy Account. Policyholders can choose to keep their Policy Account Value as close to zero as possible-in other words, they can choose not to pay any more premiums than the absolute minimum to cover COI and the other administrative expenses.

The argument here is that minimum funded policies are particularly sensitive to COI increases and that these policies have been unfairly singled out by AXA.

Of critical importance in the Brach complaint is the following policy language:

> Changes in policy cost factors (interest rates we credit, cost of insurance deductions and expense charges) will be on a basis that is equitable to all

> policyholders of a given class, and will be determined based on reasonable assumptions as to expenses, mortality, policy and contract claims, taxes, investment income, and lapse. . . . Any change in policy cost factors will be determined in accordance with procedures and standards on file, if required, with the insurance supervisory official of the jurisdiction in which the policy is delivered. [Emphasis added].

The plaintiffs argue that it was this provision which created the breach of contract, since the COI increases were made only on policies where the insured was over age 70 and the face amount exceeded $1 million. The thrust of the argument is that this group of insureds is not a "class." Rather, they argue, all insureds of this particular policy is “the class”. The issue of what is a class may lie at the heart of any court decision.

In the 37 Besen Parkway case, the plaintiffs made a unique argument, stating that John Hancock agreed to review COIs every five years. They continued by asserting that Hancock breached the contract by not lowering the COIs, which they should have done since mortality is improving. The main thrust of the complaint is similar to Brach. Hancock had an age 100 mortality rider, which extended the death benefit beyond age 100. The policy provided that the cost of this rider is to be borne by insureds age 32 or younger. However, Hancock raised the COIs for all policies which had the rider. The plaintiffs here are insureds on a second-to-die policy who are now well into their 80s. Their argument is that raising the COIs on insureds older than age 32 is a breach of contract and that the class of insureds older than age 32 are being discriminated against.

The California Case

The California case is interesting in that a consumer watch-dog organization is participating in the suit. The suit alleges that the COI increases are a device to raise profitability due to persisting low interest rates. The complaint alleges that a reasonable person would believe that COIs are based solely on mortality and that mortality is getting better - not worse – so the raising of COI rates is unfair.

A second claim is made based on a theory of "breach of an implied good faith and fair dealing." The complaint addresses this with the following:

> As alleged above, Transamerica has breached these duties in connection with the MD Rate Increase, frustrating the reasonable expectations of Plaintiffs and

> the Class Members under the Policies and tortiously depriving them of benefits under the Policies. In increasing the Monthly Deduction, Transamerica did not give proper consideration to the welfare of Plaintiffs and the Class Members and served solely its own interests at their expense. In addition, Transamerica has failed to truthfully, let alone reasonably, disclose or describe its course of conduct, or the basis and reasons for its course of conduct.

Yet another cause of action listed in the complaint is a violation of California's unfair competition statute. The complaint outlines the unfair practice as follows:

> Marketing and selling the Policies on the premise that they were a solid and good life insurance product that would provide a certain death benefit for a certain cost and duration and subsequently taking steps to prevent Policyholders from receiving the promised benefits from those Policies by suddenly, massively, and unlawfully increased mortality upon which the original MD Rate schedule is based - in order to increase premiums, recoup past losses, and/or force its insureds to surrender (cancel) their Policies, all of which was, and is, contrary to, and precluded by, the express terms of the Policies.

The final allegation relates to California's elder protection law, as the plaintiffs are all older than age 65. The complaint alleges:

> Transamerica is guilty of oppression, fraud, and malice in the commission of the above-described acts of abuse. At a minimum, Transamerica knew or should have known that its conduct was likely to be harmful to elders.

The Florida Case

This case against Transamerica also alleges that the COI increases are really meant to recoup losses due to interest rates remaining very low. Specifically, the suit alleges breach of contract on three grounds, expressed, as follows:

> Transamerica breached the policies by increasing COI to recoup past losses, which is not one of the permissible, implied, or express bases for increasing COI;…
>
> > b. Transamerica breached the policies by increasing COI on bases that do not apply equitably to the class of insureds; and

c. Transamerica breached the policies because Transamerica's COI increase was not based on the permissible factors stated in the policies, which are tied to expectations of future experience and not recoupment of past losses;

In addition, like the California case, the plaintiffs allege a breach of an implied covenant of good faith and fair dealing. The arguments to support this claim are as follows:

Transamerica breached the implied covenant of good faith and fair dealing by, among other things:

a. Undermining Plaintiff's right to pay premiums as needed to cover the monthly deductions;

b. Exercising its discretion to increase the COI to recoup past losses;

c. Misrepresenting to Plaintiff and the Class members the reasons for the COI increase; and

d. Negating the value of what were intended to be guaranteed interest rates, which Transamerica has no right to do.
