

SchulteRoth&Zabel



# Legal Update

## **ELSA & BVZL International Life Settlement Investor Conference 2016**

Stephen G. Foresta  
Partner  
Orrick, Herrington & Sutcliffe  
+1 212.506.3744 | sforesta@orrick.com

Thomas R. Weinberger  
Partner  
Schulte Roth & Zabel LLP  
+1 212.756.2762 | thomas.weinberger@srz.com

September 26, 2016

# Life Settlement Policies Affected



Insurers that have increased COI rates:

Phoenix	PHL Variable Phoenix Life
AXA	<b>AXA Equitable</b> US Financial MONY
Aegon	<b>Transamerica</b> Western Reserve
Voya (ING)	Reliastar Security Life Of Denver Voya America
Conseco	Conseco Life
Legal & General	William Penn Banner Life
Lincoln Financial	Aetna <b>Lincoln National</b>

# COI Increases and Litigation Activity



Group	Subsidiaries	Increase Dates	Increases	Litigation Status
AXA	US Financial AXA Equitable	August 2015 March 2016	25%-70%	Pending Class Action in NY
Aegon	Transamerica	August 2015	5%-38%	Pending Class Action in CA
Aegon	Transamerica	March 2016	90%-100%	No new actions filed
Legal & General	William Penn Banner Life	August 2015 Sept 2015	95%-600%	Pending Class Action in MD
Voya (ING)	Reliastar Security Life Of Denver	Oct 2015	10%-42%	No actions filed
Lincoln	Aetna (as reinsurance administrator)	May 2016	30%-55%	No actions filed
Lincoln	Lincoln National (Jefferson Pilot book)	August 2016	60%-80% (?)	No actions filed



- **Life Settlement Trade Organizations: ILMA, LISA, BVSL, ELSA**

- ILMA sent complaint letter to insurance regulators in nine U.S. states

- **Consumer Federation of America (CFA)**

- Letter sent to state insurance commissioners to take action and prohibit any unfair price increases being imposed on consumers who own UL policies

- **Class Action Litigation**

- Hancock Class Action (filed December 2015)
- AXA Class Action (filed February 2016)
- Transamerica Class Actions (filed February/April/May 2016)

- **Sole Investor Lawsuit**

- Provides complete control and autonomy over litigation, including settlement
- Avoids “herd mentality”
- High visibility as name plaintiff has pros and cons
- May not align with the interest of trade organizations or other investors

- **Investor Consortium**

- Strength (and value) in numbers
- Aligns interests with other investors
- Participation grants access to influence the litigation
- Provides a seat at the table for settlement discussions

# Regulatory Considerations: Actuarial Opinion



- **Model Actuarial Opinion and Memorandum**
  - **Asset Adequacy Test**
    - **A detailed review of actuarial assumptions and methods used to determine to reserves.**
    - **As part of the review, the company actuaries undertake a detailed and complex cash flow testing.**
    - **Consideration is given to the relevant policy provisions and the assumptions used in preparing the insurer's annual report.**

# Regulatory Considerations: Memorandum



- **The actuarial memorandum accompanying the asset adequacy analysis provides details regarding each product, including:**
  - **the reserves established for each product,**
  - **the liabilities associated with each product, and**
  - **the assumptions used to test reserves.**
- **Key assumptions used to test reserves include:**
  - **mortality,**
  - **persistency,**
  - **investment income, and**
  - **expenses.**

# Regulatory Filings: COI Increases



- **Flexible Factor Life Insurance Products**
  - **New Jersey used to require prior notification and prior approval before a carrier implemented a change to any policy charges.**
  - **In 2003, after undertaking a review of the standards and practices in other states, New Jersey determined that this requirement was unique to New Jersey. As a result, the New Jersey Insurance Code was amended and the prior notification and approval requirement was eliminated.**
- **There is no current requirement to seek regulatory approval to increase COI or to provide prior notice.**



## Await Outcome of Pending Class Litigation

- No litigation expenses
- No publicity and potential reputational risk
- But, no control over litigation
- No seat at the table in settlement discussions.

## File Own Complaint

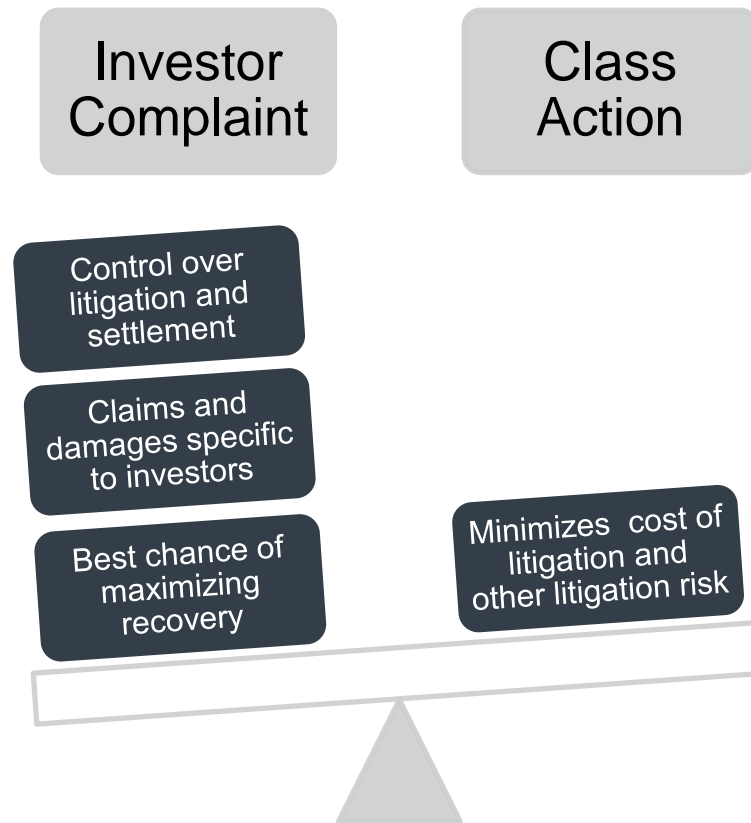
- Complete autonomy and control over litigation and settlement
- Can determine strategy and control expenses
- Avoid “herd mentality”
- High visibility as plaintiff

## Join/Create Investor Consortium

- Strength in numbers
- Share litigation costs
- Influence over litigation and settlement
- But, influence is not control
- Interests of consortium members may diverge as litigation progresses.



# Investor Complaint vs. Class Action





## Allegations in Brach Family Foundation, Inc. v. AXA Equitable Life Insurance Company, No. 16-cv-740, S.D.N.Y. (filed Feb. 1, 2016)

- Putative class action on behalf of all owners of AXA policies subject to COI increase announced in October 2015
- AXA's COI increase targeted investors, who typically minimally fund policy accounts
- Neither of the stated reasons for AXA's COI increase (adverse expectations for mortality and investment income) justifies the increase
- By targeting policies with issuance age >70 and face value >\$1M, AXA is unfairly discriminating within a class of insureds
- AXA violated N.Y. Ins. Law by submitting fraudulent or misleading illustrations to policyholders and answers to interrogatories to regulators



Allegations in *George and Mary Feller, et al. v. Transamerica Life Insurance Company*, Case 2:16-cv-01378 C.D. Cal. (filed Feb. 28, 2016)

- Filed in response to June 2015 increases
- Putative class action brought on behalf of five subclasses: California and National current and surrendered policyholders and California senior policyholders
- Transamerica's COI increase is an illegal attempt to offset high interest crediting rates and to induce lapses
- Constitutes a breach of express and implied terms of policies and violates Cal. Unfair Competition Law Cal. Elder Abuse Statutes
- Plaintiffs are seeking money damages, punitive damages, injunctive relief and reinstatement of lapsed policies

# Contractual Considerations: Changes in Policy Cost Factors



- **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 lapses.**

# Policy Cost Factors: More than Mortality?

- **In determining cost of insurance is a carrier limited to traditional “mortality” factors?**
  - **NO**
    - ***Thao v. Midland Nat. Life Ins. Co.* (E.D. Wisconsin, 2013)**
      - Thao argued that expenses cannot be considered when setting COI rates as there is a separate expense charge.
      - The court held that mortality factors (such as, age, gender, underwriting class) are not the exclusive factors.
    - ***Norem v. Lincoln Benefit Life* (N.D. Illinois, 2012)**
      - The court argued that the policy provided that COI is based on sex, issue age, policy year and payment class, but the carrier considered other factors when it increased rates.
      - “So long as the rates remained below the guaranteed rates, defendant had discretion in setting those rates under the policy.”

# Policy Cost Factors: More than Mortality?

- **In determining cost of insurance is a carrier limited to traditional “mortality” factors?**
  - **YES**
    - ***In re Conseco* (N.D. California, 2013)**
      - **Conseco used policy duration to determine COI increases where the policy provided that “monthly cost of insurance rates, and any change in the monthly cost of insurance as provided herein, are and will be determined on a uniform basis for insureds of the same age, sex, and classification for all policies issued with like benefits and provisions.”**
      - **The court found that the contract does not provide for “duration” as a factor.**
      - **Also, the court held that Conseco may not raise COI rates without regard to changes in mortality rates.**
        - » **Whether the increase was entirely divorced from mortality rates and whether it was done to recoup past losses is an issue of fact to be determined at trial.**

# Insights from the Phoenix Class Action



- In *Fleisher v. Phoenix Life Ins. Co.* the court noted that the policy enumerated six factors that may be considered when raising COI rates; specifically:
  - mortality, persistency, investment earnings, expense experience, capital and reserve requirements and tax assumptions.
- The court held that it was reasonable to conclude that these are the only factors when calculating COI rates.
  - The *Fleischer* court explicitly rejected the reasoning in *Norem*.
  - The court, however, found that policy values were a component of “investment earnings”. The court refused to limit “investment earnings” to the spread.

# The Wisconsin ALJ Decision



- **The Wisconsin Administrative Law Judge found that:**
  - **“These flexible premium universal life policies allow the policyholder to minimally fund the policy if he or she so chooses. The [October 16, 2014] decision found PHL’s policy terms do not permit it to impose monthly substantial increases in cost of insurance charges based on the funding ratio or policy value maintained by the individual policyholder. Yet, in 2010 this is what PHL started doing on a monthly basis.”**





**Partner  
New York**

**T:** +1 212 506 3744

**E:** [sforesta@orrick.com](mailto:sforesta@orrick.com)

**Practice Areas**

- Complex Business Disputes
- Insurance Recovery
- Mass Torts & Product Liability
- International Arbitration

Steve Foresta is a partner in Orrick's New York office and leads the firm's Complex Litigation and Dispute Resolution Practice Group.

Steve also chairs Orrick's Life Settlements Working Group and has extensive experience litigating all aspects of life settlement-related disputes, including insurable interest/STOLI allegations, cost of insurance rate increases, enforcement of contestability clauses, claims of elder abuse, fraud, unfair competition, and others.

He has achieved favorable results in state and federal courts in California, New York, Minnesota, Florida, Oklahoma, and Pennsylvania, as well as before arbitration panels in New York, Minnesota and California. Most recently, Steve led a team that secured a significant victory for an investor in PHL Variable Insurance v. Bank of Utah, when the U.S. Court of Appeals for the Eighth Circuit effectively ruled that under Minnesota law, an insurer cannot contest a life insurance policy outside the contestability period based on lack of insurable interest grounds.

He also successfully defended a life insurance trust in Hartford Life & Annuity Insurance Company v. Doris Barnes Family 2008 Irrevocable Trust, a case brought by a life insurer in the U.S. District Court for the Central District of California seeking to rescind a policy and keep the premiums paid based on an alleged lack of insurable interest and misrepresentations in the policy application.

Steve represented investors in a number of cases brought against Phoenix Life Insurance Company relating to cost of insurance rate increases and death benefit denials, and is currently advising various market participants in connection with the recent wave of COI rate increases.

# Thomas R. Weinberger



## **Thomas R. Weinberger**

Partner

Schulte Roth & Zabel LLP

919 Third Avenue

New York, NY 10022

+1 212.756.2762 | [thomas.weinberger@srz.com](mailto:thomas.weinberger@srz.com)

Thomas R. Weinberger is a partner with Schulte Roth & Zabel, where his practice focuses on asset-backed securities and corporate finance, with an emphasis on insurance and risk-linked securities and specialty finance companies. He has expertise in life settlements, reserve funding transactions, premium finance, longevity and pension risk transfer, alternative risk transfer and marketplace lending and other non-bank finance products. He advises clients on the formation of domestic and offshore funds that invest in the life settlement and premium finance asset classes.

Tom lectures on matters relating to the mortality and longevity markets, and he writes on topics involving life settlements and securities, as well as the financial aspects of alternative energy and climate change disclosures. He earned his J.D. from Columbia Law School, where he was a Harlan Fiske Stone Scholar and Note Editor of the *Columbia Journal of Environmental Law*. He earned his B.S., *magna cum laude*, from Yeshiva University.