Class Backwards: A Discussion of Developments in Market Conduct and Variable/Investment Product Litigation

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by

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I. Historical Perspective – Market Conduct Cases

A. Refresher – Class action litigation based on the plaintiffs' focus on the sale of fixed products.

1. Cases involving vanishing premium, churning, and life insurance as an investment allegations.

The traditional market conduct class action suit emerged on the scene in the mid-1990s. "Market conduct" involves how an insurer and/or its sales force interacts with or carries out its duties to policyholders or applicants. In particular, the manner in which insurance sales transactions were initiated and accomplished and the nature of the information supplied to the policyholder or applicant about the product being sold garnered the most attention from plaintiffs. There were (and are) three primary themes underlying the allegations in these cases.

The majority of class action suits were focused on the sale of so-called "vanishing premium" policies. These complaints alleged "top-down" conspiracy theories premised on alleged home-office sales illustrations. The complaints further alleged that such sales illustrations and other alleged "uniform" sales material had depicted hypothetical rates of return that showed cash values increasing rapidly enough to be able to satisfy premium payments after a specified period of time, therefore, causing premiums to "vanish." When interest rates dropped in the early 1990s, plaintiffs alleged that the failure of the policies to perform in accord with the hypothetical illustrations constituted a breach of contract and fraud. *See, e.g.*, *In re New England Mutual Life Ins. Co. Sales Practices Litigation*, 183 F.R.D. 33 (D. Mass. 1998); *In re Jackson Nat'l Life Ins. Co. Premium Litigation*, 183 F.R.D. 217 (W.D. Mich. 1998).

The second theory of liability in these complaints involved allegations that policyholders were misled about the true nature of the products they purchased, *i.e.*, plaintiffs thought they had purchased a traditional savings or retirement investment product when instead they had a

mere life insurance policy. *See, e.g., Banks v. New York Life Ins. Co.*, 722 So. 2d 990 (La. 1998); *Duhaime v. John Hancock Mut. Life Ins. Co.*, 177 F.R.D. 54 (D.C. Mass. 1997); *Kirkham v. American Liberty Life Ins. Co.*, 717 So. 2d 1226 (La. App. 2d Cir. 1998). Finally, plaintiffs also alleged that they were improperly induced to replace existing insurance products with new insurance policies without being advised of the many disadvantages such as costly surrender charges, and the need to start over building cash value. *Willoughby v. John Hancock Mut. Life Ins. Co.*, No. 96.00307, slip op. (N.Y. Sup. Ct. Feb. 3, 1997); *Banks v. New York Life Ins. Co.*, 722 So. 2d 990 (La. 1998); *Cope v. Metropolitan Life Ins. Co.*, 82 Ohio St. 3d 426; 696 N.E.2d 1001 (1998).

B. Recent decisions.

1. Factual issues continue to defeat predominance in federal courts.

a. Life Insurance/Annuity Class Actions Finding Differing Oral Representations Defeat Predominance.

- **Moore v. Paine Webber, Inc., No. 96-CIV-6820,** 2001 WL 228120 (S.D.N.Y. March 7, 2001).

The United States District Court for the Southern District of New York declined to certify plaintiffs' class, which was allegedly sold policies packaged as "retirement and/or savings plans" as suitable alternatives to individual retirement accounts. Plaintiffs portrayed Paine Webber's alleged fraudulent conduct as a uniform, consistent scheme and submitted materials showing that it promoted its insurance products as retirement plans. Paine Webber argued that plaintiffs purchased the Provider (the insurance product at issue) in reliance on the individual representations of their brokers, rather than on any materials generated by the company. Plaintiffs, nonetheless, submitted two alleged sales scripts used by Paine Webber to sell the insurance. However, the Court noted that the two scripts were not identical. Further, Paine Webber submitted a variety of scripts and sales

material as well as the affidavits of five brokers who stated they "did not follow or use any suggested sales scripts or telephone scripts when discussing the (insurance product) with customers." Thus, the Court found that "it would be difficult . . . to conclude . . . that Paine Webber's representations about the Provider 'did not vary appreciably among classmembers.' "

- **Begley v. Academy Life Ins. Co**., 200 F.R.D. 489 (N.D. Ga. 2001).

Begley involved allegations that members of the armed forces were sold unnecessary and expensive life insurance policies through the Non-Commissioned Officers Association of America ("NCOA"). Plaintiffs contended that defendant, Academy Life, trained NCOA counselors to exploit prospective customers' trust in the NCOA to induce them to buy policies which "are the most expensive, have the highest surrender charges, and have the poorest income performance of any of the listed insurance products" through a series of training videotapes. The Court held:

> [E]ven though the plaintiffs allege a uniform sales policy, the limited evidence before the court reveals that this "uniform scheme" may not have always, or ever, been used by the counselors. The defendants contend that the videos were but a few examples of how to recruit and sign up prospective NCOA members and customers for their insurance products. Because the common scheme does not appear to have been followed on a consistent basis, individual issues of whether a material fact was misrepresented to a particular class member and whether such class member detrimentally relied thereupon predominates over any common issues.

Id. at 498.

- **<u>In re LifeUSA Holding, Inc.</u>**, 242 F.3d 136 (3d Cir. 2001).

LifeUSA appealed the January 13, 2000 order of the District Court certifying a class of LifeUSA annuity purchasers. The United States Court of Appeals for the Third Circuit ruled that the District Court's holding was an abuse of discretion as the evidence clearly showed that individual issues predominated over common ones. According to the Third Circuit's opinion:

> The District Court's principle reliance on (*Prudential*) in certifying the LifeUSA class was misplaced and unfortunate. In *Prudential*, we affirmed the certification of a *settlement* class action involving Prudential's allegedly deceptive sales practices affecting over eight million claimants nationwide. However, Prudential, unlike this case, involved uniform, scripted, and standardized sales presentations. The district court opinion in *Prudential* found that "the oral component of the fraudulent sales presentations did not vary appreciably among class members. Plaintiffs' allegations and the evidence presented to the Court demonstrate that throughout the country, Prudential agents uniformly misled class members with virtually identical oral misrepresentations."

Id. at 146 (emphasis in original). The Court contrasted the highly individual nature of LifeUSA's marketing and sales efforts. The Third Circuit also noted that the District Court had failed "to consider how individualized choice of law analysis of the forty-eight different jurisdictions would impact on Rule 23's predominance requirement."

- **<u>Van West v. Midland National Life Insurance Co</u>**., 199 F.R.D. 448 (D.R.I. 2001).

In *Van West*, Chief Judge Torres of the United States District Court for the District of Rhode Island rejected plaintiffs' attempt to certify a "vanish" class. While finding that alleged misstatements contained in sales

literature presented a common issue that could be litigated on a class-wide basis, the fact that different statements were made to individual class members by a variety of agents and brokers required "proof of what each class member was told and the nature of the relationship between Midland and the particular agent or broker making the statements." In fact, Van West's claim was based on both the literature allegedly distributed to all class members and oral representations made to him by his agent. Plaintiffs attempted to argue around this obstacle by asserting that because Midland uniformly trained its agents and supplied them with uniform marketing material, the misrepresentations made to Van West must have been made to other class members. Chief Judge Torres refused to accept this argument. "[T]here is no justification for such an inferential leap," he wrote. The Court distinguished this case from *In re Prudential Ins. Co. America Sales Litigation*, 148 F.3d 283, 314-15 (3d Cir. 1998) since it could not be gathered from the evidence that Midland was engaged in consistent and uniform company-wide conduct.

- **Wilner v. Sunset Life Insurance Co**., No. SC051573 (Cal. Super. Ct., County of Los Angeles, 2001).

Plaintiff sought class certification on her causes of action for common law constructive fraud and unfair business practice under California Business and Professions Code § 17200 related to an allegation of improper replacement of her universal life policies. Regarding the fraud claim, the Court reviewed the recent history of insurance market conduct class actions and denied class certification. Individual oral representations precluded predominance. Concluded Superior Court Judge Dunn:

> Plaintiff did not offer any evidence . . . of what actually happens at a typical sales transaction at the "point of sale", the point in time that plaintiff considers to be critical to its claim, and whether in fact the standardized forms were actually used in a systematic fashion. For purposes of a certification hearing, even if the court were to infer that the forms were so used, this still does

> not dispense with the individual inquiries regarding what the agent told the purchaser or whether the purchaser obtained the omitted information from some other source or was otherwise fully informed. Nor is there evidence that agents used a common script in their sales presentations.

Id. at 9-10.

- **Markarian v. Connecticut Mutual Life Ins. Co**., 202 F.R.D. (D. Mass. 2001).

In this "vanish" case, plaintiff asserted claims of fraudulent inducement, negligent misrepresentation, breach of fiduciary duty, unjust enrichment, reckless, wanton, and/or negligent supervision, breach of contract, declaratory and injunctive relief, reformation, violation of Mass. Gen. Laws ch. 93A, and violation of deceptive trade practices laws. The United States District Court for the District of Massachusetts likened the facts of plaintiff's case to that in *Cohn v. Massachusetts Mutual Life Ins. Co.*, 189 F.R.D. 209 (D. Conn. 1999). The Court found that the named plaintiff gained his understanding about the policy at issue from reading part of an illustration and from his agent's oral description of the policy. Thus, he could not meet the predominance standard. The Court was not moved by plaintiff's characterization of the central issue as one of omission in an attempt to avoid the destructive impact on class certification of different oral representations to each class member. The Court also noted that evidence demonstrated that agents did not receive uniform training or use a common sales script. Moreover, information provided by Connecticut Mutual to its agents varied over the class period.

b. Life Insurance/Annuity Cases Finding the Predominance Requirement Satisfied.

- **Grove v. Principal Mutual Life Ins. Co**., 200 F.R.D. 434 (S.D. Iowa 2001).

The United States District Court for the Southern District of Iowa certified this "vanish" settlement class, citing dicta in *Amchem Prod. Inc. v. Windsor*, 521 U.S. 591, 625 (1997) that predominance "is a test readily met in certain cases alleging consumer fraud." Here:

> The Court is confronted with a class of readily identifiable consumers allegedly defrauded over a nearly 20-year period of time by Principal's sales agents using the same or similar deceptive sales techniques. Unlike the asbestos plaintiffs in *Amchem*, the money damages sought in this case are subject to objective quantification, calculable through standardized formulas. Class members do not have to fear, as some did in *Amchem*, that financial recovery by one group of Plaintiffs will be to the detriment of others.

Id. at 440-41.

- **<u>Franze v. Equitable Life Assurance Society</u>**, (S.D. Fla., Case No. 94-2036-CIV-NESBITT), appeal pending (11th Cir., Case No. 01-115-75)

On September 9, 1994, plaintiffs commenced a putative class action in federal court alleging that Equitable Life agents obscured the nature and costs of variable life insurance contracts as part of an overall scheme perpetrated by Equitable to withhold from prospective purchasers, entirely or until late in the sales process, information that these variable products were, in fact, insurance products. Plaintiffs' complaint contained two counts: violation of the Securities Act of 1933 sections 12(2) and 15 and violation of the Securities Exchange Act of 1934 sections 10(b) and 20(a) and Rule 10b-5 promulgated under those sections of the Exchange Act.

In terms of predominance, the Magistrate was satisfied that the action focused primarily on Equitable's sales practices and the disclosures or lack thereof in the prospectuses. *Id.* at 16. More significantly, the Magistrate found that "claims predicated on violations of the Securities Act and Exchange Act are particularly well-suited

for class certification, especially in cases where a common course of conduct is credibly alleged." *Id.* Moreover, he noted that the Eleventh Circuit had endorsed certification of a securities class action involving oral misrepresentations that were not part of a standardized sales presentation. *Id.* at 17, citing *Kirkpatrick v. J.C. Bradford & Co.*, 827 F.2d 718, 725 (11th Cir. 1987). Judge Nesbitt certified the class on September 29, 2000, based upon the Magistrate Judge's Report and Recommendation. Equitable's petition to the Eleventh Circuit for permission to appeal was granted on March 27, 2001.

- **Simmons v. American General Life and Accident Ins. Co.**, 748 N.E.2d 122 (Ohio Ct. App. 2000).

In *Simmons*, plaintiff filed a class action alleging that, due to a computer logic error, defendant's life insurance policyholders were misled as to the amount of death benefit due under lapsed policies. The Court rejected Defendant's contention that each class member would have to prove, on an individual basis, that he or she learned of the computer error and reasonably relied on that error by purchasing additional life insurance or refraining from such a purchase. The Court, citing *Cope v. Metropolitan Life Ins.*, 696 N.E.2d 1001, 1004 (Ohio 1998), noted that a class action was particularly appropriate "where a wide variety of claims can be established by 'common proof in cases involving similar form documents or the use of standardized procedures and practices.' "

c. Life Insurance/Annuity Class Actions Finding Individual Reliance/Causation Issues Preclude a Finding of Predominance.

- **In re Lutheran Brotherhood Variable Insurance Products Co. Sales Practices**, 201 F.R.D. 456 (D. Minn. 2001).

Judge Magnuson bifurcated the state consumer protection law claim from the breach of fiduciary duty claim for purposes of determining class certification. Concerning the latter, the Court relied upon earlier decisions in *Parkhill* and *In re Hartford* for the proposition that "even

if Defendant and its representatives owed Plaintiffs a fiduciary duty, a showing of breach and causation still requires individual inquiry." Thus, the Court denied class certification on that issue. Judge Magnuson found, however, that because reliance was not a substantive element of the state consumers protection claim, that common issues would predominate, and he would certify that class.

- **Markarian v. Connecticut Mutual Life Ins. Co**., No. 96-10421 (D. Mass. Aug. 13, 2001).

Plaintiff asserted that because Mass. Gen. Laws Ch. 93A did not require proof of reliance, the statute also permitted a relaxed causation standard similar to Minnesota's consumer protection statutes as applied in *In re Lutheran Brotherhood*. The Court rejected such an argument, pointing out that the *In re Lutheran Brotherhood* court itself noted the "unusual breadth of Minnesota's consumer protection statutes" which permitted such a relaxed causation requirement in the first place.

d. Life Insurance/Annuity Class Actions Finding Individual Reliance/Causation Issues Do Not Preclude a Finding of Predominance.

- **In re Lutheran Brotherhood Variable Insurance Products Co. Sales Practices**, 201 F.R.D. 456 (D. Minn. 2001).

As noted above, Judge Magnuson found that as to the allegation that the defendant insurer violated the Minnesota Prevention of Consumer Fraud Act, the recent Minnesota Supreme Court decision, *Group Health Plan, Inc. v. Philip Morris, Inc.*, 621 N.W.2d 2 (Minn. 2001), compelled him to ignore issues of individual reliance or even a strict showing of causation. While noting that the Minnesota Supreme Court's ruling, in some respects, engendered more confusion than it resolved, the Judge held that plaintiffs could potentially offer direct or circumstantial proof as to the nexus between damages

claims and the alleged prohibited conduct. Consequently, he certified the class on this state law claim.

- **<u>Wilner v. Sunset Life Insurance Co</u>**., No. SC051573 (Cal Super. Ct., County of Los Angeles, 2001).

While denying plaintiff's class proposal on a fraud claim, the Court certified the class on her claim under California Business and Professions Code § 17200 because "this same issue of reliance is not present as the standard for proving reliance is relaxed and plaintiff need only prove that the misrepresentations or omissions were 'likely to mislead.' "

2. Treatment of plaintiffs' argument that reliance should be presumed.

a. Life Insurance/Annuity Class Actions Finding Reliance Cannot Be Presumed.

- **<u>Spragins v. Jackson Nat'l Life Ins. Co</u>**., 193 F.R.D. 505 (W.D. Mich. 2000).

Plaintiffs acknowledged that reliance was an element of their fraud claims and that the need to prove reliance on the part of each putative class member has proven a virtually insurmountable obstacle in other vanishing premium cases. *Id.* at 509. However, they argued that reliance should be presumed because the alleged misrepresentation at issue consists of a failure to disclose information relating to material facts the defendant allegedly had a duty to disclose. The district court found that there was no basis to conclude that *Jackson National* had a class-wide fiduciary relationship with the putative class members, and therefore had no class-wide duty to disclose. The court then found that absent a class-wide duty to disclose, there was no basis to find a class-wide rebuttable presumption of reliance. *Id.* at 512.

In rejecting plaintiffs' plea that reliance be presumed, the district court distinguished and disagreed with a recent holding by the Northern District of Texas in *In re Great Southern Life Ins. Co. Sales Practice Litigation*, 192

F.R.D. 212 (N.D. Tex. 2000), in which reliance was presumed (discussed below).

b. Life Insurance/Annuity Class Actions Finding Reliance Can Be Presumed.

- **Simmons v. American General Life and Accident Ins. Co**., 748 N.E.2d 122 (Ohio Ct. App. 2000).

The Court of Appeals of Ohio rejected the notion that individual evidence of knowledge and reliance required in a fraud case precluded class certification. Citing an Ohio Supreme Court case, *Baughman v. State Farm Mut. Auto. Ins. Co*., 727 N.E.2d 1265, 1274-75 (Ohio 2000), the Court explained that "where there are common omissions, or in this case common misrepresentations, across the entire class, certification (is) proper, and ... in fact, inducement and reliance could be inferred."

- **Franze v. Equitable Life Assurance Society**, (S.D. Fla., Case No. 94-2036-CIV-NESBITT), appeal pending (11th Cir. Case No. 01-115-75).

With respect to the federal securities law claims in this case, the Magistrate rejected Defendants' argument that the issue of reliance would destroy requisite commonality since each policyholder would have different factual circumstances related to the issue. With respect to Section 12(2) actions, the Magistrate noted that plaintiffs need not prove scienter or reliance and that there is no causation element. In Section 10(b) claims, a presumption of reliance emerges where plaintiffs' case is based primarily on omissions.

- **In re Great Southern Life Ins. Co. Sales Practice Litigation**, 192 F.R.D. 212 (N.D. Tex. 2000).

In the one decision which has allowed a presumption of reliance with respect to state law fraud claims, plaintiffs argued they were entitled to the presumption of reliance articulated in *Affiliated Ute Citizens v. United States*, 406 U.S. 128 (1972). The district court agreed, and concluded that:

> [W]here a party had no opportunity to learn the truth, a presumption of reliance is warranted to a greater degree than where there is a misrepresentation. [ ] Plaintiffs' allegations pertain to *Great Southern's* alleged omission of material actuarial, interest and mortality expectations from the materials it provided its agents, not, as Defendant urges, misrepresentations at the point of sale. The Court concludes that this is in large part a non-disclosure case, to which it finds that the presumptions of *Vasquez* and *Ute* applies.

Id. at 220.

3. Effect of variations in state law.

a. Recent Life Insurance/Annuity Class Cases Finding that Divergent State Laws Defeat a Finding of Predominance.

- **Simmons v. American General Life and Accident Ins. Co.**, 748 N.E. 2d 122 (Ohio App. 2000).

While noting that federal courts have expressed that differences from state-to-state among common law claims such as fraud, negligent misrepresentation, and negligence are not so great that they preclude class treatment, the Court criticized appellees' lack of effort to analyze the state law applicable to their claims and demonstrate that common questions of law predominate. Since the trial court neglected to order such a demonstration of uniformity, the Court concluded that it abused its discretion in certifying the case as a class action.

- **Begley v. Academy Life Ins. Co**., 200 F.R.D. 489 (N.D. Ga. 2001).

The *Begley* Court found that:

> [B]ased on the state law claims and the plaintiffs' review of the applicable laws of the varying jurisdictions and their effect on the individual issues of reliance, damages, and individual representations, the class cannot be certified as

requested by the plaintiffs because individual issues would predominate over common issues.

Id. at 497.

b. Recent Life Insurance/Annuity Cases Finding that Divergent State Laws Do Not Defeat a Finding of Predominance.

No new opinions.

C. Views on why "traditional" market conduct class action litigation is slowing.

The nature of life insurance market conduct litigation is fast changing. The days of the "traditional" market conduct class action litigation, involving allegations of vanishing premium, churning, or life insurance as an investment seems to have peaked. Perhaps this is a result of numerous defeats.[1]

1. Denials of class certifications.

In 1996, the American Council of Life Insurance ("ACLI") estimated that since September 1995, one market conduct lawsuit has been filed against one of its member insurers every three business days. [Stephen Piontek, Whew!, (changing dynamics of insurance industry) National Underwriter, Life & Health/Financial Services Edition, June 3, 1996, at 41.] Since that time, insurers have had great successes defeating traditional market conduct allegations, for a variety of reasons. For one, the weight of authority is mounting on the side of insurers which argue that claims that are based primarily on oral representations cannot be classed. See, *e.g., Johnston v. HBO Film Management, Inc.*, 265 F.3d 178, 190 (3d Cir. 2001) ("[i]n cases raising issues similar to those here, it has become well-settled that, as a general rule, an action based substantially on oral rather than written communications is inappropriate for treatment as a class action.") (citing *In re LifeUSA Holding, Inc.*, 242 F.3d 136, 145-146 (3d Cir. 2001)).

In the aftermath of LifeUSA, a further reduction in the prevalence of these traditional cases can be expected.

II. Variable and Investment Products Litigation

A. Pre-SLUSA Cases.

1. Cases filed before November 3, 1998, were treated very much like cases involving fixed insurance and annuity products.

Variable insurance and annuity class action cases filed before November 3, 1998 were, aside from causes of action arising specifically under securities statutes, treated very much like cases involving fixed insurance and annuity products. Prior to the enactment of SLUSA, state court causes of action were often brought even when plaintiffs filed federal securities law claims in federal court.

a. Variable life cases focused on allegations of vanishing premiums, churning and life insurance as an investment.

The variable life insurance cases included in this outline tend to involve "traditional" market conduct cases; that is, plaintiffs alleged they were induced to purchase these policies via material misrepresentation or omission involving (1) "vanishing premium" marketing schemes, (2) improper replacement of policies and (3) life insurance marketed solely as an investment vehicle.

See *In re Prudential Ins. Co. of America Sales Practices Litigation*, 148 F.3d 283 (3d Cir. 1998) (plaintiffs brought a putative class action alleging that Prudential sold them variable and fixed life insurance products based on the three traditional misrepresentation claims, alleging violations of the Securities Exchange Act Sections 10(b) and 20(a), breach of contract, bad faith, negligent misrepresentation, negligence, unjust enrichment, and breach of state consumer fraud statutes; the Third Circuit certified the class for settlement purposes); *Duhaime v. John Hancock Mut. Life Ins. Co.,* 177 F.R.D. 54, 1997

(D. Mass. 1997) (plaintiffs brought a putative class action alleging that John Hancock sold them variable and fixed life insurance products based on the three traditional misrepresentation claims and violations of the Securities Exchange Act Sections 10b-5 and 10b-6, breach of fiduciary duty, negligent misrepresentation, breach of contract, fraudulent inducement, fraudulent concealment and deceit, reckless, wanton and/or negligent supervision, and breach of duty of good faith and fair dealing; the district court granted class certification for settlement purposes); *Bussie v. Allmerica Financial Corp.*, 50 F. Supp. 2d 59 (D. Mass. 1999)(plaintiffs brought a putative class action alleging that Allmerica sold them whole life, universal life and variable universal life insurance products based on the three traditional misrepresentation claims, and alleged breach of contract, fraud, breach of fiduciary duty, breach of the covenant of good faith and fair dealing, negligence, unjust enrichment, and breaches of various statutes including the federal Truth in Lending Act ("TILA"); the district court granted class certification for settlement purposes); *Franze v. Equitable Life Assurance Society*, Case No. 94-2036-CIV-NESBITT (S.D. Fla. 2000) (plaintiffs brought a putative class action lawsuit in federal court alleging that Equitable Life agents obscured the nature and costs of variable life insurance contracts, hiding that these variable products were, in fact, insurance products; plaintiffs alleged violation of the Securities Act of 1933 sections 12(2) and 15 and violation of the Securities Exchange Act of 1934 sections 10(b) and 20(a) and Rule 10b-5 promulgated under those sections of the Exchange Act; after the court dismissed the claims because plaintiffs' "broad allegations" failed to allege misrepresentation with the degree of specificity required by Federal Rule of Civil Procedure 9(b), plaintiffs filed their amended complaint, alleging the same claims, presumably with the requisite specificity, and the court certified the class, pursuant to Rule 23 (a) and (b)), appeal pending (11th Cir. Case No. 01-115-75).

b. Variable annuities cases focused primarily on the suitability of variable annuities as an investment in a deferred compensation plan.

The pre-SLUSA variable annuity cases discussed below mostly involve the suitability of the product as an investment in a deferred compensation plan. One case, however, involves the identity of a "clone" fund and another involves an alleged misrepresentation concerning the performance of an annuity.

- **Pre SLUSA "suitability" complaints.**

See *Castillo v. Nationwide Financial Services, Inc.*, No. 98-CVH10-8393 (Ohio C.P., Franklin Cty.), *Douglas v. American United Life Ins. Co.*, No. 29 D03-9810 (Ind. Super. Ct., Hamilton Cty.), *Thoresen v. American Express Financial Corp.*, *et al.*, No. MC98-015681 (Minn. Dist. Ct., Hennepin Cty.), and *McMurdie v. SunAmerica, Inc.*, No. BC194082 (Cal. Super. Ct., Los Angeles Cty.), four apparently identical nationwide class action complaints filed simultaneously in October 1998 in which plaintiffs allege that deferred annuities are an improper investment for a deferred compensation plan because the main selling point of deferred annuities is that their earnings accumulate on a tax-deferred basis, which is already accomplished by the deferred compensation plan. In January 2000, American Express offered $215 million to settle three class action lawsuits, including the October 1998 suit. The other two lawsuits involved allegations of churning and annuity replacement practices. The settlement was reached prior to a court ruling on class certification and includes approximately two million policyholders who bought life insurance or annuities from American Express since January 1, 1985. In the *Sun America* case, the court dismissed seven of the nine claims asserted by the plaintiffs. The court allowed plaintiffs to proceed on their claims of "false and misleading advertising" and "unfair or fraudulent business practices." In the *Nationwide* case, the court denied *Nationwide's* motion to dismiss in March of 2000.

Two class action suits, *Morgan v. Hartford Financial Services Group, Inc.,* No. 715498 (Cal. Super. Ct., San Diego Cty.), and *Bender v. Hartford Fin. Servs. Group, Inc.*, No. BC181018 (Cal. Super. Ct., Los Angeles Cty.), involve Hartford Financial Services Group's offer of a variable annuity in its deferred compensation plans supplied to various California employees. Plaintiffs in both suits allege that the variable annuity option is an improper investment for a deferred compensation plan because the principal benefit of variable annuities is deferring taxes, which is already accomplished by the deferred compensation plan.

- **The Clone Fund complaint.**

In *Young v. Nationwide Life Ins. Co.*, No. G-97-628 (S.D. Tex.), plaintiffs' putative class action complaint, filed on October 31, 1997, alleged that Nationwide sold variable annuities in which one of the investor's options was the TCI Growth Fund Subaccount. The investors were told that they would achieve the same gains as investors in the TCI Growth Fund by Nationwide buying shares of TCI Growth Fund for the subaccount. The plaintiffs complained, however, that the subaccount did not do as well as the TCI Growth Fund and that the money was instead invested in a phantom mutual fund. American Century was also a defendant in the case. Plaintiffs alleged that American Century, the current manager of the TCI Growth Fund, conspired with *Nationwide*. On April 27, 1998, defendants' Motion to Dismiss the First Amended Complaint was granted in part and denied in part. 2 F. Supp. 2d 914 (S.D. Tex. 1998). The court refused to dismiss plaintiffs' federal securities fraud allegations, and plaintiffs' Investment Company Act claim concerning breach of fiduciary duty. The court did, however, dismiss the alleged Investment Company Act violation concerning deceptive or misleading names because it believed that the SEC was required to find that the name was materially deceptive or misleading before a private right of action could exist. *See* 15 U.S.C. § 80a-34(d). As for the common law causes of action, the court dismissed the gross negligence count because the

possibility that plaintiffs could suffer a decline in their annuities' value does not rise to the required level of extreme risk or conscious indifference. The court refused to dismiss any of the other common law allegations. *Id.* On December 2, 1998, the court denied plaintiffs' motion for class certification on the ground that common questions of law and fact did not predominate over individual issues. 183 F.R.D. 502 (S.D. Tx. 1998). The court rejected the plaintiffs' argument that the case was an omissions case, not requiring proof of reliance as long as the omission was material, because plaintiffs' complaint essentially alleged that defendants represented that the fund was one thing while, in reality, it was another. Likewise, the court rejected the plaintiffs' fraud-on-the-market theory because the mutual fund share price is not affected by the misrepresentations. *Id.*

- **Alleged agent misrepresentations**.

In *Soranno v. New York Life Ins. Co*., 1999 WL 104403 (N.D. Ill. Feb. 24, 1999), plaintiffs alleged that their agent made false representations about the safety and expected performance of annuities, insurance policies, and mutual funds by stating that the principal amounts of the annuities were safe and secure and would earn interest of at least 19.5%. Plaintiffs contended that the insurance companies should be held responsible for holding the agent out as a trustworthy financial advisor and agent, and also that the agent stole money from their accounts. The complaint alleged causes of action under RICO, the Federal securities laws, fraud, negligent hiring, supervision and retention, Illinois Consumer Fraud Act, breach of contract, and conversion.

The court granted in part and denied in part defendants' motions to dismiss. With regard to the misrepresentation claims relating to the safety and performance of annuities, the court dismissed the federal securities claims holding that plaintiffs did not adequately allege that the annuities were variable annuities and thus securities. Moreover, the plaintiffs violated the three year statute of repose on the securities claims. As for the common law fraud claim concerning misrepresentations

at the time of purchase, the court denied the motion to dismiss, finding that plaintiffs adequately pled fraud. The court dismissed, however, the negligent misrepresentation count concerning a failure to provide accurate information at the time of sale on the ground that the agent was not a broker. The court also dismissed the breach of fiduciary duty counts on the ground of no allegation of any special relationship or undue dominance and influence.

B. Post-SLUSA Cases.

1. SLUSA's coverage.

The Securities Litigation Uniform Standards Act of 1998 ("SLUSA") applies to actions filed after November 3, 1998, and provides that actions brought on behalf of more than 50 persons claiming misrepresentations or omissions in connection with the purchase or sale of a "covered security" could only be brought under federal law in federal court.

"Covered security" was defined in SLUSA by reference to sections 18(b)(1) and (2) of the 1933 Act, provisions that were added by National Securities Markets Improvement Act of 1996 ("NSMIA"), Pub. L. No. 104-290 Section 205, 110 Stat. 3417. Section 18(b)(2) covers any security that "is a security issued by an investment company that is registered, or that has filed a registration statement, under the Investment Company Act of 1940."

a. Why SLUSA was enacted.

In the years following the enactment of the Private Securities Litigation Reform Act of 1995 ("PSLRA"), Pub. L No. 104-67, 109 Stat. 737 (enacted to correct various perceived abusive practices in securities litigation and imposed a number of requirements on actions brought under the Securities Act of 1933 ("1933 Act") and the Securities Exchange Act of 1934 ("1934 Act")), plaintiffs found that they could avoid its restrictions by simply bringing common law claims in state court (typically in a manner designed to avoid removal under

diversity jurisdiction). Even when plaintiffs filed federal securities law claims in federal court, they sometimes brought parallel state court actions so as to be able to conduct discovery at a time when discovery in federal court was stayed by a motion to dismiss. To prevent such efforts to avoid the PSLRA, Congress enacted SLUSA, Pub. L. No. 105-353, 112 Stat. 322.

b. What PSLRA and NSMIA Require in Tandem with SLUSA

1) Strict Disclosure Requirements & PSLRA

PSLRA requires that a plaintiff "seeking to serve as a representative party on behalf of a class shall provide a sworn certification" with the complaint. This sworn certification must attest to the fact that the plaintiff (1) reviewed and authorized the filing of the complaint; (2) did not purchase the securities in question in order to facilitate or participate in the lawsuit; and (3) is willing to serve as lead plaintiff on behalf of the class. The certification must also identify the relevant transactions between the plaintiff and defendant securities issuers. This is not considered a major hurdle and, in fact, is often viewed as obviating the need for expensive "class certification discovery" by defense counsel.[2]

A) Appointment of Lead Plaintiffs/Lead Counsel

PSLRA essentially requires the district court to appoint a lead plaintiff and lead counsel at the beginning of class action litigation. The lead plaintiff is selected, among those aspiring to be lead plaintiff, on the basis that he or she is the "most adequate plaintiff" or the prospective plaintiff with the greatest financial stake in the lawsuit.

The statute lets the lead plaintiff choose counsel "subject to the approval of the court." A court may overrule the lead plaintiff's choice in counsel only if doing so appears to be in the best interests of the entire class.

This requirement was clearly designed to alter the attorney-driven class action and certainly complicates the life of a class action litigator with ambitions to go after variable products providers. Now, this attorney must wait for the court to select the "most adequate plaintiff" and hope that the selectee is an ally.

B) Pleading With Particularity Beyond 9(b)

Federal Rule of Civil Procedure 9(b) requires allegations of fraud to be specific enough to give defendants notice of the particular misdeed so that they can ably defend against the charge. In the context of a 10b-5 claim, the plaintiff's complaint must identify the time, place, and contents of any alleged misrepresentations as well as the identity of the individual or entity making the representation.

Under PSLRA, a complaint must go further. The plaintiff must specify each allegedly misleading statement, the reason(s) why the statement is misleading, and, if the allegation is based on information and belief, the complaint must specifically state all facts on which the belief is based.

Plaintiffs have attempted to plead around these pleading requirements by alleging that their claims are based upon "investigation of counsel" or "information obtained from former employees" of the defendant company, with limited success.[3]

C) Pleading Scienter

PSLRA requires that scienter be plead with particularity "giving rise to a strong inference that the defendant acted with the required state of mind."[4] 15 U.S.C. section 78u-4(b)(2). Prior to the enactment of PSLRA, scienter could be established in a 10b-5 case by alleging facts that (1) described strong circumstantial evidence of conscious recklessness by defendants or (2) show that defendants had the motive and opportunity to commit securities fraud.

Now, the circuits are split. Some, like courts within the Second and Third Circuits, apply the same pre-PSLRA test. Others, like those in the Sixth and Eleventh Circuits, have pronounced heightened pleading standards under PSLRA.

D) "Group Published" Doctrine

In the arena of securities fraud litigation, prospectuses, registration statements, annual reports, press releases, and other group published information are presumed to be the product(s) of collective work. Some courts have held that the enactment of PSLRA eliminated the "group published" doctrine because PSLRA requires plaintiffs to set forth facts raising a strong inference that each defendant acted with the required scienter.

E) Safe Harbor for "Forward-Looking" Statements

PSLRA provides a "safe harbor" from liability for some "forward-looking statements." Defendants may avoid liability for forward-looking statements if the statement is "accompanied by meaningful cautionary statements identifying important factors that could cause actual results to differ materially from those in the forward-looking statement." Even if the forward-looking statement contained no meaningful cautionary statement, the plaintiff still must prove that the statement was made with actual knowledge of the statement's misleading nature.[5]

F) Limitation on Damages

If the plaintiff sells or repurchases the security at issue within 90-days of the beginning of the class period, PSLRA limits damages to the difference between the plaintiff's sale or repurchase price and "the mean trading price of the security during the period beginning immediately after dissemination of information correcting the misstatement or omission and ending on the date on which the plaintiff sells or repurchases the security." 15 U.S.C. section 78u-4(e)(2).

G) Mandatory Rule 11(b) Review

PSLRA mandates that "upon final adjudication of the action, the court shall include in the record specific findings regarding compliance by each party and each attorney representing any party with each requirement of Rule 11(b)." 15 U.S.C. section 78u-4(c)(1). If the court finds that any party failed to comply with Rule 11(b) (and filed a frivolous claims), the court must impose sanctions in the form of reasonable attorneys' fees and costs. 15 U.S.C. section 78u-4(c)(2)-(3).

2) NSMIA

Under NSMIA, no state law, rule or order "requiring, or with respect to, registration or qualification of securities, or registration or qualification of securities transactions, shall directly or indirectly apply" to any "covered security" or to a security that would become a covered security upon completion of the transaction. Congress passed NSMIA to amend the federal securities laws "in order to promote efficiency and capital formation in the financial markets." Pub.L. No. 104-290, 110 Stat. 3416 (1996).

2. SLUSA has been a bar to class action suits, preventing federal courts from even reaching a Rule 23 analysis.

Although the types of allegations found in most of the cases discussed below do not differ materially from the types found in market conduct class action suits filed prior to November 3, 1998, the results have changed dramatically. SLUSA has been an effective bar to class action suits alleging state law claims for material misrepresentations and/or omissions in the sale of variable products.

With the application of SLUSA, federal courts are not even reaching a Rule 23 analysis. Plaintiffs have attempted to argue that variable products are not "covered securities" as defined by SLUSA and NSMIA or that SLUSA, as applied, preempts state insurance

regulation of variable insurance products and, therefore, violates McCarran-Ferguson. These arguments have failed so far.

Recently, plaintiffs have taken a different approach. At least one court, the U.S. District Court for the Northern District of Alabama in *Henry v. Lincoln National Life Insurance Co.*, (section II.B.2.b.) has held that where an " 'untrue statement or omission of material fact' " and/or " 'manipulative or deceptive practice' permeate(s) each cause of action," SLUSA applies. Plaintiff in *Henry* also asserted that because she sued Lincoln Life, as opposed to Lincoln National Variable Annuity Account C, the provisions of SLUSA did not apply because Lincoln Life was not registered under the Investment Act of 1940. While the court rejected this argument because SLUSA does not concern itself with the identity of the issuer, an argument could be made that, under NSMIA, in order to be a "covered security," the product must be issued by a registered investment pursuant to the Investment Act of 1940. Perhaps the Henry court might have established a more helpful signpost had it stated that suing Lincoln National Life instead of Lincoln National Variable Annuity Account C was merely an attempt at forum shopping sleight-of-hand that would not preclude application of SLUSA since one entity was simply the holding company of the registered investment company. This is an attack that might be seen in the future.

a. Variable Life.

To this point, class actions involving variable life insurance products filed after the enactment of SLUSA have not differed materially from those filed pre-SLUSA.

- **Kocher v. Western Reserve Life Assurance Co. of Ohio,** CA 8:00 CV1344-T-17F (M.D. Fla.).

On June 30, 2000, a putative nationwide class action was filed in Federal District Court in Tampa against Western Reserve Life Assurance Co. of Ohio alleging fraud and deception in the marketing of universal life insurance and variable universal life insurance. The named plaintiffs

allege that they were told that they would only have to pay a single premium in order to purchase and maintain their life insurance policies, and that contrary to such representations, their policies lapsed or are in danger of lapsing for failure to pay additional premiums. Plaintiffs allege that the insurer engaged in vanishing premium sales practices, improper replacement activity, and selling insurance disguised as an investment or retirement vehicle. The insurer is charged with breach of fiduciary duty, negligent misrepresentation, fraudulent inducement, fraudulent concealment and deceit, and negligent supervision.

Defendants filed a motion to dismiss plaintiffs' complaint in September of 2000 arguing: "To the extent this action raises claims regarding the sale of ***variable*** life insurance, it is a covered class action pursuant to SLUSA and, as such, all state common law causes of action related to misrepresentations or omissions in the sale of variable life insurance are preempted." The district court granted in part Western Reserve's motion to dismiss on the basis of SLUSA. While plaintiffs appealed to the United States Court of Appeals for the Eleventh Circuit, the court of appeals ruled that it had no jurisdiction to decide the matter. On March 25, 2002, the district court granted Western Reserve's motion for summary judgment.

- **In re Lutheran Brotherhood Variable Insurance Products Co. Sales Practice Litigation**, 105 F. Supp. 2d 1037 (D. Minn. 2000).

This consolidated putative class action arose out of a number of cases filed in both state and federal courts in Minnesota and Ohio alleging that Lutheran Brotherhood sold plaintiffs variable and fixed life insurance products based on the three traditional misrepresentation claims: (1) that they were induced to purchase the policies via representations that the premiums necessary to support them would vanish after a limited number of annual payments; (2) that they were induced to purchase life insurance through agent representations that the policies were savings or retirement vehicles; and (3) that Lutheran

Brotherhood agents improperly “churned” policies by failing to disclose to plaintiffs the true costs of replacing old policies with new ones.

Although each case differed slightly in the causes of action alleged by plaintiffs, they were generally for fraud, negligent misrepresentation, negligence, breach of contract, breach of fiduciary duty, bad faith, fraudulent inducement, and violation of state consumer fraud and deceptive trade practices statutes (where applicable).

Lutheran Brotherhood removed the four state suits. The suits did not state federal causes of action, but removal was justified by Lutheran Brotherhood on the basis that the variable insurance products at issue were registered securities under the Securities Act of 1933, 15 U.S.C. 77 et. seq. The state suits, *Thompson*, *Eifler*, *Locke* and *Watson* were consolidated with a like federal class action, *Paulson*, and transferred by the Judicial Panel on Multidistrict Litigation to the United States District Court for the District of Minnesota. Prior to consolidation, the plaintiffs in *Thompson* filed a motion to remand the case back to state court, taking the position that SLUSA did not apply to variable insurance policies. The motion was denied. The *Thompson* plaintiffs then filed a second motion to remand with a motion for leave to amend their complaint to remove the counts concerning variable insurance products. These motions were also denied, the District Court stating that plaintiffs were trying to “forum shop” and avoid application of federal law, which has denied class certification in similar circumstances.

Plaintiffs, once more, filed a motion to remand all of the state cases back to state court in the spring of 2000. They reiterated their assertion that SLUSA did not apply because the variable products sold by Lutheran Brotherhood were not covered securities under the statute. The court rejected this argument, finding that the statute defines “covered securities” by referencing NSMIA, which provides that covered securities are registered securities listed on national exchanges or those issued by registered investment companies. Plaintiffs

also argued that the Gramm-Leach-Bliley Act, 15 U.S.C. §6701 et. seq. shows an intent of Congress to leave to the states the regulation of variable insurance products. Thus, SLUSA and PSLRA should be interpreted as preserving the regulation of insurance to the states. The court rejected these arguments, stating that federal laws will not be read to invalidate state insurance law absent clear Congressional intent. In addition, the court elaborated, the SEC has applied federal securities laws to variable insurance products on a consistent basis. Further, even if the variable products at issue were purely insurance products, plaintiffs' suit does not rely on or discuss a state insurance law that is allegedly invalidated.

The court, therefore, concluded that plaintiffs' state law claims concerning variable life insurance could not survive SLUSA and that it should retain supplemental jurisdiction over plaintiffs' state law claims related to non-variable products, notwithstanding plaintiffs' claim that approximately 90% of the proposed class claims would involve non-variable products.

- **Lasley v. New England Variable Life Insurance Co.**, 126 F. Supp. 2d 1236 (N.D. Cal 1999).

On February 2, 1999, plaintiffs filed a class action complaint in state court alleging multiple causes of action in connection with the marketing of whole and variable life insurance policies allegedly represented as retirement annuities.

On March 3, 1999, defendants removed the action to federal court. In opposition to plaintiffs' motion to remand, defendants cited SLUSA preemption. Plaintiffs contended that the complaint was not preempted because all the claims related solely to non-variable life insurance policies. In its May 3, 1999 opinion, the United States District Court for the Northern District of California rejected this notion, stating that the complaint clearly contemplated the inclusion of variable products in its definition of "life insurance products." Thus, because (1) variable products are a "covered security"; (2) the action

was a class action brought on behalf of more than 50 persons; and (3) the action alleges untrue statements or omission of a material fact made in connection with the purchase of a variable life insurance product, SLUSA clearly provided for removal and dismissal.

b. Variable Annuities.

With the exception of the *Olmsted* case (*infra*), which involves allegedly excessive mortality and expense charges, each class action discussed below involves the same general allegation: that plaintiffs were induced to purchase deferred variable annuities to fund their tax-qualified retirement plans when the central basis of buying such a product – tax-deferred investment – was already accomplished by the their retirement plans. The purchase of an annuity allegedly did little but increase administrative costs. One case, the Iowa *Dudek* case (*infra*), simply removes all allegations of misrepresentation from a very similar complaint.

- **<u>Gilmore v. MONY Life Insurance Co. of America</u>**, 165 F. Supp. 2d 1276 (M.D. Ala. 2001).

December 10, 1999, the purchaser of a variable annuity contract from MONY filed suit in state court; the matter was removed to federal court. In this typical variable annuity claim, the plaintiff alleged that a MONY sales agent erroneously advised him that in order to invest in mutual funds on a tax-deferred basis thru this IRA, he needed to buy a variable annuity. On MONY's motion for summary dismissal or judgment on the pleadings, the federal district court went through the variable annuity as insurance vs. security analysis. The court noted that the MONY variable annuity requires that the annuitant make purchase payments to MONY, which are allocated, at the annuitant's choice, to MONY's Guaranteed Interest Account and/or to its subaccounts of MONY America Variable Account A. The court found that the MONY variable annuity contains a portion which places all of the investment risk on the purchaser (MONY Variable Account A), and a portion that offers the annuitant a fixed return (the Guaranteed Interest Account or GIA).

However, because the plaintiff did not allocate any of his purchase payments to the GIA, the court examined the MONY America Variable Account A separately to determine whether it was insurance or a security. The court determined that because the annuitant bears the risk of the investment, the variable product was not insurance. The court then determined that the MONY America Variable Account A was an "investment contract" and thus a "security" because it satisfied the test stated in *SEC v. W. J. Howey Co.*, 328 U.S. 293, 298-99 (1946) ("a contract, transaction or scheme whereby a person invests his money in a common enterprise and is led to expect profits solely from the efforts of the promoter or a third party").

The plaintiff had argued that MONY, as an insurance company is expressly exempted from the definition of "investment company." The court rejected this argument and found that for purposes of the Investment Company Act of 1940, the MONY America Variable Annuity Account A is separate from MONY as an insurance company and that MONY America Variable Account was an investment company. Thus, the product was a "covered security" and the complaint was subject to dismissal pursuant to SLUSA.

- **Lander v. Hartford Life and Ann. Co.**, 251 F.3d 101 (2d Cir. 2001).

On December 21, 1999, a putative nationwide class action was filed in state court against Hartford Life and Annuity Insurance Company (HLAIC) and Hartford Life Insurance Company (HLIC), alleging fraud and deceit in the marketing of deferred annuities. Specifically, plaintiffs alleged that they were induced to purchase variable annuities from HLAIC and HLIC to fund their qualified retirement plans and that such purchases were inappropriate and unsuitable for placement in a retirement plan. Plaintiffs further alleged they were induced by omissions of fact regarding the alleged true nature of the investment, the insurance features, high fees, and loss of liquidity in exchange for unnecessary tax deferral.

Plaintiffs argued that Congress did not intend to include variable insurance products in the National Securities Markets Improvement Act of 1996 ("NSMIA") provision cross-referenced by SLUSA and therefore did not intend for SLUSA to apply to such products. Relying on the language of SLUSA, the District Court rejected plaintiffs' argument that variable annuities were not a "covered security" and denied the motion to remand. After denying remand, plaintiffs' claims were dismissed under SLUSA preemption. The Court also rejected plaintiffs' argument that their complaint included allegations relating to fixed annuities which, they insisted, meant that such claims needed to be remanded to state court.

Plaintiffs appealed to the United States Court of Appeals for the Second Circuit. On January 23, 2001, at the invitation of the Second Circuit, the SEC filed an amicus brief in which it agreed that variable annuity contracts were, in accordance with the plain language of the definition incorporated from NSMIA, "covered securities" under SLUSA. The SEC agreed with plaintiffs that NSMIA was not intended to preempt state insurance regulation of variable products, but disagreed that this resulted in "covered securities" not including variable annuities. "There is no indication that Congress intended NSMIA to have any impact on existing or future state insurance regulation or, indeed, that anyone ever recognized the potential that such an argument could be made." (emphasis in original).

In addition, the SEC clarified its position that if variable annuities were not "covered securities" under NSMIA, "states could regulate variable annuities as securities without running afoul of NSMIA's preemption provision. This would be inconsistent with Congress' evident intent in NSMIA to eliminate blue sky regulation for financial products, such as mutual funds, that are regulated similarly to variable annuities under federal securities laws."

On May 25, 2001, the United States Court of Appeals, Second Circuit affirmed the District Court's holding. The

Court examined the legislative intent behind the enaction of SLUSA and detailed the "commonsense proposition" that variable insurance products were envisioned by Congress to be a "covered security" under SLUSA. It upheld the District Court's holding that SLUSA did not preempt state insurance law, concluding: "[P]laintiffs have failed to bring forward any policy of the State of Connecticut, as articulated by a statute or administrative regulation, that identifies private class action litigation as part of the Connecticut insurance regulatory system."

Guided in part by the SEC's amicus brief, the Court said "that Congress intended to provide national, uniform standards for the securities markets and nationally marketed securities." There was no indication, however, that Congress sought to upset the over forty years of Investment Act treatment of variable insurance products as securities. "When legislating," the Court held, "Congress did so not only knowing that variable annuities were subject to securities laws, but, in the case of NSMIA, with variable annuities specifically in mind."[6]

Moreover, the Court opined that McCarran-Ferguson guides the judiciary in cases where a statute inadvertently interferes with state insurance regulation, not in the present case "where the preemptive force of SLUSA is explicit, and where we have strong indications that Congress intended just such an effect." Such application of McCarran-Ferguson "would undermine, rather than uphold, the will of Congress."

- **Patenaude v. Equitable Life Assurance Society**, Case No. 00-CV-1437-K (S.D. Cal.).

On July 15, 2000, plaintiff filed a class action complaint in the Superior Court of the State of California, County of San Diego, alleging deceptive marketing practices in Equitable's sale of deferred variable annuities. Plaintiff alleged that he and other members of the proposed class were induced to purchase variable annuities to fund their qualified retirement plans and that such purchases were inappropriate and unsuitable. Plaintiff further alleged

that he was induced by omissions of fact regarding the alleged true nature of the investment, the insurance features, high fees, and loss of liquidity in exchange for unnecessary tax deferral.

Plaintiff alleged two class causes of action: violation of California's unfair business practices statute and its false advertising statute. His complaint also alleged the following claims on his own behalf: fraud; fraudulent concealment and deceit; negligent misrepresentation; and negligence. Defendants removed the action to federal court on July 19, 2000 pursuant to SLUSA. After plaintiff's motion to remand was filed, the court ruled:

> Plaintiff did not dispute that the variable insurance products at issue are subject to federal securities regulation, but argued that SLUSA preempts state insurance regulations of the product. The court first determined that variable insurance products were "indisputably" a "covered security" under the plain language of both SLUSA and NSMIA. Further, the court determined that plaintiff's argument that the McCarran-Ferguson Act prevented the court from construing the "covered securities" preemption provision of SLUSA to preempt state insurance law failed because the state laws under which he sued could not be read as having been enacted "for the purpose of regulation the business of insurance." The court concluded, "Although the statutes might be applied to insurance policies, the statutes are so general in scope that it would wreak havoc with their plain language to construe them to have been enacted specifically to regulate insurance." Therefore, pursuant to SLUSA, the court denied plaintiff's motion to remand and granted Equitable's motion to dismiss the action with prejudice because plaintiff "[could not] state a claim in a representative capacity without violating SLUSA."

- **Shaner v. Aetna Life Insurance and Annuity Co.**, Civil Action No. CV-00-S-1110-NW (N.D. Ala.).

On March 28, 2000, a putative nationwide class action was filed against Aetna Life Insurance and Annuity Company, alleging fraud and deceit in the marketing of deferred annuities. In particular, plaintiff alleged that she was induced by Aetna to purchase variable annuities written by a defendant insurer to fund her tax qualified IRA accounts, and that such purchases were inappropriate and unsuitable for placement in an IRA. Plaintiff further alleged that she was induced by omissions of fact regarding the alleged true nature of the investment, the insurance features, high fees, and loss of liquidity in exchange for unnecessary tax deferral.

On behalf of the proposed class, plaintiff alleged that Aetna's conduct subjected it to liability under Alabama's common law remedies for unjust enrichment, money had and received, conversion, breach of contract, negligence, negligent and/or wanton training, negligent and/or wanton supervision and breach of fiduciary duty.

Defendants removed the action asserting that this was a "covered class action" involving a "covered security" that easily satisfied the requirements for removal under SLUSA. On August 31, 2000, the United States District Court for the Northern District of Alabama applied the "complete preemption doctrine," as elucidated in *Caterpillar, Inc. v. Williams*, 482 U.S. 386 (1987), to hold that while plaintiff's complaint, on its face, did not contain a "civil action arising under the Constitution, laws, or treaties of the United States," plaintiff should not be able to rely solely on "artful pleading" in order to avoid federal jurisdiction.

As variable deferred annuity contracts were clearly securities subject to the registration requirements of the Securities Act of 1933 and the Investment Company Act of 1940, the court concluded that it possessed subject matter jurisdiction, that plaintiff's claims were completely preempted, that her motion to remand must be denied and that the complaint must be dismissed.

- **Henry v. Lincoln National Life Insurance Co.**, Civil Action No. CV-B-1014-S (N.D. Ala.).

On March 10, 2000, plaintiff brought a national putative class action in the Circuit Court of Jefferson County, Alabama, asserting claims related to her 1998 purchase of a variable annuity from Lincoln for inclusion within a Roth IRA. Plaintiff alleged the following causes of action against Lincoln National: fraud, unjust enrichment, money had and received, conversion, breach of contract, negligence, negligent training, negligent supervision, and breach of fiduciary duty.

Defendant removed suit to federal court, alleging federal question jurisdiction based upon ERISA. Lincoln National later amended and supplemented its ground for removal, based upon SLUSA. Plaintiff's motion to remand was based on the following contentions with regards to SLUSA: (1) a variable annuity is not a "covered security"; (2) a variable annuity is an insurance product regulated by the States; (3) Congress did not intend for SLUSA to preempt state regulation of variable annuities; (4) the McCarran-Ferguson Act prevents application of SLUSA to variable contracts; (5) Lincoln National Insurance was not a registered investment company under the Investment Act of 1940; (6) the proposed class, by purchasing Lincoln National variable annuities, became holders of equity securities of Lincoln National and consequently fell within SLUSA's "savings clause" applying to transactions exclusively with existing shareholders of the issuer; and (7) SLUSA was specific to fraud claims and, therefore, did not extend to plaintiff's non-fraud claims.

The Court rejected plaintiff's contentions on the basis that (1) plaintiff's variable annuity clearly met the SLUSA definition of a "covered security"; (2) plaintiff's variable annuity was not purely insurance as it was regulated by federal securities laws; (3) federal securities were not "reverse preempted" by McCarran-Ferguson; (4) Lincoln National's sale of the variable annuity at issue was not part of the business of insurance; (5) under SLUSA, any covered class action in any state court is

removable if it involves any covered security, regardless of the identity of the defendant; (6) the proposed class did not purchase securities in Lincoln National when purchasing the variable annuity in question, thus SLUSA's "savings clause" did not apply; and (7) plaintiff's contention that her non-fraud claims do not require any element of "statements or omissions of fact" or "manipulative or deceptive device" was contradicted by the plain language of the complaint itself. "SLUSA," the court stated, "does not speak in terms of separate counts of the complaint." Thus, the court held that the lawsuit was a "covered class action" involving a "covered security" within the meaning of SLUSA and removal was appropriate. The court gave plaintiffs 15 days to amend to state a claim in accordance with SLUSA.

On February 26, 2001, the court dismissed the action without prejudice as a result of plaintiff's decision to pursue her individual claims in state court, rather than attempting to represent a class.

- **Dudek v. Prudential Securities Inc.**, Linn County, Case No. LACV038375 (Iowa Dist. Ct.).

On September 15, 2000, a nationwide putative class action was filed in Iowa state court alleging that the defendant insurers improperly sold fixed and variable annuities written by a defendant insurer to fund their tax-qualified IRA accounts, and that such purchases were inappropriate and unsuitable for placement in an IRA, and that defendant insurers had a duty, due to their superior knowledge, to ensure that the members of the proposed class "did not invest their funds in inherently inappropriate and unsuitable investment products."

Plaintiffs allege that deferred annuities sold by the defendants are never appropriate investments for placement in tax-deferred retirement plans because earnings on any investment placed in such plans are already tax-deferred, and purchase of a deferred annuity represents a completely useless approach which simply increases carrying costs. Plaintiffs assert that sellers of these annuities receive commissions in excess of rates

applicable to "regular investment products," and because of the daily "mortality and expense-risk" (M&E) charge and "administration" charge, purchasers are deprived of substantial portions of account value, as compared to other investment products. The following causes of action were alleged: breach of trust, conspiracy, unjust enrichment and imposition of constructive trust, declaratory and injunctive relief, and reformation.

On October 23, 2000, the matter was removed to the United States District Court for the Northern District of Iowa. Defendants moved to dismiss the complaint pursuant to SLUSA on December 15, 2000. On June 14, 2001, Judge Edward J. McManus granted defendant's motion, stating:

> It is the court's view that for the reasons discussed in *Lander v. Hartford Life*, 2001 WL 568093 (2d Cir. 2001), and in light of the plain language of SLUSA, this class action by plaintiffs, the gravamen of which involves an untrue statement of substantive omission of a material fact in the purchase or sale of a covered security (failure to disclose the claimed unsuitability of the tax deferred annuities), must be dismissed.

Plaintiffs filed an appeal to the United States Court of Appeals for the Eighth Circuit on September 26, 2001.

- **<u>Olmsted v. Pruco Life Ins. Co. of New Jersey</u>**, No. 00-9511, __ F.3d __, 2002 WL 362654 (2d Cir. March 7, 2002).

On March 7, 2000, a nationwide annuity class action was filed in the United States District Court for the Eastern District of New York. Plaintiffs sought to represent a class consisting of all holders of variable annuity contracts issued by defendants since March 10, 1997. Plaintiffs alleged that defendants imposed excessive mortality and expense charges in addition to the management fees charged by the investment advisors, thereby violating Sections 26 and 27 of the Investment Company Act of 1940. Specifically, plaintiffs contended

that defendants justified the allegedly excessive insurance charges through offering a death benefit guarantee in the event that an annuitant dies prior to his/her first annuity payment. Plaintiffs claimed, however, defendants would almost never be in a situation that would warrant the payment of the death benefit as opposed to the value of the investment in the annuity, and thus the monies collected for the allegedly excessive charges represented undue profit to defendants.

On October 30, 2000, the district court dismissed plaintiffs' claims upon holding that the Congress did not intend to give investors a private right of action under sections 26(e) and 27(i) of the Investment Company Act of 1940. 134 F. Supp. 2d 508 (E.D.N.Y. 2000). Plaintiffs filed a notice of appeal on November 16, 2000. Argument was heard before the Second Circuit on September 4, 2001. On March 7, 2002, the Second Circuit affirmed the judgment of the district court, agreeing that Congress did not intend to create a private right of action for violations of sections 26(f) and 27(i). One might reasonably wonder why plaintiffs, who asserted that the death benefit guarantee was "illusory," did not file a 10b-5 claim against Pruco since they were already filing a securities lawsuit.

3. Recent filings involve attempts to plead 10b-5 claims in variable annuity and variable life insurance cases in order to overcome SLUSA problems.

- **Drnek v. The Variable Annuity Life Insurance Company**, No. CV01-242-TUC-WDB (D. Ariz.).

Drnek began as a typical deferred annuity class action claim, brought on behalf of purchasers of variable deferred annuities issued by VALIC. It was filed in Arizona state court in April, 2001 and removed by defendants to the federal district court in May, 2001. Plaintiffs' original complaint asserted various state law claims. After defendant's filed a motion to dismiss, plaintiffs, perhaps anxious about facing a possible defeat pursuant to SLUSA, filed an amended complaint, re-alleging their state law claims, and adding multiple federal securities law claims. Thus, in this post-SLUSA

era, this appears to be the first case in which plaintiffs have attempted to comply with SLUSA, which mandates that class plaintiffs alleging misrepresentation in the sale/marketing of "covered securities" bring federal securities law claims. Defendants filed a motion to dismiss plaintiffs' amended complaint on November 13, 2001.

- **Malhotra v. Equitable**, No. 00-6386 (E.D.N.Y.).

Again, plaintiffs have attempted to comply with SLUSA by alleging federal securities law claims. The case was filed in October, 2001, in the Eastern District of New York.

- **Johnson v. Aegon USA, Inc., et al.**, No. 101 CV-2617 (N.D. Ga.).

Like *Drnek* and *Malhotra*, *Johnson* would be a typical deferred annuity class action claim except that instead of asserting solely state law causes of action, plaintiffs assert federal securities law causes of action. The complaint, filed October 1, 2001, specifically alleges that the deferred annuities sold by the defendants are never appropriate investments for qualified retirement plans, and that defendants actively and fraudulently recommended and sold deferred annuities to individuals and small business owners for use in tax-deferred retirement plans.

Unfortunately for plaintiffs in *Drnek, Malhotra and Johnson*, however, they still must satisfy the rigorous hurdles established by the Private Securities Litigation Reform Act of 1995 ("PSLRA"), Pub. L No. 104-67, 109 Stat. 737. PSLRA imposes a number of requirements on actions brought under the Securities Act of 1933 ("1933 Act") and the Securities Exchange Act of 1934 ("1934 Act"). Some of the requirements were limited to class actions, such as restrictions on who can be a class representatives, and limitations on attorneys' fees. Other requirement for certain elements of a securities fraud claim, a stay of discovery by plaintiff while a motion to dismiss is pending, certain limitations on damages, sanctions for abusive litigation, and procedures for

proportionate liability. It should be interesting to see whether plaintiffs in these cases will have any success attempting to comply with SLUSA, or will suffer the defeats levied upon their counterparts who unsuccessfully attempting to bull-doze their way through SLUSA.

C. CONCLUSION

1. General Standards Under SLUSA

The standards for filing a class action fraud suit involving any "covered security" are rigid. Attempts by plaintiff attorneys to circumvent SLUSA by arguing that variable insurance is not a security or that the defendant entity is not registered pursuant to the 1940 Act have been fruitless. Likewise, efforts to characterize allegations of unsuitability or non-disclosure of material details as something other than that based upon misrepresentation or omission have and should continue to lead nowhere.

There remain a number of issues, however, which result in a different analysis under federal securities law counts, as evidenced by the opinions discussed above, such as those in *Prudential, Duhaime and Franze.*

2. Reliance May be Presumed

In the context of securities fraud actions, courts have cited to *Affiliated Ute Citizens of* Utah *v. United States*, 406 U.S. 128 (1972), and its progeny for the proposition that a presumption of reliance could be permitted where the plaintiffs make a credible material omissions allegation, thereby overcoming the need to individually prove reliance with respect to such class members. However, depending upon the nature of the allegations, such presumption may not be appropriate (See*, e.g.*, *Young v. Nationwide*, discussed in II, B, 4 of this outline).

3. Liability Standards Are Uniform

As discussed by Professor Tribe, federal securities law provide a uniform liability standard which has been argued as a basis for satisfying predominance by plaintiffs in previous cases.

4. Common Document

As mentioned in *Prudential*, securities issuers are required to use the common document of a prospectus in the sale of their securities, a fact often relied upon by courts in their predominance assessment. However, as spelled out in numerous opinions denying certification in connection with the sale of non-variable life insurance, the insurance sales process, including the sale of variable insurance, is inherently different and far more individualized than that of the normal sale of a security. As a result, courts will still be required to focus on the particular sales activities of the agents of the insurers.

III. Recent Variations On the Original Market Conduct Themes

Although, as discussed above, traditional market conduct class action litigation is slowing, insurers remain vulnerable to class action lawsuits. Plaintiffs' attorneys have focused on new and different areas to exploit in the class action arena.

A. Litigation involving "Equity Index" products.

In what appears to be the first class action lawsuit involving equity-indexed products, a plaintiff filed a putative class action lawsuit on September 28, 2001, in Florida's Orange County Circuit Court against American Equity Investment Life Insurance Company of West Des Moines, Iowa, and Creative Marketing International Corporation, a marketing company out of Shawnee, Kansas. *Strube v. American Equity Investment Life Ins. Co, et. al.* The lawsuit alleges that the defendants fooled seniors throughout the nation into purchasing "risk-free" annuities that would not mature until well beyond their life expectancies. Plaintiff seeks more than $75 million in damages from these defendants.

The putative class representative claims that an American Equity agent persuaded him to cash in more than $800,000 of his annuity contracts to buy a retirement product known as an "equity indexed annuity." While plaintiff's contract disclosed that the annuities would not mature until he was 95 years of age, and that he was subject to penalties for cashing in his old policies, plaintiff alleges that the disclosures were

found only in fine print. Plaintiff alleges that American Equity procured in excess of $800 million of premiums nationwide as a result of similar sales.

Plaintiff alleges that American Equity designed, marketed and sold the equity indexed annuity in a manner that would exploit elderly consumers. In this regard, it is alleged that the equity indexed annuity was crafted in a manner that is deceptively similar to the variable annuity, but in a way that allows the insurer to avoid compliance with stringent federal securities laws that govern the marketing and sale of variable annuities.

The complaint also contains verbiage that is consistent with that of other market conduct suits, including that the defendants' sales force was purposefully uninformed about the nature of the product they were selling, and that the commissions-structure associated with the sale of the product was beneficial to the selling agents. In particular, it is alleged that substantial commissions were subtracted from the premiums. Moreover, it is alleged that while the mostly elderly consumers were told that the equity indexed annuities were a safe version of a variable annuity and that the premiums paid for them represented a dollar for dollar investment value, only a small portion of the premiums were used to buy significantly discounted call options in the bond market, and the majority of the premiums ere actually invested in additional bonds in the name of and for the benefit of American Equity Investment. In addition, plaintiffs allege that the agents used brochures and made oral representations that consisted of "vague and oblique terms" in order to disguise the true complex nature of the equity indexed annuities. As a result, the elderly consumers were mislead into believing that using the cash value of existing annuities to purchase the new products was in their best interest, the annuities had minimum guaranteed contract values, annuitants would realized gains on the entire investment, there would be no up-front sales charges, the invested funds would be easily acceptable, withdrawals would be virtually penalty-free.

Strube v. American Equity Investment Life Ins. Co, et al., was removed to the U.S. District Court for the Middle District of Florida (Case no. 01-CV-1236). Plaintiff amended his complaint on February 2, 2002, to add three plaintiffs/ putative class representatives (Wilbert Norris, Lillian Beebe, and Lillian Kirchner). Defendants' motions to dismiss are pending: American Equity moved to dismiss plaintiffs' first amended complaint on March 25; co-defendant Creative Mktg. Int'l moved to dismiss on April 5. Plaintiffs' responses to the motions are not due until May 5.

B. Litigation attacking contract pricing and expense "discrimination" issues.

1. Alleged unlawful race based discriminatory pricing structures.

The sale and administration of industrial policies, so called "burial insurance," to low income and minority groups has garnered an impressive deal of attention from class action plaintiffs' firms. Industrial policies are typically policies with relatively low face values maintained through modest premium payments. Plaintiffs in both individual and class actions allege that over the normal life expectancy of the typical industrial policy owner, the amount of premium payments far exceeds the face value of the policies. Plaintiffs in these suits further contend that the insurance companies purposefully target the sale of these policies to unsophisticated minorities, specifically African Americans, who are unable to assess the alleged long-term disadvantages of such policies. In addition to the lawsuits which have been filed, the NAIC adopted a resolution to seek restitution for policyholders who were charged higher life insurance premiums based on their race, and to conduct an investigation into small face-value policies. In July, 2000, the Florida and Georgia Insurance Commissioners issued cease and desist orders to approximately 30 life insurance companies, ordering them to stop collecting premiums on burial/industrial policies if race is a factor in the premium charged. Some recent decisions include:

- **Irvin v. Liberty Ins. Co.**, 2001 WL 246408 (E.D. La. March 12, 2001).

Plaintiffs alleged race discrimination in the pricing of industrial life insurance policies. The United States District Court of the District of Louisiana granted a stay pending conclusion of administrative process by five states that were conducting regulatory examinations.

- **Thorn v. Jefferson-Pilot Ins. Co.**, No. 3:00-2782-10 (D.S.C. 2001).

Plaintiffs brought a class action suit claiming discrimination both in rates and selection as to alleged improper and overly priced industrial life insurance. While the original thrust of the complaint appeared to be based on race discrimination, there was a component alleging that industrial life insurance policies are simply, per se, unsuitable or defective because premium payments would far exceed the face value of the policies. On June 15, 2001, the District Court issued a single-sentence order summarily denying Jefferson-Pilot's Motion to Dismiss, despite having ordered the parties to submit lengthy proposed opinions. On August 10, 2001, the District Court certified the question of whether the McCarran-Ferguson Act bars plaintiffs'§ 1981 claim.

- **Moore v. Liberty National Ins. Co.**, 267 F.3d 1209 (11th Cir. 2001).

Plaintiffs brought putative class action alleging systematic, institutional practice of race discrimination in the provision of industrial life insurance to African-Americans, from the 1940s to the present. After the insurer's motion for judgment on the pleadings was granted on the ground of untimeliness of the complaint, plaintiffs moved for reconsideration and sought to amend their complaint. The Court permitted plaintiffs to amend their complaint and denied insurer's motion for judgment on the amended complaint on the following bases: (1) plaintiffs sufficiently pled fraudulent concealment under Fed. R. Civ. Pro. 9(b); (2) the Alabama rule of repose does not apply to federal discrimination claims; (3) §1981 and §1982 claims do not conflict with

Alabama's scheme of insurance regulation; and (4) abstention under *Burford v. Sun Oil Co.*, 319 U.S. 315 (1943) was not appropriate. 108 F. Supp. 2d 1266 (N.D. Ala. 2000). The question of whether the rule of repose should apply to plaintiffs' federal law claims was certified to the Eleventh Circuit.

The Eleventh Circuit affirmed the district court, holding that Alabama's common-law rule of repose did not apply to the insureds' claims, and the plaintiffs' federal claims were not reverse pre-empted by Alabama's anti-discrimination insurance statute under the McCarran-Ferguson Act, because §1981 and §1982 did not invalidate or supersede terms of the state statute, did not frustrate Alabama's scheme of insurance regulation, and were not inconsistent with Alabama's interest in preventing discrimination.

- **<u>In re Industrial Life Insurance Litigation</u>**, No. Civ-A-MDL-1371, slip op. (E.D. La. 2002).

All motions and orders filed pre-consolidation were stayed until class certification and jurisdiction issues are resolved. Defendants filed a motion to challenge jurisdiction based on the filed-rate doctrine and a McCarran-Ferguson objection. The Court held that such questions were merits-based and denied the motion as being premature. 148 F. Supp.2d 719 (E.D. La. 2001).

On April 2, 2002, the district court denied plaintiffs' motion to certify a class composed of: "All African-Americans who own, or owned at the time of policy termination, an industrial life insurance policy that was issued as a substandard plan or at a substandard rate." Plaintiffs sought certification under Rule 23(b)(2)[7] because they claimed to be primarily seeking equitable relief. However, the court said that it was "not persuaded." Slip op. at p. 1. Specifically, the district court concluded that plaintiffs failed to establish that the injunctive relief sought predominated over any monetary damages sought. The court explained that a determination of whether plaintiffs' request is one primarily for monetary or injunctive relief " 'involves consideration of

the pragmatic ramifications of adjudication and the effect of the relief sought, rather than any special attributes of the class involved.' " *Id.* at p. 5. Applying this standard to the facts before it, the district court observed that "many of plaintiffs' proposed class members, such as those who have already had their policies adjusted by the defendants, or those whose policies have lapsed, or those on which death benefits have been paid, would not benefit in any way from the injunctive relief requested, and thus, the request for declaratory relief only serves to bootstrap a more genuine interest in an award of monetary damages." *Id.* Notably, the district court pointed out that "injunctive relief will not benefit anyone seeking to buy industrial life insurance in the future because the defendants no longer sell so-called industrial life insurance and have not done so since the mid-1980's."

2. Modal premium litigation.

a. Background

"Modal premium" actions allege that insurers failed to adequately disclose in the policy what differing premium payment options would cost the policyholder and the "annual interest rate" charged the policyholder when paying their premium on a basis other than annually. Plaintiffs contend that insurers possess a duty to disclose in the actual policy (not merely the policy summary or sales illustrations): (1) the calculation of the "dollar difference" between the premium if payment is made annually, and the modal payment amount multiplied by the number of payments made during the policy year, and (2) the so-called "effective annual percentage rate of interest" ("APR") which plaintiffs mistakenly claim is charged to all consumers who elect to pay premiums other than on an annual basis.

The most recent tally indicates that at least twenty-two insurers have already been sued in New Mexico state court in separate nationwide putative class actions. Similar actions have been brought in Florida, Texas and Colorado. Plaintiffs in New Mexico seek to recover

treble or punitive damages measured by the difference between the annual premium amount and the aggregate annual premiums paid by "modal"-paying policyholders.

State Insurance Departments have recognized for decades that legitimate business reasons justify charging different premium amounts depending on the frequency of payment, and regulators routinely approve life insurance and other policy forms that contain such differing premium scales. These legitimate business reasons include: (1) increased administrative costs for processing multiple payments; (2) the time value of money not received up front; (3) increased lapse rates for those who opt to pay on a more frequent basis; and (4) payment of premium taxes.

b. Settlements

In spite of unanimous regulatory approvals of insurers' use of modal premium options, New Mexico state courts have entered rulings favorable to plaintiffs. In *Wilson v. Massachusetts Mutual Life Ins.*, No. D0101-CV-98-02814 (1st Judicial Dist. Ct. N. Mex. 1999), the Court granted partial summary judgment for plaintiffs and certified a nationwide class of all MassMutual policyholders who "paid one or more additional fractional (or "modal") premiums, that is, additional premiums for paying their total annual premiums over time by installments (i.e., on a semi-annual, quarterly or monthly basis)." Faced with the threat of catastrophic damages, MassMutual agreed in the spring of 2002 to settle this case. The monetary terms of MassMutual's settlement (subject to court approval) include plaintiffs' counsel fees of $10.5 million, and for class members, a certificate worth $100 toward the purchase of new insurance with MassMutual or a cash-in value of $30. Class size is estimated to be up to three million policyholders.

Primerica had reached a settlement in its litigation, *Miera v. Primerica Life Insurance Co.*, No. #D-202-CV-99-5595, in November 2000, agreeing to pay approximately

$7 million to plaintiffs' lawyers and to make certain future disclosures in its policies regarding differing premium amounts due depending on frequency of payment. Primerica did not, however, agree to include a disclosure of "APR" information. Plaintiffs' counsel admitted, "there are serious legal questions as to whether the modal charges are interest, or could be fairly described as either an annual percentage rate or annual interest rate." No monetary benefits were paid to the class as part of this settlement.

In April, 2002, Travelers, in *Campbell v. The Travelers Insurance Company, et al.*, No. #D-101-CV 2000-175, reached a nationwide settlement of its modal litigation, involving payment of $6.5 million in attorneys fees for a 230,000 member class. This settlement also does not require APR disclosures in the policy. A monetary benefit will be paid to the class based upon a class member's age and a percent of the annualized premium paid by the class member who dies within a certain period of time after the settlement has been finalized. In effect, class benefits constitute free term insurance in an amount and for a term depending upon a class member's annual premium and age, respectively. The additional modal disclosures required by the settlement (subject to court approval) will be in the class notice, and will not be inserted in the policy; thus requiring no regulatory approvals.

c. Appellate Review

In *Azar v. Prudential Ins. Co. of America*, No. D1314-CV-99-613 (13th Judicial Dist. Ct. N. Mex. 2001), the trial court entered summary judgment in favor of plaintiffs on all counts, stayed its decision, and granted Prudential's request for an interlocutory appeal to the New Mexico Court of Appeals. The New Mexico Court of Appeals has accepted the case for review. (Both the American Council of Life Insurers and the National Association of Insurance Commissioners had filed *amicus* briefs urging the Court of Appeals to accept Prudential's appeal.) Oral argument took place on

February 21, 2002, and a decision from the New Mexico Court of Appeals is expected by this summer.

A second case on appeal before the New Mexico Court of Appeals is *Smoot v. Physicians Life Insurance Company*, #D-101-CV2001-1207 (N.M. Dist. Ct. 2002). No briefing schedule has been set in this case as this paper went to press.

d. Recent Adverse Rulings

On April 23, 2002, the trial court in *Enfield v. The Old Line Insurance Company*, No. #D-202-CV-2001-1367 (N.M. Dist. Ct. 2002), certified a nationwide class action against Old Line Insurance Company on (1) a breach of contract claim, and (2) a failure to disclose claim. The Court failed to certify the class on an unfair trade practices claim. In the first week of April, 2002, the trial court in *Berry v. Federal Kemper Insurance Company*, No. #D-101-CV-2000-2602 (N.M. Dist. Ct. 2002), certified the case as a class action in that litigation as well. No written trial court opinion was available as this paper went to press.

In what may be a case of first impression nationwide, the Ohio Superintendent of Insurance attempted to intervene as a party in the *Old Line* litigation and oppose class certification, on the theory that his ability to regulate in Ohio was adversely impacted by plaintiffs' attempt to apply contrary New Mexico law to insurers doing business in Ohio. The Superintendent's motion was rejected as being untimely.

IV. CONCLUSION

"Traditional" market conduct sales practices class litigation involving allegations of abuse in the marketing of insurance products appears to have peaked. Class actions will, however, continue to haunt businesses' normal operations, as new "consumer/product liability" class actions are brought alleging that the products themselves are defective.

ENDNOTES

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1 See, *e.g.*, recent insurance market conduct cases denying motions for class certification where, inter alia, differing oral or nonuniform representations defeat predominance: *Parkhill v. Minnesota Mut. Life Ins. Co*., 188 F.R.D. 332 (D. Minn. 1999), *aff'd*, 2002 WL 575765 (8th Cir. Apr. 18, 2002); *Begley v. Academy Life Ins. Co.*, 200 F.R.D. 489 (N.D. Ga. 2001); *Van West v. Midland Nat'l Life Insurance Co*., 199 F.R.D. 448 (D.R.I. 2001); *Markarian v. Connecticut Mut. Life Ins*. Co., 202 F.R.D. 60 (D. Mass. 2001); *Kent v. SunAmerica Life Ins. Co*., No. 97-12317, 2000 U.S. Dist. LEXIS 139 (D. Mass. Jan. 4, 2000); *M.C. Sullivan Inv. Co. Pension Trust v. Jackson Nat'l Life Ins. Co*., No. 97-548796 (Mich. Cir. Ct. Aug. 13, 1999); *Keyes v. The Guardian Life Ins. Co.*, No. 3:97CV439 (S.D. Miss. Feb. 15, 2000); *Solomon v. Massachusetts Mut. Life Ins. Co.*, No. 9602-0025 (Pa. Dist. Ct., Phila. County Jan. 19, 2000); *In re Hartford Sales Practices Litig*., Civ. No. 97-MD-1204 (D. Minn. June 10, 1999); *Cohn v. Massachusetts Mut. Life Ins. Co*., 189 F.R.D. 209 (D. Conn. 1999).

2 See Kevin P. Roddy, "What's News From the Front?" The Litigation Experience of Four and One-half Years Under the Private Securities Litigation Reform Act of 1995, 1194 PLI/Corp. 423, 432 (Aug. 2000).

3 *Id.* at 446.

4 *Id.* at 473.

5 Although PSLRA's "safe harbor" provision applies to statements relating solely to future circumstances or conditions, a prospectus containing statements of current conditions may still qualify as long as the misrepresentation/omission allegations only apply to the forward-looking statement.

6 In its detailed discussion of the differences between fixed and variable annuities and why variable annuities are not treated as pure insurance products under the law, the Court relied centrally on *A Vocabulary of Variable Insurance Products*, 813 PLI/Comm 11 (2001) by Joan E. Boros and W. Randolph Thompson of Jorden Burt LLP. The work of Ms. Boros and Mr. Thompson, acknowledged experts in this area, comprises the greater part of the Court's factual analysis.

7 Certification of a class pursuant to Federal Rule of Civil Procedure Rule 23(b)(2) requires satisfaction of the requirements found in subpart (a) of Rule 23, as well as demonstration that: "the party opposing the class has acted or refused to act on grounds generally applicable to the class, thereby making appropriate final injunctive relief or corresponding declaratory relief with respect to the class as a whole."