UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

TIGER CAPITAL, LLC, Plaintiff, vs. PHL VARIABLE INSURANCE COMPANY, Defendant.	ECF Case Case No. 12 Civ. 2939 (CM) (JCF)

MEMORANDUM OF LAW IN SUPPORT OF DEFENDANT PHL VARIABLE INSURANCE COMPANY'S MOTION FOR SUMMARY JUDGMENT

DORSEY & WHITNEY LLP
Patrick J. Feeley (PF-4931)
Jonathan R. Montcalm (JM-8866)
51 West 52nd Street
New York, New York 10019
Telephone: (212) 415-9200
Facsimile: (212) 953-7201

JORDEN BURT LLP
Waldemar J. Pflepsen, Jr. (*pro hac vice*)
Email: wjp@jordenusa.com
Stephen J. Jorden (SJ-5009)
Jason H. Gould (JG-2012)
Ben V. Seessel (BS-5933)
Michael C. Kentoff (*pro hac vice*)1025
Thomas Jefferson Street, N.W.
Suite 400 East
Washington, DC 20007
Telephone: (202) 965-8100
Facsimile: (202) 965-8104

Dated: December 6, 2013
Washington, DC

Attorneys for Defendant
PHL Variable Insurance Company

TABLE OF CONTENTS

Page

PRELIMINARY STATEMENT 1

UNDISPUTED MATERIAL FACTS 3

I. The Universal Life Insurance Policies At Issue 3

A. The PAUL Policies 3

B. The COI Rate Adjustment Language 4

II. Tiger's Purchase And Maintenance Of The Policies 5

III. The 2011 Cost Of Insurance Rate Adjustment 7

A. PHL's Future Expectations As To Pricing Assumptions On Policies Subject To The 2011 COI Rate Adjustment Departed From Those Originally Anticipated 7

B. PHL's Determination Considered The Factors Required By The Policy Language 8

C. PHL Notified Affected Policyholders Of The COI Rate Adjustment 9

SUMMARY JUDGMENT STANDARDS 9

ARGUMENT 9

I. PHL Determined The COI Rate Adjustments In Accordance With Applicable Policy Terms 9

A. Plaintiff Improperly Seeks *De Novo* Review Of Determinations Made By PHL In The Exercise Of Its Contractual Discretion 9

B. PHL Had The Contractual Right To Adjust COI Rates 12

1. PHL has discretion to adjust COI rates subject to the guaranteed maximum rates in the Policies 12

2. The COI rate adjustments were based on the enumerated Pricing Factors contained in the Policy 14

3. Plaintiff's restrictive construction of the "persistency" Pricing Factor improperly rewrites the contract 15

a. The testimony of Plaintiff's expert undermines such a restrictive construction..........15

b. Principles of contract construction require that "persistency" be construed to include all of its recognized facets, including both policy and premium persistency 16

c. In any event, the meaning of "persistency" is irrelevant to the breach of contract issue 17

C. The Policies Committed To PHL's Discretion The Determination Of The Classes Of Insureds To Which The COI Rate Adjustments Would Apply..........18

D. The Policies Committed To PHL's Discretion The Determination That The COI Rate Adjustments Were Prospective And Did Not Recoup Prior Losses..........20

II. Tiger Asks The Court To Impermissibly Re-Write The Terms Of The Policies..........21

CONCLUSION..........21

TABLE OF AUTHORITIES

Page(s)

Cases

131 Heartland Blvd. Corp. v. C.J. Jon Corp., 82 A.D.3d 1188 (N.Y. App. Div. 2011) 16, 21

Anderson v. Liberty Lobby, Inc., 477 U.S. 242 (1986) 9

Baymiller v. Guarantee Mut. Life Co., No. SA CV 99–1566 DOC AN, 2000 WL 1026565 (C.D. Cal. May 3, 2000) 12, 13

Coffman v. Pruco Life Ins. Co., No. 10-CV-03663 (DMC) (MF), 2011 WL 4550152 (D.N.J. Sept. 29, 2011) 16

Hamister v. Liberty Mut. Ins. Co., No. 06-CV-0600A, 2008 WL 4365893 (W.D.N.Y. Sept. 22, 2008) 13

Health Ins. Ass'n of Am. v. Corcoran, 531 N.Y.S.2d 456 (N.Y. Sup. Ct. 1988), *modified and aff'd*, 551 N.Y.S.2d 615 (N.Y. App. Div. 1990)..19, 20

Kentucky Home Mut. Life Ins. Co. v. Duling, 190 F.2d 797 (6th Cir. 1951)................................20

Kentucky Home Mut. Life Ins. Co. v. Rogers, 270 S.W.2d 188 (Tenn. 1954)..............................20

Lebowitz v. Dow Jones & Co, Inc., 847 F. Supp. 2d 599 (S.D.N.Y. 2012), *aff'd*, 508 F.App'x 83 (2d Cir. 2013)...13

Lightfoot v. Union Carbide Corp., 110 F.3d 898 (2d Cir. 1997)..9

Matter of Allstate Ins. Co. (Stolarz), 81 N.Y.2d 219 (N.Y. 1993)..11

Nolan v. Transocean Air Lines, 365 U.S. 293 (1961)...11

Norem v. Lincoln Benefit Life Co., No. 10 C 2233, 2012 WL 1034495 (N.D. Ill. Mar. 20, 2012) 12, 18

Priori v. Prudential Ins. Co. of Am., 92 F. Supp. 2d 1264 (M.D. Ala. 2000)..........................15, 19

Rhine v. New York Life Ins. Co., 6 N.E.2d 74 (N.Y. 1936) 18

White v. Cont'l Cas. Co., 9 N.Y.3d 264 (N.Y. 2007) 11

Statutes and Rules

Fed. R. Civ. P. 56 9

Miscellaneous

Louis J. Lombardi, *Valuation of Life Insurance – Establishing Reserves for Life Insurance Policies and Annuity Contracts* 139 (4th ed. 2006) 3

McGill's Life Insurance § 5.20 (Edward E. Graves ed., 8th ed. 2011)..4

New York Insurance Law Section 4224(a)(1) Re Unfair Discrimination Among Members of the Same Class, NY Office of General Counsel Op. No. 2000-150 (Dec. 13, 2000) 19

Permanent Life Policies: Whole vs. Universal, Investopedia.Com (March 19, 2012)....................3

Re New York Life Insurance Company – Dividend Illustrations On In-Force Policies – Insurance Law § 3209, General Counsel Opinion 3-10-86 (#2) (New York General Counsel Mar. 10, 1986) 17

PRELIMINARY STATEMENT

This is a dispute over the interpretation of universal life insurance policies issued by defendant PHL Variable Insurance Company ("PHL"). Plaintiff Tiger Capital, LLC ("Plaintiff" or "Tiger"), a company created for the sole purpose of purchasing a large number of life insurance policies as investments, contends that PHL breached certain of Tiger's PHL policy contracts by increasing the Cost of Insurance ("COI") rates. Plaintiff never specifies how PHL breached the policies' terms, but alleges that it has suffered damages due to the COI rate increase, and that PHL "cannot provide any basis to increase the cost of insurance" nor "any basis that the increase . . . does not unfairly discriminate within any class of insureds." Compl. ¶¶ 18-21. Plaintiff also avers that PHL has not provided "proof that such increase is in accordance with the terms of the Policies," notwithstanding that there is no contractual provision requiring the provision of such proof. Compl. ¶ 25, Ex. B. Plaintiff also seeks an injunction barring PHL from raising COI rates in the future "unless PHL provides proof that such increase is in accordance with the terms of the Policies" but concedes that no provision in the contracts requires PHL to do so.

As in the related cases pending in this Court,[1] Plaintiff's attempt to portray itself as a victim of an unjustified or discriminatory rate increase by PHL requires a reading of the relevant policy language that subverts the ordinary and plain meaning of its terms and ignores the factual, actuarial, and historical context behind those terms and PHL's actions. Summary judgment on Tiger's claims is, therefore, appropriate for the following reasons:

[1] *See U.S. Bank Nat'l Ass'n v. PHL Variable Ins. Co.*, 12-CV-06811-CM-JCF; *U.S. Bank Nat'l Ass'n v. PHL Variable Ins. Co.*, 13-CV-1580-CM-JCF (collectively "*US Bank*"); *Martin Fleisher, et al. v. Phoenix Life Ins. Co.*, 11-CV-8504-CM-JCF (*"Fleisher"*).

First, the 2011 COI rate adjustments were based on contractually appropriate and enumerated factors, the consideration of which is committed to the insurer's discretion. The policies provide that COI rates "will be based on our expectations of future mortality, persistency, investment earnings, expense experience, capital and reserve requirements, and tax assumptions." Plaintiff concedes that these contractually-identified pricing assumptions are actuarially sound and fair bases for determining or adjusting the policies' COI rate. Plaintiff instead asserts that PHL cannot provide proof of its compliance – a claim that would plunge every discretionary determination of a non-guaranteed contractual element by any insurer into a *de novo* judicial review.[2]

Second, PHL did not unfairly discriminate among policyholders receiving the adjustment when it made changes to the COI rates in 2011. Again, Plaintiff fails to indicate precisely how PHL breached the contractual promise not to "discriminate unfairly within any class of insureds," but the record demonstrates that PHL undertook a determination that the group of policies impacted by the 2011 rate adjustment was actuarially sound, fair, reasonable, and consistent with industry practice and guidelines.

Third, PHL did not use the 2011 rate adjustment to recoup prior losses or distribute prior contributions to surplus, nor did it exceed the maximum COI rates specified in the Policies.

In short, the facts in this case refute any notion advanced by Plaintiff that it is a casualty of PHL's 2011 COI rate adjustment. PHL's rate adjustment – contractually permissible,

[2] The same holds true for the part of the policy provision which states that "[a]ny change in rates will be determined prospectively. We will not distribute past gains or recoup prior losses, if any, by changing the rates." While the Complaint never expressly alleges that PHL breached this provision, the facts clearly show that PHL determined the COI rate adjustment prospectively – based on expected future profits – and not to recoup past losses.

actuarially sound, and, furthermore, foreseen by Plaintiff – was enacted to (and did) protect both the future profitability of the policies at issue and the interests of all of PHL insureds.

UNDISPUTED MATERIAL FACTS

I. The Universal Life Insurance Policies At Issue

A. The PAUL Policies

PHL's adjustment of COI announced in September and October, 2011 and effective in November that same year (the "2011 Adjustment") applied only to universal life policies called Phoenix Accumulator Universal Life ("PAUL") policies in series IIIa, IIIb, and IIIc with face amounts of $1 million or more, and only to policies issued when the insured was age 65 and older (for PAUL IIIb and IIIc) or 68 or older (for Paul IIIa) (the "Policies"). SOMF ¶ 1. These policies at issue ("Policies") are high death benefit, flexible-premium universal life insurance policies issued by PHL, called "Phoenix Accumulator Universal Life" or "PAUL" policies. SOMF ¶ 2.

Universal life insurance is characterized by two primary features: (1) a lifetime of coverage and (2) the ability for policyholders to "accumulate" cash value or savings (often termed the "cash value," "policy value," or "accumulated value"). SOMF ¶ 3; *see also Permanent Life Policies: Whole vs. Universal*, INVESTOPEDIA.COM (March 19, 2012), http://www.investopedia.com/articles/pf/07/whole_universal.asp. [REDACTED]

[REDACTED]

[REDACTED] SOMF ¶ 4. These excess premium payments – which usually occur in the early years of a policy's life while the insured is relatively young – create a policy value that in later years provides a cushion for escalating COI charges or for alternative uses by the policy owner. Louis J. Lombardi, *Valuation of Life Insurance – Establishing Reserves for Life*

Insurance Policies and Annuity Contracts 139 (4th ed. 2006); *McGill's Life Insurance* § 5.20 (Edward E. Graves ed., 8th ed. 2011). PHL credits a declared interest rate to the cash value, subject to a guaranteed minimum, but also debits from it certain expenses and charges, including cost of COI charges. SOMF ¶ 5. [REDACTED] SOMF ¶ 6.

[REDACTED] SOMF ¶ 7. [REDACTED] SOMF ¶ 8. [REDACTED] SOMF ¶ 9. [REDACTED] SOMF ¶ 10.

B. The COI Rate Adjustment Language

The PAUL III Policies are current assumption policies – they allow pricing adjustments that deviate from original assumptions based on the insurer's expected future experience (*i.e.,* expenses, investment earnings, mortality, premium persistency, policy persistency). *McGill's Life Insurance* 5.34 (Edward E. Graves ed., 8th ed. 2011). COI rates, credited interest rates, and certain expenses (the monthly "service charge") are "non-guaranteed elements," meaning that PHL has the contractual discretion to revise them on in-force policies subject to contractually-defined maximums for COI rates and minimums for the credited interest rates. SOMF ¶¶ 11-12. Plaintiff concedes that PHL, in adjusting its COI rates, did not exceed the maximum COI rates. SOMF ¶ 47.

The Policies make clear that PHL periodically reviews its COI rates and "may re-determine" them "at such time on a basis that does not discriminate unfairly within any class of insureds[,]" will do so prospectively, not distributing past gains or recouping prior losses, and has the discretion to adjust its COI rates based on, among other things, "our expectation of future mortality, persistency, investment earnings, expense experience, capital and reserve requirements, and tax assumptions." SOMF ¶ 13. With respect to the factors the company may consider when adjusting COI rates, the Policies do not articulate the specific methodology or calculations the company must use with respect to these determinations. SOMF ¶ 14.

II. Tiger's Purchase And Maintenance Of The Policies

Tiger was formed in 2010 as a joint venture led by AmTrust, a property and casualty insurer that wrote $2 billion in premium in 2012, in order to purchase a large number of life insurance policies from distressed premium finance lender, the Global Secured Capital Fund, LP ("Global Secured"). SOMF ¶¶ 15-16. Tiger is run by AmTrust's "Unique Risk Underwriting" division. SOMF ¶ 17. Before the Global Secured purchase, and on each of its subsequent, far smaller, purchases, Tiger consulted with Madison Strategic Partners, LLC ("Madison"). SOMF ¶ 18. Madison, which is staffed with experts in life insurance investing and structured finance (such as collaterally-backed mortgage obligations), helps Tiger maintain the hundreds of policies it owns and has a 20% profit sharing agreement with Tiger. SOMF ¶ 19. [redacted]

[redacted] SOMF ¶ 20.

[redacted]

[redacted] SOMF ¶ 21. [redacted]

[redacted] SOMF ¶ 22. As a

result, Global Secured became distressed, “desperate” to sell, and looked to unload its policies. SOMF ¶ 23.

SOMF ¶ 24. SOMF ¶ 25. Tiger made several subsequent smaller purchases that included a few PHL policies. SOMF ¶ 26. Tiger was aware that PHL had already raised the COI on a different block of policies when it purchased its first PHL policies in July 2010. SOMF ¶ 27. SOMF ¶ 28.

Tiger uses very sophisticated models to determine the minimum amount of premium that can be paid in order to keep the Policies in force—what Tiger calls the “optimized premium.” SOMF ¶ 29. SOMF ¶ 30. SOMF ¶ 31.

Tiger assigns each policy a value and AmTrust records gain when the value of the policies increases, and realizes gain when a policyholder dies. SOMF ¶¶ 32-33. When an insured’s health deteriorates, this a “positive impairment” to value because the death benefit gets closer to being paid. SOMF ¶ 34. Those involved in the acquisition and administration of

Tiger's life insurance policies stand to be paid millions in bonuses based on the "performance" of Tiger's portfolio. SOMF ¶ 35.

Tiger alleges that it "is the owner of 138" PHL policies listed in Exhibit A to the Complaint (Compl. ¶ 3), though it has claimed during discovery that an additional small number of policies that are no longer in force are also subject to this lawsuit. SOMF ¶ 36 n.1. Though the 2011 rate adjustment raised the COI rate on most of the policies Tiger purchased, it lowered the COI rate on certain of Tiger's policies. SOMF ¶ 37. Tiger continues to pay premiums on its PHL policies. SOMF ¶ 38. PHL also has paid death benefits to Tiger on a number of policies in its portfolio. SOMF ¶ 39.

III. The 2011 Cost Of Insurance Rate Adjustment

A. PHL's Future Expectations As To Pricing Assumptions On Policies Subject To The 2011 COI Rate Adjustment Departed From Those Originally Anticipated

Consistent with its practice of periodically reviewing the levels of its nonguaranteed charges and benefits, PHL reviewed its experience assumptions in 2011, and found that there had been significant changes to PHL's expectations for its future mortality, persistency (both policy and premium persistency), and investment earnings for the PAUL IIIa, IIIb and IIIc product series, causing the initial pricing assumptions underlying its COI rates for certain policies in these product series to no longer be appropriate. SOMF ¶ 40. PHL relied on a combination of factors, including experience studies, to determine its new future expectations. SOMF ¶ 41.

PHL concluded that changes in the relevant experience factors materially and negatively impacted future profitability and grouped policies into "policy classes" within the meaning of Actuarial Standard of Practice (ASOP) No. 2 based on similarities in those experience factors. *See* SOMF ¶ 44. This process resulted in the 2011 COI rate adjustment applying to *all* policies

with face amounts of one million dollars or more in the PAUL IIIa policy series with issue ages of 68 and above and *all* policies with face amounts of one million dollars or more in the PAUL IIIb and PAUL IIIc policy series with issue ages of 65 and above. *See* SOMF ¶ 1.

PHL calculated the COI rate adjustments such that the anticipated future profitability using the updated expectations approximated, but did not exceed, the anticipated future profitability under the original pricing assumptions. SOMF ¶ 42. In addition, the anticipated future profitability was calculated prospectively, from the effective date of the rate change going forward. PHL determined that this approach prevented past losses or gains from being recouped or redistributed. SOMF ¶ 43.

B. PHL's Determination Considered the Factors Required By the Policy Language

PHL strictly complied with the policy terms at issue in the life insurance policies purchased by Plaintiff, which provide that COI rates "will be based on our expectations of future mortality, persistency, investment earnings, expense experience, capital and reserve requirements, and tax assumptions" and applied a uniform methodology for determining the rate to be applied to the class. SOMF ¶¶ 13, 45, 48-49.

PHL, in making its 2011 COI rate adjustment determination, also considered the other contractual requirements relevant here: namely, that the redetermination not discriminate unfairly within any class of insureds, that any change in rates be determined prospectively, and that it would not distribute past gains or recoup prior losses by changing the rates. SOMF ¶¶ 42-43. Neither did the adjusted COI rates exceed the maximum permitted under the Policies. SOMF ¶ 47.

C. PHL Notified Affected Policyholders of the COI Rate Adjustment

In September and October 2011, PHL sent letters to all Policy owners announcing the cost of insurance rate adjustment. SOMF ¶ 50. The letter explained that COI rates were reviewed periodically, and that Phoenix only made changes to the rates when such rates were "too low or too high relative to…[PHL's] current actuarial and financial expectations related to the policies." SOMF ¶ 51. The letter further confirmed that the rate adjustment was in accordance with the Policies' terms, and that the COI rates remained below the maximum guaranteed rate articulated in the policies. SOMF ¶ 52.

SUMMARY JUDGMENT STANDARD

Summary judgment is designed "to flush out those cases that are predestined to result in a directed verdict." *Lightfoot v. Union Carbide Corp.*, 110 F.3d 898, 907 (2d Cir. 1997). Thus, a party is entitled to summary judgment when there is "no genuine issues as to any material fact" and the undisputed facts warrant judgment as a matter of law. Fed. R. Civ. P. 56; *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 247-48 (1986).

ARGUMENT

I. PHL Determined The COI Rate Adjustments In Accordance With Applicable Policy Terms

A. Plaintiff Improperly Seeks *De Novo* Review Of Determinations Made By PHL In The Exercise Of Its Contractual Discretion

The Complaint in this case alleges that PHL failed to "provide any basis to increase the [COI] . . . [or] that the increase in [COI] does not unfairly discriminate within any class of insureds." Compl. ¶¶ 18-21. While never identifying any contractual provision obligating PHL to "provide[] proof that such increase is in accordance with the terms of the Policies" (because there is none), Plaintiff appears to suggest, in concert with the *U.S. Bank* and *Fleisher* actions, that PHL's 2011 COI rate adjustment breached the Policies in that they (1) were not based on

factors stated in the Policies; (2) discriminated unfairly within a class of insureds; and (3) were designed to recoup past losses.[3]

Plaintiff predicates its breach of contract claim on a fundamental mischaracterization of the nature of the obligations undertaken by PHL in the Policies. The claim also flies in the face of established case law, which acknowledges that insurers have every right to exercise discretion reserved to them in the insurance contract. As explained below, the Policies, in clear and unambiguous language, afford PHL broad discretion to adjust COI rates in the event of changed future expectations with respect to pricing considerations, subject to the maximum guaranteed rates set forth in the Policies. Central to PHL's discretion is that the Policies do not prescribe or limit the methodologies to be used in determining whether a rate adjustment is appropriate or how to implement the adjustment. PHL committed to provide specific policy benefits while making rate determinations pursuant to this framework, and it has done just that.

Plaintiff's breach of contract claim conflicts squarely with this framework by second guessing the methodologies PHL employed in evaluating internal pricing considerations and determining whether and how to implement any necessary rate adjustments. If allowed to proceed, the claim would improperly override the discretion afforded PHL under the Policies. Indeed, it would enable a policyholder of *any* insurance policy to challenge and obtain *de novo* review of any decision by an insurer concerning the determination of any non-guaranteed pricing element (*i.e.*, credited interest rates, cost of insurance rates, and expense charges) by simply proffering a purported alternative actuarial or financial methodology. In effect, courts and juries would be rendered "insurance pricing departments," acting as the ultimate authority with respect

---

[3] *See* Expert Report of Jeffrey G. Stevenson ("Stevenson Report") at 6, 7, 9, 10, 12, 13, attached as Exhibit 4 to the Declaration of Waldemar J. Pflepsen, Jr. in Support of Defendant's Motion for Summary Judgment (the "Pflepsen Decl.").

to all decisions relating to non-guaranteed elements in insurance policies. An insurer's already difficult job of responsibly managing such long-term contractual commitments for the benefit of all policyowners would quickly become unworkable, subject to the continuing uncertainty of potentially conflicting policyholder demands and judicial outcomes. The Policies here do not allow such second-guessing as to which is the more "appropriate" or "reasonable" approach for the insurer to have used. Nor does the law contemplate that such an unworkable burden be placed on insurers, let alone on the courts.

The interpretation of unambiguous contract provisions like those at issue here is a matter of law for the court. *See White v. Cont'l Cas. Co.*, 9 N.Y.3d 264, 267 (N.Y. 2007) ("As with any contract, unambiguous provisions of an insurance contract must be given their plain and ordinary meaning, and the interpretation of such provisions is a question of law for the court.") (citations omitted).[4]

Thus, Plaintiff's breach of contract claim presents a straightforward issue that the Court may dispose of on summary judgment. Because the undisputed record demonstrates that PHL lawfully exercised the discretion afforded under the Policies, PHL is entitled to judgment as a matter of law.

---

[4] A federal court exercising its diversity jurisdiction applies the choice of law rules of the state in which it sits. *Nolan v. Transocean Air Lines*, 365 U.S. 293, 294 (1961). In New York, "[t]he first step in any case presenting a potential choice of law issue is to determine whether there is an actual conflict between the laws of the jurisdictions involved." *Matter of Allstate Ins. Co. (Stolarz)*, 81 N.Y.2d 219, 223 (N.Y. 1993). Here, the Policies were issued to trusts located in Minnesota, South Dakota, New Jersey, and California. However, as no conflict exists with respect to these jurisdictions' basic rules of contract interpretation where, as here, the contract is unambiguous, PHL is entitled to summary judgment regardless of which state's law is applied.

B. PHL Had The Contractual Right To Adjust COI Rates

1. PHL has discretion to adjust COI rates subject to the guaranteed maximum rates in the Policies

It is undisputed that the Policies afford PHL the contractual authority to adjust COI rates after a Policy is issued. *See* SOMF ¶ 13. PHL's discretion to adjust COI rates is subject, however, to one ultimate limitation on their magnitude: the COI rates may not exceed the maximum rates specified in the Policies. *Id.* ("The Maximum Monthly rates at any Age are shown in Section 2 . . . .").

Here the COI rate adjustments did not result in PHL charging rates that exceeded the guaranteed maximum rates specified in the Policies, and Plaintiff neither contends nor suggests otherwise. This undisputed fact supports summary judgment for PHL on the breach of contract claim because PHL possessed a contractual right under the Policies to, in its discretion, charge COI rates up to the guaranteed maximum rates.[5]

An insurer's decision to change rates to levels that do not exceed the guaranteed maximums constitutes an appropriate exercise of the insurer's contractual discretion. *See*, *e.g.*, *Baymiller v. Guarantee Mut. Life Co.*, No. SA CV 99–1566 DOC AN, 2000 WL 1026565, at *2 (C.D. Cal. May 3, 2000) ("As to the cost of insurance charges, the policies explicitly state that Defendants 'may use cost of insurance rates that are lower than the guaranteed rates' . . . . In other words, Guarantee Mutual had the discretion to consider more than the Plaintiff's sex, age and rating class."); *Norem v. Lincoln Benefit Life Co.*, No. 10 C 2233, 2012 WL 1034495, at *2 (N.D. Ill. Mar. 20, 2012) ("So long as the rates remained below the guaranteed rates, defendant had discretion in setting those rates under the policy [and] Defendant did not breach the contract

[5] *See also* testimony of Timothy Pfeifer [REDACTED] *See* SOMF ¶ 47. Plaintiff does not allege that PHL exceeded the maximum COI rates. *Id.*

by considering the factors it considered in setting the COI rate of plaintiff's policy …") (*citing Baymiller*).

Furthermore, relevant authorities recognize that when a contract affords a party discretion, as is the case with the Policies, there is no breach of the contract's express or implied terms unless the exercise of that discretion renders the contract illusory. *See Baymiller*, 2000 WL 1026565, at *3. *See also Lebowitz v. Dow Jones & Co, Inc.*, 847 F. Supp. 2d 599, 604 -605 (S.D.N.Y. 2012) (granting summary judgment for publisher in action alleging breach of contract in connection with subscription-related changes where subscriber agreement expressly permitted publisher to change or discontinue services, and rejecting contention that interpretation of contract to allow such changes rendered it illusory), *aff'd*, 508 F.App'x 83 (2d Cir. 2013); *Hamister v. Liberty Mut. Ins. Co.*, No. 06-CV-0600A, 2008 WL 4365893, at *8 (W.D.N.Y. Sept. 22, 2008) ("Having granted Liberty Mutual discretion to handle claims, NHCA may not claim that Liberty Mutual's exercise of that discretion breaches the express terms of the contract."). Plaintiff here can make no demonstration that any action by PHL rendered the Policies illusory (or otherwise reflected an abuse of discretion). Indeed, Tiger continues to pay premiums on the PHL Policies and PHL has paid death benefits to Tiger on a number of policies in its portfolio. SOMF ¶¶ 39-40. Accordingly, Plaintiff's claim fails as a matter of law.

The rate adjustments here did not result in PHL charging COI rates that exceeded the guaranteed maximum rates specified in the Policies, and Plaintiff neither contends nor suggests otherwise.[6] To the contrary, the Policies' language reflects PHL's reservation of the discretion to

---

[6] Nor does Plaintiff allege that PHL incorrectly calculated the COI *charge* under the Policies, which provide for a monthly COI charge calculated by a formula that applies a Policy's COI rate to its Net Amount at Risk. *See* SOMF ¶ 13 ("The Cost of Insurance Charge for a specific Policy Month is the charge for the Net Amount at Risk. The charge for the Net Amount at Risk is an amount equal to the per dollar cost of insurance rate for that month multiplied by the Net

declare a COI rate lower than the maximum COI rates in the policy. *See* SOMF ¶ 13. Moreover, Plaintiff cannot establish that any action by PHL rendered the Policies illusory or otherwise reflected an abuse of discretion. In short, the undisputed material facts support summary judgment for Defendant on the breach of contract claim because PHL properly exercised its discretion under the Policies to charge COI rates up to the guaranteed maximum rates.

2. The COI rate adjustments were based on the enumerated Pricing Factors contained in the Policy

While reserving the discretion of PHL to declare rates lower than the guaranteed maximum rates, the Policies provide that adjustments to COI rates will be "based on" PHL's expectations with respect to a variety of enumerated Pricing Factors all of which may affect an insurer's profitability and, therefore, are relevant to the pricing of universal life insurance. SOMF ¶ 13. In particular, the PAUL III series policy form provides that the COI rate "will be based on our expectations of future mortality, persistency, investment earnings, expense experience, capital and reserve requirements, and tax assumptions." *Id*. (the "Pricing Factors"). The inclusion of the enumerated Pricing Factors identifies for the policy owner in broad terms basic considerations that will guide PHL's determinations regarding COI rates, but nothing in the contracts suggests that such a basic listing obviates or limits PHL's discretion in considering such factors and commits all such pricing determinations to *de novo* challenge by policyholders to be decided by the courts and juries.

Fundamentally, however, it is undisputed that the Policies do not prescribe or circumscribe the methodologies PHL may use in evaluating any of these specifically enumerated factors. SOMF ¶ 14. Thus, the Policies, in granting PHL the discretion to adjust COI rates, based on its expectations of future actuarial and financial factors affecting the profitability of the

---

Amount at Risk . . . ."). ***This is the only instance where the Policies specify any calculation or formula relating to cost of insurance or applicable rates.***

subject insurance, likewise committed to PHL the discretion as to the methodology and calculation used in that process. *Cf. Priori v. Prudential Ins. Co. of Am.*, 92 F. Supp. 2d 1264, 1266-69 (M.D. Ala. 2000) (rejecting beneficiary's challenge to insurer's method of calculating dividends where contract provided that dividends shall be determined by company's board of directors but did not set out methods of calculation of dividends; consequently, dividends will be determined in the discretion of company's board of directors).

3. Plaintiff's restrictive construction of the "persistency" Pricing Factor improperly rewrites the contract

Plaintiff offers in opposition to this discretionary exercise by PHL (through its expert, not in the Complaint) the argument that the enumerated Pricing Factors do not permit PHL to consider "accumulated value" or "funding level" in its analysis and implementation of the COI rate adjustments. Policy value or funding level is a function of premiums paid, *i.e.* premium persistency. *See Supra* I.A.; SOMF ¶ 4. The other pricing assumptions considered by PHL are conceded to be within the enumerated Pricing Factors. Yet Plaintiff asserts that the Pricing Factor "persistency" must be read to mean *only* "policy persistency" (or lapse) and not "premium persistency," [REDACTED]

[REDACTED] *See* Stevenson Report at 6-7; SOMF ¶ 10.

(a) The testimony of Plaintiff's expert undermines such a restrictive construction

As the Policies do not set forth – strictly or otherwise – any methodology to which PHL must adhere with respect to its consideration of any enumerated factors, what aspects of "persistency" PHL may decide to consider is left to PHL's discretion. Plaintiff's unreasonably limited construction of "persistency" also runs counter to the testimony of its own actuarial expert. In particular, Plaintiff's expert testified that premium funding levels and lapse assumptions were "two of the key [profitability] assumptions" with respect to the Policies'

profitability, "absolutely" agreeing that premium persistency is a valid pricing assumption with respect to UL policies. SOMF ¶ 10. Premium payments made by policyholders affect a company's profitability as "premiums are revenue . . . the more premium, the merrier . . . ." *Id.*

(b) Principles of contract construction require that "persistency" be construed to include all of its recognized facets, including both policy and premium persistency

[redacted] (SOMF ¶ 10), [redacted] Construing the general term "persistency" to exclude the consideration of premium persistency finds no basis in common law principles of contract construction, which do not permit a court to rewrite the umbrella term "persistency" to mean "only policy persistency or lapsation." *See 131 Heartland Blvd. Corp. v. C.J. Jon Corp.*, 82 A.D.3d 1188, 1189 (N.Y. App. Div. 2011) ("The court's role is limited to interpretation and enforcement of the terms agreed to by the parties, and the court may not rewrite the contract or impose additional terms which the parties failed to insert."). *See also*, *e.g.*, *Coffman v. Pruco Life Ins. Co.*, No. 10-CV-03663 (DMC) (MF), 2011 WL 4550152, at *3 (D.N.J. Sept. 29, 2011), appeal voluntarily dismissed, No. 11-4026 (3d Cir. Feb. 17, 2012) ("While Plaintiff correctly asserts that this Court cannot rewrite the Policy, ironically, that is exactly what Plaintiff is asking this Court to do because that is the only way to sustain Plaintiff's claim for breach of contract. There are several ways Plaintiff wants this Court to rewrite the terms of the Policy. For example, Plaintiff wants this Court to insert the word 'only' and/or 'true' into 'expected cost of mortality' . . . .").

(c) In any event, the meaning of "persistency" is irrelevant to the breach of contract issue

First, Plaintiff's myopic focus on the term "persistency" is, ultimately, a red herring because "persistency," whether construed as policy or premium persistency, is not a necessary term in the Policies. A divergence in actual premium funding levels, like changes in lapse rates, from those originally anticipated can materially change pricing expectations as to both future investment earnings and mortality and, consequently, expectations as to an insurer's future profitability. SOMF ¶¶ 40, 44. [redacted] *See* SOMF ¶¶ 10, 45. [redacted] SOMF ¶¶ 13, 46. Therefore, even if the term "persistency" were interpreted to mean only "policy persistency," indeed even if the Policies omitted "persistency" entirely (whichever meaning were ascribed to it), the result would be the same: PHL did not breach the Policies because they contain the enumerated Pricing Factors – investment earnings and mortality – which would be expected to generate the margins impacting profitability that resulted in the COI adjustments.

Second, the enumerated Pricing Factors need not, as a matter of law, be considered an exhaustive listing. Consequently, they would not restrict PHL from considering other relevant factors such as premium persistency, assuming it were not encompassed by the term "persistency," or the term were absent. Any other reading would conflict with principles of contract construction by failing to give "based on" its plain and ordinary meaning. *See Re New York Life Insurance Company – Dividend Illustrations On In-Force Policies – Insurance Law § 3209*, General Counsel Opinion 3-10-86 (#2) (New York General Counsel Mar. 10, 1986) (interpreting "based on" as a "starting point" and rejecting suggestion that "based on" should be

interpreted to mean "equal to" because "[h]ad the Legislature intended 'equal to' when it enacted [the statute], it would have utilized different words."). *See also*, *e.g.*, *Norem*, 2012 WL 1034495, at *1 ("'***[B]ased on*** the insured's sex, issue age, policy year, and payment class' means those factors are the foundation, principal components, or fundamental ingredients of the COI rates but not the exclusive factors to be considered in setting those rates. They are the starting point.") (emphasis added).

C. The Policies Committed To PHL's Discretion The Determination Of The Classes Of Insureds To Which The COI Rate Adjustments Would Apply

Plaintiff alleges that "PHL cannot provide any basis that the increase in [COI] does not unfairly discriminate within any class of insureds." Compl. ¶ 21. In effect, Plaintiff claims that a COI rate adjustment on anything less that all owners of PAUL policies breaches the Policies. [7] Here, again, Plaintiff's claim amounts to a challenge to PHL's exercise of its contractual discretion and fails as a matter of law.

The Policies provide that rate adjustments will be made "on a basis that does not unfairly discriminate within ***any class of insureds.***" SOMF ¶ 13 (emphasis added). This provision expressly contemplates that a rate adjustment would and may apply to only *certain* PAUL policies, and not to *all* of them as Plaintiff's claim would be required. Nothing in these provisions, however, defines what constitutes a "class" or otherwise specifies or restricts how PHL may define a class or the actuarial analyses underlying its determination of a class. The Policies again leave PHL with discretion – in this case, to determine and define the actuarial "class" of insureds who may be affected by a COI rate adjustment. *See Rhine v. New York Life Ins. Co.*, 6 N.E.2d 74, 76 (N.Y. 1936) (rejecting claim that insurer unfairly discriminated by not apportioning the insurer's surplus equitably among all life policies, and finding that New York's

[7] Stevenson Report at 9, 10; Deposition Transcript of Jeffrey G. Stevenson ("Stevenson Tr.") at 201:1-5, Pflepsen Decl. Ex. 5.

UITPA prohibiting unfair discrimination "leaves discretion to each company as to what constitutes an 'equitable' apportionment, and when 'directors have exercised their discretion in regard thereto the courts will not interfere unless there is bad faith, or willful neglect, or abuse of such discretion'"); *see also New York Insurance Law Section 4224(a)(1) Re Unfair Discrimination Among Members of the Same Class*, NY Office of General Counsel Op. No. 2000-150 (Dec. 13, 2000) (recognizing that "[a]n insurer is free to impose any appropriate rules for classifying, selecting, and pricing risks that it believes are required based on sound underwriting practices and in accordance with accepted insurance and actuarial principles, provided such rules are not contrary to law") (*citing Health Ins. Ass'n of Am. v. Corcoran*, 531 N.Y.S.2d 456 (N.Y. Sup. Ct. 1988), *modified and aff'd*, 551 N.Y.S.2d 615 (N.Y. App. Div. 1990)). *Cf. Priori v. Prudential Ins. Co. of America*, *supra*.

Here, PHL's determinations as to the classes of insureds to which the COI rate adjustments would apply were not only pursuant to its contractual discretion, the rate adjustments themselves applied uniformly *within* the classes PHL defined and did not discriminate within those classes. Specifically, PHL concluded that changes in the relevant experience factors materially and negatively impacted future profitability and grouped policies into "policy classes" within the meaning of Actuarial Standard of Practice (ASOP) No. 2 based on similarities in those experience factors. *See* SOMF ¶ 44. This process resulted in the 2011 COI rate adjustment applying to *all* policies with face amounts of one million dollars or more in the PAUL IIIa policy series with issue ages of 68 and above and *all* policies with face amounts of one million dollars or more in the PAUL IIIb and PAUL IIIc policy series with issue ages of 65 and above. *See* SOMF ¶ 1. Thus, PHL adjusted COI rates for the groups of policies that were responsible for the changes in future expectations that necessitated the rate adjustments. In

seeking to impose the effects of these adjustments upon the Policies prompting them, PHL did not discriminate unfairly.[8]

Because Plaintiff cannot establish that PHL unlawfully exercised its discretion under the Policies to determine the classes of insureds that would be subject to the COI rate adjustments, the breach of contract claim fails as a matter of law.

D. The Policies Committed To PHL's Discretion The Determination That The COI Rate Adjustments Were Prospective And Did Not Recoup Prior Losses

[9] The Policies provide that "[a]ny change in rates will be determined prospectively" and that PHL "will not distribute past gains or recoup prior losses, if any, by changing the rates." SOMF ¶ 13. The Policies do not specify or restrict the methodology used by PHL to make the these required determinations of prospective application, again leaving the methodology to PHL's discretion.

[8] Courts have recognized an insurer's right to alter its pricing for groups or "classes" of insureds. For example, in *Kentucky Home Mut. Life Ins. Co. v. Rogers*, 270 S.W.2d 188, 191-92 (Tenn. 1954), an action involving policies issued to members of an employee society, at issue was the insurer's decision to implement a change to its rate calculations from a "step rate schedule" to an "attained age rate schedule." The change "resulted in causing all the older members to pay much higher rates and the younger members to pay lower rates than they would have paid under the step rate schedule." Although the court ultimately found that the particular method adopted by the insurer to amend the contract was not authorized, the court recognized that the insurer's decision to change the rates was indeed "justified" based on "their classified group mortality experience and was really required by sound actuarial principles."). *See also Kentucky Home Mut. Life Ins. Co. v. Duling*, 190 F.2d 797 (6th Cir. 1951) (same). *Cf. Corcoran,* 551 N.Y.S.2d at 619 (noting that insurance law provisions barring unfair discrimination have been "authoritatively construed not to apply when differential treatment has a proper underwriting basis").

[9] Stevenson Report at 13-17; Expert Rebuttal Report of Jeffrey G. Stevenson ("Stevenson Rebuttal") at 6, 13-20, Pflepsen Decl. Ex. 18.

PHL calculated the COI rate adjustments such that the anticipated future profitability using the updated expectations approximated, but did not exceed, the anticipated future profitability under the original pricing assumptions. SOMF ¶ 42. In addition, the anticipated future profitability was calculated prospectively, from the effective date of the rate change going forward. PHL determined that this approach prevented past losses or gains from being recouped or redistributed. SOMF ¶ 43.

To counter this conclusion, Plaintiff proffers only an alleged competing actuarial opinion. Such disagreements alone do not establish an unlawful abuse of discretion.

II. Tiger Asks The Court To Impermissibly Re-Write The Terms Of The Policies

In the Complaint's Second Cause of Action, Tiger requests an order preventing PHL from increasing the COI rate in the future without first providing "proof that such an increase is in accordance with the terms of the Policies." Compl. ¶ 25. As Tiger has admitted, however, "there is no specific provision" in the Policies requiring PHL to provide such proof. SOMF ¶ 53. Tiger nonetheless asks the Court to create a contractual duty where none exists. It is well established that the Court cannot create policy terms or rewrite the parties' contract. *See*, *e.g.*, *131 Heartland Blvd. Corp., supra*. Accordingly, PHL is entitled to summary judgment on the Complaint's Second Cause of Action.

CONCLUSION

For all of the foregoing reasons, PHL respectfully submits that there are no genuine issues as to any material fact and that the undisputed facts warrant judgment as a matter of law in favor of PHL. Therefore, PHL asks the court to issue an order granting it summary judgment regarding all claims contained in Tiger's Complaint.

Dated: December 6, 2013
Washington, DC

DORSEY & WHITNEY LLP
Patrick J. Feeley (PF-4931)
Jonathan R. Montcalm (JM-8866)
51 West 52nd Street
New York, New York 10019
Telephone: (212) 415-9200
Facsimile: (212) 953-7201

- and -

JORDEN BURT LLP

By: /s/ Waldemar J. Pflepsen, Jr.
Waldemar J. Pflepsen, Jr. (*pro hac vice*)
Email: wjp@jordenusa.com
Stephen J. Jorden (SJ-5009)
Jason H. Gould (JG-2012)
Ben V. Seessel (BS-5933)
Michael C. Kentoff (*pro hac vice*)
1025 Thomas Jefferson Street, NW
Suite 400 East
Washington, DC 20007
Telephone: (202) 965-8100
Facsimile: (202) 956-8104

Attorneys for Defendant
PHL Variable Insurance Company