CARLTON FIELDS

Shareholders Stake Shaky Claim in Unclaimed Property Cases

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Shareholders of publicly held insurance companies have joined state regulators, life insurance beneficiaries and policyholders in staking a claim in unclaimed property. Two recent decisions in these cases highlight the dangers and the weaknesses of this type of litigation in addition to other theories being asserted against the life insurance industry. A federal court in New York dismissed the case in City of Westland Police & Fire Retirement System v. MetLife. Meanwhile, the federal court in New Jersey certified a class action in City of Sterling Heights Gen. Employees' Retirement System v. Prudential Financial Inc. **Shareholders allege improper use of the Death Master File.** In both cases, the shareholder plaintiffs claim that the insurers overstated their earnings and financial strength because they did not hold enough reserves for death benefit claims that were incurred but not reported. Although the insurers used the Social Security Administration's Death Master File (DMF) to terminate annuity benefits, the insurers did not use the DMF consistently enough to trigger life insurance benefits. The shareholders claim that it was only after regulators began investigating this activity that the insurers revealed the scope of the regulatory investigations, and that they also took tens of millions of dollars in charges against their reserves. The complaints allege that stock prices fell after these revelations, causing shareholders economic harm. **A federal court in New York rejected the class claims.** Most recently, the U.S. District Court for the Southern District of New York granted MetLife's motion to dismiss all but one small subset of those claims. The plaintiffs identified three purported misrepresentations: the amount of the allegedly inadequate reserves; qualitative statements about MetLife's mortality results, underwriting practices and approach to risk; and that the regulatory investigations were without merit. However, in the first purported misrepresentation, the plaintiff did not claim that MetLife believed, prior to checking its policies against the DMF, that its reserves were inadequate. Regarding the qualitative statements, the court found that most of them were mere puffery. Part of one claim survived, however. The plaintiffs claimed that the reported mortality ratio — a number that compares the observed number of deaths to the expected number and is indicative of the company's underwriting and experience — was an untrue statement. The court found that MetLife did not make those statements with an intent to deceive; however, that was not required under one subsection of the securities laws. Finally, the court decided that the plaintiffs had not claimed any facts suggesting MetLife believed that the regulatory investigations had merit during the class period. Nor should MetLife have expected that its supposedly inadequate reserves would trigger fines or liability that would have a material impact on the company's future financial performance. Thus, the vast majority of the claims against MetLife were dismissed. The plaintiffs have since refiled their complaint in that same court. **A federal court in New Jersey certifies a class.** In the Sterling Heights v. Prudential case, the U.S. District Court of New Jersey allowed many of those same claims raised in Westland v. MetLife to survive the pleading stage. The court also certified the shareholder class. Prudential argued that the stock drop following the charge to reserves was caused by other disclosures. The court rejected that contention and found that Prudential had not successfully proved a lack of price impact. Because the court found that issues of common proof predominated over any individual issues, it certified the class. Prudential appealed, and the parties settled the case for $33 million. **Broader Implications** In other cases involving insurers' use of the DMF to identify deceased policyholders, these courts can make persuasive discussions of whether there was a misrepresentation or omission, whether it was intentionally made, and whether it caused damage. For example, in the MetLife case, the court's determination that the insurer did not believe that its reserves were inadequate until it checked its policies against the DMF is critical. Despite regulatory investigations and cross-checks of other blocks of life insurance policies against the DMF occurring years before, MetLife cannot knowingly have made misrepresentations prior to the date it actually checked the group of policies at issue against the DMF.   Nor are these theories susceptible only to claims under the securities laws. A class of policyholders, for example, might bring suit against an insurer claiming that, due to the various misrepresentations, the policies they purchased either were worth less or were inherently more risky than represented. While the "worth less" theory has been rejected by some courts, it has served as an adequate foundation to certify a class in other recent decisions. In Walker v. Life Insurance Co. of the South West, the court ruled that the worth-less model is not a viable theory of damages. In Abbit v. ING, the court certified a class where alleged damages were predicated on the worth-less theory. Claims that plaintiffs paid premiums for policies that are less financially secure than the insurer represented them to be also have met with mixed results. In Ross v. AXA Equitable Life Insurance, the court dismissed a similar claim. The reasoning in the MetLife case might be fatal to such claims, but a court could gloss over the deficiencies of a complaint just as in the Prudential case, exposing insurers to potential class liability. Cross-checking insurance policies against the DMF has now become a common and consistent practice in the industry, but lawsuits such as these are brought to cover classes from prior years, when perhaps the practice was not so consistent. If faced with such a lawsuit, take a cue from MetLife — focus on the lack of intent to deceive or to harm policyholders. Attempt to distinguish your case from Prudential by emphasizing that everyone had different reasons for purchase and was affected differently. After the MetLife claims were dismissed, the plaintiffs changed their tune, slightly. They claimed that MetLife cross-checked their block of individual life insurance policies against the DMF in 2007 – and then increased their reserves. This new allegation did not alter the outcome of the case on most of plaintiff's claims. But by failing to cross-check their group life insurance policies, the court found that plaintiffs adequately alleged that MetLife did not actually believe that its reserves were adequate, rendering MetLife's statements misleading under some of the securities statutes, and allowed the slightly broadened lawsuit to proceed. **What We Can Learn From Recent Court Cases** Cross-checking insurance policies against the Death Master File has become a common practice in the industry today. But recent lawsuits teach us that failing to do so had legal consequences. *City of Sterling Heights Gen. Employees' Retirement System v. Prudential* The parties settled the case for $33 million. The retirement system claimed those who invested in Prudential stock suffered damages when the stock dropped in price after the company disclosed it had to increase its reserves in light of its DMF practices. *City of Westland Police & Fire Retirement System v. MetLife* The majority of the claims against MetLife were dismissed in federal court in New York, although the plaintiffs have refiled their complaint in the same court. The court initially ruled MetLife lacked the intent to deceive or to harm policyholders. Plaintiffs in both cases claim that the insurers overstated their earnings and financial strength because they did not hold enough reserves for death benefit claims that were incurred but not reported.

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