JS-6

UNITED STATES DISTRICT COURT

CENTRAL DISTRICT OF CALIFORNIA

JOYCE WALKER, KIM BRUCE HOWLETT, and MURIEL SPOONER, on behalf of themselves and all others similarly situated, Plaintiffs, v. LIFE INSURANCE COMPANY OF THE SOUTHWEST, Defendant.	Case No. CV 10-9198 JVS (RNBx) ORDER REGARDING POST-JURY TRIAL UCL PROCEEDINGS

Presently before the Court are equitable claims tried to the Court concurrently with a trial by jury. The jury returned a defense verdict.

Today the Court makes the following findings of fact and conclusions of law and rules in favor of Life Insurance Company of the Southwest ("LSW"), and against Joyce Walker, Kim Bruce Howlett, and Muriel Spooner, and the class they were certified to represent as to all remaining issues.

I. PROCEDURAL HISTORY

On September 24, 2010, Plaintiffs filed this lawsuit in the Superior Court of the State of California for the City and County of San Francisco, asserting claims for common-law fraud and violation of the Unfair Competition Law, Business and Professions Code § 17200 et seq. (“UCL”). (Class Action Complaint, Docket 1, Ex. A.)

LSW removed this case in a timely manner to the United States District Court for the Northern District of California. It was then transferred, without opposition, to this District and to this Court. (Notice of Removal, Docket 1; Order Granting Life Insurance Company of the Southwest’s Motion to Transfer, Docket 16; Order re Transfer Pursuant to General Order 08-05, Docket 29.)

LSW filed a motion to dismiss Plaintiffs’ complaint, which the Court granted in part and denied in part, with leave to amend. (Order Granting in Part and Denying in Part Defendant’s Motion to Dismiss and Denying Defendant’s Motion to Strike, Docket 59 (“MTD Order”).)

Plaintiffs thereafter amended their complaint. LSW timely answered and filed a motion for judgment on the pleadings, which the Court granted in part and denied in part. (First Amended Class Action Complaint, Docket 65; Answer and Affirmative Defenses to First Amended Class Action Complaint, Docket 69; Order Granting in Part and Denying in Part Defendant’s Motion for Judgment on the Pleadings, Docket 112 (“MJP Order”).)

Plaintiffs sought, and the Court granted, leave to file a Second Amended Complaint over LSW’s opposition. Plaintiffs filed the Second Amended Complaint, and LSW answered in a timely manner. These remain the operative pleadings in this action. (Order Granting Plaintiffs’ Motion for Leave to File

Second Amended Complaint, Docket 203; SAC; Answer; Final Pretrial Conference Order, Docket 669 at 2.)

The SAC asserts five theories, which have been referred to as the "Volatility" claim, the "Tax" claim, the "Nondisclosure of Fees" claim, the "Guaranteed Interest" claim, and the "Monthly Administrative Charge" claim. (Special Verdict, Docket 769.)

On Plaintiffs' motion, and over LSW's opposition, the Court initially certified two classes in this action on November 9, 2012, each asserting claims of common-law fraud and violations of the UCL based on different factual allegations. These two classes were: All Provider and Paragon policyholders who purchased their policies on or after September 24, 2006 (the "Pure Omissions class"), asserting the Volatility and Tax claims (the "Pure Omissions claims"); and All Provider and Paragon policyholders who purchased their policies on or after September 24, 2006, and who were provided a policy illustration at or before policy application (the "Illustrations subclass"), asserting the Nondisclosure of Fees, the Guaranteed Interest, and the Monthly Administrative Charge claims (the "Illustrations claims"). (Order Granting in Part and Denying in Part Plaintiff's Motion to Certify Class and Order Denying Motion to Strike, Docket 353 ("Class Cert. Order") at 27, 40.)

On May 29, 2013, the Court decertified the Illustrations subclass because it concluded that individualized issues of illustration receipt predominated over any common questions for the Illustrations claims. (Order Decertifying Illustration Subclass, Docket 447 ("Decert. Order") at 5.)

Plaintiffs proceeded to trial, asserting their Pure Omissions claims on behalf of the Pure Omissions class and the Illustration claims on an individual basis.

(Final Pretrial Conference Order at 3-5.)

Trial in this case started on April 8, 2014 and lasted three weeks. A jury heard Plaintiffs' common-law fraud claims, and the Court heard Plaintiffs' UCL claims. (Civil Minutes, Docket 694; Final Pretrial Conference Order at 1-2.)

Over the course of the trial, the Court received testimony from each of the Plaintiffs, Plaintiffs' expert witness (Dr. Patrick Brockett), certain of Plaintiffs' insurance agents, and LSW employees. All told, eight witnesses testified in person and three testified by deposition. All but one of these witnesses were called by Plaintiffs in their case-in-chief.

In addition, the Court received more than 150 exhibits into evidence.

The Court provided each of the parties with a time limit of 26.5 hours to present evidence and provided daily updates on each side's progress toward that limit. Neither party utilized its full allotment of time. (Final Pretrial Conference (Order at 1; Trial Time Log, Docket 770.)

Additionally, both parties were allowed substantial time to present opening and closing arguments to the jury after a lengthy voir-dire process.

Ultimately, the jury found LSW not liable on all of Plaintiffs' common-law fraud claims. (Special Verdict, Docket 769.)

Thus all that remains are Plaintiffs' UCL claims. The Court permitted Plaintiffs to introduce certain additional evidence related solely to their UCL claims, but (with the exception of damage figures based on the UCL's four-year statute of limitations) Plaintiffs chose not to seek to admit additional evidence. (Order re Additional UCL Evidence, Docket 778.)

II. FINDINGS OF FACT

The Court makes the following findings of fact.

A. TRIAL

From April 8, 2014 to April 25, 2014, the parties appeared before the Court for trial by jury. At the close of trial, the jury found LSW not liable for fraud as to the class and as to the individual Plaintiffs' claims. (See Docket No. 769 (Special Verdict form).) Pursuant to the Court's Order, the parties filed post-trial briefs regarding the remaining issues regarding Plaintiffs' claims pursuant to the Unfair Competition Law ("UCL"). (See Docket 778 & 780.)

B. THE PLAINTIFFS

Plaintiff Joyce Walker, née Schmidtbauer, lives in San Diego, California. (4/16 Trial Tr. 209:3-13.) Plaintiff Kim Bruce Howlett lives in San Diego. (4/16 Trial Tr. 82:8-10.) Plaintiff Muriel Spooner lives in San Diego. She and Mr. Howlett have been married at all times relevant to this lawsuit. (4/15 Trial Tr. 69:16-25; 4/16 Trial Tr. 82:11-16.)

C. DEFENDANT LSW

LSW is a corporation organized and existing under the laws of the State of Texas and with its principal place of business in Texas. (Second Amended Complaint, Docket 205 ("SAC") ¶ 28; Answer and Affirmative Defenses to SAC, Docket 223 ("Answer") ¶ 28.) LSW is a subsidiary of National Life Insurance Company ("National Life"), a life insurance company based in Montpelier, Vermont. These two companies are members of the National Life Group ("NLG"), which also includes businesses not relevant to the claims in this litigation. (4/18 Trial Tr. 78:12-79:10.) National Life is the third-oldest life insurance company in the United States, having been in business for 165 years. (4/18 Trial Tr. 80:15-18.)

National Life and LSW are ultimately owned by a mutual holding company. (4/18 Trial Tr. 78:25-80:14.)

LSW issues life insurance policies, including life insurance policies in California. Two types of policies acquired by California purchasers are at issue in this litigation, SecurePlus Provider and SecurePlus Paragon. Each of the Plaintiffs purchased one or the other of these policies. (SAC ¶¶ 30-32; Answer ¶¶ 30-32; Final Pretrial Conference Order, Docket 669 at 3.) National Life employees perform all underwriting, issuing and administration functions, including product design, for the life insurance policies at issue in this litigation. (4/17 Trial Tr. 146:9-18.)

D. THE LIFE INSURANCE MARKET

LSW and National Life offer many different types of life insurance, including term insurance, whole life insurance, fixed universal life insurance, variable universal life insurance, and indexed universal life insurance. (4/18 Trial Tr. 88:3-6, 89:10-13, 90:2-4, 91:14-25, 93:9-12, 95:8-13, 96:22-97:23.) LSW and National Life offer many different life insurance products to allow policyholders, with input from additional sources including their agents and advisors, to choose the product that is best for them given their needs and risk tolerance. (4/18 Trial Tr. 88:7-17, 95:8-13; 4/23 Trial Tr. 56:6-58:2, 123:5-23.) None of these categories of life insurance issued by LSW and National Life is unique; they are offered by other companies in the life insurance industry. (4/18 Trial Tr. 96:22-97:4.)

Term life insurance provides coverage for a defined period of time, and pays a death benefit if the insured dies within that period of time. It does not accumulate any cash value. Term insurance premiums are level throughout the term of the policy. (4/9 Trial Tr. 134:7-135:20; 4/18 Trial Tr. 88:18-89:7.)

Unlike term life insurance, both whole and universal life insurance offer the policyholder the option of providing insurance for their entire life. Both categories also offer the option of cash value accumulation, allowing policyholders the option to borrow cash value. (4/18 Trial Tr. 89:14-90:15.) Whole life insurance allows the policyholder to keep the policy in force indefinitely, so long as the policyholder pays a certain, fixed amount in premiums. When the insured dies, whole life insurance pays a death benefit. (4/9 Trial Tr. 134:7-135:20; 4/18 Trial Tr. 89:14-21.)

Universal life insurance allows for flexible premium payments and flexible death benefit amounts, within a certain range. If, for example, a policyholder wanted to pay more premiums to accumulate additional cash value, universal life insurance would permit him to do so. If a policyholder wanted to reduce premium payments, or skip a payment, universal life insurance would permit the policyholder to do so as well. (4/9 Trial Tr. 135:21-136:11; 4/17 Trial Tr. 159:9-22; 4/18 Trial Tr. 90:7-91:13.) However, this premium payment flexibility is not unlimited. The Internal Revenue Service sets a ceiling on the premiums that can be paid if the policy is to be categorized as, and receive the favorable tax treatment associated with, life insurance. On the other end of the spectrum, policyholders have to pay sufficient premiums to keep their policy in force. (4/9 Trial Tr. 126:18-127:7; 4/17 Trial Tr. 159:17-22.)

Three varieties of universal life insurance are available to policyholders: fixed, variable, or indexed. Each calculates interest credits in different ways. (4/18 Trial Tr. 91:14-21, 92:5-20, 93:25-94:4.)

In the case of fixed universal life insurance, cash value accumulates at a fixed interest rate declared by the insurance company, so that the policyholder knows in advance each year what the rate will be. Fixed universal life insurance interest credits are not dependent upon the performance of stock market or the S&P 500 Index. (4/10 Trial Tr. 152:14-19; 4/18 Trial Tr. 91:14-21.)

In the case of variable universal life insurance, cash value is invested in accordance with the policyholder's selection, which can include any number of stock market and bond funds. The policyholder is "fully exposed" to the market in a variable universal policy, because the cash value of his or her policy is completely tied to the performance of the market. (4/9 Trial Tr. 136:12-137:13; 4/10 Trial Tr. 152:20-153:5; 4/18 Trial Tr. 92:5-93:16.)

Whereas fixed universal life offers no exposure to the market, and variable universal life offers full exposure to the market, indexed universal life insurance ("IUL") offers limited market exposure, placing IUL products "in between" the other options in terms of risk exposure. (4/18 Trial Tr. 93:25-94:4.) IUL policies offer cash value accumulation at a rate that is tied in part to a stock market index, such as the S&P 500 Index, but with a cap on the upside and a floor on the downside in any given year, with an additional guaranteed minimum rate of accumulation over a period of time. (4/9 Trial Tr. 137:17-138:2; 4/10 Trial Tr. 155:20-22; 4/18 Trial Tr. 93:25-95:7.)

Policyholders may choose which option they prefer based upon their risk tolerance. A policyholder with a low risk tolerance may avoid the volatility of the stock market completely by choosing a fixed universal life insurance policy. A policyholder with a high risk tolerance may risk the volatility of the stock market (and in some circumstances reap the rewards of that risk) by choosing a variable universal life insurance policy. A policyholder whose risk tolerance falls between the two extremes may want limited exposure and can choose to purchase an IUL.

Such limited exposure to risk due to the volatility of the stock market is a hallmark of any IUL product. (4/10 Trial Tr. 153:16154:2, 156:2-13; 4/18 Trial Tr. 88:7-17, 93:25-94:4, 95:8-16.)

E. LSW COMPLIANCE WITH LIFE INSURANCE REGULATIONS

The life insurance industry is extensively regulated, including by the California Department of Insurance (the "Department of Insurance"). California statutes and Department of Insurance regulations, for example, govern the terms of the policy contract, the language of the contract, the reserves supporting the policy, the applicable charges and fees, and the documents provided to policyholders, among other things. (4/18 Trial Tr. 142:24-144:23, 149:22-25.)

Before any insurance policies can be sold in California, they must be submitted to the Department of Insurance for its consideration. (4/17 Trial Tr. 249:2-6; 4/18 Trial Tr. 145:10-16.) This review can involve back-and-forth between the insurer and the Department of Insurance over a number of months. In the case of the products at issue in this case, the filings and correspondence with the Department of Insurance are documented in hundreds of pages. (4/18 Trial Tr. 145:17-146:7, 148:3-149:21; Trial Exs. 87; 88.)

To ensure compliance with these extensive regulations, a number of LSW employees are responsible for monitoring compliance. One compliance group is dedicated to reviewing LSW's policy forms and illustrations, and corresponding with state regulators in order to ensure that LSW's products comply with the applicable regulations. (4/18 Trial Tr. 146:8-22; Trial Ex. 87.) A market conduct and compliance group oversees materials to be distributed to the public. (4/18 Trial Tr. 146:23-147:22; Trial Ex. 57 at 57.0009-57.0011.)

LSW also trains agents who sell LSW products. This training effort includes being one of the first insurance companies to establish a video library of materials on a comprehensive internal website. In addition, LSW offers online presentations on a variety of topics and presentations conducted by the independent agencies with whom LSW contracts. All told, this training effort, in one way or another, involves most of LSW's employees and independent agents. (4/23 Trial Tr. 64:5-68:8.)

LSW has invested substantial time and resources in developing these training capabilities, including working with experts in adult education to ensure that agents understand any insurance products that they sell and can fully describe them to potential consumers, and in expanding the number and quality of LSW's inside sales associates who conduct face-to-face training with agents. (4/23 Trial Tr. 68:9-70:4.) LSW maintains an internal sales desk to answer any questions from field agents about the policies. This is part of LSW's effort to work closely with agents to educate and train the agents to answer any questions a consumer may have and provide quality customer service. (4/23 Trial Tr. 68:19-22, 70:5-71:9.) All of these training materials are reviewed and approved in advance by LSW's compliance group to ensure that the training is compliant with all applicable rules and regulations, and to ensure that all of the information being conveyed to agents during training is accurate. (4/23 Trial Tr. 72:7-73:4.)

F. SecurePlus PROVIDER AND SecurePlus PARAGON POLICIES

The two policies at issue in this lawsuit, SecurePlus Provider and SecurePlus Paragon, are indexed universal life insurance policies. (SAC ¶ 32; Answer ¶ 32.)

LSW began developing Provider in 2004, and the policy was first issued in

2005. The product was designed and developed by a team of individuals led by an actuary named Mike Tivilini, and supervised by another actuary, Elizabeth MacGowan. The policies were issued to policyholders in California throughout the relevant period. (4/18 Trial Tr. 48:8-13, 120:4-121:19; Final Pretrial Conference Order at 2.)

Ms. MacGowan testified at trial over the course of three days, and was a credible witness. She is a licensed actuary and fellow of the Society of Actuaries. As the Chief Life Product Officer for LSW and National Life, she is currently the highest ranking actuary at the company in charge of life insurance product development and pricing. She has been involved in designing and pricing life insurance products for nearly 15 years. (4/18 Trial Tr. 76:22-77:11, 83:17-86:1.)

LSW launched Paragon in 2007. The product was also designed and developed by a team of individuals led by Mr. Tivilini and supervised by Ms. MacGowan. Paragon policies were issued in California during the relevant period, but LSW no longer issues Paragon policies. (4/18 Trial Tr. 120:9-121:19; Final Pretrial Conference Order at 2.)

LSW was not the first company to introduce IUL policies into the marketplace. By the time LSW began issuing IUL products, approximately six to twelve competitor insurance companies were already offering similar products in California. When LSW began developing its own IUL products, it evaluated the features of the products already being sold in the market and used those as a model in developing its own products. (4/18 Trial Tr. 97:8-98:6, 120:18-20; Tivilini Dep. Tr., (Docket 735) Ex. B at 22:3-24:5.) Today, approximately fifty different insurance companies offer IUL products. (4/18 Trial Tr. 120:21-121:12.)

Although there are some differences between the features on Provider and

Paragon policies, in most respects relevant to this litigation they are substantially similar to each other. (4/18 Trial Tr. 120:12-17.) Provider and Paragon are very similar to every other IUL product being offered by every other insurance company in the market. In particular, with respect to the features that are challenged in this litigation, there are no significant differences between Provider, Paragon, and other IUL products sold in the market. (4/18 Trial Tr. 97:5-98:22, 99:12-16.)

1. Interest Crediting

Like other universal life insurance policies (whether fixed, variable, or indexed), Provider and Paragon include a cash value component, which accumulates interest. (4/18 Trial Tr. 90:7-91:16; Trial Exs. 30 at 30.0004; 48 at 48.0004; 86 at 86.0003; 804 at 804.0003; 934 at 934.0028-934.0029; 935 at 935.0028-935.0029.) Provider and Paragon permit the policyholder to choose between several different methods for calculating interest, called "strategies." The policyholder can elect to allocate all of his or her cash value to one strategy, or to spread that cash value across many different strategies. This ability to choose between multiple strategies in a single product is common among IUL products in the market. (Trial Exs. 30 at 30.0010-30.0012; 48 at 48.0010-48.0012; 86 at 86.0003; 804 at 804.0005; 934 at 934.0028-934.0029; 935 at 935.0028-935.0029.)

Both Provider and Paragon offer policyholders a "fixed" strategy, which accumulates interest at a fixed rate declared in advance by LSW, subject to a specified minimum. It is not tied to the performance of the S&P 500 Index. Thus, even if a policyholder purchased an indexed universal life insurance policy but did not want to have any risk from the performance of the S&P 500 Index, he or she could eliminate any such risk by allocating cash value to the fixed strategy. (Trial Exs. 30 at 30.0010-30.0012; 48 at 48.0010-48.0012; 86 at 86.0003-86.0004; 804 at

804.0005; 934 at 934.0028; 935 at 935.0028.)

In addition to a fixed crediting strategy, Provider and Paragon offer policyholders the ability to choose between several different equity indexed strategies. These strategies all calculate the interest to be credited by reference to the performance of a stock market index, but differ from each other in the method by which that performance is calculated (point-to-point or point-to-average) and the applicable participation rates and earnings caps. (Trial Exs. 30 at 30.0010-30.0012; 48 at 48.0010-48.0012; 86 at 86.0003-86.0004; 804 at 804.0005-804.0006; 934 at 934.0029; 935 at 935.0029.)

A participation rate is a multiple applied to the calculated stock market index performance in order to determine the rate to be credited to a policy's cash value. Thus, if a policyholder has a participation rate of 100 per cent, his or her cash value will grow by the same factor as the stock market index did in a given policy year, subject to the policy's earnings caps and floors. If a policyholder has a participation rate of 140 per cent, his or her cash value will grow at a factor 40 per cent greater than the stock market index, again subject to applicable caps and floors. (Trial Exs. 30 at 30.0010-30.0011; 48 at 48.0010-48.0011; 86 at 86.0004; 804 at 804.0005; 934 at 934.0030; 935 at 935.0030.)

An earnings cap limits the interest to be credited to a policy in any given policy year. If a policyholder has an earnings cap of 10 per cent, his or her cash value will not grow by more than 10 per cent in any given policy year, regardless of how the stock market performs in any given year. (Trial Exs. 30 at 30.0010-30.0011; 48 at 48.0010-48.0011; 86 at 86.0004; 804 at 804.0005; 934 at 934.0030; 935 at 935.0030.)

In addition to a cap on the interest to be credited in any given year, Provider and Paragon also include a floor of zero percent every year. Therefore, no matter how poorly the stock market may perform in a particular year, Provider and Paragon policies will never be credited a negative interest rate to reflect poor stock market performance. For example, while the S&P 500 Index lost 38 per cent in 2008, Provider or Paragon policyholders did not receive negative interest credits. (Trial Exs. 30 at 30.0010; 48 at 48.0011; 86 at 86.0003-86.0004; 804 at 804.0007; 934 at 934.0030; 935 at 935.0030; 947.)

Given these participation rates, earnings caps, and floor, IUL policies are not intended to, and do not, mirror the performance of the stock market. Instead, the purpose of the products is to provide some limited market exposure by eliminating downside risk (by setting a zero per cent interest floor) and limiting upside returns to a fixed rate. (4/9 Trial Tr. 144:15-145:20; 4/18 Trial Tr. 92:22-93:4; Trial Ex. 804 at 804.0004, 804.0006 ("Purchasing an Indexed Universal Life contract is not equivalent to investing directly in the stock market.").) These participation rates, earnings caps, and a floor of zero percent are standard in IUL products available from many insurers. (4/9 Trial Tr. 137:17-138:2; 4/18 Trial Tr. 93:22-94:9, 98:24-99:2.)

Although it offers an insurance product that credits policies based on the performance of stock market indices, LSW does not attempt to predict how the stock market will perform in the future. It is not necessary for LSW to predict the market because it does not invest premium proceeds into the stock market directly. To the contrary, LSW invests premium proceeds in fixed income and derivative products with the objective of replicating what the LSW will need to pay policyholders at the end of the year, regardless of how the stock market performs. LSW does not make any profit on the difference between the performance of the stock market and the earnings cap. (4/9 Trial Tr. 137:17-138:2; 4/18 Trial Tr. 159:19-162:15, 163:1-164:13.)

In order to accomplish this goal, LSW uses most premium proceeds to purchase long-term fixed-income products (e.g., corporate bonds). The interest earned on these fixed-income products, along with the principal invested, affords LSW with the money on hand at the end of the year to provide the zero percent floor on Provider and Paragon policies. (4/18 Trial Tr. 159:23-160:25.) LSW then uses the balance of the premium proceeds to purchase one-year options on the stock market index, designed to return the amount that would be credited to the policyholder if the stock market index grows in a given year. (4/18 Trial Tr. 159:23-161:17, 163:1-20.) For example, if a policyholder allocated $1,000 to a given strategy, LSW may invest $950 of that amount into fixed-income products that paid roughly five percent interest, in order to ensure that $1,000 would remain at the end of the year. It would then use the remaining $50 to purchase options that would provide additional return in the event that the S&P 500 Index appreciated in a given year. (See 4/18 Trial Tr. 159:23-161:17.)

Participation rates and earnings caps for a Provider and Paragon policies are determined in advance by LSW, subject to limitations set forth in each policy. LSW might adjust participation rates and caps, for example, to reflect the cost of options in the marketplace. Because LSW must purchase these options every year, short-term changes in the price of options may require LSW to adjust the participation rate and cap up or down to ensure that it is able to cover any interest credits. However, historically LSW has tried to minimize changes in participation rates and caps, even when doing so hurt LSW's bottom line. (4/18 Trial Tr. 163:1-167:10; Trial Exs. 30 at 30.0010; 48 at 48.0010; 934 at 934.0030; 935 at

935.0030.) LSW does not adjust participation rates and earnings caps simply for the purpose of increasing its own profits by reducing the interest that it would credit to policyholders. (4/18 Trial Tr. 161:5-162:2, 163:1-167:10.)

2. Guaranteed Accumulation

In addition to the annual floor of zero percent, Provider and Paragon also provide that, over a certain period of time, the policy's cash value will be credited a certain minimum amount of interest. This minimum guarantee is calculated and credited retrospectively on a look-back basis. (4/18 Trial Tr. 94:14-95:7; Trial Exs. 86 at 86.000486.0005; 804 at 804.0007; 934 at 934.0030-934.0031; 935 at 935.0030.) In the case of Provider, the guaranteed accumulation provides that if a policyholder's cash value has not accumulated by at least two percent per year compounded over a five-year period, upon surrender of the policy, or upon the death of the insured, LSW will credit an additional amount to the policy as necessary to ensure at least two percent per annum compounded growth. (4/18 Trial Tr. 94:14-95:7; Trial Exs. 86 at 86.0004-86.0005; 934 at 934.0030 -934.0031.) In the case of Paragon, the guaranteed accumulation provides that if a policyholder's cash value has not accumulated by at least two-and-a-half percent per year compounded upon surrender of the policy or the death of the insured, LSW will credit an additional amount to the policy as necessary to ensure at least two-and-a-half percent per annum compounded growth. (4/18 Trial Tr. 94:14-95:7; Trial Exs. 804 at 804.0007; 935 at 935.0030.) This retrospective method of crediting guaranteed interest is standard in the industry for IUL products. (4/18 Trial Tr. 99:3-6.)

LSW trains its agents to understand how the guarantees for Provider and Paragon operate, and directs agents to call LSW's sales desk to answer any remaining questions their clients may have about guarantees. (Trial Ex. 96 at 96.0014.)

3. Charges and Fees

Charges and fees are deducted from Provider and Paragon policies. There are slightly different names given to, and amounts charged for, certain of the charges and fees associated with Provider and Paragon. (4/18 Trial Tr. 126:21-130:8; Trial Exs. 934 at 934.0007-934.0010, 934.0031-934.0032; 935 at 935.0007-935.0010, 935.0031.) In the case of Provider, the charges include a premium expense charge deducted from any premiums paid, a monthly cost of insurance charge, a monthly administrative charge, and a monthly policy fee. (4/9 Trial Tr. 139:10-23; 4/18 Trial Tr. 127:4-128:22; Trial Exs. 49 at 49.0012 ("There are administrative, cost of insurance and other charges associated with the LSW Provider IUL policy"); 86 at 86.0007 (additional premium payments may be necessary "if the policy's cash value is not sufficient to cover the monthly fees and cost of insurance charges"); 934 at 934.0007-934.0010, 934.00319-34.0032.) In the case of Paragon, the charges include a premium expense charge deducted from any premiums paid, a monthly cost of insurance charge, a monthly administrative charge, a monthly policy fee, and a monthly percent of accumulated value charge. (4/9 Trial Tr. 139:10-140:1; Trial Ex. 935 at 935.0007-935.0010, 935.0031-935.0032.)

These different categories of charges are common among IUL products on the market, although different companies vary in the terminology that they use to describe, and the amounts they deduct for, the different charges. For example, one insurer may charge less than LSW for its "cost of insurance" charge, but a higher "policy fee." (4/18 Trial Tr. 98:24-99:16, 128:23-130:8.) Each charge or fee charged under the Provider and Paragon policies, and the amount of the charge or fee, is described in the policy. (4/18 Trial Tr. 127:14-128:22; Trial Exs. 934 at 934.0007-934.0010, 934.0031-934.0032; 935 at 935.0007-935.0010, 935.0031.)

The Provider and Paragon policies set forth maximum amounts that LSW could deduct for a certain charge or fee, thereby guaranteeing that the amount will never exceed this maximum level. However, during the relevant period, LSW voluntarily charged policyholders less than the maximum amount permissible under the policies. For example, Provider and Paragon policies guarantee that the cost of insurance shall not exceed a certain rate prescribed by California regulations, but LSW has in practice never imposed this maximum rate. (4/18 Trial Tr. 150:6-151:24; Trial Exs. 934 at 934.0007; 935 at 935.0007.)

In addition, LSW has the ability to further reduce certain charges or fees in the future. In particular, LSW intends and expects that the monthly administrative charge will be substantially reduced (in the case of Provider) or eliminated (in the case of Paragon) after a policy has been in force for ten years. LSW has already programmed its computer systems to implement this reduction and has designed and priced Provider and Paragon on the assumption that the reduction will in fact occur. (4/22 Trial Tr. 26:17-29:13; Trial Exs. 30 at 30.0021; 48 at 48.0021.)

By guaranteeing that charges will never exceed some higher amount, but actually charging much less, LSW is able to hold smaller reserves for Provider and Paragon policies. These smaller reserves accrue to the benefit of the policyholders, because higher reserves would mean more expensive policies and less value being returned to policyholders. (4/22 Trial Tr. 22:10-24:6.)

4. Policy Loans

Provider and Paragon, like any other whole or universal life insurance policy, permit policyholders to use accumulated cash value in a variety of different ways. (4/9 Trial Tr. 125:14-20, 128:1-5.) Policyholders can use accumulated cash value to pay policy charges and fees, thus reducing or even eliminating the need to make additional out-of-pocket premium payments. They can use the cash value to increase the amount of the death benefit to be paid to their beneficiaries. Or they can take the cash value out of the policy and use it for their own purposes, either by withdrawing the cash value or borrowing against the value of the policy. This income can be used for any purpose, including retirement and college savings. (Trial Exs. 86 at 86.0005-86.0006; 804 at 804.0004, 804.0007; 934 at 934.0033-934.0035; 935 at 935.0033-935.0035.)

Loan amounts and timing are flexible, and are not set in stone when a policy is issued. As disclosed in the policy, a policyholder can take a loan at any time after the first year, in any amount up to the limits described in the policy. For example, if the S&P 500 Index performs better than anticipated, a policyholder may be able to take larger loans. If the S&P 500 Index performs worse than anticipated, a policyholder may not be able to take as much income from the policy. (4/10 Trial Tr. 174:2-8; 4/18 Trial Tr. 134:16-135:20; Trial Exs. 48 at 48.0009 ("[l]ess favorable results may significantly reduce both policy values and the size of distributions available to the policyholder"); 674 at 674.0006 ("Remember that nobody knows what will happen in the future. You should be ready to adjust your financial plans if the cash value doesn't increase as quickly as shown in the illustration"); 934 at 934.0033; 935 at 935.0033.)

As long as the policy complies with certain rules set by the Internal Revenue

Service, policy loans can be taken out on a tax-free basis so long as the policy stays in force until the loans are repaid or the death of the insured. When the insured dies, death benefit proceeds are paid tax-free and used to repay the loan. (4/9 Trial Tr. 126:18-127:10, 150:22-153:14; Trial Exs. 86 at 86.0003, 86.0006; 804 at 804.0002, 804.0007; 934 at 934.0035; 935 at 935.0035.) However, if a loan remains outstanding and the policy does not remain in force, any loan proceeds above the policyholder's basis (i.e., the amount of premiums paid by the policyholder) are considered and taxed as ordinary income. (4/9 Trial Tr. 152:15-153:14; Trial Exs. 86 at 86.0003, 86.0006; 804 at 804.0002, 804.0007 ("If the policy were to lapse prior to death, a portion of the loaned amount may be taxed as income to the policyholder").) These tax benefits are well-known. The potential tax consequences of a loan if a policy ceases to be in force are also very well-known. (4/9 Trial Tr. 149:12-150:4.)

5. Policy Termination

At any point, a policyholder is free to surrender his or her Provider or Paragon policy. Within ten days of receiving a copy of his or her policy, the policyholder can cancel the policy without penalty and receive a full refund for any reason. This so called "free look" right is required by law, and prominently displayed on the front page of the policy contract. (4/18 Trial Tr. 118:21-119:10; Trial Exs. 934 at 934.0004; 935 at 935.0004.) After ten days, a policyholder is still free to surrender his or her Provider or Paragon policy at any time by submitting a written request. LSW returns the accumulated cash value of the policy to the policyholder, including any additional credits due to the look-back minimum guarantee provision of the contract, less the surrender charge (if applicable) and any outstanding debt on the policy (if applicable). (4/18 Trial Tr. 122:9-18, 136:12-19; Trial Exs. 30 at 30.0007; 48 at 48.0007; 934 at 934.0032; 935 at 935.0032.)

If the surrender occurs during the first ten years of a policy, LSW deducts a surrender charge. LSW imposes a surrender charge for policyholders who cancel their policy early in order to cover the up-front expenses associated with issuing a policy (e.g., underwriting expenses, administrative expenses, and commissions). The surrender charge also offsets the up-front costs associated with the long-term investments that LSW makes to fund the interest credits on the policies, which are purchased on the assumption that the policy will remain in force over a long time horizon. If LSW did not impose a surrender charge, these up-front expenses would be borne by those policyholders who chose to hold onto their Provider and Paragon policies, resulting in higher charges and fees. (4/18 Trial Tr. 122:19-124:19.) After the tenth policy year, however, the surrender charge reduces to zero, meaning that policyholders can access the entire cash value of their policies without penalty. (4/18 Trial Tr. 122:9-18, 136:12-19; Trial Exs. 30 at 30.0007, 30.0021; 48 at 48.0007, 48.0021; 934 at 934.0010, 934.0032; 935 at 935.0010, 935.0032.) The amount and duration of the surrender charge applicable to a policy are disclosed in every illustration and every policy. (4/18 Trial Tr. 125:8-126:20; Trial Exs. 4 at 4.0021; 30 at 30.0021; 48 at 48.0021; 934 at 934.0010, 934.0032; 935 at 935.0010, 935.0032; 936 at 936.0010, 936.0032.)

Ten-year surrender charges are a common feature of universal life insurance policies offered in the market. The amount of any surrender charges are disclosed to and regulated by the Department of Insurance, and LSW has voluntarily set the surrender charges on Provider and Paragon for shorter durations and lower levels than it could otherwise permissibly collect under those regulations. (4/18 Trial Tr.

99:7-8, 122:12-18, 124:20-125:7, 142:24-144:23, 155:3-157:21.) If a policyholder chooses not to make premium payments sufficient to cover the charges and fees in his or her policy, it may lapse. As disclosed in the policy, a policy enters a 60-day grace period when the cash value drops to the point that the cash surrender value (meaning the accumulated value of the policy less any then-applicable surrender charge) is not enough to cover the next month's charges. If the policy enters the grace period, LSW sends a notice to the policyholder. Additional premium must be paid to keep the policy in force beyond the grace period; otherwise, the policies will lapse. (4/18 Trial Tr. 138:14-140:21; Trial Exs. 86 at 86.0005; 804 at 804.0004; 934 at 934.0006, 934.0021-934.0023; 935 at 935.0006, 935.0021-935.0023.)

As Plaintiffs' expert testified, the only way that a Provider or Paragon policy may lapse is if a policyholder stops paying sufficient premiums to cover the charges and fees, or takes too much out of the policy in loans and withdrawals. (4/10 Trial Tr. 44:23-45:12; 4/18 Trial Tr. 133:11-22.) The definition of lapse used in Provider and Paragon, when the cash surrender value reaches zero, is common among universal life insurance policies. In fact, the LSW lapse definition is the presumptive definition adopted by the National Association of Insurance Commissioners in its model universal life insurance regulation. (4/18 Trial Tr. 141:2-18.)

Provider and Paragon policies are not lapse-prone. While it is true that the policies may lapse, that is a product of policyholder choices not to pay for the life insurance benefits provided by the policy — a circumstance that would cause any universal life insurance policy to lapse, regardless of any other factors. If a policyholder funded his or her policy, the probability that it would ever lapse is virtually zero. (4/22 Trial Tr. 30:9-32:22, 61:1-8; Trial Ex. 874.) Plaintiffs' expert also testified that if a policyholder maximally funded the policy or chose not to take loans, he or she could ensure that the policy would never lapse. (4/10 Trial Tr. 44:23-45:12, 173:19-174:1.)

While it is true that some Provider and Paragon policies have lapsed since the products were first introduced, this is because those policyholders have chosen not to pay their premiums. (4/22 Trial Tr. 30:12-21.) In fact, Dr. Brockett's testified that, even in his own testing, no policies lapsed within the first ten years assuming that the policyholder made premium payments. (4/10 Trial Tr. 161:18-165:15.)

LSW did not, and does not, run any Monte Carlo analysis to determine the likelihood that a Provider or Paragon policy will lapse based upon the particular funding and withdrawal pattern selected by any policyholder when applying for a policy. Nor does LSW attempt to project how the stock market may perform in the future to determine its impact on policy values. The unrebutted testimony at trial is that no insurance company performs such analysis for IUL products. (4/18 Trial Tr. 31:17-22, 162:3-19; 4/22 Trial Tr. 38:9-23.)

G. <u>POLICY SALES</u>

Provider and Paragon are sold by independent life insurance agents, who are not employees of National Life or LSW. These independent agents can sell a variety of types of insurance from a number of different insurance companies. (4/18 Trial Tr. 101:18-102:6; 4/23 Trial Tr. 51:2-18.) In addition to receiving information from agents, policyholders are free to, and do, obtain information about their policies by conducting their own research or by consulting with third party advisors. (<u>See, e.g.</u>, 4/16 Trial Tr. 222:13-223:23, 224:5-226:3; 4/17 Trial Tr.

47:4-20, 72:4-12, 72:25-75:15, 76:21-77:6; Trial Ex. 743.)

There was no evidence that Paragon and Provider sales were conducted in a uniform manner. There were no sales scripts. Instead, the policies were sold by tens of thousands of agents who had at their disposal any of thousands of marketing pieces for use. As Matthew DeSantos, LSW's Senior Vice-President of Distribution and Business Development (himself a former insurance agent) testified, each sale is like a snowflake. In particular, Provider and Paragon offer a number of different benefits within one product, including death benefit protection, premium flexibility, cash value accumulation, income potential for retirement or any other purpose. No two customers are alike, and each consumer will have his or her own reasons and purposes for deciding to purchase a Provider or Paragon policy. (4/23 Trial Tr. 50:1-14, 55:5-16, 56:6-23, 58:23-60:15, 92:27.)

LSW trains agents to explain what the indexed strategies are and how they work, so that the client understands the index crediting strategies. LSW also trains agents to work together with the client to understand the client's unique needs. (4/23 Trial Tr. 74:3-75:5; Trial Ex. 59 at 59.0008; 96 at 96.0005.) During the course of any given sale, an agent will meet with the customer several times, sometimes gathering information about their needs and their financial situations, and explaining the features of the available product options. The agent also answers any questions that a customer may have about the products they are considering. (4/23 Trial Tr. 56:24-58:22, 89:3-14.) In addition to these oral communications, agents may provide any number of marketing, sales, or other written materials out of thousands that are made available to them. All told, there is a multitude of documents that can be provided to a policyholder during the sales process. (4/18 Trial Tr. 55:17-56:2; 4/23 Trial Tr. 91:22-92:16.)

The actuaries responsible for developing Provider and Paragon, Ms. MacGowan and Mr. Tivilini, wanted LSW to lead the insurance industry in its disclosure and explanation of all of the policies' features. Mr. Tivilini testified that he never encountered any resistance at LSW to that goal. (Tivilini Dep. Tr., Docket 735 Ex. B at 60:4-15.) Among the available materials are Buyer's Guides, which are specific to Provider and Paragon. These documents may be provided to policyholders at any time, and LSW requires that every policyholder receive a Buyer's Guide, at the latest, when they receive a copy of the policy. (4/18 Trial Tr. 112:3-18; 4/22 Trial Tr. 11:15-16; Trial Exs. 86; 792; 804.)

Another document that may be used during a sale is an illustration. An illustration is not meant to replace the policy contract or contain all of the details of a policy, but provide a brief summary that demonstrates the mechanics of the Provider and Paragon policies with certain, specified "what-if scenarios." 4/18 Trial Tr. 55:17-56:11; Trial Exs. 30 at 30.0010 ("Please refer to the policy for complete details. In the event of any conflict, the policy language will control"), 30.0012 (describing different scenarios); 48 at 48.0010, 48.0012.)

Illustrations are heavily regulated by the Department of Insurance. These regulations specify the content that may appear in an illustration, and require that certain disclosures be made in all illustrations. LSW and other insurers are required to submit an example of an illustration to the Department of Insurance as part of the Department's initial review and approval of a product. (4/18 Trial Tr. 64:21-65:4, 143:14-146:17.) By regulation, LSW (like any other insurer) has appointed an illustration actuary who is responsible for ensuring that the illustrations comply with these regulations. Craig Smith and Elizabeth MacGowan, LSW's illustration actuaries since the Provider and Paragon policies were launched, testified at trial. (4/17 Trial Tr. 195:12-19; 4/18 Trial Tr. 86:5-16, 147:13-22; 4/22 Trial Tr. 161:14-20.)

The illustrations are generated by agents using software designed and updated by designated employees under Elizabeth MacGowan's supervision. (4/17 Trial Tr. 160:2-13; 4/18 Trial Tr. 48:11-13; Trial Exs. 4; 30; 48.) Illustrations are customized documents, which may be prepared based on conversations between the consumer and his or her agent. Once the illustration is generated by the agent, they sit down again and discuss the illustration, how the product may work, and some of the features associated with the policy. Each of these conversations is different, because every policyholder is different. (4/23 Trial Tr. 91:3-21.)

LSW's Provider and Paragon illustrations show how the policies may perform in the future under three scenarios: Guaranteed, Current Basis A and Current Basis B. The Guaranteed scenario reflects the low end of what a policyholder could receive, using the maximum charges and minimum guaranteed growth. Current Basis B represents the highest of these scenarios, reflecting annual accumulation at a rate chosen by the policyholder and his or her agent (but never more than the maximum level allowed by the illustration regulation). Current Basis A represents a middle scenario and is included as a point of comparison so that policyholders can understand the effects of a lower rate of accumulation. (4/10 Trial Tr. 149:2-150:23, 151:2-152:1, 172:11-173:3, Trial Exs. 30 at 30.0007-30.0008, 30.0011-30/0012, 30.0014-30.0020; 48 at 48.0007-48.0008, 48.0012, 48.0014-48.0020.) Each of these scenarios is based on assumed consumer behavior in the future, including out-of-pocket premium payments, loan amounts and timing, and index strategy allocation. (4/16 166:16-25; Trial Exs. 4 at 4.0012-4.0023; 30 at 30.0012-30.0023; 48 at 48.0012-48.0023.)

Of these three scenarios, and as the designation implies, only the "Guaranteed" values are guaranteed. Current Basis A and Current Basis B values are not guaranteed and the possibility that a policyholder will achieve those results depends upon the actual future performance of the S&P 500 Index. Guaranteed values are calculated using the guaranteed minimum accumulation on the policy (2 per cent for Provider and 2.5 per cent for Paragon) and guaranteed maximum charges. (4/10 Trial Tr. 149:20-151:5; 4/15 Trial Tr. 155:20-23 (Ms. Spooner "knew that the guaranteed column in the scenario . . . was really the only one that LSW was guaranteeing"); Trial Exs. 30 at 30.0014-30.0020; 48 at 48.001448.0020.)

Current Basis B values illustrate cash value accumulation at a rate chosen by the policyholder and his or her agent. There is, however, a limit on how high this accumulation rate can be. Under the Department of Insurance's illustration regulation and applicable Actuarial Standards of Practice, the maximum rate that can be used in calculating any value for any duration is the so-called "disciplined current scale," which is determined by the past average annual growth of the stock market index as filtered through the policy's participation rates and earnings cap. (4/18 Trial Tr. 51:25-53:10; Trial Ex. 48 at 48.0012.)

The illustration regulation requires that an illustration provide the Current Basis B values (based on the maximum illustrated rate) and the worst case Guaranteed values. LSW decided to go beyond the minimum required by the regulation and include a third, middle set of values (Current Basis A), to disclose to policyholders what might happen if the stock market does not perform as well as reflected in Current Basis B. (4/18 Trial Tr. 66:8-69:10, 154:10-18; Trial Ex. 48 at 48.0009 ("Current Basis A reflects projected values under . . . a less favorable scenario for the policyholder. This second projection is useful as a point of comparison").)

In each of these three illustrated scenarios (Guaranteed, Current Basis A and Current Basis B), policy values are reflected for every year until the policyholder turns 120 years old. The represented values are net of all charges and fees associated with the policy, so they represent the bottom-line numbers that a policyholder would get in each of the respective scenarios. (4/18 Trial Tr. 129:6-132:2; Trial Exs. 30 at 30.001430.0020; 48 at 48.0014-48.0020.)

Illustrations can also reflect loans in a certain amount and frequency determined by the customer. The default case does not assume loans in an illustration, and the majority of illustrations received by policyholders in this litigation did not reflect loans. Even among those illustrations that do reflect loans, each one is different — there are a variety of ways for the policyholder to determine the amount and frequency of any loans. (4/11 Trial Tr. 74:4-75:3; 4/18 Trial Tr. 108:16-109:16; Trial Exs. 30 at 30.0014-30.0020; 48 at 48.0014-48.0020.)

An illustration can also include pages breaking out the individual charges and fees associated with the policy. This, too, is not included in the default case, but can be easily added with one click by using a drop-down menu on the illustration software. LSW trains its agents that they should explain all charges and fees associated with the policies, and tells agents that they should generate the additional reports if their clients desire additional detail. (4/18 Trial Tr. 109:17-110:6; 4/23 Trial Tr. 76:4-79:8; Trial Ex. 96 at 96.0011.)

Illustrations can be presented to a policyholder at any time. If a policyholder received an illustration reflecting the policy as applied for, he or she signs the illustration and submits it along with the application. Both parties have referred to any illustration dated on or before the date of application as a "sales illustration." (4/10 Trial Tr. 37:24-38:20; 4/23 Trial Tr. 91:3-21; Trial Ex. 30 at 30.0024.) Although all policyholders receive an illustration at some point at or before the time they receive a copy of their policy, not all policyholders receive sales illustrations. In fact, at least a quarter of LSW's policy files do not contain any sales illustrations. And even among those policies where there was a sales illustration in the policy file, Plaintiffs did not provide any evidence of the frequency with which policyholders actually received a sales illustration. (4/11 Trial Tr. 59:11-60:16.)

If the policyholder did not receive a sales illustration before applying for a policy, or if the policy as issued differs from the policy for which he or she applied (e.g., a different underwriting class), LSW generates an illustration of the policy as issued and requires that this illustration be delivered to and signed by the policyholder along with a copy of the policy. Both parties have referred to a post-application illustration generated by LSW as a "batch illustration." (4/10 Trial Tr. 38:21-39:5, 39:24-40:8; 4/11 Trial Tr. 60:14-16; 4/18 Trial Tr.112:3-8; 4/23 Trial Tr. 89:3-14.)

Batch illustrations often differ from sales illustrations in important ways. If a policy as issued differs from the policy as applied for, such differences necessarily would result in different illustrated values. For example, if a policy is issued at a more favorable underwriting class than was applied for, some of the charges and fees assumed in the batch illustration will be lower than those depicted in a sales illustration prepared assuming the less favorable underwriting class. Moreover, batch illustrations are based only on information reflected in an application; they do not depict loans and show premium payments persisting throughout the life of the policy — a funding pattern that Plaintiffs' expert admitted would prevent the policies from ever lapsing. (4/10 Trial Tr. 173:17-22; 4/11 Trial Tr. 62:1-22, 93:6-11; 4/15 Trial Tr. 55:24-56:25; 4/18 Trial Tr. 110:7-16.)

All illustrations make clear the possibility of disagreement between a sales illustration and a batch illustration and explain that, in the event of any disagreement, the batch illustration controls. (4/18 Trial Tr. 110:21-111:14; Trial Exs. 30 at 30.0009 (in the event of conflict, "the actual values illustrated with the policy shall control"); 48 at 48.0009 (same).)

LSW trains agents to review any illustrations with the client, explain their contents, and answer any questions that the policyholder may have, including in particular those questions concerning the costs, guaranteed interest, non-guaranteed accumulation, and death benefit information. (Trial Ex. 59 at 59.0008; 96 at 96.0017.)

H. PLAINTIFFS' PURCHASES

1. Joyce Walker

Ms. Walker applied for an LSW SecurePlus Provider policy on November 14, 2007, with a death benefit of $2,464,759. (4/16/14 Trial Tr. 210:8-14; 4/17/14 Trial Tr. 86:16-22; Trial Ex. 784.) Before she decided to apply for her policy, Ms. Walker spent months educating herself about the policy. It was a deliberate decision that she took seriously. As a part of this process, she had several substantive meetings with her independent insurance agents, Jeffrey Stemler and Michael Botkin. Each of these meetings lasted about an hour. (4/16 Trial Tr. 211:8-13; 4/17 Trial Tr. 48:1-49:6, 57:24-58:14, 61:4-11.) During these meetings, Ms. Walker discussed various features of the Provider product with her agents, including how the policy's indexing feature operated, the various charges and fees associated with the policy (and the amount of some of those fees), and the existence of a zero percent annual floor. (4/16 Trial Tr. 226:23-227:12, 228:3-18; 4/17 Trial Tr. 71:14-72:3, 83:5-85:3; Trial Ex. 772.)

In addition to these meetings and conversations with her agents, Ms. Walker also consulted with third parties, including her personal financial planner and an insurance agent for a different insurance company. They discussed the charges and fees associated with the policy and provided some comparative information about other products that were available to Ms. Walker, in order to "make sure that [she] was making the right decision with the LSW product." (4/16 Trial Tr. 222:13 -223:23, 224:5-226:3; 4/17 Trial Tr. 47:4-20, 72:4-12, 72:25-75:15; Trial Ex. 743.) Ms. Walker also conducted online research to "gain a little bit more of an understanding of the product." Based on her research, Ms. Walker created a list of questions she wanted answered regarding Provider. Ms. Walker's agents answered all of the questions she asked them. (4/16 Trial Tr. 226:15-227:5; 4/17 Trial Tr. 76:21-78:14, 81:8-82:2; Trial Exhibit 744.)

Ms. Walker reviewed at least two illustrations before deciding to apply for her Provider policy, including during meetings with her agents. Among other things, this review included the fact that Current Basis B and Current Basis A values were not guaranteed, the policy's guaranteed values, the possibility that the policy would lapse, and "the various costs" associated with the policy. Ms. Walker's agents also made handwritten notations on the illustration. (4/16 Trial Tr. 215:6-216:1, 217:5-12, 219:19-220:15, 221:3-16, 222:7-12, 230:3-14, 231:3-15; 4/17 Trial Tr. 53:15-54:6, 57:24-58:14, 69:12-71:9; Trial Ex. 781 at

781.0023-781.0024, 781.0026, 781.0029-781.0035.)

Ms. Walker "extensively reviewed" the illustration she received dated October 3, 2007. This illustration assumed that Ms. Walker would make five premium payments of $112,637 each, and loans beginning in year 15. (4/17 Trial Tr. 58:15-18; Trial Ex. 48 at 48.0014.) Ms. Walker's agents made clear that her ability to take loans of any particular amount was not set in stone, and that they would need to re-assess the amount and timing of any loans when Ms. Walker reached her retirement age based upon how the stock market had actually performed. (4/24 Trial Tr. 55:14-56:14, 60:23-62:15, 66:1267:2.)

Ms. Walker's agents generated the October 3, 2007 illustration using a Current Basis B rate of accumulation of less than the maximum interest rate allowed. (4/16 Trial Tr. 218:19-219:4; 4/17 Trial Tr. 13:23-14:7; 4/24 Trial Tr. 57:19-59:16, 60:222; Trial Ex. 48 at 48.0012.) The October 3, 2007 illustration showed the risk that her policy would lapse, reflecting a lapse under both the worst-case Guaranteed and middle-case Current Basis A scenarios. Ms. Walker understood that the illustration "show[ed]" that lapse "could happen even after making [her] entire required $560,000 contribution" of premium payments. (Trial Exs. 781 at 781.0003 (email); 48 at .00018 (illustration showing lapse after year 23 (Current Basis A scenario)), .00014 (illustration showing lapse after year 16 (Guaranteed scenario).)

Ms. Walker claims to have relied on the information in her October 3 illustration in deciding to purchase her policy. However, Ms. Walker did not sign the illustration. In fact, when she applied for her policy, she certified that she had "NOT received an illustration of the policy applied for." (4/17 Trial Tr. 53:15-54:6; Trial Exs. 48 at 48.0024; 784 at 784.0002.)

Ms. Walker's policy had an effective date of December 27, 2007. A copy of the policy, along with a batch illustration, a Provider Buyer's Guide, and a National Association of Insurance Commissioners Buyer's Guide, was delivered to and signed for by Ms. Walker on January 11, 2008. (4/17 Trial Tr. 15:11-17, 91:4-92:9; Trial Exs. 49; 86; 674; 676; 934 at 934.0004.) The cover of Ms. Walker's policy stated that she had the right to review her policy and return it within ten days for a full refund of any premiums paid. Ms. Walker is aware of this free-look right to return her policy. The cover of the policy also said, in all capital letters, that Ms. Walker should "READ [HER] POLICY CAREFULLY." (4/17 Trial Tr. 91:1-3; Trial Ex. 934 at 934.0004 (capitalization in the original).)

Nevertheless, Ms. Walker did not read her policy or the two buyer's guides that accompanied the policy, and she did not review the batch illustration she received along with her policy. (4/17 Trial Tr. 16:6-18:6, 90:3-91:3, 93:6-17.) The batch illustration showed no loans. (Trial Ex. 49 at 49.0015-49.0026.) However, she did sign the last page of the batch illustration, stating that she "received a copy of this illustration and understand[s] that any non-guaranteed elements illustrated are subject to change and could be either higher or lower" and that she "UNDERSTAND[S] THAT HISTORICAL PERFORMANCE OF THE S&P 500 INDEX SHOULD NOT BE CONSIDERED A REPRESENTATION OF THE PAST OR FUTURE PERFORMANCE FOR ANY OF THE INDEXED STRATEGIES IN THE POLICY." (Trial Ex. 49 at 49.0027 (capitalization in the original).) After receiving these documents Ms. Walker wrote a check for the first premium payment in the amount of $112,000, made payable to Life Insurance Company of the Southwest. The memo line of the check indicated it was for a "life insurance premium." (Trial Ex. 877.)

At the end of her first policy year, Ms. Walker received an annual statement. Although the S&P 500 Index had gone down by more than 35 percent in 2008, the floor on her policy prevented her from losing any value as a result of the index performance. Instead, she received a small positive credit to her policy because of fixed returns in the policy. (4/17/14 Trial Tr. 105:4-18; Trial Exs. 94; 947.) This annual statement also itemized each of the charges and fees that had been assessed on a month-by-month basis since her policy was issued. (Trial Ex. 94 at 94.0003, 94.0005.)

Ms. Walker also wrote to Mr. Stemler and asked how much interest had been credited to her policy in the prior year. Ms. Walker was informed that no interest had been credited to her policy in 2008. (4/17 Trial Tr. 108:1-111:3; Trial Ex. 867-A.) Although she knew that she had received zero indexed credit in the first year and that she had been charged $19,606.58 in charges and fees, Ms. Walker sent another premium check to LSW for her second premium payment of $112,000 in February 2009. (4/17 Trial Tr. 18:18-19, 111:9-112:7, 113:19-22.) Ms. Walker did not make any further premium payments. Thus she made only two of the five payments reflected in her illustration. (4/17 Trial Tr. 18:12-24; Trial Exs. 48 at 48.0014; 877.)

In March 2009, Ms. Walker lost her job. She also suffered substantial losses in her other investments, such that she became unable to make any of her future premium payments. She began consulting other financial advisors for assistance in getting her money back from LSW. (4/17 Trial Tr. 118:6-25, 123:9-13, Trial Ex. 673; 675; 723.)

At trial, Ms. Walker denied that her financial difficulties were the real cause of her trying to get out of her policy. However, the Court credits the more persuasive contemporaneous documents, which tell a different story, and which tie Ms. Walker's need to assess her financial condition in light of other market losses. For instance, those documents reveal that Ms. Walker experiencing substantial losses across the board in several accounts and owed more on her house than it was worth. Indeed, in an email to one of her financial advisors, Ms. Walker stated: "What happened so that I was going to be unable to continue the premiums? The stock market slide of 2009!!!!!!! Lost about half." In another message to the same advisor, she wrote: "I have the next $100,000 available but don't have the next two payments amassed yet due to stock market losses." (4/17 Trial Tr. 121:3-11; Trial Exs. 673; 675; 723.)

In an effort to get back her premiums in light of her economic difficulties, Ms. Walker worked with these advisors to write a complaint letter to LSW. This letter does not include any reference to allegedly undisclosed fees, the zero percent annual floor, reduction in the monthly administrative charge, or the possible effects of stock market volatility. (4/17 Trial Tr. 114:7-24,118:6-25; Trial Ex. 781 at 781.0003-781.0004.) Based on its review, LSW denied Ms. Walker's complaint. (Trial Ex. 670.)

Ms. Walker then reached out to another advisor, Steve Burgess of the Center for Life Insurance Disputes, to enlist his assistance with preparing another complaint, this time to the Department of Insurance. (4/17 Trial Tr. 141:9-142:20.) Ms. Walker sought to make "a compelling enough argument to prompt [LSW] to return [her] premiums." As she explained to the Department of Insurance investigator assigned to her case, Ms. Walker was looking for a "loophole" that would "work in [her] favor in terms of getting all [her] money back." (Trial Exs. 683; 732; 733.)

On May 27, 2010, after her complaints proved unsuccessful, Ms. Walker surrendered her policy. She received $142,633.79 upon surrender. She had not taken any loans against her policy and did not pay any taxes upon surrender. (Trial Ex. 780; Final Pretrial Conference Order at 2.)

Before bringing this lawsuit, Ms. Walker told one of her economic advisors that she was not "sure [LSW] won't come back and tell [her she] should have read [her] policy and looked at the illustration more closely." Later, she wrote to Mr. Burgess, asking him "how do we get around the fact that I signed the contract." (Trial Exs. 706; 732.)

On September 24, 2010, Ms. Walker joined in filing this lawsuit. (4/17 Trial Tr. 142:10-14; Class Action Complaint, Docket 1 Ex. A.)

2. <u>Kim Howlett and Muriel Spooner</u>

As noted previously, these two named Plaintiffs are married to each other. Mr. Howlett applied for an LSW SecurePlus Paragon policy on July 30, 2007, with a death benefit of $1,602,311. (4/16 Trial Tr. 84:1-11; Trial Ex. 633.) Ms. Spooner applied for an LSW SecurePlus Paragon policy on July 30, 2007, with a death benefit of $1,069,608. (4/15 Trial Tr. 71:10-21; Trial Ex. 891.)

Mr. Howlett and Ms. Spooner were sophisticated investors, with substantial net worth and a number of complex investments. They were well aware, among other things, that the stock market was volatile. (4/15 Trial Tr. 98:14-101:16; 4/16 Trial Tr. 24:3-17, 177:20-180:4.) Before applying for their Paragon policies, Mr. Howlett and Ms. Spooner had a number of meetings to discuss insurance options over the course of more than a year with their independent insurance agent, Jacob Cooper. These included a seminar on retirement planning and several subsequent in-person meetings. During these meetings, Mr. Cooper provided written materials and answered any questions that Mr. Howlett and Ms. Spooner asked. (4/15 Trial Tr. 73:8-74:3, 75:3-16, 77:11-78:11, 123:11-23, 124:1318; 4/16 Trial Tr. 13:8-16, 21:21-22:2, 86:10-15, 126:7-127:1; Trial Ex. 632.)

These discussions made clear that the life insurance policies being described to Mr. Howlett and Ms. Spooner would include charges associated with the policy, including mortality and expense charges. Additionally, Mr. Cooper described to Mr. Howlett and Ms. Spooner all of the charges and fees associated with the policies. Ms. Spooner was aware that there were multiple charges associated with the policies. (4/15 Trial Tr. 132:4-133:8, 133:16-135:4, 176:11-16; 4/16 Trial Tr. 61:6-62:9, 63:5-63:24, 64:9-18.) After these conversations, Mr. Howlett and Ms. Spooner decided that they wanted to "move forward" with the Paragon policies, including completing a medical examination and an application, before even seeing an illustration. (4/15 Trial Tr. 79:12-80:10; Trial Ex. 637.)

Mr. Howlett and Ms. Spooner did not see any illustrations for their Paragon policies until July 30, 2007. (4/15 Trial Tr. 80:6-10; 4/16 Trial Tr. 88:9-14; Trial Ex. 4.) Mr. Cooper extensively explained these illustrations to Mr. Howlett and Ms. Spooner. Among other things, he read certain statements from the illustration aloud to them, including that they understood the historical performance of the stock market should not be considered a representation of the past or future performance of the policies. (4/15 Trial Tr. 163:3-164:13; 4/16 Trial Tr. 28:12-23, 88:15-20.)

Mr. Cooper's best recollection is that during these meetings he made clear that failure to make premium payments could cause Mr. Howlett's and Ms. Spooner's policies to lapse. Additionally, as he reviewed the illustration, Mr. Cooper pointed out the possibility that the policies could lapse. (4/16 Trial Tr.

36:5-37:17, 50:2251:9, 58:4-20; Trial Ex. 30 at 30.0007-30.0008, 30.0014-30.0020.) Mr. Cooper also explained that their illustrations stated that the policies could lapse on a guaranteed basis. Mr. Cooper found it "very easy" to discuss this with his clients based on the information in the illustration. (4/16 Trial Tr. 79:7-22; Trial Ex. 30 at 30.0007-30.0008, 30.0014-30.0020.)

Mr. Howlett and Ms. Spooner expected to receive retirement income from their Paragon policies, but they knew that the amount of retirement income they would receive was not guaranteed and that this retirement income could be subject to ordinary income tax unless they kept their policies in force. (4/15 Trial Tr. 139:13-140:11; 4/16 Trial Tr. 102:23-103:16; Trial Ex. 632 at 632.0028.)

Even though their illustrations indicated, in all capital letters, that the historical performance of the S&P 500 Index should not be considered a representation of the past or future performance for any of the indexed strategies in their policies, Mr. Howlett and Ms. Spooner nevertheless assumed that the stock market would perform like it had in the past. (4/15 Trial Tr. 82:21-83:22, 84:6-18, 158:15-160:6, 163:3-18; 4/16 Trial Tr. 139:20-25, 147:4-10, 149:7-20, 180:5-181:22; Trial Exs. 4 at 4.0011; 30 at 30.0011.) In fact, LSW disclosed (and Mr. Howlett and Ms. Spooner understood) that the Current Basis B values contained in their illustration were not guaranteed, and that there was the possibility that the stock market would perform poorly in the future. They also knew that the Current Basis B values were just the best case scenario reflected in the illustration, and that the illustration included the Guaranteed Basis values that were the worst case scenario. (4/15 Trial Tr. 155:9-23; 4/16 Trial Tr. 132:10-19, 136:4-19, 138:21-139:1; Trial Ex. 4 at 4.0002, 4.0004, 4.0007, 4.0011, 4.0014-4.0020, 4.0024.) Mr. Howlett, for example, testified that, based on the documents he received from LSW and his own understanding, he knew when he applied for his Paragon policy "that the stock market was volatile, that it was not likely to return rates that were steady every year, and that as a result the results may be more or less favorable" than illustrated for his Paragon policy. (4/16 Trial Tr. 179:22-181:11.)

Mr. Cooper also suggested that Mr. Howlett and Ms. Spooner read a book called Missed Fortune 101 to familiarize themselves further with IUL products. (4/16 Trial Tr. 164:8-14.)

At the time that they applied for their policies, Mr. Howlett and Ms. Spooner were still uncertain whether to accept them. After applying, Mr. Howlett and Ms. Spooner continued to review their illustrations "extensively." (4/15 Trial Tr. 84:21-85:11; 4/16 Trial Tr. 90:4-16, 131:2-12.) At the time that they applied for their policy, Mr. Howlett and Ms. Spooner had not even considered how the guaranteed minimum accumulation under their policy would be calculated. (4/16 Trial Tr. 172:18-21.) Mr. Howlett did not decide that he wanted to purchase the LSW policy until September 2007, two months after he applied. (4/16 Trial Tr. 90:17-20, 92:12-15; Trial Ex. 633.) Ms. Spooner also decided that she wanted to purchase the LSW policy after she had applied for her policy. (4/15 Trial Tr. 85:2-15; Trial Ex. 891.)

Based on the result of their medical examinations, both Mr. Howlett and Ms. Spooner were issued policies with less favorable underwriting classes than had been depicted in their illustrations, so that the earlier sales illustrations did not represent the policy as issued (including, in particular, that the charges associated with the policy as issued were higher than reflected in the sales illustration). (4/15 Trial Tr. 114:15-18, 115:1-3; 4/16 Trial Tr. 111:11-111:17, 143:21-144:2; Trial

Exs. 4 at 4.0009 (sales illustration at Elite Non-Tobacco); 30 at 30.0009 (same); 935 at 935.0007 (policy issued at Standard Non-Tobacco); 936 at 936.0007 (same).)

Mr. Howlett's policy was also issued at a higher issue age, and with a different strategy selection, than reflected in his illustration, which also dramatically changed the various values available under his policy from the scenarios set forth in his sales illustration. (4/16 Trial Tr. 141:17-142:25, 192:17-24, 195:6-17; Trial Exs. 30.0009 (sales illustration at issue age 57 with 100 per cent allocated to Indexed Strategy 1); 31.0012 (policy issued with 50 per cent allocated to Indexed Strategy 1 and 50 per cent allocated to Indexed Strategy 2); 935.0006 (policy issued at issue age 58).)

Mr. Howlett signed for and received a copy of his policy, a batch illustration (which did not reflect any loans), a Paragon buyer's guide and a National Association of Insurance Commissioners buyer's guide on October 11, 2007. That same day, he provided Mr. Cooper with a check for his premium in the amount of $105,750. (4/16 Trial Tr. 73:19-74:2, 92:16-93:8, 107:20-108:3; Trial Exs. 31; 664; 888; Final Pretrial Conference Order at 2.) Ms. Spooner signed for and received a copy of her policy, a batch illustration (which did not reflect any loans), a Paragon buyer's guide and a National Association of Insurance Commissioners buyer's guide on October 11, 2007. That same day, she provided Mr. Cooper with a check for her premium in the amount of $59,500. (4/15 Trial Tr. 88:15-89:7; 4/16 Trial Tr. 73:19-25; Trial Exs. 625; 889; 890; Final Pretrial Conference Order at 2.) Mr. Howlett and Ms. Spooner did not read their policies, their batch illustrations, or any buyer's guides, even though the cover of their policies said they should read their policies carefully and Mr. Cooper told them to read their policies and ask any questions they may have. (4/15 Trial Tr. 89:2-15, 151:1-24, 170:18-171:5, 177:8-25; 4/16 Trial Tr. 32:13-24, 93:917; Trial Exs. 935 at 935.0004; 936 at 936.0004.)

Correspondence with friends and independent advisors confirm that Mr. Howlett and Ms. Spooner became unable or unwilling to make any further premium payments for their policies. (4/15 Trial Tr. 191:5-193:9, 194:21-195:4; Trial Exs. 644; 649; 665; 941.)

Triggered by these economic difficulties, Mr. Howlett and Ms. Spooner reached out to Steve Burgess of the Center for Life Insurance Disputes, seeking his assistance to get their premiums back. (4/15 Trial Tr. 103:15-104:5; 4/16 Trial Tr. 101:19-102:1.) In December 2009, Mr. Burgess prepared, and Plaintiffs carefully reviewed and edited, a complaint letter that was sent to LSW alleging certain misrepresentations being made by Mr. Cooper. (4/16 Trial Tr. 101:22-102:16, 103:25-104:2, 120:4-121:13, 124:4-22.)

Mr. Howlett and Ms. Spooner both admit that this complaint contained numerous false statements, "overstatements," and "exaggerations" that Mr. Cooper had "promised" or "guaranteed" that the policies would perform in a manner consistent with Current Basis B. Mr. Howlett and Ms. Spooner knew these to be untrue statements. (4/15 Trial Tr. 105:13-23; 4/16 Trial Tr. 102:23-103:16, 123:13-23, 124:4-22.) This complaint letter to LSW did not raise any of the claims that Plaintiffs have brought in this case. (4/15 Trial Tr. 106:16-20, 107:3-108:12, 109:21-24, 118:14-17, 119:4-6, 207:2-24.) LSW declined to refund Mr. Howlett and Ms. Spooner's premiums. (4/15 Trial Tr. 108:13-15; 4/16 Trial Tr. 104:3-4.)

Ms. Spooner surrendered her policy on June 1, 2010. Upon surrender, she received $4,813.17. Ms. Spooner had not taken any loans on her policy and did not pay any taxes upon surrender. (4/15 Trial Tr. 138:19-24; Trial Ex. 85; Final Pretrial Conference Order at 2.) Mr. Howlett's policy lapsed as of December 30, 2010, more than three years after it was issued. He had not taken any loans on his policy and did not pay any taxes upon lapse. (4/15 Trial Tr. 138:19-24; 4/16 Trial Tr. 116:21-22; Trial Ex. 89; 896 at 896.0009.) Mr. Howlett and Ms. Spooner each made only one premium payment out of the four that were reflected in their sales illustrations. This is why their policies lapsed. (4/15 Trial Tr. 119:16-18, 153:22-24; 4/16 Trial Tr. 166:16-167:16; Trial Exs. 4 at 4.0014; 30 at 30.0014.)

III. PLAINTIFFS' THEORIES OF LIABILITY

A. VOLATILITY CLAIM

Plaintiffs' volatility claim alleges that "LSW knew and concealed from policyholders the fact that [Provider and Paragon policies are] subject to a high probability of lapse . . . before the death of the insured." (Final Pretrial Conference Order at 3.)

B. TAX CLAIM

Plaintiffs' tax claim follows from their volatility claim. They allege that LSW failed to disclose the probability that a policy will lapse, and therefore that any outstanding loans above basis would be taxed as ordinary income. Therefore, all of the Court's findings with respect to the volatility claim apply with equal force to their tax claim. (4/9 Trial Tr. 28:12-21 (Plaintiffs' counsel in opening stating that the tax defect "is related to the volatility defect); 4/10 Trial Tr. 33:25-34:19.) Specifically, the so-called tax defect depends upon the assumption that an illustration "tells" policyholders that they will "have planned withdrawals and income that come out as tax-free income," that they will "get a death benefit," and that there "is no tax liability because the policy stays in force in the illustration" when what "actually happens" is that there is a probability of lapse. (4/10 Trial Tr. 70:20-71:13.)

C. NONDISCLOSURE OF FEES CLAIM

Plaintiffs' first individual claim asserts that they were misled because their illustration did not disclose the charges associated with their policies. (4/15 Trial Tr. 112:21-25; 4/16 Trial Tr. 109:16-20; 4/17 Trial Tr. 33:19-22; Final Pretrial Conference Order at 5.)

D. GUARANTEED MINIMUM INTEREST CLAIM

Plaintiffs' second individual claim asserts that they were misled because their illustration did not disclose that the annual floor on indexed credits for Provider and Paragon was zero percent (with retrospective guaranteed growth), rather than an annual floor of 2-2.5 per cent. (4/15 Trial Tr. 118:18-119:3; 4/16 Trial Tr. 115:17-116:4; 4/17 Trial Tr. 37:23-38:6.)

E. MONTHLY ADMINISTRATIVE CHARGE CLAIM

Finally, Plaintiffs claim that they were misled into believing that the reduction in the Monthly Administrative Charge set forth in their illustrations was guaranteed when, in fact, the reduction is not guaranteed. (4/15 Trial Tr. 117:20-118:7; 4/16 Trial Tr. 114:25-115:13; 4/17 Trial Tr. 36:25-37:18; Final Pretrial Conference Order at 5.)

IV. CONCLUSIONS OF LAW

A. JURISDICTION

This Court has jurisdiction over this action pursuant to 28 U.S.C. § 1332(a). The required diversity under 28 U.S.C. § 1332(a)(1) exists because LSW is a citizen of Texas,[1] and Plaintiffs are citizens of California. Additionally, because two of the three Plaintiffs made premium payments in excess of $100,000, the amount in controversy exceeds $75,000, exclusive of interests and costs.

The Court also has supplemental jurisdiction over the remaining Plaintiff, Ms. Spooner, under 28 U.S.C. § 1367 regardless of whether she independently satisfies the amount in controversy requirement. See Exxon Mobil Corp. v. Allapattah Servs., Inc., 545 U.S. 546, 566-67 (2005) (supplemental jurisdiction over plaintiff who does not meet amount in controversy requirement proper if other plaintiffs in case do satisfy amount in controversy requirement).

This Court also has jurisdiction over this action pursuant to 28 U.S.C. § 1332(d). This case has been certified as a "class action," with a class of approximately 46,000 members, within the meaning of § 1332(d)(1)(B). The exclusions of 28 U.S.C. § 1332(d)(5)(A) do not apply, and there is more than $5,000,000 in controversy in the aggregate across all class members. 28 U.S.C. § 1332(d)(6).

The requisite "minimum diversity" of citizenship exists under 28 U.S.C. §§ 1332(d)(2) and (d)(7). Plaintiffs, all citizens of California, represent a class of

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[1] Texas is LSW's state of incorporation and its principal place of business. See 28 U.S.C. § 1332(c)(1) (a corporation is deemed a citizen of the state in which it was incorporated and the state in which it has its principal place of business).

LSW policyholders who are also citizens of California. As noted, Defendant LSW is a citizen of Texas. Thus, LSW is a citizen of a state different from at least one putative class member (and indeed is a citizen of a state different from all putative class members), and the requisite diversity exists under 28 U.S.C. § 1332(d)(2)(A).

B. <u>CLASS CLAIMS (VOLATILITYAND TAX)</u>

Plaintiffs' claims involve violation of the fraudulent, unlawful and unfair prongs of the UCL. Plaintiffs bear the burden of proving their claims, and must do so by the preponderance of the evidence. <u>People v. First Fed. Credit Corp.</u>, 104 Cal. App. 4th 721, 732 (2002).

1. <u>Class-Wide Proof</u>

To prevail on the class claims, Plaintiffs must prove liability as to each class member with "common proof that allows a fact-finder to make a class-wide determination." <u>Marlo v. United Parcel Serv., Inc.</u>, 251 F.R.D. 476, 484 (C.D. Cal.) (aff'd 639 F.3d 942 (9th Cir. 2011)); <u>Wal-Mart Stores, Inc. v. Dukes</u>, 131 S. Ct. 2541, 2552 n.6 (2011) (plaintiffs "surely have to prove [class-wide liability] at trial in order to make out their case on the merits"). It is not enough to "bring[] a claim on a class-wide basis that raises individualized issues, but fail[] to provide common proof that would have allowed a jury to determine those issues on a class-wide basis." <u>Marlo</u>, 251 F.R.D. at 485. Instead, even if liability as to the named Plaintiffs was established, there must be "common evidence to support extrapolation from individual experiences to a class-wide judgment that is not merely speculative." <u>Id.</u> at 486.

Plaintiffs allege, on behalf of the "Pure Omissions" class, that LSW violated the UCL by failing to disclose what they term to be a "defect" in Provider and

Paragon — the risk of policy lapse or reduced value due to the impact of stock market volatility on policy values and the tax consequences of lapse. Plaintiffs' trial theory revolves around the proposition that class members are not warned that the receipt of non-guaranteed Current Basis B values shown on illustrations is unlikely as a result of volatility. (See 4/9 Trial Tr. 16:18-17:11 (Plaintiffs' counsel stating in opening that "illustrations were not depicting reality because they did not account for volatility" and policies had "a very substantial risk of expiring, lapsing, if the plaintiffs tried to use them for retirement income as was illustrated.").) However, despite this well-developed theory, Plaintiffs failed to support this theory with class-wide evidence.

At the outset, the Court notes that the evidence introduced at trial does not show the type of uniformity in the sales process that might lend itself to a class-wide finding of a failure to disclose. As discussed, the policies are sold by independent life insurance agents, who can sell from different insurers and who, although trained by LSW regarding the features of the Provider and Paragon policies, nevertheless remain free to decide the best format for their sales presentations. Moreover, as noted, the policies are sold to consumers for a variety of different types of benefits, including the insurance protection, the premium flexibility, the cash value accumulation, the retirement income potential, and the potential tax benefits. Indeed, evidence presented at trial reveals that IUL policies in general, and the Provider and Paragon policies specifically, are often merely a part of a the more complex financial plan that varies for each policyholder. Plaintiffs offered no evidence that the individualized sales methods of thousands of independent agents to policyholders with varying financial needs and plans could have resulted in the type of across-the-board non-disclosures that could support a their class claims here. This failure alone is fatal to Plaintiffs' class claims.

Reasons related to the opinions of Plaintiffs' expert, Dr. Brockett, also support a finding in favor of LSW as to Plaintiffs' class claims. Significantly, Dr. Brockett's opinion regarding relative risk of lapse or relative value of the Paragon and Provider policies lack any point of comparison. Dr. Brockett offered an opinion regarding risk of lapse and relative value of Paragon and Provider policies, but he did not offer any testimony about the lapse rates or reduced policy values of any other insurance policies. Dr. Brockett's opinions regarding the risk of lapse or reduced value are instead based on a so-called Monte Carlo model he developed to simulate future stock market performance using a distribution with the same average as the historical average of the S&P 500 index. (4/10 Trial Tr. 6:4-16:25, 22:5-15.) Without a point of comparison, his opinions regarding relative risk of lapse or value of the Paragon and Provider policies are not "based on sufficient facts or data." See Fed. R. Evid. 702(b). Thus, they are inadmissible. Moreover, in the absence of such a point of comparison, the opinion, even if admissible, would be of no probative value. Thus, Dr. Brockett's opinion about whether these risks of lapse or reduced value for the Paragon or Provider policies are "high," "low," or otherwise does not constitute class-wide proof of the volatility or tax defect.

Moreover, Dr. Brockett's analysis of a sample of the policies still shows that in some cases the expected value was greater than the non-guaranteed Current Basis B values; thus, it cannot constitute class-wide proof of volatility or tax defect. Specifically, Dr. Brockett calculated the risk of a lower expected value than what he calculated as the non-guaranteed, highest illustrated rate using a sample of 140 Provider policies and 140 Paragon policies where the files included a sales illustration. He calculated for each the expected value of cash flows for the policy "as illustrated" under Current Basis B. He then compared this value "as illustrated" to the expected value of cash flows for the policy as it performed under his simulations holding loan amounts and timing, participation rates, earnings caps, and other features constant. Dr. Brockett concluded that in 90-95% of cases, the expected value of Provider and Paragon policies were below the expected value illustrated under non-guaranteed Current Basis B. (4/9 Trial Tr. 143:20-144:14, 182:3-12, 183:5-11; 4/10 Trial Tr. 13:4-24, 37:6-23; Trial Ex. 565-58.) Thus, in 5%-10% of cases, Dr. Brockett found that the expected value of the policy was in fact better than what was illustrated under non-guaranteed Current Basis B — that is, S&P volatility actually increased policy value.

Even if that were not the case, Plaintiffs failed to establish that Dr. Brockett's analysis of the sample can be extrapolated to the class as whole. In the first instance, the sample itself included only policies with sales illustrations, and the class includes a significant percentage of policyholders who did not receive sales illustrations. Thus, the sample is not fairly representative of the class as a whole. (<u>But see</u> 4/10 Trial Tr. 111:21-112:8 (testimony from Dr. Brockett that the results of his analysis could be extrapolated to the class as a whole).) Additionally, the sample Dr. Brockett used for analyzing the likelihood of lapse was further limited in that Dr. Brockett selected a 105-policy subset of the sample with sales illustrations that had loans above a selected amount illustrated. (4/10 Trial Tr. 27:4-21, 29:7-11.) There is no evidence that this 105-policy sub-sample is capable of being extrapolated to the entire class (or even some discernable subset of the class) to a reasonable degree of statistical certainty.

There are further problems with Dr. Brockett's analysis. First, Dr. Brockett's analysis ignored all Current Basis A values. Thus, he does not know what he would have learned had he conducted an analysis of future performance by comparison with Current Basis A. (4/10 Trial Tr. 171:17-23, 189:12-190:2, 190:21-191:20.) Because the Current Basis A values are lower than Current Basis B values, had Dr. Brockett compared his estimate of future performance against Current Basis A, his conclusion that the policy was worth less than illustrated would be undermined.

Next, Dr. Brockett's calculation of expected value of the policy as illustrated assumed that policyholders developed their subjective expectations by assigning a 100% weight to the probability of getting non-guaranteed Current Basis B. But Plaintiffs presented no evidence that Dr. Brockett analyzed how likely any class member expected to achieve Current Basis B, as compared to Current Basis A, Guaranteed values, or any other values. For instance, when questioned, he testified that he had no knowledge of any of the named Plaintiffs' expectations regarding whether the Current Basis A or Current Basis B was more likely. (4/10 Trial Tr. 176:14-178:11.) Dr. Brockett asserted that prospective policyholders focus on Current Basis B values because that scenario is based on the historical performance of the S&P 500 index; thus, in his view, if a policyholder wants to know how the policy will perform if the S&P 500 Index performs on average in the future as in the past, they will focus on Current Basis B. (4/11 Trial Tr. 193:15-25.) However, there is no evidence to support such an assumption, and such an assumption by a policyholder would not be reasonable in light of the disclaimer found in the illustrations that historical S&P 500 performance cannot be assumed to be an indicator of future performance.

Finally, in analyzing the data regarding increased lapse rate, Dr. Brockett admitted on cross-examination that he arbitrarily omitted much-lower lapse rates in later years. Specifically, on direct, Dr. Brockett testified that he analyzed the Provider and Paragon lapse rates during the first four policy years only. (4/10 Trial Tr. 71:14-73:17.) On cross, he revealed that he had also calculated lapse rates for beyond the fourth policy year, and that the lapse rate in later years was "much lower" than in the first four years. (4/11 Trial Tr. 10:11-15:3.) On re-direct, Dr. Brockett attributed this omission to the untrustworthiness of the data. (4/11 Trial Tr. 168:3-170:4.) On re-cross, Dr. Brockett acknowledged that his testimony about the uncertainty of the later years was "certainly misleading." He admitted that these much-lower later year lapse rates were not untrustworthy, uncertain, or shaky, and were in fact "reliable" and "based on large samples." (4/15 Trial Tr. 62:12-65:22.) This concession not only detracts from the probative value of Dr. Brockett's opinion regarding a class-wide volatility defect, it also considerably undermines Dr. Brockett's overall credibility. The Court therefore concludes that Plaintiffs have offered no reliable or valid statistical evidence to establish that Paragon and Provider policies purchased by the class are prone to lapse.

In sum, in order to prevail on behalf of the class on this theory, Plaintiffs were required to prove at trial that there was a particular disclosure or disclosures about the policies that LSW was required to make, but that LSW uniformly failed to make to every class member. The Court has previously discussed the difficulty of proving a negative; however, that difficulty does not lessen Plaintiffs' burden of supporting their claim with evidence that is applicable to all class members. As set forth herein, Plaintiffs have failed to meet their burden to show the volatility defect on a class-wide basis. Because the tax defect theory is dependent upon the volatility defect theory, Plaintiffs have also failed to meet their burden to show the tax defect on a class-wide basis.

Additionally, Plaintiffs' class claims fail for other reasons that are explained more fully in the subsections that follow.

2. UCL Fraud Claim

Under the fraudulent prong of the UCL, Plaintiffs must prove that LSW had a duty to disclose the allegedly omitted fact. (Class Cert. Order at 21); Gray v. Toyota Motor Sales, U.S.A., No. 08-1690 PSG (JCx), 2012 WL 313703, at *3 (C.D. Cal. Jan. 23, 2012) (UCL claim must include a duty to disclose "because a failure to disclose a fact one has no affirmative duty to disclose is not 'likely to deceive' anyone within the meaning of the UCL") (internal quotation marks and citation omitted); Daugherty v. Am. Honda Motor Co., 144 Cal. App. 4th 824, 838 (2006) (same); Berryman v. Merit Prop. Mgmt., Inc., 152 Cal. App. 4th 1544, 1557 (2007) (same). Plaintiffs must also prove consumer expectations in order to establish that allegedly omitted information — assuming it was in fact omitted — was contrary to those expectations. Daugherty, 144 Cal. App. 4th at 838.

Plaintiffs must prove by a preponderance of the evidence that LSW made an omission that was likely to mislead the public. See In re Tobacco II Cases, 46 Cal. 4th 298, 328 (2009) (elements of knowledge, justifiable reliance, and resulting damages not applicable to UCL fraud claims); Berger v. Home Depot USA, Inc., 741 F.3d 1061, 1068 (9th Cir. 2014) (applying In re Tobacco II and noting that "[a]ctual falsehood, the perpetrator's knowledge of falsity, and perhaps most importantly, the victim's reliance on the false statements — each of which are elements of common-law fraud claims — are not required to show a violation of California's UCL"); In re Google Android Consumer Privacy Litig., No. 11-MD-02264 JSW, 2014 WL 988889, at *6 (N.D. Cal. Mar. 10, 2014) (same).

In the present case, the Court must determine whether Plaintiffs have proven each of these elements on a class-wide basis. A failure to prove any one of these elements on a class-wide basis will result in a failure to meet their burden of proof and will require judgment in favor of LSW as to Plaintiffs' UCL fraud claim.

As noted to previously, Plaintiffs have the difficult burden of proving a negative. (Docket No. 478 at 6-7.) Specifically, the Court previously observed that to do so, Plaintiffs had to identify required disclosures and show that those disclosures were not made in any communication between LSW and its policyholders. (Id.) Plaintiffs have identified two disclosures that it contends should have been made, but were not:

> [T]he values shown in current basis B assume a constant rate of return for the index strategies. Because actual returns to the S&P 500 will be volatile, not constant, the current basis B values may understate the level of risk inherent in this product even if the S&P 500 performs in the future at the same average rate as is used in calculating the current basis b values.

(Ptlfs.' Prop'd FOF (Docket No. 785) ¶ 561.)

> The values shown in current basis B assume a constant rate of return for the indexed strategies because actual returns to the S&P 500 will be volatile, not constant. The current basis B values may be overstated even if the S&P 500 performs in the future at the same rate on average as is used in calculating the current basis B values.

(Id. ¶ 563.)

This Court's analysis therefore considers whether LSW had a duty to disclose, whether an omission was contrary to consumer expectations, and whether the omission identified by Plaintiffs was likely to mislead in light of LSW's extensive disclosures.

a. Duty to Disclose

LSW cannot be held liable for non-disclosure in the absence of any duty to disclose. (Class Cert. Order at 21); Gray, 2012 WL 313703 at *3 (UCL claim must include a duty to disclose "because a failure to disclose a fact one has no affirmative duty to disclose is not 'likely to deceive' anyone within the meaning of the UCL"); Berryman, 152 Cal. App. 4th at 1557 (same); Daugherty, 144 Cal. App. 4th at 838 (same).

There is no duty to disclose information when the desired disclosure is prohibited by law. See, e.g., Bassidji v. Goe, 413 F.3d 928, 936 (9th Cir. 2005) ("federal law and California law begin from the core proposition that" a court will not direct a party "to perform an act that is in direct violation of a positive law directive"); Loeffler v. Target Corp., 58 Cal. 4th 1081, 1126 (2014) ("The UCL cannot properly be interpreted to impose on retailers a duty with respect to sales tax that is contradicted by the statutory scheme governing the sales tax"); In re Marriage of Reuling, 23 Cal. App. 4th 1428, 1436 (1994) (refusing to compel "disclosures" of insider information in divorce proceedings because the "state cannot impose obligations on parties which require them to violate" the law).

Before the Court discusses the substance of Plaintiffs' proposed disclosures, the Court considers whether LSW could have made those or similar disclosures through its use of illustrations. LSW was under no duty to disclose any risks unique to S&P volatility by use of an illustration. This is because depicting S&P volatility based on historical performance would require assumption of a rate during some years that would exceed the maximum policy rate, an assumption that may not appear in an illustration governed by California law. (See 4/18 Trial Tr. 50:13-54:20.) Specifically, California insurance law prohibit insurers from illustrating any non-guaranteed elements that are "based on a scale more favorable to the policy owner than the insurers' illustrated scale at any duration." Cal. Ins. Code § 10509.956(a)(7). Similarly, insurers are prohibited from using "an illustration that at any policy duration depicts policy performance more favorable to the policy owner than that produced by the illustrated scale of the insurer whose policy is being illustrated." Cal. Ins. Code § 10509.955(b)(5). Thus, LSW is prohibited from producing an illustration that assumes, for "any duration," a rate of return that exceeds the policy maximum rate of return.

Thus, LSW was under no duty to use its illustrations to depict the possible effects of S&P 500 Index volatility.

b. No Class-Wide Consumer Expectations

Plaintiffs must prove consumer expectations in order to establish that allegedly omitted information — assuming it was, in fact, omitted — was contrary to those expectations. This is because an alleged omission cannot be actionable unless "members of the public . . . had an expectation or an assumption about the matter in question." Daugherty, 144 Cal. App. 4th at 838; Bardin v. Daimlerchrysler Corp., 136 Cal. App. 4th 1255, 1275 (2006) (same); In re Sony Grand Wega KDF-E A10/A20 Series Rear Projection HDTV Telev. Litig., 758 F. Supp. 2d 1077, 1089 (S.D. Cal. 2010) (same); Martinez v. Welk Group, Inc., 907 F. Supp. 2d 1123, 1140 (S.D. Cal. 2012) (same); Hodges v. Apple Inc., No. 13-CV-01128-WHO, 2013 WL 6698762, at *9 (N.D. Cal. Dec. 19, 2013) (same); Morgan v. Harmonix Music Sys., Inc., No. C08-5211 BZ, 2009 WL 2031765, at *5 (N.D. Cal. July 30, 2009). Anecdotal evidence may in some instances suffice to prove class-wide expectations, but a named plaintiff's "personal experience," "personal assumptions" and "personal expectations" are insufficient to establish consumer expectations on a class-wide basis. Clemens v. DaimlerChrysler Corp., 534 F.3d 1017, 1026 (9th Cir. 2008).

Only omissions that are inconsistent with specific and particularized expectations support a UCL claim. For instance, in Daugherty, 144 Cal. App. 4th at 838, the court upheld the dismissal of a UCL claim where the defendant did not disclose that after the expiration of a vehicle warranty, an oil seal in the engine could dislodge and create an oil leak. Similarly, in Bardin, 136 Cal. App. at 1275, the court upheld a dismissal of a UCL claim where plaintiffs failed to allege that the public made any particular assumptions about the specific materials used to manufacture the exhaust manifold on a vehicle. In Clemens, 534 F.3d at 1026, the court affirmed judgment in favor of defendant on UCL claim where plaintiff "produced no evidence to suggest that a reasonably consumer would have expected or assumed any particular head gasket lifespan." In Berenblat v. Apple, Inc., No. 08-4969 JF (PVT), 2010 WL 1460297, at *9 (N.D. Cal. Apr. 9, 2010), the court found no UCL claim was stated because general statements about memory upgrades did not give rise to an expectation or assumption about the functionality of memory slots. In Martinez, 907 F. Supp. 2d at 1141, the court found that general statements of hotel cleanliness and safety insufficient to support a UCL claim absent "evidence to suggest that a reasonable consumer would have expected or assumed that the entire Resort was, and has always been, free of any mold, mildew, or water intrusion."

Here, Plaintiffs failed to present evidence to establish the specific and particularized expectations of consumers regarding S&P performance on policy value or the risk of policy lapse sufficient to support a UCL claim. Plaintiffs did not present any survey or other evidence from the class or its agents. And Dr. Brockett testified that he could not opine on the expectations of class members. (4/10 Trial Tr. 178:5-11.) Dr. Brockett further testified that, in order even to attempt to ascertain class members' expectations, he would need to gather information from each one (e.g., a survey or interview), and that he did not do so. (4/11 Trial Tr. 81:11-18, 90:14-92:18, 103:8-19.)

Moreover, as set forth below, even if consumers held such specific and particularized expectations, those expectations would not be reasonable in light of LSW's other disclosures.

c. Other Disclosures Inform Policyholder

Most fundamentally, Plaintiffs' volatility claim fails because they have not proven that consumers are likely to be misled in light of LSW's existing disclosures that the depicted Current Basis B values were not likely, could be higher or lower, and were not intended to be a representation of the values that could be expected under the policies.

"Under the reasonable consumer standard, plaintiff is required to show not simply that the defendants' [statements] *could* mislead the public, but that they were *likely* to mislead the public." Haskell v. Time, Inc., 965 F.Supp. 1398, 1406-07 (E.D. Cal. 1997) (emphasis in original). "'Likely to deceive' implies more than a mere possibility that the [statement] might conceivably be misunderstood by some few consumers viewing it in an unreasonable manner. Rather, the phrase indicates that the [statement] is such that it is probable that a significant portion of the consuming public or of targeted consumers, acting reasonably under the circumstances, could be misled." Lavie v. Proctor & Gamble Co., 105 Cal. App. 4th 496, 508 (2003). In order to prove a likelihood of misleading consumers, Plaintiffs must provide more than "a few isolated examples of actual deception," and must prove "a likelihood of confounding an appreciable number of reasonably prudent purchasers exercising ordinary care." Clemens, 534 F.3d at 1026 (internal quotation marks and citation omitted); see also Martinez, 907 F. Supp. 2d at 1140 (same).

Plaintiffs have not proven that a significant portion of the consuming public, acting reasonably, are likely to be misled, particularly in light of LSW's extensive warnings of the risk that policyholders would not attain non-guaranteed Current

Basis B. Where a policyholder received allegedly omitted information, "there is absolutely no likelihood that they were deceived by the alleged false or misleading statements." Pfizer v. Superior Ct., 182 Cal. App. 4th 622, 632 (2010).

At their delivery, the policies at issue are accompanied by a batch illustration that by its terms controls over any previous sales illustrations provided to a policyholder. These illustrations contain disclosures that, taken together, are sufficient to inform the policyholder regarding the risks inherent in relying the Current Basis B values as illustrated. Specifically, the batch illustrations state:

> This illustration assumes that the currently illustrated non-guaranteed elements will continue unchanged for all years shown. This is not likely to occur and actual results may be more or less favorable than those shown.

(Trial Exs. 4 at 4.0004; 30 at 30.0004; 48 at 48.0004; emphasis supplied.)

> The illustrated assumed interest rates cannot exceed the maximum illustration rates allowed by the company, as shown above. The maximum illustration rates are based on applying the current cap rates and participation rates to the S&P 500® Index historical performance from 1984 through 2006. The historical performance of the S&P 500® Index should not be considered a representation of past or future performance for any of the Indexed Strategies available in this policy, nor is it an estimate of the returns that a policyholder can

> expect based on the current caps and participation rates. The future yield performance for any of these strategies may be less than or greater than the non-guaranteed assumed interest rates used in this illustration.

(Trial Exs. 4 at 4.0011; 30 at 30.0011; 48.0011; emphasis supplied.)

> I have received a copy of this illustration and understand that any non-guaranteed elements illustrated are subject to change and could be either higher or lower. The agent has told me they are not guaranteed. I UNDERSTAND THAT HISTORICAL PERFORMANCE OF THE S&P 500® INDEX SHOULD NOT BE CONSIDERED A REPRESENTATION OF THE PAST OR FUTURE PERFORMANCE FOR ANY OF THE INDEXED STRATEGIES.

(Trial Exs. 4 at 4.0011; 30 at 30.0011; 48.0011 (capitalization in the original).)

A comparison of Plaintiffs' proposed disclosures and the disclosures actually set forth in the batch illustrations lead the Court to conclude that no significant portion of the consuming public, acting reasonably, was likely to be misled by any omission by LSW. Specifically, in comparing the disclosures actually made and Plaintiffs' proposed disclosures, the latter represent a more specific articulation of the former.

Plaintiffs would rephrase LSW's more general disclosures to inform the policyholder that (a) the Current Basis B assumes a constant rate of return, but that

(b) but that the S&P 500 Index has historically been volatile rather than constant, and (c) should the S&P 500 Index perform in that volatile manner in the future, because (d) the Current Basis B values do not reflect any potential adverse effect of that volatility, (e) the Current Basis B values understate the level of risk inherent in the product. (See Pltfs.' Prop'd FOF ¶¶ 561, 563.) All these points are made to the policyholders by LSW's disclosures, although they are made in a more general manner.

Like Plaintiffs' proposed disclosures, LSW's disclosures (quoted above) inform the policyholder that the illustrations assume non-guaranteed elements will continue unchanged. This disclosure addresses Plaintiffs' point (a), that the Current Basis B values "assume[] a constant rate of return."

LSW's disclosures state that the constant rate of return is a circumstance that is not likely to occur. One way in which a constant rate of return may not occur is if the S&P 500 Index performance is volatile, which is consistent with its historical performance. This disclosure addresses Plaintiffs' points (b) and (c).

LSW's disclosures reference the interaction between the policy's interest rate caps and policy returns. Although these disclosures do not specifically reference S&P volatility as a factor that might limit returns, they do caution specifically against using S&P 500 Index performance as a representation of policy performance, especially in light of interest rate caps, which would have the tendency to limit returns in years the S&P 500 Index performs well. In this manner, this disclosure addresses the same point as Plaintiffs' point (d).

LSW's disclosures make the point that actual policy performance may be different than those illustrated, including being less favorable than those values shown. This disclosure is another way of making Plaintiffs' point (e), that "the Current Basis B values understate the level of risk inherent in the product."

In short, LSW's disclosures address the issues identified by Plaintiffs, although in a more general manner than Plaintiffs would have them addressed. Thus, LSW's disclosures, as given, inform the policyholders of the risk of attempting to estimate policy performance based on historical S&P 500 Index performance. As noted in the illustration language quoted above, LSW's disclosures make the repeated point that historical performance of the S&P 500 Index is not a reliable estimate of policy returns or performance. Therefore, the Court concludes that LSW's omissions are unlikely to mislead a significant portion of the consuming public or targeted consumers. Such consumers, acting in a reasonable manner, would have been informed in a general manner of the risk of estimating policy performance based on S&P 500 Index projected or historical performance.

On the record before the Court, in light of all of these disclosures, Plaintiffs have failed to offer evidence that reasonable consumers were likely to be misled into thinking that volatility could not result in policy values below what was illustrated, or that volatile or poor performance of the S&P 500 Index could not result in tax consequences.

3. <u>UCL Unlawful Claim</u>

In addition to the fraudulent prong, Plaintiffs have also asserted claims under the unlawful prong of the UCL. Under the unlawful prong of the UCL, Plaintiffs must prove by a preponderance of the evidence that: (a) LSW engaged in a practice that is prohibited by law and that may be enforced by a private right of action; and

(b) the unlawful conduct caused injury. (See MTD Order at 9-10.)

Plaintiffs have identified only one class-wide basis for their unlawfulness claim: Cal. Civ. Code § 1572, which codifies common-law fraud, and has identical elements to the claim that was tried to the jury. Nugent v. Fed. Home Loan Mortg. Corp., No. 2:12-CV-00091-GEB-EFB, 2013 WL 1326425, at *9 (E.D. Cal. Mar. 29, 2013) (setting forth elements of § 1572 claim that are identical to fraud); Maynard v. Wells Fargo Bank, N.A., No. 12CV1435 AJB (JMA), 2012 WL 4898021, at *5 n.3 (S.D. Cal. Oct. 15, 2012) (§ 1572 "essentially codifies the elements of common law fraud").

In light of the jury's verdict that LSW was not liable for common-law fraud, Plaintiffs' claim that LSW violated Cal. Civ. Code § 1572 necessarily fails as well. See Brown v. Option One Mortg. Corp., No. C 09-5705 MHP, 2010 WL 1267774, at *2 (N.D. Cal. Apr. 1, 2010) (where Plaintiff failed to establish common-law fraud, the "same deficiencies doom" their claim under § 1572); Mosarah v. SunTrust Mortg., No. 1:11-cv-01739-AWI-SKO, 2012 WL 2117166 (E.D. Cal. June 11, 2012) (dismissing § 1572 claim that was "essentially duplicative" of common law fraud claim).

Given Plaintiffs' failure to establish any violation of any underlying law, Plaintiffs' unlawfulness claim fails. Campos v. Bank of Am., Inc., No. C11-0431SBA, 2012 WL 2862603, at *7 (N.D. Cal. July 11, 2012) ("[w]here a plaintiff cannot state a claim under the 'borrowed' law, he or she cannot state a UCL claim either"); see also Ingels v. Westwood One Broad. Servs., Inc., 129 Cal. App. 4th 1050, 1060 (2005) (upholding dismissal of UCL claim based on dismissal of claim asserted under predicate statute).

4. Unfair Prong

The legal standard applied to "unfair" UCL claims is unsettled. Yanting Zhang v. Superior Court, 57 Cal. 4th 364, 380 n.9 (2013) (declining to resolve conflicting lower court opinions). A number of tests have been applied by California courts. The first test focuses on whether the challenged conduct violates a public policy that is tethered to specific constitutional, statutory or regulatory provisions. Id. (citation omitted). A second test balances the impact of the act or practice on victim against reasons, justifications and motives of the alleged wrongdoer. Id. (citation omitted). A third test applies the same balancing test of the second, but also examines whether practice offends established public policy or is immoral, unethical, oppressive, unscrupulous or substantially injurious to consumers. Id. (citation omitted). The final test is the test set forth in Cel-Tech Comm'cs, Inc. v. Los Angeles Cellular Telephone Co., 20 Cal. 4th 163, 182-83 (1999), which requires that (1) the consumer injury must be substantial; (2) the injury must not be outweighed by any countervailing benefits to consumers or competition; and (3) it must be an injury that consumers themselves could not reasonably have avoided. Zhang, 57 Cal. 4th at 380 n.9 (citation omitted).

The Court discusses a number of factors, below, and concludes that Plaintiffs have not established an unfair business practice under any of these tests.

a. Injury

Plaintiffs have not proven any class-wide injury as a result of LSW's omissions. No actual lapse has occurred in any policy when the premiums were made as indicated in the illustrations. Even employing Dr. Brockett's Monte Carlo simulations, no lapse occurred in the first ten years of any policy he examined.

To the extent that Plaintiffs contend that the increased risk of loss and the attendant reduction in present value of the policy constitute an injury, this loss is not actionable. First, this theory that the policies are worth less than they paid for them is dependent upon acceptance of their contention that there was an undisclosed risk. As noted above, the disclosures made are sufficient to warn the policyholders not to estimate policy performance based on historical S&P 500 Index performance.

Additionally, this theory does not result in an actionable injury for reasons similar to the rationale articulated in a number of cases that do not find actionable UCL injury where motor vehicle parts fail beyond the warranty period. In those cases, manufacturers guarantee the parts for a specified period of time, and courts refuse to extend obligations beyond that specified period of time. See, e.g., Clemens, 534 F.3d at 1026-27 (no UCL claim based on "any particular head gasket lifespan"); Daugherty, 144 Cal. App. 4th 824, 838-39 (2006) (no UCL claim based on malfunction of parts likely to occur after expiration of warranty); Marchante v. Sony Corp. of Am., Inc., 801 F. Supp. 2d 1013, 1018 (S.D. Cal. 2011) (same); Berenblat, 2010 WL 1460297, at *7 (same).

Similarly, here, LSW provided guaranteed values and then an estimate of possible values, including the Current Basis B value. Like the possibility that vehicle or computer parts may continue to perform long after the manufacturer's warranty has expired, so too can a policyholder achieve the policy performance depicted in the Current Basis B illustration. But those that performance is not promised, as parts are not guaranteed past their warranty date. No actionable injury results in either situation.

b. <u>Countervailing Benefits</u>

Even assuming that Plaintiffs have proven class-wide substantial injury, they have not satisfied the requirement that this injury outweighs countervailing benefits. Here, the availability of IUL products is a substantial benefit to policyholders. Many policyholders, like the named Plaintiffs in this action, purchase the policies as part of more complex financial planning strategies. In comparing the countervailing benefits of a business practice to the injury suffered by a plaintiff, the Court must examine the practice's impact on its alleged victim, "balanced against the reasons, justifications and motives of the alleged wrongdoer." <u>Zhang</u>, 57 Cal. 4th at 380 n.9 (citation omitted).

As previously noted, LSW has provided sufficient disclosures regarding the potential risks of estimating policy performance by referencing the historical S&P 500 Index performance. LSW provided an illustration reflecting the guaranteed values, and beyond this, any estimate regarding policy performance achieving the Current Basis B value was just that — an estimate. It was labeled as such, and ample warning regarding the risks of not achieving these values were given. Also as noted above, LSW could not provide illustrations advocated by Plaintiffs that include the Monte Carlo simulations that might otherwise flesh out potential risks uniquely related to S&P volatility. These actions demonstrate that LSW took steps to conform its policies, illustrations, and disclosures with California insurance law and to inform the policyholder not to consider historical S&P performance in estimating policy returns. <u>See, e.g.</u>, <u>McMahon v. Take-Two Interactive Software, Inc.</u>, No. EDCV 13-02032-VAP (SPx), 2014 WL 324008, at *11 (C.D. Cal. Jan. 29, 2014) (general disclaimer that online feature of video game might not be available precluded UCL unfair claim notwithstanding fact that defendant could have taken further steps to notify consumers and provide more specific information); Fabozzi v. Stubhub Inc., No. C-11-4385 EMC, 2012 WL 506330, at *8 (N.D. Cal. Feb. 15, 2012) ("repeated disclosures . . . further undermine" an unfairness claim).

The evidence does not show that LSW acted with anything other than good faith in its dealings with consumers. (E.g., 4/18 Trial Tr. 48:17-23.) The uncontroverted testimony is that LSW believed that its illustrations and other disclosures complied with California law. (4/18 Trial Tr. 144:24-145:16.) In fact, Ms. MacGowan testified to her belief that LSW was actually forbidden from including any information in an illustration that was "based on" volatility in the S&P 500 Index. (4/18 Trial Tr. 51:25-54:23.) The evidence instead reveals that LSW's motive in formulating its disclosures was to comply with the illustration regulation while making substantial disclosures about the risks associated with Provider and Paragon (like any other indexed life insurance policy).

c. Avoidance of Injury

Even assuming that Plaintiffs proved substantial injury, the evidence established that Plaintiffs and other policyholders could have avoided any such injury. For example, the evidence is undisputed that no policy has lapsed where the policyholders have paid their illustrated premiums. Moreover, policyholders could reduce the amount or frequency of any planned loans in the event of poor S&P 500 Index performance. The loans from these policies are part of a larger financial strategy, and the need to adjust this strategy in light of market performance should be unsurprising.

They could allocate cash value to the fixed strategy in their policy. They could repay loans before policy lapse. Each of these would substantially reduce or eliminate the risk of injury identified by the Plaintiffs. Cf. Camacho v. Auto. Club of S. Calif., 142 Cal. App. 4th 1394, 1406 (2006) (no unfairness where consumer could have reasonably avoided injury by purchasing and paying for insurance as required by law); Fabozzi, 2012 WL 506330, at *7 (no unfairness claim where consumers voluntarily paid above face-value prices for resold tickets).

Furthermore, Plaintiffs and other policyholders could have cancelled their policies within the first ten days after delivery. This period of time gave them the opportunity to fully review the materials LSW provided them (including their policy contracts, illustrations, and Buyer's Guides) and to consult with financial advisors.

d. Public Policy

If Plaintiffs must establish that the unfairness they allege is tethered to a legislatively-declared public policy, they have not done so. Plaintiffs' claims that LSW violated statutes prohibiting fraud were rejected by the jury.

5. Conclusion Regarding Class Claims

As set forth above, Plaintiffs failed to establish class-wide violations of the fraudulent, unlawful or unfair prong of the UCL.

C. INDIVIDUAL CLAIMS

The named Plaintiffs maintain that they were misled because their illustrations did not adequately disclose three items. First, they contend that LSW failed to fully itemize the charges associated with their policies. Second, they contend that LSW did not explain the method by which guaranteed values are calculated and interest is applied. Finally, Plaintiffs contend that LSW did not disclose the non-guaranteed nature of the eleventh-year reduction in the policies' Monthly Administrative Charge.

As was the case with the class claims, the jury verdict precludes a finding in favor of the named Plaintiffs as to the UCL claim under the unlawful prong. Therefore the Court discusses below the named Plaintiffs' UCL claim asserted under the fraud and unfair prongs of the UCL. The first two items are subject to the same analysis and are therefore discussed together.

1. UCL Claims Based on Policy Fees and Charges and Interest Accumulation

a. UCL Fraud Claim

In light of the disclosures regarding the policy fees and charges in the relevant policies, the Court does not find that the failure to itemize the various fees charges as separate line items on the illustrations was likely to deceive a significant portion of the targeted consumers. Similarly, because the manner in which interest is calculated and credited to the policies is likewise disclosed in the policies,[2] the Court does not find any omission by LSW on this issue to be likely to deceive.

The evidence before the Court is that the named Plaintiffs consulted financial planners and otherwise took great care in making the decisions to

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[2] Specifically, the Provider policy guaranteed two percent per annum return as determined and credited each five-year period. (4/18 Trial Tr. 94:14-95:7; Trial Exs. 86 at 86.0004-86.0005; 934 at 934.0030-934.003l.) The Paragon policy guaranteed a two-and-a-half percent per annum determined and credited upon surrender or the insured's death. (4/18 Trial Tr. 94:14-95:7; Trial Exs. 804 at 804.0007; 935 at 935.0030.)

purchase their policies. Although by illustrating the charges as separate line items, LSW could have highlighted those fees and charges more prominently, LSW's witness also testified as to the benefits of showing projected policy values net of those fees to allow for comparison with other policies. (4/18 Trial Tr. 98:24-99:16, 128:23-130:8.) Moreover, whether the fees are "high" or not, they are disclosed in policyholders' policy contracts, and reflected in all values shown in any illustration. (4/18 Trial Tr. 129:6-132:2; 4/23 Trial Tr. 100:2-102:6; e.g., Trial Ex. 49 at 49.0012; Trial Ex. 935 at 935.0007-935.0010, 935.0031-935.0032.) Because the evidence reveals that the categories of fees charged by LSW are common among IUL products, the Court cannot conclude that the charges are inconsistent with specific and particularized expectations of the targeted consumers.

As to the interest calculation, the sales illustrations provided to the named Plaintiffs show that the annual growth to policy value is subject to a zero per cent floor. (Exs. 4 at 4.0010, 30 at 30.0010, 48 at 48.0011.) The policies explain how guaranteed accumulation is calculated and credited. (Trial Exs. 934 at 934.0030; 935 at 935.0030; 936 at 936.0030.) The Buyer's Guides provide explanations as well. (Trial Exs. 86 at 86.0003-86.0005, 804 at 804.0001.) Therefore, the Court makes the same conclusion regarding interest accumulation as well.

Accordingly, the Court finds in favor of LSW as to the named Plaintiff's UCL fraud claim based on policy fees and charges and guaranteed interest accumulation.

b. <u>UCL Unfair Claim</u>

The balancing factors considered in UCL unfair claims weigh in favor of finding no liability. Certainly, the named Plaintiffs had fees and charges assessed to their policies, which decreased policy value. For instance, in Plaintiff Walker's case, those fees amounted to approximately $20,000 in 2008. Although this amount is substantial, those fees were disclosed to her when her policy was delivered, at a time when she still had a 10-day period of time in which to cancel her policy without penalty. Fees incurred by the other named Plaintiffs were also disclosed in this manner.

A similar point can be made regarding the time at which guaranteed interest is credited to policy value. The named Plaintiffs' sales illustrations disclosed that annual growth was subject to a zero per cent floor. The manner and time the guaranteed returns of 2 per cent or 2.5 per cent were to be credited to policy value were more fully described in the policies themselves.

The countervailing benefits of the IUL products (identified in the previous section in connection with the class claims) are equally applicable to the named Plaintiffs' claims. Additionally, similar to the Court's observation regarding LSW's specific choice of what disclosures to provide regarding policyholder reliance on the S&P 500 Index as an indicator of policy performance (discussed above), the Court likewise discerns no bad faith in LSW's decision to illustrate policy performance net of fees rather than to illustrate those fees as separate line items in all instances. The same is true regarding LSW's decision to disclose in the sales illustrations the zero percent floor of annual growth.

In any event, even if these countervailing benefits did not outweigh any injury, the evidence establishes that the named Plaintiffs could have avoided any injury by cancelling their policies within the first ten days after delivery. As with the class claims, this period of time gave them the opportunity to fully review the materials LSW provided them (including their policy contracts, illustrations, and Buyer's Guides) and to consult with financial advisors.

Moreover, as was the case with the class claims, if Plaintiffs must establish that the unfairness they allege is tethered to a legislatively-declared public policy, they have not done so. Plaintiffs' claims that LSW violated statutes prohibiting fraud were rejected by the jury.

2. Eleventh-Year Reduction in Fees

Plaintiffs' final theory places at issue LSW's illustration of the eleventh-year reduction in the Monthly Administrative Charge when the policy does not itself guarantee such a reduction.

a. UCL Fraud Claim

The Court cannot conclude that this action is likely to deceive the public. Plaintiffs did not establish that the illustration eliminating the eleventh-year Monthly Administrative Charge depicted the elimination as a "guaranteed value," and as a general matter, the illustrations' clear disclaimer provides that the only items that are guaranteed are those clearly labeled as such.

Moreover, no named Plaintiff kept his or her policy in force more than ten years; thus, no named Plaintiff was denied the reduction in the Monthly Administrative Charge. Indeed, at the time of trial, no Paragon or Provider Policy had been in force more than ten years. Nevertheless, the evidence at trial established that LSW intends to and has taken steps in preparation to extend the illustrated reduction in the Monthly Administrative Charge.

b. UCL Unfair Claim

The balancing factors considered in UCL unfair claims weigh in favor of finding no liability. As noted above, there was no harm to any named Plaintiff because no named Plaintiff kept his or her policy in force for more than ten years. Indeed, no Provider or Paragon policy had been in force for more than ten years. In any event, the evidence at trial established that LSW intended to make the illustrated reduction to the Monthly Administrative Charge beginning in each policy's eleventh year.

3. Conclusion Regarding Individual Claims

As set forth above, the named Plaintiffs failed to establish their individual claims for violations of the fraudulent, unlawful or unfair prong of the UCL.

V. CONCLUSION

On the findings of fact and conclusions of law set forth above, the Court finds in favor of LSW as to all remaining claims. LSW shall submit a proposed judgment within ten days of the entry of this Order.

IT IS SO ORDERED.

Dated: April 14, 2015

James V. Selna
United States District Judge