

ORAL ARGUMENT SCHEDULED FRIDAY, MAY 8, 2009

No. 09-1021 (consolidated with 09-1056)

IN THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

AMERICAN EQUITY INVESTMENT
LIFE INSURANCE COMPANY, *et al.*,
Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,
Respondent.

No. 09-1021

UNITED STATES COURT OF APPEALS
FOR DISTRICT OF COLUMBIA CIRCUIT

FEB 17 2009

RECEIVED

NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS, also known as NAIC, and
NATIONAL CONFERENCE OF INSURANCE LEGISLATORS, also known as NCOIL,
Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,
Respondent.

No. 09-1021 (consolidated with 09-1056)

On Petition for Review of Final Rule of the
United States Securities and Exchange Commission

Opening Brief of Petitioner NAIC

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CERTIFICATE AS TO PARTIES, RULINGS, AND RELATED CASES

Pursuant to Circuit Rules 15(c)(3) and 28(a)(1), Petitioners state as follows:

I. Parties and *Amici*.

In addition to the parties and *Amici* indicated in the Am. Equity Pet'r Br, the National Association of Insurance Commissioners ("NAIC") provides the following information.

On February 10, 2009, NAIC and the National Conference of Insurance Legislators ("NCOIL") jointly petitioned for review in case number 09-1056. Concurrent with this petition, NCOIL is filing a motion to withdraw as a petitioner and is filing a third party *amicus* brief to affirm the arguments and statements presented within this brief. All parties have consented to NCOIL's motion and entry of its *amicus* brief.

The Association of American Retired Persons has also entered an appearance as *Amici*.

II. Disclosure Statement.

The NAIC is a 501(c)(3) non-profit organization of insurance regulators from the 50 states, the District of Columbia, and the five United States territories. NAIC is organized under the General Corporation Law of the State of Delaware and has no parent corporations and no publicly held companies that own 10 percent or more of its stock. The mission of the NAIC is to assist state insurance regulators, individually and collectively, in serving the public interest and achieving the following fundamental insurance regulatory goals in a responsive, efficient and cost effective manner, consistent with the wishes of its members: protect the public interest; promote competitive markets; facilitate the fair and equitable treatment of insurance consumers; promote the reliability, solvency and financial solidity of insurance institutions; and support and improve state regulation of insurance.

III. Rulings Under Review.

This case seeks review of Rule 151A of the Securities and Exchange Commission (“Commission”), which establishes new standards for determining when an indexed annuity is not considered to be an “annuity contract” or an “optional annuity contract” under Section 3(a)(8) of the Securities Act of 1933 (the “Securities Act”), 15 U.S.C. § 77c(a)(8) (2007). The Commission adopted Rule 151A at an Open Meeting on December 17, 2008, and the final rule was published in the Federal Register on January 16, 2009. (JA 26.)

IV. Related Cases.

Case number 09-1056 was consolidated with Am. Equity Inv. Life Ins. Co. v. S.E.C., No. 09-1021 (D.C. Cir. filed Jan. 16, 2009), on February 13, 2009, for purposes of this appeal. NAIC is not aware of any other cases pending before this Court, another United States Court of Appeals, or any other federal or local court within the District of Columbia, that relates to the issues in this appeal.

Respectfully submitted by,
Petitioner NAIC

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TABLE OF CONTENTS

CERTIFICATE AS TO PARTIES, RULINGS, AND RELATED CASES.....	i
I. Parties and <i>Amici</i>	i
II. Disclosure Statement.	i
III. Rulings Under Review.....	ii
IV. Related Cases.	ii
TABLE OF CONTENTS.....	iv
TABLE OF AUTHORITIES.....	vi
GLOSSARY	xiii
JURISDICTIONAL STATEMENT	1
ISSUES PRESENTED.....	1
RELEVANT STATUTES AND REGULATIONS.....	1
STATEMENT OF FACTS	2
I. NAIC.....	2
II. FIAs are Regulated by State Insurance Laws.	2
III. Final Rule.....	8
STANDARD OF REVIEW.....	9
SUMMARY OF ARGUMENT.....	9
STANDING.....	9
I. Associational Standing.....	9
II. Constitutional Standing.....	10
(A) Injury-In-Fact.....	10
(B) Causation and Redressability.....	12
III. Permission to Sue an Agency.	12
ARGUMENT.....	12

I. Rule 151A is an Impermissible Encroachment upon the Traditional Power of States to Regulate Insurance.....12

II. The Commission’s Failure to Consider Persuasive Evidence that There Is No Widespread Abuse in the Sale of FIAs and that FIAs Are Already Sufficiently Regulated Renders Rule 151A Arbitrary and Capricious.....13

III. The Commission’s Failure to Consider the Inefficiency of a Dual Regulatory System Violates its Responsibilities under 15 U.S.C. § 77b(b).....14

CONCLUSION.....16

CERTIFICATE OF COMPLIANCE.....17

CERTIFICATE OF SERVICE.....18

ADDENDUM

TABLE OF AUTHORITIES

Cases

<u>Ass'n of Data Processing Serv. Org. v. Camp</u> , 397 U.S. 150 (1970).....	15
* <u>Chamber of Commerce of the U.S. v. S.E.C.</u> , 412 F.3d 133 (D.C. Cir. 2005).....	18
<u>Commonwealth of Pennsylvania ex rel. Shapp v. Kleppe</u> , 533 F.2d 668 (D.C. Cir. 1976).....	15
<u>Conference of State Bank Supervisors v. Conover</u> , 710 F.2d 878 (D.C. Cir. 1983).....	14
<u>Conference of State Bank Supervisors v. Lord</u> , 532 F. Supp. 694 (D.D.C. 1982).....	14
<u>Crank v. United States</u> , 539 F.3d 1236 (10th Cir. 2008).....	15
<u>Edward J. DeBartolo Corp. v. Fla. Gulf Coast Bldg & Constr. Trades Council</u> , 485 U.S. 568 (1988).....	16
<u>Hunt v. Washington State Apple Adver. Comm'n</u> , 432 U.S. 333 (1977).....	13
<u>Lujan v. Defenders of Wildlife</u> , 504 U.S. 555 (1992).....	14
<u>Md. People's Counsel v. Fed. Energy Regulatory Comm'n</u> , 760 F.2d 318 (D.C. Cir. 1985).....	15
<u>Neusse v. Camp</u> , 385 F.2d 694 (D.C. Cir. 1967).....	14
* <u>Sierra Club v. E.P.A.</u> , 292 F.3d 895 (D.C. Cir. 2002).....	13, 14
* <u>Solid Waste Agency of N. Cook County v. U.S. Army Corps of Eng'rs</u> , 531 U.S. 159 (2001).....	16
<u>State of Alaska v. U.S. Dep't of Transp.</u> , 868 F.2d 441 (D.C. Cir. 1989).....	15, 16
<u>United States v. Bass</u> , 404 U.S. 336 (1971).....	16
<u>Washington Utils and Transp. Comm'n v. F.C.C.</u> , 513 F.2d 1142 (9th Cir. 1975).....	14

Statutes

02-031 Me. Code R. §§ 1 to 10 (2007).....	7
---	---

11 N.C. Admin. Code 12.0601 to 12.0611 (1985).....	8
14 Va. Admin. Code §§ 5-30-10 to 5-30-100 (1982)	8
14 Va. Admin. Code §§ 5-40-10 to 5-40-80 (1982)	6
* 15 U.S.C. § 1011 (2007).....	15, 17
15 U.S.C. § 77b(a)(2) (2007).....	17
* 15 U.S.C. § 77b(b) (2007)	1, 19
15 U.S.C. § 77c(a)(8) (2007)	ii, 15
15 U.S.C. § 77i(a) (2007).....	17
18 Del. Code Regs. § 1214 (2006).....	10
210 Neb. Code R. § 19 (1984).....	8
210 Neb. Rev. Stat. § 50 (1990).....	5
211 Mass. Code Regs. 34.01 to 34.09 (1987).....	7
211 Mass. Code Regs. 96.01 to 96.10 (2006).....	10
27-29 R.I. Code R. §§ 001 to 011 (1980)	8
31 Pa. Code §§ 81.1 to 81.9 (1986)	8
5 U.S.C. § 702 (2007)	17
760 Ind. Admin. Code 1-16.1-1 to 1-16.1-13.5 (2007).....	7
760 Ind. Admin. Code 1-72-1 to 1-72-6 (2007).....	10
806 Ky. Admin. Regs 12:120 (2007).....	10
806 Ky. Admin. Regs. 12:080 (1983).....	7
806 Ky. Admin. Regs.12:150 (2007).....	3
82 Ark. Code R. (2004).....	10
917 Me. Code R. § 02-031 (2007).....	10
Ala. Admin. Code R. § 482-1-137 (2007)	10
Ala. Admin. Code R. § 830-X-3-.28 (2008)	9

Ala. Admin. Code R. §482-1-132 (1981)	5
Ala. Admin. Code R. §482-1-133-.01 to 482-1-133-.11 (2005).....	6
Ala. Admin. Code R. 482-1-129 (2003)	3
Alaska Admin. Code 3, §§ 26.750 to 26.769 (2008).....	3
Alaska Admin. Code 3, §§ 26.790 to 26.819 (2008).....	6
Ariz. Admin. Code § 20-6-202 (1969).....	5
Ariz. Admin. Code § 20-6-212.01 (2004).....	3
Ariz. Admin. Code § 20-6-215 (1983).....	7
Ariz. Rev. Stat. Ann. §§ 20-1241 to 20-1241.09 (2003)	7
Ariz. Rev. Stat. Ann. §§ 20-1242 to 20-1242.05 (2003)	3
Ariz. Rev. Stat. Ann. §§ 20-1243.01 to 1243.06 (2006).....	10
Cal. Admin. Code §§ 2547 to 2547.11 (1975).....	5
Cal. Ins. Code §§ 10509 to 10509.9 (1990).....	7
Cal. Ins. Code §§ 789.10, 10127.13 (2008).....	4
Colo. Code Regs. § 4-1-11 (2004).....	10
Colo. Code Regs. § 4-1-12 (2006).....	3
Colo. Code Regs. § 4-1-4 (1982).....	7
Conn. Agencies Regs. §§ 38a.432A-1 to 38a.432A-7 (2005)	10
Conn. Agencies Regs. §§ 38a.819-21 to 38a.819-31 (1976).....	5
Del. Code Regs. 18, § 1204 (1984).....	7
Fla. Admin. Code Ann. R. §§ 69O-150.101 to 69O-150.122 (1973)	5
Fla. Admin. Code Ann. R. §§ 69O-151.001 to 69O-151.012 (1981).....	7
Fla. Stat. § 627.4554 (2004).....	10
Ga. Comp. R. & Regs. 120-2-11 (1980).....	5
Ga. Comp. R. & Regs. 120-2-24 (1972).....	7

Ga. Comp. R. & Regs. 120-2-94-.01 to 120-2-94-.10 (2006)	10
Haw. Rev. Stat. §§ 431:10D-501 to 431:10D-510 (2001).....	7
Idaho Admin. Code R. 18.01.09 (2005).....	10
Idaho Admin. Code R. 18.01.41 (1983).....	7
Idaho Code Ann. § 41-1940 (2005).....	10
Ill. Admin. Code 50, §§ 3120.10 to 3120.80 (2007).....	10
Ill. Admin. Code 50, §§ 909.10 to 909.112 (1976).....	5
Ill. Admin. Code 50, §§ 917.20 to 917.110 (1970).....	7
Ind. Code §§ 27-4-9-1 to 27-4-9-6 (2005).....	10
Iowa Admin. Code R. 191-10.19 (2009).....	9
Iowa Admin. Code R. 191-15.68 to 191.15.73 (2006)	10
Iowa Admin. Code R. 191-16.21 to 191-16.30 (2000).....	7
Iowa Admin. Code R.191-15.61 to 191-15.67 (2003).....	3
Kan. Admin. Regs. § 40-2-12 (1971)	7
Kan. Admin. Regs. §§ 40-9-118 (1977)	5
Ky. Rev. Stat. Ann. § 304.12-030 (1970).....	7
La. Admin. Code §§ 37:11701 to 37:11717 (2006).....	10
La. Admin. Code §§ 37:XIII.4101 to 37:XIII.4123 (Regulation 60) (1997).....	5
La. Admin. Code §§ 37:XIII.8901 to 37:XIII.8925 (Regulation 70) (2000).....	7
Md. Code Regs. §§ 12.01 to 12.09 (2007).....	10
Md. Code Regs. 31.09.05.01 to 31.09.05.12 (1962).....	7
Me. Code R. § 915 (2004)	3
Mich. Admin. Code R. 500.1371 to 500.1387 (1984).....	5
Mich. Admin. Code R. 500.4151 to 500.4165 (2006).....	10
Mich. Admin. Code R. 500.601 to 500.606 (1971).....	7

Minn. Stat. §§ 61A.53 to 61A.60 (1996).....	7
Miss. Code R. § 99-2 (2001).....	7
Mo. Code Regs. Ann. 20, § 400-5.100 (1976).....	5
Mo. Code Regs. Ann. 20, § 400-5.400 (1979).....	7
Mo. Code Regs. Ann. 20, §§ 400-5.410 (2008).....	3
Mont. Admin. R. 6.6.301 to 6.6.310 (1978)	8
Mont. Admin. R. 6.6.801 to 6.6.806 (1998)	3
Mont. Code Ann. §§ 33-20-801 to 33-20-806 (2007)	10
N.C. Admin. Code §§ 0424 to 0433 (1978).....	5
N.C. Gen. Stat. §§ 58-60-120 to 58-60-145 (2005).....	3
N.C. Gen. Stat. §§ 58-60-150 to 58-60-180 (2007)	11
N.D. Admin. Code §§ 45-04-10-01 to 45-04-10-08 (1988)	5
N.D. Cent. Code §§ 26.1-34.2-01 to 26.1-34.2-05 (2007).....	11
N.H. Code Admin. R. Ann. Ins. 2602.01 to 2602.11 (2008).....	5
N.H. Code R. Ins. 302.01 to 302.09 (2001).....	8
N.J. Admin. Code §§ 11:2-23.1 to 11:2-23.10 (1985).....	5
N.J. Admin. Code §§ 11:4-2.1 to 11:4-2.9 (1972).....	8
N.M. Code R. §§ 12.11.17.1 to 12.11.17.12 (2008)	9
N.M. Code R. §§ 13.9.6.1 to 13.9.6.14 (1997)	8
N.M. Code R. §§ 9.12.1 to 9.12.13 (1997)	3
N.Y. Admin. Law §§ 219.1 to 219.7 (Regulation 34-A) (1980)	5
N.Y. Admin. Law §§ 51.1 to 51.8 (1998).....	8
N.Y. Ins. Law § 3209(b)(2)(A) (2008)	4
Nev. Admin. Code § O76-05 (2005)	11
Nev. Admin. Code §§ 686A.510 to 686A.570 (1980).....	8

Ohio Admin. Code § 3901:6-05 (1983).....	8
Ohio Admin. Code § 3901-6-14 (2007).....	3
Okla. Admin. Code §§ 365:10-3-30 to 365:10-3-39 (1990).....	5
Okla. Admin. Code §§ 365:25-17-1 to 365:25-17-11 (2005).....	11
Okla. Admin. Code §§ 365:25-19-1 to 25-19-9 (2007).....	3
Or. Admin. R. 836-051-0900 to 836-051-0925 (2008).....	4
Or. Admin. R. 836-80-0001 to 836-80-0043 (1968).....	8
R.I. Code R. §§ 27-12-1 to 27-12-10 (2006).....	11
S.C. Code Ann. Regs. 69-12.1 (1986).....	8
S.D. Admin. R. 20:06:08 (1989).....	8
S.D. Codified Laws. §§ 58-33A-13 to 58-33A-27 (2008).....	11
Tenn. Comp. R. & Regs. § 0780-1-24 (1985).....	8
Tenn. Comp. R. & Regs. §§ 0780-1-33-.01 to 0780-1-33-.13 (1976).....	5
Tenn. Comp. R. & Regs. §§ 0780-1-86-.01 to 0780-1-86-.09 (2008).....	11
Tex. Ins. Code Ann. §§ 1114.001 to 1114.007 (2007).....	8
Utah Admin. Code R. 590-229-1 (2004).....	4
Utah Admin. Code R. 590-230-1 to 590-230-9 (2004).....	11
Utah Admin. Code R. 590-93 (1984).....	8
Vt. Code R. § 2001-3 (1989).....	8
W. Va. Code R. §§ 114-11-1 to 114-11-11 (2008).....	6
W. Va. Code R. §§ 114-11B-1 to 114-11B-7 (2008).....	11
W. Va. Code R. §§ 114-8-1 to 114-8-9 (1970).....	8
Wash. Admin. Code 284-23-010 to 284-23-550 (1975).....	6
Wash. Admin. Code 284-23-400 to 284-23-485 (1980).....	8
Wis. Stat. § 628.347 (2004).....	11

Wyo. Code R. § 12 (1986)..... 8

Other Authorities

D.C. Cir. R. 15(c)(3)..... i

D.C. Cir. R. 28(a)(1)..... i

* Indexed Annuities and Certain Other Insurance Contracts, 74 Fed. Reg.
3,138 (Jan. 16, 2009) ii, 10, 12, 13, 15

JURISDICTIONAL STATEMENT

NAIC incorporates by reference American Equity Investment Life Insurance Company's Petitioners Brief, filed February 17, 2009 ("Am. Equity Pet'r Br."), in its entirety and adopts its Jurisdictional Statement.¹

ISSUES PRESENTED

1. Whether the Commission's regulation of FIAs impermissibly encroaches on states' regulation of insurance as protected by the McCarran-Ferguson Act.
2. Whether the Commission's failure to consider evidence that there is no widespread abuse in the sale of FIAs and the existence of an effective states' regulatory system renders Rule 151A arbitrary and capricious.
3. Whether the Commission's failure to consider Rule 151A's impact on efficiency violated its obligations under 15 U.S.C. § 77b(b) (2007).

RELEVANT STATUTES AND REGULATIONS

Statutes relevant to this petition have been provided with the opening brief of the American Equity Petitioners and in the Addendum provided with this Brief.

¹ Because of the difference in identities as to the parties, NAIC does not adopt American Equity Investment Life Insurance Company's Certificate as to Parties, Ruling, and Related Cases, except as noted herein. NAIC adopts all other sections of American Equity's brief.

STATEMENT OF FACTS

I. NAIC.

NAIC is an organization of the insurance regulators from the 50 states, the District of Columbia, and five U.S. territories. Its mission is “to assist state insurance regulators . . . in . . . Protect[ing] the public interest; Promot[ing] competitive markets; Facilitat[ing] the fair and equitable treatment of insurance consumers; Promot[ing] the reliability, solvency and financial solidity of insurance institutions; and Support[ing] and improv[ing] state regulation of insurance.” NAIC, http://www.naic.org/index_about.htm (last visited Feb. 14, 2009). Through its committees, NAIC engages in consumer protection activities, including helping coordinate state market regulatory functions such as antifraud efforts, consumer complaints, and regulatory interventions. Id.

II. FIAs are Regulated by State Insurance Laws.

NAIC adopts the Section entitled “Fixed Indexed Annuities” set forth in Am. Equity Pet’r Br. and supplements this Section by outlining the additional attributes of such products and the state regulatory structure governing them.

Fixed Index Annuities (“FIAs”) are, in their essential attributes, identical to traditional fixed annuities, and thus, are subject to a wide range of state laws aimed at protecting consumers and ensuring the solvency of insurance companies. For example, FIAs are subject to state “nonforfeiture” laws requiring a guaranteed minimum contract value regardless of the performance of the relevant index. JA 242. State insurance laws specify the kinds of “permitted investments” in which an insurer’s general account may invest. JA 243. Such “permitted investments” consist primarily of high-quality fixed income securities, U.S. and government agency bonds, and other approved assets. Id. State insurance laws also require FIA issuers to maintain elevated levels of capital, and most states provide purchasers at least \$100,000 in

insurance in the event of the issuer's insolvency. Id.

As is the case with other fixed annuities, state insurance laws also regulate the sale and marketing of FIAs and the conduct of the agents who sell them. JA 259-60, 211, 416. In general, prior to being sold, FIAs must be filed with and reviewed by state regulators. Add. 180. State disclosure laws require that purchasers receive certain minimum information regarding the contents, terms, and conditions of FIA contracts to help the purchaser understand the contract's basic features. JA 210. For example, the Annuity Disclosure Model Regulation (NAIC 1999)—which has been adopted by 15 states—specifies the minimum information which must be disclosed and the method for disclosing it in connection with the sale of an annuity product.² Add. 38. The Annuity Disclosure Model Regulation requires FIA contracts to disclose guaranteed and non-guaranteed amounts, administrative charges, how the contract is assessed, death benefits, a summary of the federal tax status, and the impact of any riders. Add. 38. In many states, the purchaser and insurance agent must sign disclosure statements as a condition of policy issuance, and the insurers must deliver a buyer's guide, written by NAIC, at the point of sale for fixed annuities, including FIAs. JA 261-2. States that have not yet adopted NAIC's model regulation have alternative, significant disclosure requirements. See, e.g., N.Y. Ins. Law § 3209(b)(2)(A) (2008); Cal. Ins. Code §§ 789.10, 10127.13 (2008).

² See Ala.Admin.CodeR. §482-1-129(2003); AlaskaAdmin.Code 3, §§26.750 to 26.769 (2008); Ariz.Rev.Stat.Ann. §§20-1242 to 20-1242.05(2003); Ariz.Admin.Code §20-6-212.01 (2004); Colo.CodeRegs. §4-1-12(2006); IowaAdmin.CodeR.191-15.61 to 191-15.67(2003); 806Ky.Admin.Reg.12:150(2007); Me.CodeR. §915(2004); Mo.CodeRegs.Ann. 20, §§400-5.410(2008); Mont.Admin.R.6.6.801 to 6.6.806(1998); N.M.CodeR. §§9.12.1 to 9.12.13 (1997); N.C.Gen.Stat. §§58-60-120 to 58-60-145(2005); OhioAdmin.Code §3901-6-14(2007); Okla.Admin.Code §§365:25-19-1 to 25-19-9(2007); Or.Admin.R. 836-051-0900 to 836-051-0925(2008); UtahAdmin.Code R. 590-229-1(2004).

State unfair trade practice laws, advertising regulations, and/or market conduct rules regulate the representations that are permitted in connection with the marketing and sale of FIAs. JA 210. The Advertisements of Life Insurance and Annuities Model Regulation (NAIC 2000) sets forth minimum guidelines to ensure a full and truthful disclosure to the public of all material and relevant information in the advertising of annuity contracts, including FIAs. Add. 73-81. Twenty-two states have adopted the NAIC model law³ and 15 have similar legislation or regulations.⁴

Many states also impose disclosure requirements that are specifically tailored to insurance products and the needs of insurance buyers. JA 210. For example, a number of state laws require that consumers receive “free-look” or “right to return” periods that permit the purchaser a specific number of days to review the FIA contract and opt out of it with a full refund of premiums paid. JA 210, 259.

³ Ala.Admin.CodeR. 482-1-132(1981); Ariz.Admin.Code §20-6-202(1969); Cal.Admin.Code §§2547 to 2547.11(1975); Conn.AgenciesRegs. §§38a.819-21 to 38a.819-31(1976); Fla.Admin.CodeAnn.R. §§ 690-150.101 to 690-150.122(1973); Ga.Comp.R.&Regs. 120-2-11(1980); Ill.Admin.Code 50, §§909.10 to 909.112(1976); Kan.Admin.Reg. §§40-9-118(1977); La.Admin.Code §§37:XIII.4101 to 37:XIII.4123 (Regulation 60)(1997); Mich.Admin.CodeR. 500.1371 to 500.1387 (1984); Mo.CodeRegs. Ann. 20, §400-5.100 (1976); 210 Neb.Rev.Stat. §50 (1990); N.H.CodeAdmin.R. Ann. Ins. 2602.01 to 2602.11 (2008); N.J.Admin.Code §§11:2-23.1 to 11:2-23.10(1985); N.Y.Admin.Law §§219.1 to 219.7 (Regulation 34-A) (1980); 11 N.C.Admin.Code §§0424 to 0433(1978); N.D.Admin.Code §§45-04-10-01 to 45-04-10-08(1988); Okla.Admin.Code §§365:10-3-30 to 365:10-3-39(1990); Tenn.Comp.R.&Regs. §§ 0780-1-33-.01 to 0780-1-33-.13(1976); 14 Va.Admin.Code §§5-40-10 to 5-40-80(1982); Wash.Admin.Code 284-23-010 to 284-23-550(1975); W.Va.Code R. §§114-11-1 to 114-11-11(2008).

⁴ Arkansas, Colorado, Iowa, Kentucky, Maryland, Minnesota, Missouri, Ohio, Pennsylvania, Rhode Island, South Dakota, Texas, Utah, Vermont, and Wisconsin.

State insurance laws have also heightened the disclosure requirements and sales practice protection rules that states impose in connection with transactions that involve the replacement of insurance contracts. The goal of such laws is to ensure that consumers are aware of any disadvantages associated with replacing an existing policy, such as a potential loss of accumulated value, and to prevent agents from “churning” such contracts. JA 210. Under the Life Insurance and Annuities Replacement Model Regulation (NAIC 2007), which has been adopted by 45 states, agents and insurers must follow structured processes that confirm that the purchaser is aware of any potential drawbacks to the replacement transaction, provide consumers with additional disclosures about the replacement, report the potential replacement to the existing and replacing insurer, and maintain records of the process.⁵ Eleven states and one U.S. territory

⁵ Ala.Admin.Coder. 482-1-133-.01 to 482-1-133-.11(2005); AlaskaAdmin.Code 3, §§ 26.790 to 26.819(2008); Ariz.Rev.Stat.Ann. §§ 20-1241 to 20-1241.09(2003); Ariz.Admin.Code § 20-6-215(1983); Cal.Ins.Code §§ 10509 to 10509.9(1990); Colo.CodeRegs. § 4-1-4(1982); Del.CodeRegs. 18, § 1204(1984); Fla.Admin.Code Ann.R. §§ 690-151.001 to 690-151.012(1981); Ga.Comp.R.&Regs. 120-2-24(1972); Haw.Rev.Stat. §§ 431:10D-501 to 431:10D-510(2001); IdahoAdmin.CodeR. 18.01.41(1983); Ill.Admin.Code 50, §§ 917.20 to 917.110(1970); 760 Ind.Admin.Code 1-16.1-1 to 1-16.1-13.5(2007); IowaAdmin.CodeR. 191-16.21 to 191-16.30(2000); Kan.Admin.Reg. § 40-2-12(1971); Ky.Rev.Stat.Ann. § 304.12-030(1970); 806 Ky.Admin.Reg. 12:080(1983); La.Admin.Code §§ 37:XIII.8901 to 37:XIII.8925 (Regulation 70)(2000); 02-031 Me.CodeR. §§ 1 to 10 (2007); Md.CodeRegs. 31.09.05.01 to 31.09.05.12(1962); 211 Mass.CodeRegs. 34.01 to 34.09(1987); Mich.Admin.CodeR. 500.601 to 500.606(1971); Minn.Stat. §§ 61A.53 to 61A.60(1996); Miss.CodeR. § 99-2(2001); Mo.CodeRegs.Ann. 20, § 400-5.400(1979); Mont.Admin.R. 6.6.301 to 6.6.310(1978); 210 Neb.CodeR. § 19(1984); Nev.Admin.Code §§ 686A.510 to 686A.570(1980); N.H.CodeR.Ins. 302.01 to 302.09(2001); N.J.Admin.Code §§ 11:4-2.1 to 11:4-2.9(1972); N.M.CodeR. §§ 13.9.6.1 to 13.9.6.14(1997); N.Y.Admin.Law §§ 51.1 to 51.8(1998); 11 N.C.Admin.Code 12.0601 to 12.0611(1985); OhioAdmin.Code § 3901:6-05(1983); Or.Admin.R. 836-80-0001 to 836-80-0043(1968); 31 Pa.Code §§ 81.1 to 81.9(1986); 27-29 R.I.Code R. §§ 001 to 011 (1980); S.C.CodeAnn.Reg. 69-12.1(1986); S.D.Admin.R. 20:06:08(1989); Tenn.Comp.R.&Regs. § 0780-1-24(1985); Tex.Ins.CodeAnn. §§ 1114.001 to 1114.007(2007); UtahAdmin.CodeR. 590-93(1984); Vt.CodeR. § 2001-3(1989); 14 Va.Admin.Code §§ 5-30-10 to 5-30-100(1982);

have adopted additional or similar legislation to the Life Insurance and Annuities Replacement Model Legislation.⁶

Additionally, the Model Regulation on the Use of Senior-Specific Certifications and Professional Designations in the Sale of Life Insurance and Annuities (NAIC 2008) (“Senior-Specific Regulation”), “set[s] forth standards to protect consumers from misleading and fraudulent marketing practices with respect to the use of senior-specific certifications and professional designations in the solicitation, sale or purchase of, or advice made in connection with, a life insurance or annuity product.” Senior-Specific Regulation § 1. To date, three states have already adopted the regulation;⁷ legislation adopting the model regulation is pending in one state,⁸ and six states have adopted legislation similar to the Senior-Specific Regulation,⁹ with pending legislation in another five states similar to the Senior-Specific Regulation.¹⁰

In addition, virtually every state also requires an assessment of whether an FIA is “suitable” in light of the prospective purchaser’s financial circumstances and objectives at the time of the purchase of the FIA. JA 209. Among other things, the Suitability in Annuity Transactions Model Regulation (NAIC 2007) requires insurance producers or insurers to make

Wash.Admin.Code 284-23-400 to 284-23-485(1980); W.Va.CodeR. §§ 114-8-1 to 114-8-9(1970); Wyo.CodeR. § 12(1986).

⁶ Arkansas, Florida, Montana, Nebraska, Nevada, New York, Oklahoma, Pennsylvania, Puerto Rico, Texas, West Virginia, and Wisconsin.

⁷ Ala. Admin. Code R. §830-X-3-.28 (2008); Iowa Admin. Code R. 191-10.19 (2009); N.M. Code R. §§ 12.11.17.1 to 12.11.17.12 (2008).

⁸ Arkansas.

⁹ Arizona, California, Maine, Missouri, North Dakota, and Wisconsin.

¹⁰ Connecticut, New Hampshire, New Jersey, Ohio, and Utah.

efforts to obtain information from the consumer about the consumer's financial and tax status and investment objectives whenever they recommend the purchase of an FIA. Add. 159-60. This model law has been adopted in 29 states,¹¹ and 19 states have adopted additional or similar legislation.¹²

State insurance regulators have created supervisory systems that permit them to enforce compliance with insurance sales practice and disclosure rules. Such regulatory systems include agent licensing and training, market conduct examinations, and sanctions for regulatory violations. JA 211. All fifty states require agents or brokers who sell insurance products within a state to maintain a license. JA 416. Licensing requirements help ensure that insurance agents or brokers are knowledgeable about the products they sell and the laws governing the sale of those products. In addition to the examinations that state regulators conduct to ensure the

¹¹ Ala.Admin.CodeR. §482-1-137(2007); Ariz.Rev.Stat.Ann. §§ 20-1243.01 to 1243.06(2006); 82 Ark.CodeR.(2004); Colo.CodeRegs. § 4-1-11(2004); Conn.AgenciesRegs. §§ 38a.432A-1 to 38a.432A-7(2005); 18 Del.CodeRegs. § 1214(2006); Fla.Stat. § 627.4554(2004); Ga.Comp.R.&Regs. 120-2-94-.01 to 120-2-94-.10(2006); IdahoCodeAnn. § 41-1940(2005); IdahoAdmin.CodeR. 18.01.09(2005); Ill.Admin.Code 50, §§ 3120.10 to 3120.80(2007); Ind.Code §§ 27-4-9-1 to 27-4-9-6(2005); 760 Ind.Admin.Code 1-72-1 to 1-72-6); IowaAdmin.Code R. 191-15.68 to 191.15.73(2006); 806 Ky.Admin.Reg. 12:120(2007); La.Admin.Code §§ 37:11701 to 37:11717(2006); 917 Me.CodeR. § 02-031(2007); Md.CodeRegs. §§ 12.01 to 12.09 (2007); 211 Mass.CodeRegs. 96.01 to 96.10(2006); Mich.Admin.CodeR. 500.4151 to 500.4165(2006); Mont.CodeAnn. §§ 33-20-801 to 33-20-806(2007); Nev.Admin.Code § 076-05(2005); N.C.Gen.Stat. §§ 58-60-150 to 58-60-180(2007); N.D.Cent.Code §§ 26.1-34.2-01 to 26.1-34.2-05(2007); Okla.Admin.Code §§ 365:25-17-1 to 365:25-17-11(2005); R.I.CodeR. §§ 27-12-1 to 27-12-10(2006); S.D.Codified Laws. §§ 58-33A-13 to 58-33A-27(2008); Tenn.Comp.R.&Regs. §§ 0780-1-86-.01 to 0780-1-86-.09(2008); UtahAdmin.CodeR. 590-230-1 to 590-230-9(2004); W.Va.CodeR. §§ 114-11B-1 to 114-11B-7(2008); Wis.Stat. § 628.347(2004).

¹² Alaska, Arkansas, California, Hawaii, Iowa, Kansas, Maine, Massachusetts, Minnesota, Missouri, Nebraska, New Jersey, North Carolina, North Dakota, Oregon, South Dakota, Texas, Virginia, and Wyoming.

solvency of domestic insurers, insurance regulators conduct market conduct examinations that include reviews of product design and marketing, advertising, licensing, complaint handling, policyholder services, and claims practices. JA 211. States can impose a wide range of penalties for market conduct violations, including suspension, revocation or non-renewal of a violator's license, issuance of cease and desist orders against violators, and civil and criminal penalties.

III. Final Rule.

NAIC adopts the discussion set forth in the Section of Am. Equity Pet'r Br., entitled "Adoption of the Rule Under Review," and directs the Court's attention to the following:

NAIC commented that the Proposed Rule required insurers to determine prior to the issuance of an FIA if it was more likely than not that the amount payable by the insurance company under an FIA would exceed the amounts guaranteed under the contract. JA 418. NAIC noted that such determinations would be conclusive if (1) both the methodology and the economic, actuarial, and other assumptions used in the determination were reasonable; (b) the computations made by the issuer in support of the determination are materially accurate; and (c) the determination is not made more than six months prior to the date on which the form of contract is first offered and not more than three years prior to the date on which the particular contract is issued. Id. NAIC expressed concern that the rule did not make clear whether federal or state insurance regulators would determine whether or not a company is in compliance with the rule. Other commentators noted that the principles based approach adopted by the Commission could result in insurance companies performing the "more likely than not" test inconsistently and thus increase enforcement and litigation risk. JA 40.

The Final Rule eliminated the provision that the determination of whether it was more likely than not that the amount payable by the insurance company under an FIA would exceed

the amounts guaranteed under the contract be made not more than three years prior to the date on which the particular contract is issued. Id. The Commission did not resolve the concerns of NAIC or other commentators about the Rule's lack of clarity.

STANDARD OF REVIEW

NAIC adopts the standard of review for each issue set forth in the American Equity Petition.

SUMMARY OF ARGUMENT

The Commission defined FIAs as securities and not annuities. As discussed in Am. Equity Pet'r Br., the Commission is wrong. The Commission also erred in the following three ways.

First, the Commission ignored the McCarran-Ferguson Act, which commits insurance regulation to the States as a matter of law. Second, the Rule fails under the APA review because it is arbitrary, capricious, and contrary to law. The Commission failed to consider evidence showing that the basis for reopening the rule and classifying FIAs as securities and not annuities – the purported widespread abuse of and complaints regarding FIAs – did not exist. Likewise, the Commission did not consider the protections already provided by the state regulatory system. Finally, the Commission failed to engage in the required analysis of efficiency and did not address the inefficiencies created by a dual regulatory system.

STANDING

I. Associational Standing.

NAIC is an association of state insurance regulators that will be harmed by The Final Rule Indexed Annuities and Certain Other Insurance Contracts, 74 Fed. Reg. 3,138, issued by the Securities and Exchange Commission (hereinafter "Rule 151A"). NAIC has associational standing because "(1) at least one of its members would have standing to sue in his own right, (2)

the interests the association seeks to protect are germane to its purpose, and (3) neither the claim asserted nor the relief requested requires that an individual member of the association participate in the lawsuit.” Sierra Club v. E.P.A., 292 F.3d 895, 898 (D.C. Cir. 2002) (citing Hunt v. Washington State Apple Adver. Comm’n, 432 U.S. 333, 344 (1977)).

As shown below, each member of NAIC has standing to challenge Rule 151A in their own right, so NAIC has associational standing to bring this action on their behalf. Preserving the states’ power to regulate annuities as insurance contracts is clearly germane to the purpose of NAIC. Supra 1. The claim asserted hinges on the statutory definition of “annuity” in the Securities Act, which is a matter of law and does not require individualized proof from NAIC members. Conference of State Bank Supervisors v. Lord, 532 F. Supp. 694, 695 (D.D.C. 1982), aff’d, Conference of State Bank Supervisors v. Conover, 710 F.2d 878 (D.C. Cir. 1983).

II. Constitutional Standing.

In order for a member of an association to have standing, it must show (1) that it would suffer injury-in-fact, (2) causation, and (3) redressability. Sierra Club, 292 F.3d at 898 (citing Lujan v. Defenders of Wildlife, 504 U.S. 555, 560 (1992)).

(A) Injury-In-Fact.

This Court has found that where there is an “admixture of national and state policies, attaching national legal force to the state policy,” then “a state official directly concerned in effectuating the state policy has an ‘interest’ in a legal controversy involving the [federal agency] which concerns the nature and protection of the state policy” sufficient to confer standing on the state official (a state banking commissioner, in that case). Neusse v. Camp, 385 F.2d 694 (D.C. Cir. 1967) (cited by Conover, 710 F.2d at 881 n.3 (D.C. Cir. 1983); Lord, 532 F. Supp. at 695. See Washington Utils and Transp. Comm’n v. F.C.C., 513 F.2d 1142, 1146 (9th Cir. 1975)

(holding that when a state agency is “charged by law with responsibilities related to the issues it seeks to raise,” then it “is a proper plaintiff to obtain review of an administrative order”). “National legal force” attaches to state insurance policy by virtue of the McCarran-Ferguson Act, 15 U.S.C. §§ 1011-15 (2007), which protects state insurance law from federal regulation, and Section 3(a)(8) of the Securities Act, which expressly exempts from Commission regulation “[a]ny . . . annuity contract . . . issued by a corporation subject to the supervision of the insurance commissioner, bank commissioner, or any agency or officer performing like functions, of any State or Territory of the United States or the District of Columbia.” 15 U.S.C. § 77c(a)(8) (2007) (emphasis added).¹³

The individual insurance regulatory officers are also representatives of the States, and thus have standing because of State interests that are injured by the Commission’s action. These include: (1) a sovereign interest “in exercising the power to create and enforce a legal code,” State of Alaska v. U.S. Dep’t of Transp., 868 F.2d 441, 443 (D.C. Cir. 1989); (2) a *parens patriae* interest in “protecting their citizens in [the state’s] traditional governmental field” of insurance regulation, which has been injured by the Commission’s unauthorized interference in that field, Md. People’s Counsel v. Fed. Energy Regulatory Comm’n, 760 F.2d 318, 321 (D.C. Cir. 1985); and (3) a *parens patriae* interest in economic supervision, which will be harmed by the substantial generalized economic effects that Rule 151A will have on the States’ citizens, Commonwealth of Pennsylvania ex rel. Shapp v. Kleppe, 533 F.2d 668, 674 (D.C. Cir. 1976).

¹³ By the same token, NAIC members have prudential standing because they are in the “zone of interest” of the Securities Act. Ass’n of Data Processing Serv. Org. v. Camp, 397 U.S. 150 (1970) (cited by Alaska, 868 F.2d at 444).

(B) Causation and Redressability.

There can be little doubt that the harm complained of by NAIC was directly caused by Rule 151A, or that the harm will be redressed by invalidating that Rule. See Wyoming ex rel. Crank v. United States, 539 F.3d 1236, 1242 (10th Cir. 2008).

III. Permission to Sue an Agency.

Finally, Congress expressly conferred standing to sue the Commission in the Securities Act, which provides that “[a]ny person aggrieved by an order of the Commission may obtain a review of such order.” 15 U.S.C. § 77i(a) (2007). The term “person” is defined to include “an individual, . . . an association, . . . or a government or political subdivision thereof.” 15 U.S.C. § 77b(a)(2) (2007). The APA also confers standing on NAIC members because they are “person[s] . . . aggrieved by agency action within the meaning of a relevant statute.” 5 U.S.C. § 702 (2007). See Alaska, 868 F.2d at 445 n.3.

ARGUMENT

NAIC adopts the legal arguments set forth in Am. Equity Pet’r Br., including that FIAs are annuities and not securities, and add the following:

I. Rule 151A is an Impermissible Encroachment upon the Traditional Power of States to Regulate Insurance.

The McCarran-Ferguson Act has long established that the regulation of the business of insurance is left to the states. 15 U.S.C. §§ 1011-15 (2007). The Commission’s reclassification of a traditional insurance product as a security through the adoption of Rule 151A is in direct conflict with Congress’ specific grant of authority to the states. In Solid Waste Agency of N. Cook County v. U.S. Army Corps of Eng’rs, 531 U.S. 159, 173 (2001) (citing Edward J. DeBartolo Corp. v. Fla. Gulf Coast Bldg & Constr. Trades Council, 485 U.S. 568, 575 (1988)), the Supreme Court reiterated that an administrative agency’s interpretation of a statute should

provide a clear indication that they are following the intent of Congress.

The Court noted in Solid Waste Agency “Congress does not casually authorize administrative agencies to interpret a statute to push the limit of congressional authority.” Id. at 173-74. In their re-interpretation of Section 3(a)(8), the Commission has altered the federal-state framework regarding the regulation of insurance and “encroached upon a traditional state power.” Id. at 174 (citing United States v. Bass, 404 U.S. 336, 349 (1971)). As in the cited cases, the Commission has encroached upon the state regulation of insurance. Rule 151A is an unlawful re-interpretation of an existing congressionally designated state right, and the Commission exceeded its administrative authority by adopting it.

II. The Commission’s Failure to Consider Persuasive Evidence that There Is No Widespread Abuse in the Sale of FIAs and that FIAs Are Already Sufficiently Regulated Renders Rule 151A Arbitrary and Capricious.

The Commission failed to consider two important aspects regarding FIAs and, accordingly, failed to offer sufficient explanation for its decision in light of the evidence before the agency. First, the rulemaking process, as discussed in Am. Equity Pet’r Br., shows that the Commission initially relied upon the alleged widespread abuse of and complaints surrounding FIAs as the rationale for reconsidering the status of FIAs under federal securities laws. Substantial evidence was submitted showing that, to the contrary, such widespread abuse did not exist. Accordingly, the basis for the Commission’s action in revisiting the annuity rule was no longer valid. The Commission, however, failed to address or take into consideration these facts contradicting a justification that it had already identified as an important aspect of the problem. To the extent that the Commission was concerned about abuse, it also neglected to consider that the state regulations provide stringent consumer protection. To the contrary, the Commission merely proclaimed that the presence or absence of abuse was “irrelevant.” JA 35.

Second, the Final Rule shows that the Commission ignored evidence that existing state

laws effectively regulated disclosure requirements, “suitability” determinations and sales practices involving FIAs. Although the comments submitted in response to the Commission’s Rule proposal provided significant evidence that a robust state regulatory scheme was already in place and regulated FIAs, the Commission ignored these comments and proceeded to adopt the rule without any evaluation of the state insurance regulatory structure or its role in regulating FIAs. JA 36. These failures render the rule arbitrary and capricious.

III. The Commission’s Failure to Consider the Inefficiency of a Dual Regulatory System Violates its Responsibilities under 15 U.S.C. § 77b(b).

When the Commission is engaged in rulemaking, 15 U.S.C. § 77b(b) (2007) requires it to consider “whether the action will promote efficiency, competition, and capital formation.” Construing Section 80a-2(c), which is nearly identical to Section 77b(b), this Court has determined that the Commission has “a statutory obligation to determine as best it can the economic implications of the rule it has proposed.” Chamber of Commerce of the U.S. v. S.E.C., 412 F.3d 133, 143 (D.C. Cir. 2005). The Commission has a further “statutory obligation to do what it can do to apprise itself – and hence the public and Congress – of the economic consequences of a proposed regulation before it decides whether to adopt the measure.” Id. at 144. The Commission’s promulgation of a rule that will create an inefficient, duplicative, and confusing regulatory regime shows that it failed to properly consider this factor.

The Commission purports to analyze the efficiency factor in its Final Rule but merely sidesteps the issue. Noting that some commentators argued that the Rule would be duplicative of state regulatory systems, the Commission stated that the State efforts cannot “substitute for the federal securities law protections.” JA 58. The question, of course, is not whether the federal securities laws offer a benefit, but whether the rule is efficient. The Commission fails to answer.

Likewise, the Commission notes that other commentators argued that the Commission

must engage in a comprehensive consideration of the existing state regulatory system in order to determine if the Rule will offer further efficiencies. Again, the Commission fails to answer this point, merely stating that securities investors are entitled to the protections of federal securities laws. *Id.* Though this statement may be true, it is also irrelevant. The Commission cannot claim to have engaged in the required consideration of efficiency without determining the impact of imposing a duplicative layer of regulation in an area where, to date, regulation of these insurance products has been under the sole jurisdiction of the states.

When Rule 151A was posted for comments, NAIC commented that the Rule requires an insurer to make a determination under the “more likely than not test.” JA 418. Under the “more likely than not test” set forth in Rule 151A, it is unclear which regulator will determine whether a company is in compliance with the requirements. The “test” created by the Commission is simply ambiguous. Unlike current state insurance regulations, Rule 151A’s “more likely than not” test does not provide a clear line as to when someone selling these products *may or may not* report to the Commission or *may or may not* report to the state insurance regulator. Those laws will remain in effect, but the Rule which purports to place these products within the Commission’s jurisdiction creates the very real likelihood that sellers will not comply with or view themselves as not subject to existing state measures. This is confusing, costly, unnecessary, and likely ineffective, duplicative regulation.

Dual regulation is not efficient. Indexed annuity products are not the bailiwick of the Commission—*since they are insurance products*—and the Commission should not insert itself in an area where it has no true expertise and which is being fully and effectively regulated at the state level.

CONCLUSION

For the aforementioned reasons, NAIC requests that the Court hold the Commission's rule unlawful under the Securities Act and the Administrative Procedures Act, to vacate the rule and its requirements, to issue a permanent injunction prohibiting the Commission from implementing and enforcing the requirements, and for such other relief as the Court deems appropriate.

Respectfully submitted,
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Dated: February 17, 2009

CERTIFICATE OF SERVICE

The undersigned certifies that a copy of this brief was caused to be served upon the attorney of record on February 17, 2009, of the following parties:

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