

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

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.

On Petitions for Review of an Order of the
Securities and Exchange Commission

**RESPONSE OF THE SECURITIES AND EXCHANGE COMMISSION
TO PETITION FOR PANEL REHEARING**

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PRELIMINARY STATEMENT

This Court should deny the request of petitioner OM Financial Life Insurance Company (“Old Mutual”) for a stay of Rule 151A “until two years after the Commission’s completion of a new § 2(b) analysis and *possible* reissuance, revision, or withdrawal of the Rule in light of that analysis.” Petition for Panel Rehearing (“Pet.”) at 2 (emphasis supplied). The relief Old Mutual is seeking is premature and unwarranted.

As Old Mutual acknowledges, Rule 151A, 17 C.F.R. § 230.151A, is not currently in effect. It is also unclear at this juncture precisely what action the Commission ultimately will take on remand—which could be any one of the three courses Old Mutual suggests. Although the release adopting Rule 151A stated that the rule would become effective on January 12, 2011, that date was set before the rule was challenged and before this Court remanded the rule for the Commission to address defects in its analysis of efficiency, competition, and capital formation under Section 2(b) of the Securities Act, 15 U.S.C. 77b(b). There is no basis for Old Mutual’s assumption that, if the Commission were to reissue the rule after addressing the requirements of Section 2(b), the Commission would refuse to extend the rule’s effective date without regard to its impact on companies that issue and sell indexed annuities. To the contrary, at every stage of the rulemaking and subsequent challenge in this Court, the Commission has

sought to accommodate the legitimate concerns of those issuers and sellers: Rule 151A was drafted to apply prospectively only to indexed annuities issued on or after the rule's effective date; in response to comments from indexed annuity issuers and sellers raising the same concerns that Old Mutual identifies at pages 7-8 of its rehearing petition, the Commission made the rule effective two years after adoption instead of one year after adoption as it had originally proposed; and, after the petitioners challenged Rule 151A in this Court, the Commission agreed to their request for expedited briefing to resolve the uncertain regulatory status of their indexed annuity products as quickly as possible.

In the unlikely event that the Commission were to reissue Rule 151A *without* providing adequate transition time for Old Mutual or other affected companies (none of which joined in the rehearing petition), they could seek a stay from the Commission or this Court. Following that route is appropriate for several reasons: It allows the Commission, in the first instance, to set an effective date that reflects its reasoned judgment. It avoids premature intervention by the Court in a manner that will likely prove unnecessary. And it enables all involved—the Commission, the Court, and those affected by any rule that may be adopted—to act in response to facts rather than to speculation about future actions that may never occur.

BACKGROUND

On January 8, 2009, the Commission adopted Rule 151A to clarify the status under the securities laws of certain indexed annuities. Section 3(a)(8) of the Securities Act, 15 U.S.C. 77c(a)(8), provides an exemption from the Act for certain “annuity contracts” and other insurance contracts but does not define the term “annuity contract.” Rule 151A provides that indexed annuities that are “more likely than not” to pay a return based on the uncertain future performance of a fluctuating index of securities (such as the Standard & Poor’s 500 Index) are not “annuity contracts” under Section 3(a)(8) and therefore are not eligible for the exemption from regulation as securities. RA151.^{1/}

In challenging Rule 151A, the petitioners argued that the rule was:

(1) inconsistent with the plain language of Section 3(a)(8); (2) based on an erroneous view of the investment risk faced by purchasers of indexed annuities; (3) contrary to Supreme Court precedent interpreting Section 3(a)(8) because the rule does not explicitly take account of the way in which indexed annuities are marketed; and (4) defective because the Commission had not assessed existing state insurance law in considering (under Section 2(b)) whether Rule 151A would

¹ “RA” refers to the Regulatory Appendix filed with the Responding Brief of the Securities and Exchange Commission in this case.

promote efficiency, competition, and capital formation. This Court found in the Commission's favor on all but the last argument, concluding that Rule 151A was based on a reasonable interpretation of the term "annuity contract" in Section 3(a)(8) but that the Commission's analysis of efficiency, competition, and capital formation was deficient. *American Equity Investment Life Ins. Co. v. SEC*, 572 F.3d 923, 929-34, 934-36 (D.C. Cir. 2009).

The Court concluded that the Commission's Section 2(b) analysis was inadequate because the Commission had not made any finding as to the level of efficiency, competition, or capital formation in the marketplace under the existing state-law regime. *Id.* at 935-36. The Court reasoned that such a finding was necessary to establish a baseline against which to assess the impact on efficiency, competition, and capital formation of subjecting indexed annuities to federal as well as state regulation. *Id.* at 935.

In reaching that conclusion, the Court addressed two legal arguments advanced by the Commission. The Court rejected the argument that, based on the Supreme Court's decisions in *SEC v. VALIC*, 359 U.S. 65 (1959), and *SEC v. United Benefit Life Ins. Co.*, 387 U.S. 202 (1967), the Commission did not need to consider existing state insurance law as part of the Section 2(b) analysis. The Court agreed with the Commission that those cases hold that the extent of state

insurance regulation is not relevant to whether an annuity contract falls within the Section 3(a)(8) exemption. But the Court disagreed with the Commission's view that *VALIC* and *United Benefit* therefore made it unnecessary for the Commission to assess the current state-law regime as part of the analysis of whether Rule 151A will promote competition, efficiency, and capital formation. 572 F.3d at 935-36 (“The SEC’s obligations under § 2(b) are distinct from the questions posed in *VALIC* and *United Benefit*. Those cases addressed whether a particular product fell within the § 3(a)(8) exemption; § 2(b) imposes on the SEC an obligation to consider the economic implications of certain rules it proposes.”).

Second, the Court noted but declined to consider the alternative argument (raised only in the Commission's brief) that the Commission was not required to conduct a Section 2(b) analysis at all because Rule 151A was adopted pursuant to Securities Act Section 19(a), 15 U.S.C. 77s(a), which grants the Commission rulemaking authority that is not subject to the requirements of Section 2(b). Without ruling on the merits of that argument, the Court concluded that, in light of the Commission's decision to conduct a Section 2(b) analysis “when it issued the rule with no assertion that it was not required to do so,” the Commission was required to “defend its analysis before the court upon the basis it employed in adopting that analysis.” *Id.* at 934.

In remanding the rule, the Court ordered the Commission to “address the deficiencies with its § 2(b) analysis” and explained that it could do so in either of two ways: by assessing whether the rule will promote competition, efficiency, and capital formation in light of existing state regulation of indexed annuities, or by explaining why Section 2(b) “does not govern this rulemaking.” 572 F.3d at 936.

ARGUMENT

Old Mutual’s request for “a two-year stay of the Rule’s effective date, in the event that [the] SEC decides that the Rule should be reissued” (Pet. 4), should be denied. In arguing for a stay of a rule that is not in effect and has not been reissued, Old Mutual struggles to fit its request within this Court’s two-pronged test for determining whether an agency rule found to be defective should be vacated or remanded without vacatur. *See Allied-Signal, Inc. v. U.S. Nuclear Regulatory Commission*, 988 F.2d 146, 150-51 (D.C. Cir. 1993). The decision whether to vacate depends on “(1) the seriousness of the deficiencies of the action, that is, how likely it is the agency will be able to justify its decision on remand; and (2) the disruptive consequences of vacatur.” *Heartland Regional Medical Center v. Sebelius*, 566 F.3d 193, 197 (D.C. Cir. 2009) (internal quotation marks and citations omitted). Even assuming that the *Allied-Signal* factors are relevant here, neither factor would support vacating Rule 151A, which Old Mutual argues

is the basis for the hybrid “remand-with-stay” relief it is seeking. Pet. 9

(“[B]ecause this case satisfies the *Allied-Signal* factors for vacatur of a rule, it also qualifies for the more limited remedy of remand-with-stay.”).

A. Old Mutual’s request for a stay should be denied because it identifies no reason to doubt that, if the Commission elects to proceed with Rule 151A, it will be able to resolve the Section 2(b) issue that was the basis of this Court’s remand.

Old Mutual has identified no reason for concluding that there is not “at least a serious possibility that the Commission will be able to substantiate its decision on remand.” *Allied-Signal*, 988 F.2d at 151. The Court held that Rule 151A was defective because the Commission conducted a Section 2(b) analysis of the rule without considering the baseline level of efficiency, competition, and capital formation under existing state-law insurance regimes. *American Equity*, 572 F.3d at 935-36. Significantly, the Court did not find that the Commission had tried but failed to adequately assess the effect of existing state insurance regulation on the Section 2(b) factors. Instead, the Court concluded that the Commission had not undertaken such an analysis based on its erroneous conclusion that, under *VALIC* and *United Benefit*, the state insurance regime was legally irrelevant to this rulemaking. Although (as discussed above at pages 4-5) the Court rejected the Commission’s reading of those cases, it did not find or even suggest that on

remand the Commission would be unable to support the reissuance of the rule after conducting the analysis of state insurance law that the Court concluded was necessary: “Indeed, after a more thorough review of the existing state law regime, the Commission may decide ultimately that Rule 151A will promote competition, efficiency, and capital formation.” *American Equity*, 572 F.3d at 936. Old Mutual fails to explain why there is not at least “a serious possibility” that such a state-law analysis could lead the Commission to permissibly conclude that it would be in the public interest to reissue Rule 151A.

Old Mutual’s argument also essentially ignores the alternative path the Court identified for rectifying the Commission’s Section 2(b) analysis. The Court ordered the Commission to “either complete an analysis sufficient to satisfy its obligations under § 2(b), *or* explain why that section does not govern this rulemaking.” *Id.*, 572 F.3d at 936 (emphasis supplied). The second alternative is based on the Commission’s argument that, by its express terms, Section 2(b) does not apply to this rulemaking. Section 2(b) provides that the Commission is required to consider whether a rule will promote efficiency, competition, and capital formation only when it is adopting a rule pursuant to a section that expressly requires the Commission to consider or determine whether the action is

in the public interest.^{2/} Section 19(a), the sole rulemaking authority the Commission invoked in adopting Rule 151A, has no such requirement. Although, as discussed above, the Court declined to consider this argument because it was made for the first time in the Commission’s appellate brief, the Court acknowledged that on remand the Commission could itself adopt the position advanced in that brief.

Nothing in the Court’s opinion suggests that the Commission could not reasonably interpret Section 2(b) as not applying to this rulemaking, and none of the parties or *amici curiae* in this case offered any alternative interpretation of Section 2(b). Old Mutual’s rehearing petition continues that path. Old Mutual asserts that the Commission’s interpretation of Section 2(b) as not applying to this rulemaking is not “plausibl[e]” (Pet. 11 n. 6) but does not offer any contrary interpretation or even attempt to explain why the Commission’s argument—which is based on the plain language of Section 2(b) and Section 19(a)—lacks merit.

² Section 2(b) provides: “Whenever pursuant to this subchapter the Commission is engaged in rulemaking and is *required* to consider or determine whether an action is necessary or appropriate in the public interest, the Commission shall also consider, in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation.” 15 U.S.C. 77b (emphasis supplied).

At bottom, nothing in the Court’s opinion or elsewhere provides any support for Old Mutual’s argument that there is substantial reason to doubt that, if the Commission proceeds with Rule 151A, it would be unable to cure the defect in its Section 2(b) analysis that led the Court to remand the rule. All indications are to the contrary.

B. Old Mutual’s contention that disruption will result if the Court does not immediately order a stay of a rule that is not currently effective is wholly speculative.

Old Mutual’s argument that a stay is necessary to avoid “disruptive consequences” that would occur if Rule 151A’s effective date is not immediately stayed is unfounded and inconsistent with both basic principles of administrative and judicial procedure and the *Allied-Signal* line of authority on which Old Mutual purports to rely.

As Old Mutual concedes, Rule 151A is not now in effect and will not go into effect until, at the very earliest, January 2011. The Commission has begun the process of deciding how to respond to this Court’s remand order and, within a reasonable time, will determine how to proceed—including whether to reissue the rule, and if so, how to address the deficiency in the Section 2(b) analysis.

Ultimately, if the Commission decides to reissue Rule 151A, it will address the rule’s effective date. All of the potential harms that Old Mutual envisions (Pet. 6-

8) derive from its concern that the Commission would reissue Rule 151A without providing adequate lead time for indexed annuity issuers to conform to the rule's requirements—a fear that is wholly inconsistent with the way the Commission has responded throughout this rulemaking and litigation.

As if to prove that point, Old Mutual devotes an entire section of its rehearing petition (Pet. 14-15) to explaining how, in response to comments in the rulemaking process highlighting the steps indexed annuity issuers would need to take to comply with Rule 151A, the Commission accommodated those concerns by extending the effective date from 12 months after adoption (as it had originally proposed) to two years after adoption. Old Mutual further acknowledges that the Commission was similarly responsive to industry concerns during the challenge to Rule 151A in this Court. Pet. 15 (“[B]y consenting to the request for expedited briefing, the SEC again recognized the major impact Rule 151A will have on the FIA industry.”). In short, the Commission's record in this case and the rulemaking demonstrates that Old Mutual's claims of harm are unlikely to transpire.

And if Old Mutual's fears are realized and—contrary to all of its past actions—the Commission *both* decides to reissue Rule 151A without adjusting the effective date as appropriate *and* refuses to stay the rule, Old Mutual can then seek

a stay from this Court.^{3/} At that point, unlike now, Old Mutual would be faced with a concrete compliance obligation and could realistically assess whether it needed additional time to comply and, if so, how much. Presented with such a motion, this Court could assess the request for relief under the established criteria for a stay of agency action. Old Mutual asserts that the relief it is seeking now will “avoid any future need to seek help” from the Court. Pet. 15 n. 7. But for the Court to intervene now based only on potential Commission action that could result in possible competitive harm would contravene basic principles governing the relationship between courts and administrative agencies. For that reason, this Court has routinely denied stay requests in comparable circumstances. *See, e.g., Wisconsin Gas Co. v. FERC*, 758 F.2d 669, 674 (D.C. Cir. 1985) (stay requests based “upon unsubstantiated and speculative allegations” of injury are denied).

Moreover, Old Mutual’s claim of potential competitive harm in the absence of a stay is wholly unlike the disruption that would occur from vacating an *existing* comprehensive regulatory scheme that the *Allied-Signal* line of cases

³ Old Mutual suggests (Pet. 2) that the Commission denied its request to stay the effective date of Rule 151A. That is based only on the Commission’s not having entered a stay in response to a suggestion in a letter from Old Mutual to the Chairman. (Pet. Add. 28). Both because of the form of the request and the fact that it involves a rule that the Commission has not yet decided to reissue, the absence of a Commission stay can hardly be viewed as a final decision regarding the effective date if the Commission *were* to reissue Rule 151A.

found significant.^{4/} In *Allied-Signal*, the Court decided not to vacate the defective rule at issue because vacatur would have required the Nuclear Regulatory Commission to refund fees already collected from those subject to the rule and likely would have barred the Commission from recovering those fees under a subsequently enacted rule that cured the defect. 988 F.2d at 151; *see also Heartland*, 566 F.3d at 198 (similarly concluding that vacatur would have caused disruption by requiring a refund of payments received under the defective rule and barring recoupment of those fees under a reissued rule); *Rodway v. USDA*, 514 F.2d 809, 817-18 (D.C. Cir. 1975) (vacating existing regulations would have disrupted “the functioning of the entire food stamp system, on which over ten million American families are now dependent”). Old Mutual’s speculative claims of harm from a rule that is not yet effective—and that the Commission has not yet decided to reissue—fall well short of the “disruption” that this Court has found relevant in assessing whether a defective rule should be vacated.

⁴ Additionally, Old Mutual’s argument is based on the view that “disruption” would occur if Rule 151A were *not* vacated, whereas the *Allied-Signal* line of cases considered only whether disruption would occur if a rule *were* vacated.

CONCLUSION

For the foregoing reasons, this Court should deny Old Mutual's petition for rehearing requesting modification of the remand order to "requir[e] the SEC to stay the effective date of the Rule for at least two years after the SEC's possible reissuance" of Rule 151A.

Respectfully submitted,

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September 2009

CERTIFICATE OF SERVICE

I hereby certify that on this 28th day of September, 2009, I caused one copy of the RESPONSE OF THE SECURITIES AND EXCHANGE COMMISSION TO PETITION FOR PANEL REHEARING, to be served upon the following, by the method indicated below:

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